THE NEED FOR CREDIT UNION REGULATORY RELIEF AND IMPROVEMENT

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HOUSE COMMITTEE ON FINANCIAL SERVICES

BARNEY FRANK, Massachusetts, *Chairman*

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THE NEED FOR CREDIT UNION REGULATORY RELIEF AND IMPROVEMENT

Thursday, March 6, 2008

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 10:03 a.m., in room 2128, Rayburn House Office Building, Hon. Barney Frank [chairman of the committee] presiding.

Members present: Representatives Frank, Kanjorski, Waters, Maloney, Watt, Sherman, Moore of Kansas, Hinojosa, Clay, Baca, Lynch, Miller of North Carolina, Scott, Green, Cleaver, Davis of Tennessee, Sires, Ellison, Klein, Wilson, Perlmutter, Donnelly; Bachus, Castle, Royce, Lucas, Biggert, Shays, Miller of California, Capito, Feeney, Hensarling, Garrett, Pearce, Neugebauer, Price, McHenry, Marchant, and Heller.

The CHAIRMAN. Good morning. This is a hearing of the Financial Services Committee on the question of the legislation that should govern the activities of credit unions. This has been a subject of considerable interest for some time. I'm very proud that, largely due to the efforts of the chairman of the Subcommittee on Financial Institutions, my colleague from Pennsylvania, Mr. Kanjorski, we are engaged in a serious legislative consideration of this for the first time in the memory of a number of people. This is an issue that has been before us, and I want to acknowledge that it was Mr. Kanjorski's accession to the chairman of the subcommittee and our working together that is the major reason that we are here today. And I am hoping that we are not just going to be talking about this but legislating.

I believe that this committee has shown a willingness with regard to all of our financial institutions to do sensible deregulation. Now deregulation can be carried too far, as it was in the origination of mortgages. I think it should be noted that the percentage of subprime mortgages that have run into difficulty that were originated by credit unions is tiny. The credit unions and the regulators who are here are to be congratulated for showing that it is possible to lend to people of moderate economic means to help them accede to homeownership without irresponsibility and fiscal crisis.

That is a model to which we want to adhere. That is, yes, we want to deregulate because we do not want bureaucratic interference with our ability to help people. But we do not want to take that to the point where abuses run rampant. And so our goal is to continue a pattern that we think has been manifest in the credit union sector of sensible regulation that allows consumers to be served and helps the economy, but does not lead to abuses.

I want to make another point. This is one of the issues that I intend to deal with as we go forward legislatively, and I hope that many of my colleagues will agree. One of the best things we can do for lower income people in this country is to get them into the depository system—credit unions and community banks.

People who are outside of that system pay a far higher percentage in the transactions they do of the cost of those transactions than any of us here, and I daresay than any of you there. Payday lending, check cashing, excessive fees for remittances; those are all problems that lower income people face if they do these transactions outside of the system of credit unions and community banks.

One of the things that I hope we will do is to enhance the ability of both sets of institutions to offer to people in that economic category an opportunity to save money. And so today we are talking about the credit unions that will be particularly our goal; to enhance the ability of credit unions to offer services to people of lower income. Because, again, we have the experience that doing it within the appropriate regulatory structure that we have allows this to go forward in a reasonable way.

I also believe that—and it is on the agenda of this committee—that there are similar deregulatory things we should do with regard to the banking system. I understand that there are conflicts, and there will continue to be. But I believe there is also a commonality of interest in both sets of institutions in reducing regulation which gets in the way of serving people, particularly people in the lower income category.

So it is my hope that this committee will be able to come up with legislation. And let me say, as I am reminded of the stimulus, if we do this well, we will come out with a bill, in my view, that will make no one deliriously happy but that I hope will make no one delirious. Those are the outer limits of our choices. But I think there is room for us to enhance the ability of regulated institutions in general to serve the entire economy, and particularly people in the lower income area, and that is where we will be proceeding.

I have other duties that I need to attend to, so I am going to turn over the hearing to the second ranking member, the chairman of the Financial Institutions Subcommittee, the gentleman from Pennsylvania, who is the main sponsor of the CURIA bill and a man of significant experience and interest in this.

I believe we have indicated—the indication I have received is that under our rules, as a matter of right, each side is entitled to 10 minutes, for a total of 20 minutes. Is that correct? No. Each side gets 20 minutes. Wishful thinking. And I have used only a little over 5 minutes, so I leave my side for the time, and we will proceed with opening statements for the full amount of 20 minutes on each side, and then we will hear the witnesses, and I thank the witnesses for their attendance.

We will begin with the ranking member of the full committee, the gentleman from Alabama, for 5 minutes.

Mr. BACHUS. Thank you, Mr. Chairman. First of all, I would like to associate myself with your remarks. I think the millions of

Americans who are members of credit unions are a testament to the important services that credit unions provide to the Nation. I think that is particularly true and valuable in some of our underserved communities, where the credit union is really the only financial institution.

And sometimes those areas, for whatever reason, are overlooked by other financial service providers. Because they are nonprofit cooperatives managed by their members, credit unions excel at providing high-quality, low-cost services that are responsive to customer needs. In some underserved and rural areas, a credit union, as I said, is the only conventional financial institution to be found. Many constituents have told me that they have been able to afford their house or repairs to their house, start new businesses or even attend colleges because of the help of a credit union loan.

In addition, I—and I know Mrs. Biggert feels the same way—am impressed by credit unions' commitment to financial literacy. It is a well-known fact that credit unions help their members become better educated customers or consumers of financial services.

As we learned during a series of hearings before the Financial Institutions Subcommittee, some of the regulations on credit unions are overly burdensome, they are unnecessarily costly, and they are largely duplicative of other legal requirements. Whenever we can identify these examples of regulatory overkill, Congress should strive to eliminate them. And I acknowledge the gentleman from California, Mr. Royce, for his leadership on these issues.

With our regulatory reform bill, we built a bipartisan consensus last year, and I hope that we can do the same thing this year with these regulatory bills. If we're serious about regulatory relief for credit unions, however, our efforts must be directed not only at eliminating excessive burdens that currently apply but resisting attempts to impose broad new regulatory mandates.

For example, there are some on this committee and in Congress who argue that CRA should be extended to credit unions that currently fall outside the law's coverage. On this point, I strongly disagree. Rather than expanding the regulatory dragnet, our focus must be on providing appropriate regulatory relief so that the credit unions are free to serve the needs of their communities, and by very definition of who they are, they do serve communities. Further, we must ask whether regulatory impositions like CRA would be counterproductive and take away from their resources to lend to their members.

In conclusion, we must keep in mind that our goal should be to improve the quality and lower the price of financial services for consumers. Experience shows that when financial institutions compete for customers, customers benefit.

Thank you, Mr. Kanjorski. I yield back the balance of my time.

Mr. KANJORSKI. [presiding] Thank you, Mr. Bachus. I am pleased that we meet today to examine the need for making statutory improvements and providing regulatory relief for our Nation's credit unions. Nearly 4 years have passed since the Financial Services Committee last met to exclusively examine the many issues of concern to the credit union movement. I therefore commend Chairman Frank for convening this long overdue hearing.

I am also optimistic that today's proceedings will lay the groundwork for swift action on legislation to modify the Federal Credit Union Act. The last time we acted on a comprehensive credit union legislation occurred a decade ago when the Congress adopted H.R. 1151, the Credit Union Membership Access Act. For the last 5 years, we have also worked to craft and build bipartisan support for the Credit Union Regulatory Improvements Act, or CURIA. I have been a leader in both of these reform efforts.

CURIA would help to fix several problems created by the rushed drafting of H.R. 1151. These fixes including putting in place a modern, risk-based capital system for credit unions, allowing credit unions of all types to expand into underserved communities, and amending conversion voting standards.

CURIA also contains a number of provisions to facilitate the ability of credit unions to make business loans. For example, CURIA would raise the current asset limit on members' business loans from 12.25 percent to 20 percent, a limit comparable to the current one of thrifts for their non-real estate commercial lending.

Some have suggested that this modest change represents a major expansion of business lending authority. I have a different view. Prior to the enactment of H.R. 1151, we had no limits on business lending activities of credit unions. CURIA would therefore provide minor but needed adjustments to the limitations on business lending currently imposed by the law.

Support for CURIA has steadily grown over time. During the 108th Congress, we had 69 supporters. In the 109th Congress, we garnered 126 supporters. To date, in the 110th Congress, we have now gained the endorsement of 147 supporters in the House. Our legislation, moreover, no longer has just bipartisan support in the House. It now enjoys bicameral support. I am very pleased that Senator Mary Landrieu announced that she would introduce CURIA in the Senate, along with Senator Joseph Lieberman. Their support clearly demonstrates that the momentum of enacting credit union statutory reforms is growing.

Although support for CURIA is building, I recognize that enacting legislation into law is often a multi-stage process. Therefore, in order to achieve some progress on these matters, I recently introduced a pared-back credit union bill known as the Credit Union Regulatory Relief Act. Like CURIA, Congressman Ed Royce joined me in these efforts. H.R. 5519 contains eight noncontroversial provisions found in CURIA and previously passed by the House.

It also includes language to permit all credit unions to assist those living and working in underserved census tracts, help individuals with short-term financial difficulties to obtain loans, and expand member business lending activities very modestly, through some narrow carveouts and clarifications.

The swift adoption of H.R. 5519 will allow us to continue to work on enacting the many other important legislative reforms contained in CURIA but not contained in this new bill.

Before I close, I would like to strike a cautionary note. At today's hearing, we will hear not only from regulators but also credit unions and banks. In the past, banks and credit unions have sometimes found themselves engaged in what might be termed a family feud. In reality, credit unions and banks have much in common. I hope that they realize this fact. In my view, we can work to expand the pie for both of them by advancing well-crafted reforms to their underlying statutes consistent with safety and soundness objectives.

In closing, I look forward to hearing from our witnesses and engaging in a thoughtful debate. I also look forward to moving a credit union bill through our committee in the very near future.

I yield back the balance of my time. And the Chair will now recognize Mrs. Biggert for 5 minutes.

Mrs. BIGGERT. Thank you, Mr. Chairman, for holding today's hearing to examine credit union regulations. Like banks, credit unions plan an important role in our communities. Credit unions serve the financial needs of upwards of 90 million Americans, some would say as many as one-third of U.S. citizens. Again, like banks, credit unions have provided millions of Americans the credit and financial services that they need to buy cars, build homes, and pay for education.

However, unlike banks, credit unions are tax-exempt organizations that are run by their members. Banks serve both customers and investors, are required to comply with the Community Reinvestment Act requirements and pay taxes. Back in 1934, in the midst of the Great Depression, when banks were failing and credit was scarce, Congress passed the Federal Credit Union Act which established requirements for chartering credit unions as well as a national regulator. Congress revisited this Act a decade ago, and here we are again today.

Based on the written testimony of today's witnesses, it is clear that competition is alive and well in the financial services industry. This is a good thing. It points to the success of this sector of our Nation's economy, but more importantly, to the fact that Americans benefit from such competition.

We are here today to examine the playing field for this competition. Is it level? Should it be level? I hope that today we can better understand the original intent of Congress for credit unions and how that intent holds up in the face of today's realities. Was it to encourage competition with banks? Did Congress intend for credit unions to fill the void left by banks in niche markets and underserved communities? What are underserved communities, or who is underserved in communities? Are credit unions fulfilling or not fulfilling their congressional directive?

Is it also important that we flesh out further what, if any, true need there is to change the capital system and expand member business lending for credit unions, which H.R. 1537 envisions? Well, this committee is always up for a good challenge, and with that, I thank my colleagues, Congressmen Kanjorski and Royce, for presenting us with another challenge, and I look forward to today's discussions.

Thank you, Mr. Chairman. I yield back.

Mr. KANJORSKI. Thank you very much, Mrs. Biggert. And now the Chair recognizes Mr. Baca for 2 minutes.

Mr. BACA. Thank you very much, Mr. Chairman. Okay. Remember I have the additional seconds because my clock didn't start yet.

[Laughter]

Mr. BACA. Thank you very much, Mr. Chairman, for calling this important meeting. I'm proud to be a cosponsor of H.R. 1537, the Credit Union Regulatory Improvement Act. I appreciate my colleagues, Representative Kanjorski and Representative Royce, for having offered this legislation again, and I look forward to doing everything possible to help provide credit unions with the Regulatory Relief and Improvement Act that they need to better serve their members.

I state, to better serve their members, and I think this is what it is all about—the quality of service, and how do we serve the members as well? There are 13 credit unions headquartered in my district that serve one hundred and—I mean, one thousand and twelve plus one hundred and twelve credit union members who live in my district. I agree that several of them contained by Mr. Dorety's testimony, especially when he talks about the services to the underserved.

And I state to the underserved. This is about the underserved, and that's what this hearing about individuals as well, who are underserved. It's hard for me to understand how anyone can complain that credit unions are not doing enough to serve the underserved, given the barriers that credit unions face today. The fact is that those who complain the loudest are the ones who fight the hardest to keep credit unions out of the underserved areas. And I state out of the underserved areas where a lot of us, minorities and others, live.

Mr. Chairman, there are reasons that we call these areas underserved. The banks aren't there, and most credit unions cannot serve these areas. One way that we can provide more services to those needs is to allow credit unions to enter the underserved areas and provide literally unbanked in our country with mainstream and affordable financial services. And this is what we have to do.

I look forward to hearing from today's witnesses on how we can help credit unions continue to reach the underserved—and I state the underserved—in our communities. I yield back the balance of my time.

Mr. KANJORSKI. Thank you very much, Mr. Baca. Now my good friend, Mr. Royce of California.

Mr. ROYCE. Thank you, Chairman Kanjorski. I want to begin just by thanking you for your efforts over the years on behalf of credit unions. I know their 90 million members across the country very much appreciate your efforts. I also want to thank you as a friend and colleague for holding this hearing and focusing our attention on this important issue.

I believe, as you do, that priority should be passage of CURIA. I think it has been a decade since we had any major credit union legislation passed through the Congress, and it is important, I think, to modernize the regulations overseeing credit unions. And I think putting credit unions, as you say, on a par with other FDIC-insured institutions is a good way to do that.

Let me say that Representative Kanjorski and I introduced H.R. 5519 in the meantime, the Credit Union Regulatory Relief Act, this week. And while this legislation does not go as far as many would like, it's important that we not let the perfect be the enemy of the good. And as we build momentum and support for CURIA, we are now looking at passage of this piece of legislation.

It does several things. It provides the NCUA with increased flexibility to determine the interest rates on loans from Federal credit unions. It authorizes credit unions to invest in non-stock investment grade securities totaling up to 10 percent of the credit union's net worth. It permits all credit unions to expand their services into underserved areas, and it exempts business loans made to members within those underserved areas from the lending caps.

And lastly, the Credit Union Regulatory Relief Act would support the community development work of nonprofit religious institutions by excluding such loans from credit union business lending caps. This is based on legislation I had introduced prior in 2003, and we have been trying to advance this particular concept, because this provision would close a long-standing liquidity gap between creditors and nonprofit organizations.

A major priority, by the way, which was left out of this legislation, is the modernization of the current capital requirements for credit unions. And as Chairman Paul Kanjorski shared with you, CURIA incorporates the net worth and prompt corrective action reform proposals of the National Credit Union Administration, the Federal regulator responsible for the safety and soundness of the credit union system.

CURIA would replace the current one-size-fits-all leverage capital requirement for credit unions with a more rigorous two-part net worth structure that would more closely monitor actual asset risk. The revised credit union capital/PCA structure would incorporate the relevant international risk-based standards for Basel I and Basel IA financial institutions, and it would very closely resemble the current risk-based capital standards for FDIC-insured banks and thrift institutions in this country.

So I believe this, along with many of the other provisions found in CURIA, but not in H.R. 5519, are important. They should not be forgotten as we continue to work toward that goal. We have 145 Members of Congress who have signed onto the legislation. It is going to remain the primary vehicle to modernize regulation of credit unions, and of course, it has also been introduced this week in the United States Senate.

So, again, I'd like to thank Chairman Kanjorski for his work on this issue. I think we have a good starting point, and as we move toward a markup on this legislation, I am hopeful we can gain a better perspective and develop a workable solution. I look forward to hearing from our extensive panel of witnesses who are with us today, and I thank them for making the trip out here. I yield back the balance of my time, Mr. Chairman.

Thank you.

Mr. KANJORSKI. Thank you very much, Mr. Royce. The gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Mr. Chairman, if I may, could I just yield to my good friend, Mr. Green? He has an appointment. Then I could come after him?

Mr. KANJORSKI. Surely.

Mr. GREEN. Thank you, sir. Thank you, Mr. Chairman. I thank the ranking member as well. I thank the members of the panel who will appear today. I am honored to be with you and regret that I will have to leave.

I just want to note that we have 8,100 credit unions across the length and breadth of the country, serving 90 million members. In Texas, we have 603 credit unions, about 6.9 million members. Credit unions are making a difference, and sometimes they can be the difference in asset acquisition and wealth building. I thank you again, and I yield back the balance of my time.

Mr. KANJORSKI. Thank you very much, Mr. Green. The gentleman from Texas, Mr. Hensarling.

Mr. HENSARLING. Thank you, Mr. Chairman. I have 89,000 members, credit union members, in my district, and I know how important the credit union movement is to them. I also have noticed in my district the important role that credit unions are playing in the subprime challenge that we have, given their relatively low exposure to that market, that they are being very helpful in a lot of workouts and a lot of financial situations.

I would also let folks in the credit union movement know, and I see several of my friends here today. They may not know it, but recently, I became a credit union member myself. But before you get too excited, no, I have yet to cosponsor CURIA. I did, however, as my friends know, along with the gentleman from Kansas—I do not see him here at the moment—Mr. Moore, helped champion regulatory relief in the last several Congresses. Many titles that were in our regulatory relief bill are also simultaneously in CURIA.

I continue to be very concerned about the regulatory burden on our financial institutions, and I continue to support regulatory relief that is generally applicable to all financial institutions. I am particularly concerned about the burden that the Bank Secrecy Act continues to play in our financial system. However, I am also very mindful that one person's regulatory relief is another person's regulatory advantage.

We do know that credit unions enjoy certain unique privileges within our system. Those privileges I am happy to defend, but there was a dramatic change a decade ago when the common bond requirements were modified. I believe tradeoffs were had at that time with respect to lending caps and capital requirements. Although I have many persuasive friends in the credit union movement, I have yet to be persuaded that balance should be upset.

Having said that, I continue to have an open mind. It is not an empty mind. So I look forward to hearing the testimony, and I am very glad to hear my good friend from California, Mr. Royce, talk about the ability to perhaps advance H.R. 5519, where we do have common ground, in hopes that these other issues may be worked out at a later time.

With that, I yield back. Thank you.

Mr. KANJORSKI. The gentleman from Georgia now, Mr. Scott, for 2 minutes.

Mr. SCOTT. Thank you very much, Mr. Chairman. This is indeed a very, very important and timely hearing. And we have what really amounts to a delicate balancing act here to accomplish.

First of all, we do have a need. The credit unions are there. They deserve the attention and relief under this bill, because they do serve an underserved community, particularly lower and moderate income communities and minority communities. And so we need to make sure we keep that in mind.

Now there are four actors here that have to be taken care of. We have the regulators. We have the banks. We have the credit unions. But the most important part of this is the consumer themselves. We have the banks, the regulators, and the credit unions here before us, but we don't have the consumer. And that is where we, who represent the consumers, must take that into consideration.

But there are areas where we can work together, particularly when you take the meltdown in the mortgage markets. There is a need that we could have for credit unions to be able to help take some of the downward pressure off of banks now that are tightening up on their requirements, to give the consumers another way and another resource with which to refinance their homes. That is one area that we have to take into consideration.

Now this is sort of like a ball game. We have to get to several bases. We have to compromise. We have to work. Any reform, it takes time, it takes patience. But if we understand our mutual goal, which is to provide that kind of relief to assist an underserved community that needs that service, an unbanked community, then I believe we have room for agreement here.

Today, with this hearing, we will certainly get to first base. Then we have to get to second base, third base, and then home. And I believe we will be able to score some runs that way.

I look forward to this hearing. It is a very important hearing. Thank you, Mr. Chairman.

Mr. KANJORSKI. Thank you very much, Mr. Scott. We now have Mr. Pearce of New Mexico.

Mr. PEARCE. Thank you, Mr. Chairman. I appreciate you convening the hearing. New Mexico is very much rural. Some counties have more land mass than States back East, and fewer than 1,000 or 2,000 residents underserved is a very key problem that we face, not just available access to lending.

I understand and appreciate the concerns of the banks. I see the large, large growing institutions that look almost like banks and have tax advantages, so we are very familiar with those. But at some point in our State, we have to address the access to liquidity. So we are interested in the hearing on the bill to hear both sides and look to see the ways that we can make the system more fair.

I would encourage the chairman to hold a hearing on the Communities First Act, H.R. 1869. I think that more than regulatory relief right now we have to be concerned with the entire aspect of our financial institutions. We had a couple of hearings last week that raised significant concerns. And so we need to be looking through this problem to making all financial institutions more sound and more competitive worldwide. So I hope that the chairman would consider that also.

I look forward to the hearing and appreciate the chairman for convening it. Thank you.

Mr. KANJORSKI. Thank you very much, Mr. Pearce. And now we'll have Mr. Cleaver of Missouri.

Mr. CLEAVER. Thank you, Mr. Chairman. I appreciate this hearing. It seems as if each hearing this committee participates in is one that deals with those who hate regulations and those who want more. I have twin sons, and when they were smaller—we have a huge backyard and they would be riding their bicycle, and one of them would say, "Daddy, would you make him get off so I can ride?"

I think that is kind of what we hear when we deal with credit unions and banks and other financial institutions. And I think that it is our responsibility to protect the consumers while at the same time making sure that there are opportunities available to the financial institutions, such as banks, and that we ought to create those opportunities with as few barriers as possible.

But I'm looking forward to getting into the question and answer period, because I think that the great conflict is always, you know, laissez-faire. And I think if we have laissez-faire, we probably don't need Congress, and I don't need any response to that. It seems to me that we have a responsibility to play this role, and I look forward to playing it.

Thank you, Mr. Chairman. I yield back the balance of my time.

Mr. KANJORSKI. Thank you very much, Mr. Cleaver. And now we will hear from the gentleman from Georgia, Mr. Price, for 1 minute.

Mr. PRICE. Thank you, Mr. Chairman. I want to thank the chairman and Ranking Member Bachus as well and add my commendation to them for holding this hearing. And I want to commend Congressman Kanjorski and Congressman Royce for their ongoing efforts to spotlight this issue.

I want to welcome all the members of the panel. I want to particularly welcome Mr. George Reynolds, who is the senior deputy commissioner of the Georgia Department of Banking and Finance. Welcome. We look forward to your testimony.

I am interested in a number of issues. One of the provisions of H.R. 1537, the CURIA Act, would update the current capital requirements for credit unions addressing some concerns that NCUA has that the current capital requirements for credit unions may be too inflexible and should become more risk-based. We are all aware of the challenges that the housing market is creating for our whole economy, and I would be interested in hearing all panel members' thoughts on whether those challenges that we're facing require or would benefit from any legislative or congressional action as it relates to credit unions.

Additionally, Chairman Kanjorski and Congressman Royce have introduced a couple of pieces of legislation on regulatory relief, and I am interested in hearing from the panel specifically on those regulatory challenges that you or your clients and those that you represent face during their daily routine. Specifically, are there compliance tasks that you feel are overly burdensome and end up costing more in compliance costs than they're worth for either the system or for consumers?

And again, I appreciate each of you coming and look forward to your testimony and the Q&A. Thank you, Mr. Chairman.

Mr. KANJORSKI. Thank you, Mr. Price. And now, we will hear from Representative Neugebauer of Texas for 2 minutes.

Mr. NEUGEBAUER. Thank you. And I thank Chairman Frank for calling today's hearing. It's good to have all of our friends from the credit unions in Washington this week. I had several from my district, from Big Spring and Abilene yesterday. And I think it's important that you come to your Nation's capital and talk to the people who represent you here and make sure that your views, which are the views of your shareholders, your stakeholders, are expressed on this important issue.

I appreciate the contribution that the many credit unions in my district make to the folks in West Texas. They are working very hard to make sure that they serve their customers. And one of the things that we're very blessed in our Nation, and particularly in our—in Texas is we have a lot of good, healthy financial institutions, banks, thrifts, and credit unions that provide for the financial needs of the folks that we serve.

I think one of the important things is that whether it is a credit union or a bank or a thrift, what I hear over and over again is we have to do something about decreasing the amount of regulation because they said—what they tell me is they spend more time now working for the regulators than they spend time working for the people that they serve. And certainly I support additional efforts on behalf of this committee to look at ways to reduce the regulatory environment and also make sure that we have a streamlined, efficient, 21st Century financial services industry.

Like many of my other colleagues, I am particularly interested in looking at the way that we assess the capital needs of credit unions in our country. I think the current system is an antiquated system today that we ought to measure the amount of capital that a financial institution has not based on what some arbitrary number that we're going to try to make one size fit all, but with a number that is based on the kinds of loans and lending practices that that particular credit union is using, as we do with other financial institutions to measure what is the risk that they are taking and then make their capital requirements to coincide with that.

And so I think that's a system that makes sense. I again thank of the panelists for being here today. We look forward to hearing from you as we try to make America's financial institutions a better place and better serve the folks for whom we all work.

Thank you, Mr. Chairman.

Mr. KANJORSKI. Thank you very much. And now we will hear from Mr. Davis of Tennessee for 1 minute.

Mr. DAVIS OF TENNESSEE. Thank you, Mr. Chairman. Living in a rural area as I do, and representing 10,000 of Tennessee's 40,000 square miles in the 4th, one of the most rural residential Congressional districts in America, we need every available resource to us that we can that will supply credit for those consumers in the 4th District to be able to at least access reasonable rates and reasonable terms.

Since 1934, 8,100 credit unions have been established across the State, representing over 90 million people. But in the district I represent, we have small, independent bankers as well. And from my perspective, there's a reason that subprime lending is not damaging our small local banks nor our credit unions. We haven't gotten involved in that, consumer lender. So I applaud the folks in 1934 and Congress who saw fit to establish—and saw the need for the credit unions.

But I also realize that as I live in a small rural area, I live in an area where there were two banks that didn't close in 1929 during the Great Depression. So I want to be sure that as we navigate through the future, we continue to allow credit unions to be able to provide the great service they are providing today, but also to be sure that our small banks in the district I represent are still going to be standing 10 years, 20 years, and 30 years down the road.

Thank you for coming today, and I look forward to the question and answer session. I yield back my time.

Mr. KANJORSKI. Thank you, Mr. Davis. I will now introduce the panel. Thank you for appearing before the committee today, and without objection, your written statements will be made a part of the record. You will each be recognized for 5 minutes for a summary of your testimony.

First, we have the Honorable JoAnn M. Johnson, Chairman of the National Credit Union Administration.

Ms. Johnson.

STATEMENT OF THE HONORABLE JOANN M. JOHNSON, CHAIRMAN, NATIONAL CREDIT UNION ADMINISTRATION

Ms. JOHNSON. Thank you, Mr. Chairman, Ranking Member Bachus, and members of the committee. I thank you for this opportunity to testify. The variety of proposals before Congress would strengthen NCUA's ability to maximize the safe and sound operations of over 8,000 federally insured credit unions, modernize important aspects of the Federal Credit Union Act, and grant greater flexibility to credit unions serving consumers.

The written statement I have submitted contains analysis of four bills: H.R. 1537; H.R. 1849; H.R. 3113; and H.R. 5519. I would like to devote most of my statement to two paramount issues—prompt corrective action reform, and extension of credit union service to consumers in underserved areas.

I want to thank Chairman Frank for his leadership and Representatives Kanjorski and Royce for their stewardship of the issues contained in CURIA, and in a new iteration, H.R. 5519, just introduced this week. You have consulted with and advised this agency on a number of occasions as you assess possible updates to the Federal Credit Union Act, and have led an informed discussion of issues that have real world benefits for consumers.

I also commend Representative Velazquez for her tireless efforts to assist credit union efforts to reach out to small business communities, and Representative Serrano for his legislation to improve credit union service in disadvantaged communities.

NCUA currently administers a system of prompt corrective action with the purpose of resolving problems at credit unions at the least possible cost to the National Credit Union Share Insurance Fund. Our experience in regulating and supervising credit unions has shown that a more fully risk-based system, such as the one contemplated in H.R. 1537, would improve the regulatory regime while at the same time enable credit unions to put more money in the hands of their members.

The legislation mirrors a proposal adopted by NCUA last summer and incorporates substantive and very helpful input from the

Department of the Treasury. It also recognizes developments that have occurred with the adoption of the new Basil II capital standards for FDIC-insured institutions. A new risk-based system promotes active management of risk in relation to capital levels.

By emphasizing risk assessment, credit unions would be able to better relate their capital to the risk they are assuming. Cash in the vault carries a different degree of risk than a 30-year fixed mortgage, and we believe our regulation should be able to recognize this. Also, NCUA oversight will be strengthened using additional tools to identify each credit union's risk profile based on their activities.

It is important to note that the proposed leverage ratio thresholds will in fact result in some credit unions being required to hold more capital than under the current system. The proposed system would be robust and would promote a regulatory regime that more accurately portrays risk. It would reduce regulatory burden on credit unions while enhancing their ability to manage their balance sheets in a more efficient, effective, and most importantly, safe manner.

What I have just described is an accountant's-eye view of PCA reform. What it means to consumers is more dollars available from their credit union for them to save, invest, and put to productive use, all in a safe and closely monitored environment.

Another important feature of my regulatory relief legislation—of any regulatory relief legislation—involves modernizing the statute to allow all types of federally chartered credit unions to adopt underserved areas. Currently, NCUA can only permit multiple group credit unions to add underserved areas in their field of membership. Single group and community chartered credit unions are not authorized to adopt these areas.

All types of federally chartered credit unions should be able to improve access, particularly at a time when so many Americans have turned to predatory lenders and are suffering the unfortunate consequences. Three different bills have language that would address the situation, and NCUA would be supportive of these approaches.

I do note that H.R. 5519 establishes new standards regarding how credit unions are serving consumers when adopting underserved areas. We want to work with Congress to make sure that all consumers have choices in financial services. NCUA takes outreach seriously.

Turning briefly to other issues addressed in regulatory relief proposals, several bills propose to improve the ability of credit unions to make member business loans. We support those efforts and note that credit union member business lending can be beneficial and productive service offered to consumers. We also underscore the importance of strong and active NCUA supervision of these activities. NCUA continues to devote significant attention to guidance for all credit unions in all types of lending. Irrespective of any statutory limits on individual or aggregate credit union member business loans, NCUA will continue to be vigilant and aggressive in its supervision.

H.R. 5519 contains a provision that builds upon the progress Congress made 2 years ago in helping consumers find lower-cost alternatives to predatory lenders. Allowing credit unions to provide payday loan services within their field of membership makes sense, and we commend the approach.

NCUA believes these modernizations represent significant improvements to our ability to regulate and supervise credit unions. We stand ready to work with Congress as you seek ways to improve the delivery of financial services to credit union members, and we feel confident that your deliberations will succeed.

Thank you very much.

[The prepared statement of Ms. Johnson can be found on page 78 of the appendix.]

Mr. KANJORSKI. Thank you very much, Ms. Johnson. As everyone knows, we have two votes on the House Floor, and rather than taking any more statements, we have about 6 minutes remaining on those votes, so we're going to recess the committee for about 20 minutes, and then we will reconvene and take further testimony.

The committee stands in recess.

[Recess]

Mr. KANJORSKI. We will now reconvene. Next, we will hear from Mr. George Reynolds, senior deputy commissioner of the Georgia Department of Banking and Finance, testifying on behalf of the National Association of State Credit Union Supervisors.

Welcome to the committee. Mr. Reynolds, if you will present your testimony?

STATEMENT OF GEORGE REYNOLDS, SENIOR DEPUTY COMMISSIONER, GEORGIA DEPARTMENT OF BANKING AND FINANCE, ON BEHALF OF THE NATIONAL ASSOCIATION OF STATE CREDIT UNION SUPERVISORS (NASCUS)

Mr. REYNOLDS. Good morning, Chairman Kanjorski, and distinguished members of the House Committee on Financial Services. I appear today on behalf of NASCUS, a professional association of State credit union regulators. NASCUS believes that H.R. 1537, the Credit Union Regulatory Improvement Act of 2007 called CURIA, is important legislation.

As State regulators, we determined our position on the provisions in CURIA after reviewing the effect on credit union safety and soundness and State law.

NASCUS supports comprehensive capital reform. First, credit unions need to be assessed using risk-based capital standards; and second, credit unions should have access to alternative capital. From a State regulatory perspective, capital reform that addresses these areas makes sense.

CURIA expands risk-based capital options to all federally insured credit unions. NASCUS has long supported that risk-based capital standards are appropriate. We believe it is a sound and logical approach to capital reform for credit unions. The implementation of prompt corrective action for credit unions doesn't just happen. It requires strong cooperation and consultation between State and Federal credit union regulators as provided by the Credit Union Membership Access Act. We believe coordination between State and Federal regulators is imperative to ensure effective capital reform.

Also, comprehensive capital reform requires more than just risk-based capital. NASCUS believes that CURIA's capital reform provisions would be enhanced by allowing a provision for the inclusion for alternative capital.

Simply put, credit unions would benefit from alternatives that allow them to raise capital other than through retained earnings. In fact, low-income and corporate credit unions currently have access to alternative capital. We understand that additional dialogue with policymakers, the credit union industry, and NCUA is necessary to reach a consensus on alternative capital. Now is the time for dialogue before capital requirements are refute and time sensitive.

Let me point out a few considerations. First, NASCUS is not the only voice advocating access to alternative capital. The Filene Research Institute released a study in November of 2007 entitled, "Alternative Capital for U.S. Credit Unions: A Review and Extension of Evidence Regarding Public Policy Reform." The report concludes that it is in the public interest to permit credit unions greater access to alternative capital. It is attached to our testimony.

Next, while the majority of credit unions were not involved in the subprime real estate market problems, all financial institutions are experiencing impacts from the residential mortgage market.

How would alternative capital help? It would allow credit unions, as it does other financial institutions, to meet these challenges and potentially thrive in an uncertain market environment.

As regulators, we realize that alternative capital requires solid regulation and rigorous regulatory review to ensure that these products are properly structured, meet proper disclosure requirements, and do not create any systemic risk. Before a credit union would be given access to alternative capital, it must demonstrate that it has the resources to properly manage alternative capital.

NASCUS supports revisions to member business lending. Changes will provide an opportunity for credit unions to better serve members. With proper underwriting and controls, these changes are not believed to be a risk to safety and soundness.

While NASCUS supports revisions, we recognize that they require proper regulatory oversight through examination and supervision. Credit unions must have a thorough understanding of member business lending and be diligent in their written policies, underwriting, and controls for provisions to be implemented in a safe and sound manner.

CURIA also outlines procedures on conversion voting requirements. NASCUS supports full transparency and disclosure. We believe that any legislation concerning conversion requirements of a State-chartered credit union should recognize State law.

NASCUS appreciates the opportunity to testify. Our discussion was limited to those provisions in CURIA that impact State-chartered credit unions. We urge this committee to be watchful of Federal preemption and to protect and enhance the viability of the dual chartering system. We welcome questions from committee members.

Thank you.

[The prepared statement of Mr. Reynolds can be found on page 124 of the appendix.]

Mr. KANJORSKI. Thank you, Mr. Reynolds.

We will now hear from Tom Dorety, president and chief executive office of the Suncoast Schools Federal Credit Union, testifying on behalf of the Credit Union National Association.

Mr. Dorety?

STATEMENT OF TOM DORETY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, SUNCOAST SCHOOLS FEDERAL CREDIT UNION, ON BEHALF OF THE CREDIT UNION NATIONAL ASSOCIATION (CUNA)

Mr. DORETY. Thank you. Chairman Kanjorski and members of the committee, on behalf of the Credit Union National Association, I appreciate the opportunity to appear before you to express our support for H.R. 1537, the Credit Union Regulatory Improvement Act.

CUNA is the largest credit union advocacy organization, representing over 90 percent of our Nation's 8,400 State and Federal credit unions and their 90 million members. I am Tom Doherty, CEO of Suncoast Schools Federal Credit Union in Tampa.

As you are well aware, we are experiencing a credit crunch in many sectors of the economy. It is ironic that credit unions are ready, willing, and able to help alleviate the problem and promote economic growth, and yet we are inhibited from doing so by outmoded laws that protect the narrow self-interests of bankers.

Mr. Chairman, the last major changes to the Federal Credit Union Act were made in 1998. These changes did not provide significant regulatory relief to credit unions. In fact, the opposite is the case. The Credit Union Membership Access Act imposed statutory burdens related to business lending and prompt corrective action.

It is now time for Congress to reconsider the applications of these statutory requirements. Credit unions support the provisions of H.R. 1537 which would increase the current limit on credit union member business loans from 12.25 percent to 20 percent of total assets and permit the NCUA to increase the threshold for defining an MBL from $50- to $100,000.

We hope that Congress will also consider eliminating the statutory business lending cap entirely. There is no economic rationale for this cap. Credit unions have been providing these loans safely for nearly 100 years. If that broader approach is not approved as an alternative, CUNA asks Congress to consider exempting MBLs made in underserved areas from that cap.

Credit unions also seek modernization of the statutory capital requirements Congress enacted in 1998. By law, not regulation as for other depository institutions, credit unions must maintain a 7 percent net worth ratio in order to be considered well capitalized. In comparison, the current ratio for banks to be well capitalized is only 5 percent.

This capital requirement for credit unions is inefficient. It unnecessarily retards member service and growth and it does not appropriately account for risk of a credit union's assets.

Under the proposal in H.R. 1537 which has been endorsed by NCUA, the new capital requirements would still be more strenuous than bank capital requirements and would accurately account for the risk for the credit union's portfolio. A more precise, risk-based capital requirement would enable credit unions to do even more to help members in these economically stressful times.

CUNA also supports a statutory clarification that all Federal credit unions may apply to NCUA to add underserved areas. This provision will enhance the ability of credit unions to assist underserved communities with their economic revitalization efforts. It provides all Federal credit unions with an opportunity to expand services to individual and groups working or residing in areas that meet unemployment and other distress criteria identified by the Treasury Department.

Mr. Chairman, it's unfortunate that credit unions must come to Congress to ask for this clarification. You, yourself, along with several members of this committee thought that had been addressed 10 years ago. We were forced to ask Congress for this provision because the American Bankers Association sued NCUA in 2005 for authorizing single sponsor and community chartered credit unions to add underserved areas to their field of membership.

In a November 2005 hearing before the House Ways and Means Committee, the ABA complained that credit unions do not do enough to serve people of modest means. Within days, the same group took credit unions to court to prevent them from doing so.

Mr. Chairman, as you know, these areas are called underserved with good reason. Banks make a business decision not to operate in underserved areas. Credit unions seek to serve the underserved. It is not just part of our congressionally mandated mission; it is part of our core mission.

Six years ago my credit union added and opened a branch in an underserved area in Immokalee, Florida. The median income in this county is $24,000. We currently have over 6,600 members, $24,000 million in deposits, and $62 million in loans from this area. We are providing quality financial services to an area that otherwise would not have it.

Those living in underserved areas lack access to mainstream financial services. For millions of lower income families, this means their only alternative is to use the high cost products provided by check cashers, payday lenders, finance companies, and pawn shops. CURIA would permit all Federal credit unions to apply to NCUA to add underserved areas. This is what many Americans need in order to have mainstream financial services.

Mr. Chairman, my written testimony provides greater detail on these and other provisions. I appreciate the opportunity to appear before the committee and look forward to any questions the members may have.

Thank you.

[The prepared statement of Mr. Dorety can be found on page 62 of the appendix.]

Mr. KANJORSKI. Thank you very much, Mr. Dorety.

Next we will hear from Mr. Michael N. Lussier, president and chief executive officer of the Webster First Federal Credit Union, testifying on behalf of the National Association of Federal Credit Unions.

Mr. Lussier?

STATEMENT OF MICHAEL N. LUSSIER, PRESIDENT AND CHIEF EXECUTIVE OFFICER, WEBSTER FIRST FEDERAL CREDIT UNION, ON BEHALF OF THE NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS (NAFCU)

Mr. LUSSIER. Good morning, Mr. Chairman, and members of the committee. My name is Michael Lussier, and I am the president and CEO of Webster First Federal Credit Union located in Webster, Massachusetts. I'm here today on behalf of the National Association of Federal Credit Unions, where I proudly serve on the board of directors.

We appreciate the opportunity to express our views and the need for credit union regulatory relief and improvements. As with all credit unions, Webster First is a not-for-profit financial cooperative governed by a volunteer board of directors who are elected by our members.

I am pleased to report to you that unlike other types of financial institutions that put many people into predatory subprime loans, credit unions work with their members to give them responsible loans at rates that they can afford. America's credit unions are vibrant and healthy. Membership in credit unions continues to grow, now serving over 90 million Americans.

According to data obtained from the Federal Reserve Board, in terms of financial assets, credit unions have just a 1.1 percent market share and, as a consequence, provide little competitive threat to other financial institutions.

NAFCU would like to thank Representatives Paul Kanjorski and Ed Royce for their leadership in introducing H.R. 1537, the Credit Union Regulatory Improvements Act; and H.R. 5519, the Credit Union Regulatory Relief Act; and the many members of this committee who have cosponsored these important pieces of legislation.

The facts confirm that credit unions are more heavily regulated than other financial institutions. We believe H.R. 5519 is a solid and non-controversial bill and urge the committee to take up and pass these needed first steps at regulatory relief in a timely manner.

I want to focus my statement today on two aspects of CURIA which are much needed by the credit union community. First, Prompt Corrective Action, or PCA reform, would modernize credit union capital requirements by redefining the net worth ratio to include risk assets as proposed by the NCUA. This would result in a new, more appropriate measure to determine the relative risk of a credit union's balance sheet and also improve the safety and soundness of credit unions and our share insurance fund.

For example, the current capital system treats a new 1-year, unsecured, $10,000 loan the same as a secured, 30-year mortgage that is on its last year of repayment; something that just simply makes no sense. It is important to note that this proposal would not expand the authority for NCUA to authorize secondary capital accounts.

Rather, we are moving from a model where one-size-fits-all to a model that considers the specific risk posed by each individual credit union. This proposal creates a level comparable to but still greater than what is required by FDIC insured institutions.

Secondly, NAFCU also asks the committee to refine the member business loan cap established as part of the Credit Union Membership Access Act in 1998, replacing the current formula with a flat rate of 20 percent of the total assets of a credit union.

At Webster First, we are currently at the cap of 12.25 percent and, as a result, each week we must turn away members requesting business loans that cannot be obtained elsewhere. The simple modification of the Member Business Lending cap would allow Webster First to provide an additional $32 million in small business loans to our members in central Massachusetts.

There are many credit unions like mine in congressional districts across the country that can provide the immediate economic stimulus to their local areas by this simple change that does not cost the government a dime.

We also support revising the definition of a member business loan by giving NCUA the authority to exclude loans of $100,000 or less from counting against the cap. The current de minimis level of $50,000 was established in 1998 and has been eroded by inflation over the last 10 years.

There is a lot of rhetoric out there on this issue, but I must note that a 2001 Treasury Department study entitled, "Credit Union Member Business Lending," concluded that "credit unions' business lending currently has no effect on the viability and profitability of other insured depository institutions."

In conclusion, the state of the credit union community is strong and the safety and soundness of credit unions is unquestionable. Nevertheless, there is a clear need to ease the regulatory burden on credit unions. It has been 10 years since Congress last enacted major credit union legislation.

NAFCU supports H.R. 5519 as important first step in providing regulatory relief and urges its passage. Furthermore, we call on the committee to follow the lead of the 145 Members of the House who are supporting CURIA and pass this important legislation.

Lastly, we ask that any efforts to provide regulatory relief to financial institutions are balanced and equitable. We look forward to working with you on this important matter and I welcome your comments and questions.

Thank you very much.

[The prepared statement of Mr. Lussier can be found on page 94 of the appendix.]

Mr. KANJORSKI. Thank you very much, Mr. Lussier. And I thank the entire panel for their testimony. It was very informative. I certainly have a few questions, as I am sure my colleagues do.

First and foremost, I am certainly going to reserve some of the questions for the banking witnesses, because I am at a loss, honestly, to understand the two elements of H.R. 1537 that I hear the most objection to from the banks: the risk-based capital question; and the conversion question.

It would seem to me that it is just good practice to put the credit union financial position on the same level with risk as other banking institutions have. It would be good for the system. It is good for the credit union movement and it would actually be good for the banking system as a whole. So I do not understand their objection to that.

Secondly, the conversion problem is almost insulting in terms of so few people today can dissolve credit unions and dispose of the assets in a favorable way to themselves as opposed to having a recognition of the built-up equity over generations that credit unions represent. I find that offensive, if for no other reason than that.

Rather than having the type of conversion system we have now, I would rather a court dispose of the assets and direct the assets to a like or similar type of entity to carry on the mission that was originally indicated for the to-be dissolved credit union. But we will save those questions.

What do the witnesses have to say in terms of, maybe I will start with Ms. Johnson. Why do you think there is such objection to the risk-based capital structure that we have put in place, since our committee and the Congress have really worked very closely with the regulators to take exactly what they have recommended in its best regards and try to put it into place and adopt it into law? Have you heard any response or comment as to what the objection is to everyone else on this point?

Ms. JOHNSON. Congressman, I think the proposal before you is one, on this risk-based capital, is one that is coming from the regulator. It is not coming from the trades. It is not coming from the credit unions that have been working on this for over 3½ years.

I think the opposition that is out there is misleading in that it is being sold as an across-the-board reduction in capital for credit unions. This is not true. What this is, it is a positive—this will have a positive impact on our insurance fund from the standpoint that it allows us as the regulator to identify problems more quickly.

Credit unions will be assessed higher risk levels for riskier activities, or higher capital levels for riskier activities; and it's actually a tool for us as a regulator. This is not a give-away. In fact, for 30 percent of the credit unions it is actually going to raise their capital levels, or those standards.

So I think it has been sold as a give-away, and by all means, it is just the opposite. It is a tool for us. It is my number one priority of all of the regulatory items that we are addressing today. This is probably the one that is most important to me as a regulator and so I would really ask for your serious consideration of this proposal that it either be included in the legislation, or put back in whatever piece might actually pass.

Mr. KANJORSKI. Well, as you may or may not know, what we broke out is H.R. 1537 to stand on its own as it was originally introduced, and maybe modified by H.R. 5519, which we recently introduced this week, which would take the less contentious elements so that we can move them through the Congress quickly and get them passed.

But of course, we are not going to accomplish the two most important things there: the conversion correction; and the risk capital correction. How can we make this strong issue?

Maybe I am asking the wrong person on this since you participated as a regulator in adopting this, but I have been sort of frustrated myself over the last several years because I thought we invited everybody's comment. It was not anything that anyone individually promoted, not the association or the credit union movement themselves, but in fact the regulator.

And we waited, if you recall, until you completed all of your studies before we wrote the bill and then incorporated what the regulator asked us to incorporate in the bill.

Ms. JOHNSON. Congressman, it is frustrating for me, too, that this item is being seen as contentious, because it shouldn't be. We have put over 3 years of work into this.

Actually I saw written quotes in the media early on from the bank and trade associations that they understood that this was probably necessary. And then I think as time went along and the fires were stoked in a competitive nature, I think it became contentious, but in my belief for the wrong reasons. This is substantive and we see it as a necessary tool.

Mr. KANJORSKI. Now you know we have made some corrections in CURIA in terms of conversion. I am just going to take another minute. Do you feel that we have made sufficient corrections to prevent abuse in conversions that have been occurring over the last several years? And as a regulator, are you satisfied with what we have done?

Ms. JOHNSON. Well, from our standpoint, we just recently put out a new ANPR that we are continuing to study some of these elements that we still find in conversions, and I think this is probably the most important ANPR that we have put out during my tenure at the agency and we're asking for additional ideas. We have been doing additional study in areas of conversions, mergers, insurance, and so we will continue to work with you. This has been an area of concern for us as well.

Mr. KANJORSKI. I remember particularly conversions so well. It had to have been about 11:00 or 12:00 at night when we were in the final consideration of H.R. 1151, and I was so frustrated with the blowing away of getting reasonable quorums to vote for conversion that I almost decided to oppose H.R. 1151, but I knew how important it was for the membership portions of it that we would have destroyed the credit union movement.

So I accepted thinking—this is 10 years ago—that we would never let this happen and continue to go on in Congress. We would come back and correct it. I anticipated that we would have a correction in a matter of years. Here we are 10 years later, still fighting the same issue.

Mr. REYNOLDS. Mr. Chairman, I just wanted to make one comment about the conversion issue from the State perspective. I just wanted to make sure that it is understood that there is sensitivity to the fact that there are State law issues.

We do have State laws in place in many of our States that deal with conversions. They have very robust disclosure and governance provisions in them and whatever solution in this area is considered, we just want to make sure that for State credit unions in particular, there is acknowledgement of the fact that there are State law issues that should be considered.

Mr. KANJORSKI. Have you—

Mr. REYNOLDS. Yes, I commented on that in our written testimony, and I alluded to it in my oral testimony as well.

Ms. JOHNSON. Congressman, I would just add that, as you know, credit unions are member-owned cooperatives, and our focus has been on the members and the transparency in this process. I have been up here to testify a couple of times on conversions, and that has always been our focus and will continue to be the focus. But these are member-owned cooperatives, and so the members' interest is our priority.

Mr. KANJORSKI. Thank you all, very much. And now, Ms. Biggert, if you will?

Mrs. BIGGERT. Thank you, Mr. Chairman. I would like to thank the panel for all of their testimony. And I would also like to recognize the Illinois credit unions that are here to hear your testimony and our questions.

Mr. Dorety, one thing that always bothers me just a little bit is that credit unions do enjoy certain advantages, such as the tax-exempt status. But it was because they are established as member-owned financial cooperatives to meet the financial needs of the members.

But given that advantage, shouldn't Congress make sure that whatever regulatory changes we make do not change the fundamental character of credit unions? And when we are taking today about raising the business lending cap or expanding into the broadly defined underserved areas, will this invite credit unions to disregard the congressional mandate that credit unions serve people of modest means, which is one of your criteria?

Mr. DORETY. Congresswoman, we totally agree with you that we should never get away from the core of who we are, which is a not-for-profit cooperative institution. The things that you refer to can only enhance our ability to serve those members that we were chartered to serve.

Underserved communities, an example is we have done five at Suncoast. The community I referred to, Immokalee, has a total of 25,000 individuals in that community. In 6 years time, we now are serving 6,600 of those individuals in that community.

If credit unions are given the ability to expand further into underserved communities, then more people of modest means will in fact be served, which is exactly what I think most folks here want us to do.

In the member business lending cap, credit unions serve a number of members and do it very well on the consumer side. Many of those members would love to have small business loans from their credit unions. But because of the cap and the expense involved in putting together a business service program, it costs a lot of money to do that. And many small credit unions are not able to fund or to spend the money to even start a member business loaning program.

So I think both of these features of the new bill would certainly help credit unions do even more in providing services to folks, and ensure that we are doing exactly what you want us to do.

Mrs. BIGGERT. How do you define what are underserved communities or who is underserved in those communities?

Mr. DORETY. Our regulator defines who are underserved communities, and it is a certain portion of folks. It has to do with income levels, and Chairman Johnson can certainly answer this better than I can. It has to do with certain income levels and the availability of services in those communities.

Mrs. BIGGERT. Maybe, Chairman Johnson, could you respond to that?

Ms. JOHNSON. That is correct. It is based on geographic areas that meet income standards. It is difficult to say. I think a better approach to what is underserved versus what the ability or what the number of institutions, etc., might be what is the access to affordable financial services.

What is the appropriate number of institutions? There is no criteria out there. Is it so many check cashers? Is it so many other financial institutions? But having access to affordable financial services is what is key.

We know that when a credit union has access to an underserved area, it is offering all of the consumers another option. And that is what the goal is. It has to be made available before they can take advantage of it.

Mrs. BIGGERT. Well, we are hearing from banks that credit unions are purchasing or participating in business loans to non-members. And how many credit unions are making these types of loans, or is that true?

Ms. JOHNSON. Credit unions only make member business loans to members. I think the figures that you are referring to, credit unions have the option or the opportunity to purchase participations from other credit unions. But these are member business loans that have been made by a credit union to a member. So credit unions don't make business loans to non-members.

Mrs. BIGGERT. Did you exclude these loans from the aggregate business loan cap?

Ms. JOHNSON. Loans that are $50,000 or less in the amount are excluded from the business lending cap. Participations are also excluded from the business lending cap.

Mrs. BIGGERT. I think that most people would agree that anything that provides lower income Americans with an alternative to high-cost short-term loans would be a good thing. Can you tell me what impediments currently prevent financial institutions from offering these alternatives, and are the impediments economic or regulatory?

Ms. JOHNSON. Well, I would say the biggest impediment is having access to the area in order to provide them.

Mrs. BIGGERT. So is there an economic impediment? That is all right.

Ms. JOHNSON. I guess I am not understanding the question.

Mrs. BIGGERT. My time is expired, and I will yield back.

Mr. KANJORSKI. Ms. Biggert, just a little point of information. On both bills that are pending, the definition that we are using in both bills for "underserved area" have been taken out of the new markets tax credit initiatives, are very restrictive to census track definition, and consistent with the existing definition, and from the CDFI definition of underserved areas. And we use in the alternative. But they are much more restrictive than other definitions in underserved areas. But it would get us into about 40 percent or less of the country of underserved areas.

Ms. Waters?

Ms. WATERS. Thank you very much, Mr. Chairman. I am sorry I was not here for an opening statement. We were tied up in another committee. But I would like to ask a question based on an anecdote that I would have mentioned in my opening statement, namely, a local credit union in my district helping to reach out to folks who had previously relied on a check cashing and payday lending franchise.

Mr. Lussier and Mr. Dorety, can you tell me, from a national perspective, what you know or understand that credit unions are doing to move people from being unbanked, so to speak, meaning without a relationship with a reputable financial institution, and thus reliant on extortionate sources of credit, interrelationships with credit unions in particular? Can you share with us something about what credit unions may be doing, collectively moving to meeting the short-term borrowing needs that many working and poor folks need?

Mr. LUSSIER. Yes. I just want to say that as far as the financial literacy programs that are out there—I will address that first—I know that our credit union itself has had educational facilities in the local high schools as well as branches in the high schools to help assist and train the young to become educated financially on their responsibilities of what is going to take place in the next few years of their lives.

We have just enhanced our program by having an educational facility within our own new operations center to address just that issue, to help financial literacy in both from people from underserved areas in the community as well as minorities and/or people who are in high school or even some of the senior citizens.

So we have gone to great strides to having additional staff put onto our staffing to assist just for the financial literacy programs. That is what we do regarding that.

As regarding the payday lending, we actually again go out to give many small loans of the $500 to $600 area, and charge no abnormal fees or underwriting costs or anything else, and just do that for many, many people within our community to help and assist them to get away from some of the payday lenders.

Ms. WATERS. Thank you very much. And let me just address this question to any of you who would like to answer: What will H.R. 5519, the Credit Union Regulatory Relief Act, which we have been discussing—what can happen with the passage of this legislation? Will you be able to expand to be of more assistance to our constituents and their ability to borrow? And would this include businesses also?

Mr. DORETY. Congresswoman, really quickly, the national efforts on serving the underserved—we have a national program called Real Solutions. It is administered by the National Credit Union Foundation, and it is in over half of the States. It provides products, services, and guidance to credit unions. It is a very popular program. It is being moved out nationally at this time.

And our State leagues are also getting involved in a program called the Real Deal. So there are national efforts on credit unions attempting to go out and provide services to the underserved.

This particular bill that we are talking about would enable more credit unions, obviously, to include underserved communities in their field of membership. It would also enable more credit unions to offer business loans to their small business members. Clearly, it would help to provide economic stimulus to the constituency that you are referring to.

Ms. WATERS. Simply put, you just would have more resources to expand out into these communities that are not available to these communities today. Is that correct?

Mr. DORETY. I couldn't put it any better myself.

Ms. WATERS. I like that. Thank you very much. I yield back the balance of my time.

Mr. KANJORSKI. Thank you very much, Ms. Waters.

And now my friend from California, Mr. Royce.

Mr. ROYCE. Thank you very much, Mr. Chairman.

I am going to Mr. Dorety with a question first, and that is: Credit unions, by their very nature, are quite risk-averse. By law, they lack any access to capital markets. The current prompt corrective action rules induce credit unions to maintain capital levels higher than those necessary to protect the share insurance fund.

So I would ask if you would explain why credit unions must maintain their current net worth requirements, and how credit union members would benefit from modifying these requirements proposed by CURIA?

Mr. DORETY. Congressman, I think the reason that we are required are basically what you suggested. First of all, we have to account for the 1 percent share insurance fund. But also, we do not have the availability, or most credit unions don't have the availability, to go into the area of alternative capital.

So I think that is probably the basis for why we are where we are. The new provisions under prompt corrective action would allow credit unions obviously to address some of that. Now, credit unions are risk averse, and many credit unions have capital levels that are above that level of 7 percent that we consider to be well capitalized.

If we were to enable to move that well-capitalized level still to a safe and sound level that our regulators would adhere to, then more credit unions would certainly be encouraged to provide more capital and spend more money, provide better products and services, and enhance their products and services to members.

The risk-based side of this provision would certainly help credit unions make more loans and allocate risks appropriately towards making those loans. The one-size-fits-all, as we heard here earlier today, just doesn't make sense any more. So we really believe that would assist credit unions in providing more economic stimulus to our membership.

Mr. ROYCE. So in theory, we have a more rigorous two-part net worth structure that is actually going to closely monitor actual risk.

So I will ask Chairwoman Johnson: What type of impact would you expect that to have, then, on the national credit union share insurance fund when we go to a risk-based capital system?

Ms. JOHNSON. Congressman, actually it will have a positive impact on our insurance fund because it will allow us to—it accelerates our ability to deal with those thinly capitalized institutions.

I would also like to point out that the other regulators have the ability to adjust their capital levels by regulation. We are held to statute. And that is why we need action in a bill such as you are proposing.

Mr. ROYCE. Going to another issue, Chairwoman Johnson, with the economy continuing to work through some pretty challenging and difficult times here, is this the time to be thinking about the prompt corrective action reform that is in the CURIA bill?

Ms. JOHNSON. It is actually the very best time, because the way we have seen the economic conditions, although credit unions have done a terrific job in the mortgage lending area, and have not gotten themselves into some of these precarious positions, their record is very good, but it is because of the focus now on the economy and where institutions are and the interest rates, etc. This is the time that we should be addressing the issue through this statute.

Mr. ROYCE. Thank you very much, Chairwoman Johnson.

I am going to go back to Mr. Dorety. There has been a lot of discussion here today about how the Credit Union Membership Access Act of 1998 was the last major piece of credit union legislation that we have enacted here in the United States Congress.

But as I think you pointed out, while this Act certainly saved a number of credit unions from disappearing, it was not regulatory relief. In fact, the legislation put additional statutory burdens on credit unions.

So the question I would ask you is: When was the last time Congress provided credit unions with change to the Federal Credit Union Act that provided some type of regulatory relief, in your memory?

Mr. DORETY. Congressman, it has been over 20 years. It was after the Garn-St Germain Depository Institutions Act of 1982, but it has been over 20 years since Congress has enabled—has given credit unions any meaningful regulatory abilities, in my memory.

Mr. ROYCE. Well, I thank you all. I thank the witnesses again for traveling out here to testify today. And Chairman Kanjorski, I yield back the balance of my time.

Mr. KANJORSKI. Thank you very much, Mr. Royce.

And now we will hear from our friend from North Carolina, Mr. Watt.

Mr. WATT. Thank you, Mr. Chairman. I want to relate an experience going back, and I am going to assume some risk today, the same risk that I did the first time I mentioned this. I will put it in context.

I represented a credit union before I came to Congress, and was a member of two credit unions at that time. And about a year or two into my service on this committee, after I came to Congress, I was at a breakfast and made the political judgment that I had enough credibility with credit unions to raise a basic question, and have incurred the wrath of some credit unions, especially the larger ones, since that.

The basic question was: What is the dividing line between what credit unions do and banks do? What should the appropriate dividing line be, given the fact that credit unions are not taxed and other financial institutions are?

I have found over the years that has been the real undercurrent of just about everything that this committee has dealt with, and continues to be the underlying question. And so I want to put that question out here as a general context again.

I think it raises itself in the context of this proposed legislation, especially modifications that may be made to the service of underserved areas. And I want to start with Ms. Johnson because one of the concerns I have—I mean, I will do anything to get more financial services access to poor people. And one of the concerns I have is that the interpretation of underserved areas may need a lot more attention than your office is giving it.

I am reading here from a report that was done in 2004, which says to me, "Treasury Department Federal Credit Union," and defines its field of membership as "persons who live, work, or regularly conduct business, worship, or attend school in, and businesses and other legal entities located in, Washington, District of Columbia. Underserved addition 12/8/04."

I am reading a provision that allows JSC, Houston, Texas, if I read this correctly, to serve a field of membership "persons who live, work, worship, or attend school in, and businesses or other entities located in Houston, Texas and underserved area."

Could it possibly be that the whole City of Houston, Texas, is an underserved area? Could it possibly be that the whole City of Washington, D.C., is an underserved area? Could it possibly be, if I look at some of these other descriptions, that the whole City of Monterey, California, is an underserved area?

Is this just a misstatement of this, or do we have a problem? Because I think part of the problem that people are having here is that if you define this area as being so broad, people don't understand what the distinction is any more between a nonprofit credit union and a for-profit financial services entity of another kind.

That is one serious problem that I think needs to be addressed here. And it entails more than just a question of serving underserved people. I think everybody is willing to serve underserved people, but if the definition is that broad, there are a lot of people in these areas who fall in that definition.

The second question, and giving my speech here, I have run out of time. But the same thing applies when you convert out of a credit union because if the owners are the people who are being served in a credit union, it is like a mutual insurance company.

I had some litigation about that before I came here, too. I stopped a conversion from a mutual insurance company to a stock-based insurance company because the people who were benefitting from the conversion disproportionately were the people at the top of that institution. The people at the bottom of that mutual insurance company were getting virtually nothing out of the conversion process. That is the issue that Mr. Kanjorski raised.

I think we have to do more work on these two issues to satisfy people that the status of credit unions is not being abused. And maybe you can shed some light on the first of those, Ms. Johnson. I will shut up and give you an opportunity to respond.

Ms. JOHNSON. Thank you, Congressman. I would be pleased to respond.

The underserved areas that have been granted do meet the statistical criteria for the definitions of the underserved. And these are statistics—

Mr. WATT. You are telling me that the entire City of Washington, D.C., and the entire City of Houston, Texas, meet that definition?

Ms. JOHNSON. Well, I would like to address the example you used of the Treasury Department Federal Credit Union.

Mr. WATT. No. I am asking you that question. Does the entire City of Houston, Texas, meet that definition?

Ms. JOHNSON. Statutorily, yes, it does, by the criteria that is already in—the criteria that we go by, yes.

Mr. WATT. So a credit union could do—could have a member—

Ms. JOHNSON. It is based on the investment areas.

Mr. WATT. —of any business that is located—any person who works in the District of Columbia?

Ms. JOHNSON. It is a consumer choice, yes. If they reside, if they are within that underserved area. And I would like to point out—

Mr. WATT. That underserved area being the entire City of Houston, Texas?

Ms. JOHNSON. If that meets the statistical criteria for those investment areas, it is anyone residing within that statistical area. That isn't—

Mr. WATT. What happened to this clear definition of neighborhood that we started out with? Does that not have any bearing any more? How is that a clearly defined neighborhood? Isn't that in the statute? Isn't that in your regulations?

Ms. JOHNSON. The term "neighborhood" is not used.

Mr. WATT. I have run out of time, but—

Ms. JOHNSON. Might I respond, though?

Mr. WATT. —you see the problem. And I am sure I am going to get abuse for even—I got abuse the last time in a private setting for putting this discussion in a breakfast setting on the table with what I thought were my friends. So I very well anticipate getting substantial abuse for putting it in this public setting.

But I don't think we need to sweep this concern under the rug. And if we don't address it, I think we are going to have some major problems on an ongoing basis really meeting the needs of underserved people. Maybe our definition is too broad now, the way you all are defining it.

Ms. JOHNSON. I would like to point out that I recently personally attended the—I wouldn't call it a grand opening, but the Treasury Department Federal Credit Union does serve—they have adopted an underserved area. And in cooperation with Operation Hope, they are working specifically with these underserved residents, these low-income residents in particular, of offering the counseling—

Mr. WATT. I have no doubt that that is what they are doing. But the language that we—

Ms. JOHNSON. That spreads out.

Mr. WATT. —that we have here is broad enough to drive megatrucks and planes and tanks and everything else though. The good things that they are doing with it are wonderful. But I am telling you that this is subject to abuse, and we have to figure out a way to find what the appropriate balance is here. Otherwise we are going to lose—we will win the battle and lose the war.

Mr. KANJORSKI. May I just add to this conversation that is going on? I think you are talking to cross points. The existing definition of an underserved area is different and much broader than the definition contained in the two bills presently pending.

The two bills presently pending adopt the definition used in the new markets tax credit, which is highly restrictive. And under the new markets tax credit, you could not get a tax credit in any portion of Washington, D.C., only in those census tracks that meet the very restricted definition contained in that Act.

And the same thing goes to Houston, Texas. I know of no city in the United States that would fully encompass a credible area of an entire community—

Mr. WATT. I am surprised to read this myself, Mr. Chairman. I am reading from the report of the regional director of the National Credit Union Administration. That is the way it is defined in the report.

Mr. KANJORSKI. Well, it is defined in that report because you are operating under some other definition presently at the credit union regulatory level, where this Act—

Ms. JOHNSON. We are operating under the current congressional—

Mr. KANJORSKI. Definition.

Ms. JOHNSON. —definition. Yes.

Mr. KANJORSKI. And the new definition under the two pending acts would be very much more restrictive, and purposefully so. But you cannot restrict it to the point that they become nonexistent. I know you have worked very closely on the new markets initiative, and we are going to be reauthorizing that this year after 5 years. That is a very restrictive act.

I come from a congressional district that is quite on the low side of income and level, and yet less than a third of my congressional district qualifies for new market tax credits. And I think we are probably in the 30 percent range.

Mr. WATT. I would just tell the chairman that is not the only concern I have with the new markets tax credit. We have had a hearing about some other concerns with it, too. So I will be looking forward to working with the chairman on that. But that is in the jurisdiction of the Ways and Means Committee, as I understand it.

Mr. KANJORSKI. Right.

Mr. WATT. So we may not get as direct a shot at it as I would like to have.

Mr. KANJORSKI. Well, I think we ought to assume any jurisdiction we possibly have to get a tax credit.

[Laughter]

Mr. KANJORSKI. I see Mr. Miller of California has returned, and so I recognize Mr. Miller.

Mr. MILLER OF CALIFORNIA. Mel, you were much easier to get along with when you had facial hair. I thought I would point that out. He is not even—Mel, you are not paying attention this morning. He is through talking. I can tell. I said, you were much easier to get along with when you had facial hair. I want you to know that.

Mr. WATT. Well, I am glad to see you are talking my place in being easier to get along with and the facial hair.

Mr. MILLER OF CALIFORNIA. I have always been easy.

You know, when I was growing up, my parents were retail clerks, and I don't think—if it wasn't for credit unions, we wouldn't have had sofas and chairs and carpets. So you have done a great job.

Are there any other institutions you are aware of that have a 7 percent requirement, as you are placed upon in capital requirements?

Ms. JOHNSON. The risk—or the prompt corrective action that we operate under is the highest level of capital that is required. Currently, credit unions have to have 7 percent in order to be considered well capitalized. The proposal that we have before you would make it approximately 6 percent, but it would actually raise it at the lowest category, and it actually would raise it for about 30 percent of the credit unions.

The banks currently are required to have 5 percent to be well capitalized.

Mr. MILLER OF CALIFORNIA. And Congress provided the banking regulators the flexibility to risk-base capital as they deemed proper. How do you look at that?

Ms. JOHNSON. Excuse me? I didn't hear the first part of your question.

Mr. MILLER OF CALIFORNIA. Congress provided the banking regulators the flexibility to risk-base the capital requirements for banks. How do you think that would apply to credit unions?

Ms. JOHNSON. Well, we would like that ability to risk-base the capital. They are able to change theirs through regulation, and ours is firmly held by statute. And we are very limited. If we had this capability, we would be able to identify problems more quickly, and credit unions would be able to manage to their risk more successfully.

Mr. MILLER OF CALIFORNIA. In conversations I have had, I understand that a number of credit unions actually want to help their members restructure or refinance troubled mortgage loans that are currently existing today, and including loans that their members may have gotten elsewhere. How does the NCUA address that issue?

Ms. JOHNSON. Credit unions have addressed the mortgage lending area very well. We have not changed our standards through this whole process. We came out with early guidance, going back as far as 1995 and addressing some of these types of loans, and have continued with strong guidance in the last few years.

We have maintained our lending guidelines based on the three Cs: collateral; character; and the capacity to repay. And we have not changed that. Now, we have encouraged credit unions to work with their members. We encourage modifications, where possible. And credit unions have been very successful in that regard.

Mr. REYNOLDS. Congressman, can I have a point on that?

Mr. MILLER OF CALIFORNIA. Yes.

Mr. REYNOLDS. From the perspective of the State system, the State regulators have been encouraging their financial institutions, including credit unions, to work diligently with consumers to try and remediate these types of situations.

And credit unions, our State-chartered credit unions, have been very effective in being able to step forward and help consumers in some situations where they have gotten themselves into subprime lending situations. And they are not always able to extricate consumers, but they are always able to assist them with being an honest broker of information on their options.

Mr. MILLER OF CALIFORNIA. So you think you can actually help your members restructure or refinance some of these troubled mortgage loans in a safe and sound fashion where they have no place else to go today?

Ms. JOHNSON. That's right.

Mr. REYNOLDS. Absolutely.

Mr. MILLER OF CALIFORNIA. And you don't think that would be unfairly involving yourself in the marketplace? That is a stupid question, but I think I know how you are going to answer that one. Should Congress extend the CRA to credit unions?

Mr. DORETY. I will take that one. The answer is "no." Congress should not extend the CRA to credit unions. CRA was brought to banks, I think in 1978, because they were doing bad things. They were redlining, and they were doing some of those characteristics that credit unions do not do.

We serve our members. We have a defined membership. There is no reason for CRA in credit unions at this time. And if you look at what credit unions are doing, and if you allow credit unions the ability to add underserved, and if you allow us to do the risk-based capital lending, and if you allow us to do the member business lending extension, we will still not need CRA. We will still not be doing the things that banks were doing which brought CRA upon them.

Mr. MILLER OF CALIFORNIA. Mr. Chairman, I think this is a good approach you are taking on this. You know, growing up, in my youth I watched my parents, retail clerks, use a credit union.

I think they are filling a void out there in the marketplace that banks really don't want to get into in many cases. I think they are doing a good job. And I think some people out there who benefit from the credit unions would have no place else to go in many cases.

I think this is a reasonable approach, and I am glad we are taking it. I wholeheartedly support it, and I yield back my time.

Mr. KANJORSKI. Thank you very much, Mr. Miller.

Now the gentleman from California, Mr. Sherman.

Mr. SHERMAN. Mr. Chairman, I hope that when we ultimately pass legislation—I do hope we pass legislation this year—that it will include a look at the credit union capital structure, the prompt corrective action structure, and that we more closely resemble the risk-based capital standards that the FDIC uses. I look forward to working with you on that.

Our colleague, Mr. Watt, brought up the interesting issue of whether credit unions are doing enough to deal with underserved areas. I think he is right that we have to be careful in crafting legislation, and we may end up crafting something more limited than the current regulatory definition of what is an underserved area.

And maybe the Ways and Means Committee did a good job with their definition of new markets, but maybe we will do a different job here, if they didn't do a good job. But I think it is important that credit unions serve underserved areas, and that we define underserved areas narrowly enough so that, for example, here in Washington, we focus their desire to serve the underserved communities to the underserved communities in Washington. We wouldn't say, well, open up a facility in Chevy Chase and you are doing something to help the underserved people of the District.

But I am often asked to define the Yiddish word "chutzpah." And I noticed that a group brought litigation which effectively prohibited well over half of the credit unions, that is to say, those with a single group or community charter, from extending credit union services to low-income areas and groups not adequately served by traditional financial institutions.

And then this same group, having used the legal system to prevent the majority of credit unions from serving underserved areas, has this beautiful ad. I don't know if you—are you folks familiar with this? Have you seen this, maybe, once? And it attacks credit unions for not serving underserved areas, having been prohibited from doing so by the litigation brought by the same people who brought you the ad.

So Mr. Dorety, I wonder if you happen to have seen this ad—which I will put into the record without objection—if perhaps you could spend a few minutes responding to it.

Mr. DORETY. Well, it has come to my attention, sir, yes. Our folks have shared it with us. And I couldn't agree with you more that the information and the questions—it is a series of 10 questions. And we have responded to those questions, and would love to put this in the record, our responses to the questions that the bankers put forth in this ad in the last couple of days.

Mr. KANJORSKI. Without objection, the ad in its totality will be entered into the record, and the 10-question response by the credit union will also be entered into the record. Without objection, it is so ordered.

Mr. SHERMAN. Perhaps you could spend a minute or two highlighting some of those answers.

Mr. DORETY. Well, I don't want to go into all 10 questions because it is kind of like a David Letterman Top Ten. The last question is the most interesting one. And they go from 10 to 1, so it is a David Letterman thing: "Why should Members of Congress cosponsor H.R. 1537 if the credit union industry cannot answer these questions?"

We have answered the questions right here, and so the answer to that question is Congress should cosponsor H.R. 1537. We can get into specifics of the others. But there are a lot of issues in these, Congressman, and I don't know that we can get into all of them at this time.

Mr. SHERMAN. Ms. Johnson, perhaps you could highlight what would be the effect of going to risk-based capital? As I understand it, some credit unions would then have to have more reserves, some less. But would we do a better job of protecting the insurance fund if, instead of a rigid simple system, we had a more complex and more sophisticated formula?

Ms. JOHNSON. The overall effect is that you would be giving the regulator the best tool that we could have in our tool box. The risk-based proposal that we have presented will actually have a positive impact on the insurance fund because it accelerates our ability to deal with those thinly capitalized institutions more quickly.

The current system does force credit unions to all—it is a one-size-fits-all. And especially in this economy, and with these changing times, and with the different amount of risk that credit unions take on, we should be able to measure it according to the risk.

And so I believe it is imperative. I think if you want to have these other regulatory relief items, this is the real tool that allows us to have this other regulatory relief.

Mr. SHERMAN. And it is my understanding—and this, I think, differs from banks and thrifts; we all remember the Federal Government having to write a check back in the 1980's—that if for any reason the insurance fund was inadequate, every credit union in the country would then have to contribute up to its full net worth to the insurance fund. Is that correct? Or if the insurance fund is inadequate, is it the Federal Treasury that is on the hook?

Ms. JOHNSON. Credit unions contribute 1 percent. We have a robust insurance fund.

Mr. SHERMAN. Well, but if for some reason—and this would be a catastrophe none of us would want to see—the fund was inadequate, would it be the taxpayers or the credit unions of the country that would be on the hook?

Ms. JOHNSON. It is not the taxpayers, Congressman. It is the credit unions. You are correct.

Mr. SHERMAN. So basically, when we change to a different formula, the real parties in interest, the entities that would be on the hook if you didn't have adequate capital, would be first the insurance fund and then all the other credit unions in the country?

Ms. JOHNSON. You are correct.

Mr. SHERMAN. And it is my understanding that none of these credit unions, who would be ultimately on the hook if one of their brother/sister organizations or several of them went under, that none of them is opposing this change in the prompt corrective action statute. Is that correct?

Ms. JOHNSON. No. It is being strongly supported, actually.

Mr. SHERMAN. So they are putting their capital on the line?

Ms. JOHNSON. That is right.

Mr. REYNOLDS. Congressman Sherman, I just wanted to add as well that the State regulatory system strongly supports risk-based capital. Risk-based capital is being used for other financial institutions, primarily because it is a risk management tool for regulators. And so I wanted to add our strong support to that issue.

Mr. SHERMAN. I thank you for that, and I believe my time has expired.

Mr. KANJORSKI. The gentleman from Florida, Mr. Feeney.

Mr. FEENEY. Thank you, Mr. Chairman. And thanks to the panel. I think that one of the great things about credit unions is that there has not been taxpayer money lost in their long years of service, and we are very grateful that is one of the things that make you unique.

You know, I got involved in elected politics for the first time in 1990 in the State legislature in Florida, and as expected, we had healthy, interesting debates over welfare reform and tax policy and education reform.

But there were very few things as spirited as, say, the fights between the commercial bingo parlors and the local VFWs over who got what nights for bingo. The only thing more energized in debate was the fights over racing dates for dog tracks in places like South Florida, if you could get the prime tourism season. And inevitably, those debates resulted in several members having to stand in between and literally stop the outbreak of fisticuffs.

And turf battles are always interesting. By the way, I never had a dog in the dog track day fights, so I just sort of sat back and enjoyed the show. And I will tell you, we have my colleagues on the committee that are huge advocates for the banks, and we have colleagues that are huge advocates for the credit unions. I find myself as somewhat of an umpire here.

But I will tell you that we saw the most recent proposal—because this is a line drawing problem. I mean, for example, the issue of whether credit unions—to what extent they can loan money to members for business enterprises. You know, I think most of us feel strongly that if it is a $20- or $30- or $50,000 startup enterprise that your member wants to be engaged in, that is terrific.

On the other hand, if we are going to get into international financing at a high level, that is another end of the scale. So it becomes a line drawing problem for a lot of us that want to do what is right ultimately for your customers.

I have to tell you, my friends in the banking industry say that there ought to be tax parity between credit unions and banks. And I may vote for tax parity one day, I tell them, but it would never be to levy a tax on the credit unions. It would be to eliminate the tax on banks.

Because ultimately what I am interested in is access to credit, on a rationale basis. Your customers and customers of banks and my constituents, we have a credit crisis in America right now. I think in some ways Congress is dramatically overreacting.

I am leading the charge to stop the primary foreclosure bankruptcy proposal, which I think would marginally increase the cost of credit for everybody and reduce the value of every American's real estate. So it is sort of the forgotten people as we try to do things that look sympathetic that I am concerned about, and I appreciate your stand on that.

But while I am on the subprime and credit—the crisis created initially from the subprime effort, Chairman Johnson, what percentage of the mortgages that credit unions nationally make roughly are held in portfolio, and what percent are packaged and sold to investors?

Ms. JOHNSON. Credit unions hold the majority of their mortgages in-house. They do sell some into the secondary market, but they sell to the GSEs.

Mr. FEENEY. Well, it is one of the great things credit unions are doing as we have this huge credit crisis because they really do fill many niches. And this is just one of them. Ben Bernanke testified here just the other day. Securitized lenders have gone from putting, annually, $1 trillion into the marketplace for borrowers of mortgages, $1 trillion, to $50 million a year; 95 percent of that market has dried up.

So credit unions once again are filling a niche and stopping what would otherwise be a worse catastrophe in the mortgage loan crisis. And as I understand it, credit unions make almost no, if any, subprime loans. Is that right, Ms. Johnson?

Ms. JOHNSON. Credit unions make approximately 2 percent of all mortgages throughout the entire country. The percentage of subprime is even less than that. I would note there is a difference between a subprime loan, which is just to a borrower with lesser credit, than some of these exotics and, you know, the mortgages that really got people into trouble. And credit unions did a fine job, I think, by following our guidance in not putting their members into loans that they couldn't afford.

Mr. FEENEY. Right.

Ms. JOHNSON. And so it was that one-on-one with the member up front.

Mr. FEENEY. Well, and I think community banks do that.

Ms. JOHNSON. Correct.

Mr. FEENEY. Often very well. But I should say that one of the problems we have had in the subprime mess is that we have a total disconnect between the people that purchase the scrutinized loans by the thousands on one end, and the people that are making loans.

You all are able to evaluate on an individual basis, and therefore are making very rational loans throughout a period where there have been, unfortunately, huge numbers of irrational loans. And now that crisis has bled over and created a credit crisis, not just in other markets in the United States but around the world.

So congratulations for what you are doing. We appreciate the fact because to the extent we are hoping for an immediate bottom of the real estate market, I think credit unions have been a reliable partner in keeping a bad situation from getting worse.

With that, I will yield back.

Mr. KANJORSKI. Thank you very much, Mr. Feeney.

Now the gentleman from Massachusetts, Mr. Lynch.

Mr. LYNCH. Thank you, Mr. Chairman. I want to thank you and Mr. Royce for focusing on this issue. And I want to thank the witnesses for helping us out.

I think there has been definitely a reconfiguration of finance in a lot of communities. I think with the mergers of a lot of large banks, especially in my area, in the City of Boston—we have seen six banks become three banks, and then at least the larger ones have really consolidated. There have also been, however, I think, a growing number of community banks that have tried to fill in that void, as well as—and I am blessed with a lot of great credit unions in my district.

Let me go back to that last question. I had a foreclosure prevention workshop in my district a couple of weeks ago, where I rented out the cafeteria of a local high school. And to my surprise, I had about 400 people show up. And we are getting hit pretty hard with foreclosures.

What can you do—I know you haven't been guilty of investing, and you haven't been pulled into the whole subprime mess. But for instance, at our event we did have a lot of the banks step up and try to do the right thing and to correct the situation as best they could.

What is the credit union community doing with respect to reaching out? What are the limitations that you have that prevent you from doing more of that? And what could we do to help you at least address this problem? It looks like it is going to be with us for a while.

Ms. JOHNSON. Well, first of all, I would applaud you for being proactive and holding your workshop. There is a need out there. And that is what we have done. We are doing the same thing with the credit unions in encouraging them, especially with the up-front counseling.

I think the most important thing we can do is to ensure that the credit unions are educating their members to the terms of the loan, understanding what they are getting into, and then not putting them into a loan that they can't afford in the first place.

Where we are seeing a little bit of residual damage is they may not have gotten their loan, their mortgage, a high risk mortgage from the credit union. They may have gotten it somewhere else. I think where credit unions have to be particularly careful is in this residual damage of their other consumer loans.

And this is where the counseling again and extending that hand to their members and working with them to modify. They have their car loans, their credit card loans, etc. And so we are encouraging that, and credit unions are doing so on a member-to-member basis.

As far as limitations, I don't know—off the top of my head, I can't think of a specific instance that is limiting us other than just continuing to put—being able to adopt more underserved areas so that these individuals that need this help then have access to the credit union itself.

Mr. DORETY. Congressman, I would like to touch on that if I might.

Mr. LYNCH. Sure.

Mr. DORETY. You know, the subprime market has touched all of us. I happen to live in Tampa, Florida, on the west coast of Florida, and we certainly have been impacted by this. We have made no subprime loans. We have made loans to people who you might consider to be qualifying for subprime loans, but the loans we make are honest, straightforward loans that don't have any of the escalation, don't have high interest rates.

And going forward, we work with all those folks. And we are looking at foreclosures. We have been working with them on a one-on-one basis. We are telling our other members that if they have one of these toxic loans, that they need to come to us and talk to us and see if there is something we can do.

We are still making mortgage loans. Actually, we have a huge increase in mortgage loan applications recently because of what has been going on through the other financial institutions. There are credit unions all over the country who are engaged in this type of effort, and they are not making those loans that caused the problems to start with.

So I think as a community, credit unions are certainly willing, and are, in fact, stepping up to the plate to help try and get us out of this mess that so many folks are in.

Mr. LYNCH. Thanks.

Yes, sir?

Mr. LUSSIER. Congressman, I have a comment as well. In Massachusetts, as you know, we have been hit with the economy as well. One of the things that I think we just recently got into, and I take my hat off to the State of Massachusetts for doing this, they came up with some type of special grant funds and so on and so forth—I think it was the Mass Housing recently, of which we were one of the first ones in there to see what we could do to try to take some of those funds to put it back to the community to assist the people to get them out of some of these subprime mortgage instruments.

It is extremely expensive for them to—expensive for people to even get out of them, if at all possible to get out. I think the State of Massachusetts has come to the forefront to try to help and assist—to help them do that as well.

So we worked with Mass Housing. That was one of the items we have done.

Mr. LYNCH. Mass Housing Finance Agency?

Mr. LUSSIER. I believe that is right.

Mr. LYNCH. MHFA? Yes.

Mr. LUSSIER. I believe that is where it is. Yes. Actually, my vice president of real estate lending was just going through that with me before I left the other day, so I had the bare minimum.

But it was a great program that he was trying to get through our board meeting this month to get involved with the Mass Housing Finance Agency to help and assist in that area, as well as the financial literacy and counseling that we actually try to do and put out in the forefront by having some of my senior executives get together if someone does have an issue with one of those loans, which I know that we had three people in our office this week that were wondering what they could do to get out of it. We brought them in personally to discuss the issues, to show them where they were, and try to assist them to see what we could do to try to help them get out of that problem.

Mr. LYNCH. Great. Thank you, Mr. Chairman. I see my time is expired. I yield back.

Mr. KANJORSKI. Thank you very much, Mr. Lynch.

And now the newest member of the committee from the great State of Nevada, Mr. Heller.

Mr. HELLER. Thank you very much, Mr. Chairman. I certainly do appreciate your hard work on this particular piece of legislation. I appreciate the opportunity for the first time to be able to approach the rest of the committee.

I apologize I was not here for your opening comments, and for that reason I may be asking questions or making comments that have been repeated before. But I will try anyway. I have a limited knowledge of the background and perhaps the scope of what your industry does as it is concerned with credit unions.

I guess my question is: I am confused as to what now is the scope of a credit union. I live in northern Nevada. I would love to have you tour my 110,000 square miles we call a district, but I will tell you, you guys play an important role in some of the smaller communities that we have in that State.

The inability to get financial institutions to come in, but when we talk to the larger communities, the scope seems to change pretty dramatically. And it is my understanding that history has told us that the purpose of a credit union was to fill a unique niche.

And I am wondering if that is getting too broad now. That is the complaint that I am hearing from the other side, that perhaps you are trying to become more and more like other financial institutions, with certain advantages. For example, you want to maintain your tax-exempt status, but you don't want to comply with CRA. You want to change your capital requirements in this particular piece of legislation, but you want fewer regulatory burdens.

And the argument is—and again, I haven't taken sides on this particular issue—but what it appears to me is you want the benefits but you don't want to take the risks. How do I respond to that when those questions are asked and I have to answer them?

Mr. DORETY. Congressman, we happen to be one of those credit unions you are talking about. We are a $6 billion credit union located in Tampa, Florida. We started in 1937 as a small teachers' credit union in Hillsborough County. Our board of directors are volunteers. We are a not-for-profit cooperative. That is the reason we were granted a credit union charter, and that is the reason we have been given a tax exemption.

If you come into our board meeting today, we are exactly the same as we were then. Our structure has not changed. And the structure is what has enabled us to have that status. It never started as saying a limited field of membership. It never started as trying to—there is no size restrictions on this. The fact of the matter is, if you are doing a good job with your members and you are providing good services and products to them, you are going to be successful, and guess what, you are going to grow.

Growth is important to financial institutions. Look at the rash of mergers. We are a $6 billion—we are the largest financial institution headquartered on the west coast of Florida. Every bank is out of Charlotte, out of Birmingham, or out of Atlanta.

And the fact that we have been successful and grown has not changed the basic structure of who we are or what we do. Our entire focus is on our member owners, as opposed to investors. And that is the difference, and that is why we deserve the tax exemptions.

Mr. HELLER. I come from a State—Nevada is in particular probably the largest foreclosure State right now, especially in the southern end of the State. Just to give you an example, I believe our foreclosure rate is 3 times higher than the national average; 1 in every 154 homes right now are being impacted, whereas I think the national average is about 1 in 555. So you can understand my concern over this.

I just want to make sure that this piece of legislation doesn't put credit union members at risk, more at risk than they were before. And can you explain to me why I shouldn't be concerned that these capital requirement changes won't put your members more at risk?

Mr. DORETY. I will be happy to. I don't want to try to one-up you, but I am in the west coast of Florida. So we have just as many issues as you do. Actually, Fort Myers is ranked the worst in foreclosures, and we have a significant presence there.

Mr. HELLER. You win.

Mr. DORETY. So I think the new regulations will only help. I think two things. One is we have strong regulatory backing, and they are going to be able to look at credit unions. As Chairman Johnson has explained, they are going to have more tools to help develop and estimate risk in credit unions.

And that is the key. Credit unions are going to be able to have the ability to measure risk when we make loans, more so than we do today. Today it is a one-size-fits-all. An unsecured credit card loan, we have to risk. The assessment is exactly the same as an investment in a government-backed security.

That just doesn't make any sense. And so when you enable us to do these types of things that we will be able to do under the new prompt corrective action guidelines that are in this law, we will be better served. Our members will be better served, and we will have no greater risk than we have today.

Our regulators—we will be on the exact same footing, well, not the exact same. We will actually have higher regulatory restrictions than other financial institutions do, even after this is imposed.

But credit unions have high capital levels today. We have never contributed. We have never had a bailout, as other financial institutions have done. We have always been a safe institution, and this particular bill will do nothing to change that.

Mr. HELLER. Mr. Chairman, I yield back. I went a little bit over my time. Please don't hold it against me in the future.

Mr. KANJORSKI. No. We welcome contributions from Nevada.

Mr. HELLER. Thank you.

Mr. KANJORSKI. The gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Yes. Thank you, Mr. Chairman. It has been a very informative hearing.

And I want to talk—first of all, what you are after is—we are dealing with two bills here, number one. And I want to get your response to find out if you are—which direction you think we ought to go on these two bills, and do either or both of them meet your primary obligations, your primary objectives? Ms. Johnson?

Ms. JOHNSON. Congressman, the CURIA bill does contain the element of the risk-based capital. And that has has been dropped from the CURIA bill. And for me, that is the priority. I would like to see the risk-based capital put into the CURIA bill, or vice versa. That is vitally important.

The underserved, extending the opportunity for all credit unions to adopt underserved areas, is vitally important. If I were to list two items, however it is combined, those would be my priorities.

Mr. SCOTT. All right. Now, let me just get it kind of focused here. Let's talk about one of the areas that I think is certainly helpful, and that is, you want to raise the limits on how much business lending you can do. And I think you stated in your testimony that credit union members' business lending cap is currently the lesser of 12.25 percent of total assets or 1.75 times the net worth.

How does this cap compare with other financial institutions, and how do credit union members' business loans compare or differ from the business loans made by these other institutions?

Ms. JOHNSON. I believe the current cap that is in place for the thrifts is 20 percent, and there has been legislation proposed that would take the cap off completely. When credit unions were first formed, there was no cap on business lending. It is only as recent as 1998 that there has been any cap in effect at all.

About 25 percent of the credit unions currently make business loans, and the average is only $190,000. So it about—I mean, it is important for those small business in these communities to be able to offer these—have access to credit. It will help these communities. And it is a valuable system for the members.

Mr. REYNOLDS. Congressman Scott, also—

Mr. SCOTT. Yes, Mr. Reynolds? And welcome up here from Georgia.

Mr. REYNOLDS. Well, thank you, sir.

Mr. SCOTT. Glad to have you.

Mr. REYNOLDS. Thank you, and we appreciate your hospitality. From the State perspective, the other point I would like to make is that in credit unions, member business lending is looked at very carefully in the examination process. We don't have member business lending being made in every credit union that we go into.

So we are very diligent. When we go in and do an examination in a credit union, we look very carefully at any credit union that is making member business loans. We are very careful to review the underwriting, the written policies and procedures, and the ability of management to properly manage that function. So it is looked at probably more in depth in a credit union than it would be in another financial institution.

Mr. SCOTT. All right. Let me ask you about prompt corrective action, Ms. Johnson. Credit unions are by nature risk-averse, and by law, they lack access to capital markets. It is my understanding that the current prompt corrective action rules induce credit unions to maintain capital levels higher than those necessary to protect the share insurance fund.

Can you explain why credit unions are forced to maintain excessive net worth requirements, and how credit union members would benefit from modifying these requirements as they are proposed in CURIA?

Ms. JOHNSON. Well, the current requirements in place are by statute. We don't have the ability, as the other regulators—

Mr. SCOTT. I see.

Ms. JOHNSON. —through regulation. So that is by statute, and that is what we are asking to be changed.

And the second—oh, credit unions are incredibly well capitalized, and they are averse to—you know, they are not risky institutions. And they have raised, through retained earnings, their capital levels. They are in excess of this required 7 percent. The current average capital is about 11.4 percent. So it demonstrates that credit unions are managing effectively.

Mr. SCOTT. All right. My time is about up. But let me get to this question. The three points, of course, you want a more flexible risk-based standard that would be determined and regulated by the regulators. You want to raise the limits on how much business lending credit unions can do to business. And you want to get into the underserved areas. Those are the three things I think you are basically asking.

So the question presents itself to me: How do you respond to the banking community's interest that if we do these three things for you, that some kind of way this is going to give you an unfair competitive advantage? That seems to me as what we have to answer.

Are there legitimate concerns—do they have a point to make here? Are you getting an unfair advantage over the banks by getting into this?

Ms. JOHNSON. I imagine my colleagues would like to jump in on this. But I will tell you from a regulator standpoint that this is not an unfair advantage in that credit unions are still held to higher regulatory requirements than other institutions. They are limited in investments. They are limited by field of membership. You don't—I mean, there is—this isn't a tradeoff. This is just giving the credit unions the tools they need to serve their members.

Mr. DORETY. Credit unions—excuse me.

Mr. SCOTT. Yes, sir. Please.

Mr. DORETY. Credit unions, to say we have an unfair advantage is—it is an illusion. We are subject to different regulatory restrictions at times. We have a totally different structure. You know, banks have the opportunity, if they care to, to change to a credit union charter.

We are a not-for-profit. We send everything back to our members, and if there is an unfair advantage, it is in that structure because we have one audience, our membership. We do not have to pay outside investors. That is our choice of charter. Banks' choice of charter is a different choice, so they are established differently and they have different economic factors that they are dealing with.

It is simply the choice of charter, and it allows us in some situations—actually, in many situations—to offer far better products and services to our members for that one very fact: We are a not-for-profit cooperative.

Mr. SCOTT. Yes, Mr. Lussier?

Mr. LUSSIER. Yes. I just want to say that I want to make sure that we remind each other that we only represent 1.1 percent of the market share out there. And I would just like to say that if banks think that it is that unfair, that they can convert to credit unions if they so wish as well.

Mr. SCOTT. All right. Thank you, Mr. Chairman.

Mr. KANJORSKI. Thank you, Mr. Scott.

The gentleman from Missouri, Mr. Cleaver.

Mr. CLEAVER. Thank you, Mr. Chairman. Let me continue on that same line.

Is it true that there are 123 credit unions with more than a billion dollars in assets, which would mean that they are larger than 82 percent of the banks?

Mr. DORETY. It is true, I believe. I am pretty certain that is the case that there are 123 credit unions that have a billion dollars in assets. All of the assets of the credit unions combined do not equal either of the three largest banks in the country. So we ought to put that in perspective as well. But yes.

Mr. CLEAVER. Generally, those who talk with us are the smaller banks, who come in to talk with us, quite frequently, I might add. And the issues, of course—I mean, I understand the two different charters and the way the Federal Government is allowing the two to exist.

But it would seem to me that if credit unions are disinterested in doing CRA, it seems to me that you have to be careful about how you say you are not wanting to do it just because I think the way you say you are not wanting—the way you make that statement can send the wrong signals. And Mr. Watt was dealing with that a little before he left. And so that does trouble me.

But in the urban core all over this country, and I am not that sure about rural areas, but in the urban care—and I represent a district that is very urban—we have a potpourri of payday loan operations and "Jenny's Come Cash Your Check Quick" companies.

And it would seem to me that one of the things that maybe credit unions could do is develop a new product that would allow—that would cause the people in those underserved areas to have a service that is desperately needed.

One of the reasons—I used to have an NPR radio show that I did live, and I did a show on these check cashing places. And it was a live show. I had a whole group of people who showed up in the poor parts of Kansas City, Missouri, angry with me because they said they needed those check cashing places. They said, there are no banks around. You know, we need a place to cash our checks. We need a place where we can get small loans.

And so, you know, with everyone—with the mantra from banks and credit unions, we want no regulations, you know, just leave—the market will take care of everything. Well, the market is not taking care of everything, and the truth is that you could develop products that would help, that would really help the community. I mean, those people are getting ripped off whether they like it or want to or not. They are getting ripped off because there are no institutions around to handle their needs.

So it seems to me that that ought to be one of the things that credit unions would consider. I mean, that is CRA without anybody having to ask you to do it. Chairman Johnson?

Ms. JOHNSON. Congressman, I would like to respond. Congressman Kanjorski's bill does have a provision in it that would allow credit unions to offer check cashing services to non-members within their field of membership, which is a good way of getting individuals into these traditional institutions.

One other thing is that federally chartered credit unions have a usury ceiling of 18 percent. And so that is a helpful limitation in this sense to these consumers of not being charged with these exorbitant fees.

Mr. CLEAVER. Yes. Mr. Watt talked about—

Ms. JOHNSON. Oh, I meant payday lending rather than check cashing. Excuse me.

Mr. CLEAVER. That is fine. They are the same, as far as I am concerned.

The neighborhood language that Mr. Watt actually—the word neighborhood is in the CRA legislation. And he mentioned neighborhood for yours. It is not, but it is in the CRA for banks, that they serve neighborhoods. We don't have neighborhood banks any more.

And even if credit unions—I mean, I belong to two credit unions. I am not anti-credit union; I belong to two. The problem is, the credit unions are not located where people need the service. That is the problem.

Mr. DORETY. Congressman, we have—actually, Congressman Scott earlier said something about the most important group in this discussion is not in this room; it is the consumers. We are owned by these consumers. Our credit union has a branch in an underserved area in East Tampa. There are four payday loan shops; you can walk out the front of our door and look at the four payday loan shops.

There are no banks in that community. We opened that branch 2 years ago to serve the people that you are talking about. Credit unions nationally have a program called Real Solutions which addresses payday loans, check cashing, and a number of products and services, exactly the type of thing that you are talking about.

Mr. CLEAVER. There are two things.

Mr. DORETY. We do CRA. We just aren't required—we aren't forced to do CRA. Credit unions are already handling those issues.

Mr. CLEAVER. Two things. One, your services would be made available, I guess, based on the charter only to members. Is that right?

Mr. DORETY. My understanding under this bill is that payday loans would be available to folks living—eligible for membership in the community who are not members. But yes, today we are.

Mr. CLEAVER. No. Say that again, if you would, Mr. Dorety?

Mr. DORETY. Under the new bill, payday loans—the provision in the new bill allows credit unions to make payday loans to residents who are in an area that they would be eligible for membership but they are not members. I believe that is correct.

Mr. CLEAVER. Eligible? They would be eligible?

Mr. DORETY. Would be eligible. Right. Therefore, the more underserved communities we were able to have, the more folks would be eligible for those payday loans.

Mr. CLEAVER. Final question: If we have one in Tampa and we have 50 States, 300 million people, I mean—

Mr. DORETY. We have one in St. Petersburg, too, sir.

Mr. CLEAVER. Okay. We have two.

[Laughter]

Mr. DORETY. But the fact of the matter is, I said the national program that credit unions are undergoing right now, we are very active in very underserved communities and we want to do more. So it is—

Mr. CLEAVER. I want you to do more. The question is, you know, will you do more? I mean, the legislation, I think, is good. But will you do more? I mean—

Mr. DORETY. Yes.

Mr. CLEAVER. —people are not standing in line trying to go in to serve these people. Now, the payday loan folks are making money or they wouldn't be there.

Mr. DORETY. Absolutely.

Mr. CLEAVER. And so, I mean, which would suggest that you can make money as well.

Mr. LUSSIER. Congressman, that is why passage of H.R. 5519 is a great start and beginning to what we need to get that job done. Credit unions would be out there trying to do it if they were permitted to do so.

Mr. CLEAVER. So you wouldn't mind a provision in this legislation that would give you a certain time in which you would have a certain number of these facilities located in underserved areas? I mean, some kind of provision that would give us some comfort in going to our districts and saying, you know, we just passed one or two of these bills and that help is on the way.

Mr. DORETY. Our regulator already requires us to put a branch in that community within 2 years of getting our charter. So they have the ability—they already are doing that, and they would have the ability going forward to require us to put a branch, a full service branch, in that community.

Mr. CLEAVER. So you want me to support Mr.—I always mess it up but—

Mr. LUSSIER. Yes, sir. We do.

Mr. CLEAVER. Yes. And then I will be happy at home, telling people that you are coming?

Mr. LUSSIER. Yes, sir.

Mr. CLEAVER. And the payday loan people will be angry and start fleeing? Thank you. Thank you, Mr. Kanjorski.

Mr. KANJORSKI. Thank you very much, Mr. Cleaver.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for Members to submit written questions to these witnesses, and to place their responses in the record. This panel is now dismissed, and I would like to welcome our second panel.

I am pleased to welcome our second distinguished panel. First we have Mr. R. Michael Stewart Menzies, Sr., president and chief executive officer of Eastern Bank and Trust Company, testifying on behalf of the Independent Community Bankers Association. Mr. Menzies?

STATEMENT OF R. MICHAEL STEWART MENZIES, SR., PRESIDENT AND CHIEF EXECUTIVE OFFICER, EASTON BANK AND TRUST COMPANY, ON BEHALF OF THE INDEPENDENT COMMUNITY BANKERS OF AMERICA (ICBA)

Mr. MENZIES. Mr. Chairman, thank you so much. It's an honor to be here in front of you again. My name is Mike Menzies and I am the president and CEO of Easton Bank and Trust in the little town of Easton, Maryland, on the Eastern shore of Maryland. We're a $140 million community bank, 14 years old. And it's also my honor to represent the Independent Community Bankers of America as the chairman-elect of that trade association of 5,000 community banks.

We do appreciate the invitation to come before this group. And as you would expect, we do strongly oppose this bill, H.R. 1537. Congress should not expand credit union powers without addressing first the tax advantage of credit unions and their inability or lack of willingness to comply with the Community Reinvestment Act.

I want to make clear that community bankers strongly support local, not-for-profit organizations. I'm the chairman of our local hospice. I have been the chairman of our United Way in Talbot County. Over my 38 years of experience in banking, I have always been involved with local charities. And community bankers throughout the Nation are also fully invested in the charities in their communities. But I believe CURIA is a misnamed, aggressive measure disguised as regulatory relief that would give credit unions expanded business lending powers and actually weaken their capital standards. It would increase the already unfair competition that credit unions currently pose to community banks.

A Congressional Research Service report notes, if I may quote, "Over the past 30 years, most of the distinctions between credit unions and other depository institutions have been eliminated or reduced because of deregulation. Consequently, the justification for the tax exemption for credit unions has been increasingly questioned."

Credit unions are seeking to expand farther into the core business of community banking, small business lending, and I can assure you, community banks are not afraid of competition. We have no shortage of competition when it comes to small business lending. We compete with large banks and finance companies and automobile dealerships, but all of those competitors pay taxes.

Credit union representatives often claim that they represent such a small percentage of the industry, and we heard that again this morning. While the banking assets total about $12.7 trillion in assets, and our 5,000 members represent roughly $982 billion, the credit union industry has grown to a $753 billion industry. And as you heard this morning, over 19 million members, and over 8,000 credit unions in this country today. We recognize that you, sir, have introduced H.R. 5519. And while we haven't totally analyzed that bill, we recognize it is a narrower bill. That's good.

Clearly, credit unions want to expand their charter because they feel inadequate in serving the needs of their community and their customers. For credit unions that truly believe they need to expand their powers, there's a wonderful solution that's out there—convert to a mutual thrift. It's a wonderful solution, because it allows credit unions to go into a business structure where they can expand their services dramatically. Unfortunately, NCOA is constantly putting up roadblocks to keep credit unions from moving into that mutual thrift structure.

So why should credit unions have to go to a new charter rather than just expand their current powers? The answer is really simple. Congress provided credit unions with a substantial tax advantage over community banks and does not require compliance with the Community Reinvestment Act. Congress put this basic tradeoff in decades ago. Limiting activities, providing credit to individuals of modest means, but valuable tax and regulatory benefits.

In 2005, the Tax Foundation calculated the credit union tax subsidy is worth about $2 billion a year and growing. On the average, credit unions found little or no effect on deposit rates or other costs, so the average member benefit is very little. But these are averages. Credit unions can use their subsidies selectively to secure business if they want. One of my customers, a retired airline pilot, very attractive 7-figure net worth, and a very attractive high-6-figure income, applied to me a year ago for an aircraft loan. I gave that individual, who has most of his deposits with us, not with his credit union, what I considered to be an extremely competitive rate, and the credit union quoted that loan on much more aggressive rates to buy a $700,000 airplane at probably a 20 percent discount to our pricing.

Several studies have shown repeatedly that credit unions have strayed far beyond their mission to serve individuals of modest means. Credit unions involved in last year's Florida real estate investment scheme, dubbed "Millionaire University," illustrates just how far credit unions have strayed. This scheme, a number of credit unions invested in a speculative land development deal far outside of their marketplace, far outside of the needs of their members, and lost hundreds of millions of dollars, causing the insurance fund one of the greatest losses in the history of the insurance fund.

For these reasons, sir, we urge Congress to reject calls to expand their powers. And instead, we hope that you consider true regulatory relief for all financial institutions.

Thank you, sir.

[The prepared statement of Mr. Menzies can be found on page 115 of the appendix.]

Mr. KANJORSKI. Thank you Mr. Menzies. Next we will hear from Mr. Bradley E. Rock, chairman, president, and chief executive officer of the Bank of Smithtown, testifying on behalf of the American Bankers Association.

STATEMENT OF BRADLEY E. ROCK, CHAIRMAN, PRESIDENT, AND CHIEF EXECUTIVE OFFICER, BANK OF SMITHTOWN, ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION (ABA)

Mr. ROCK. Thank you, Mr. Chairman. We appreciate the opportunity to comment on expanding the powers of credit unions. These issues are sometimes filled with emotion on both sides. The banking industry is sometimes portrayed as attacking the entire credit union industry. Let me assure you, Mr. Chairman, this is not our goal.

Most of the credit union industry today continues to focus on their mandated mission to serve people of small means. I would suppose that most of the credit unions that have been present in this room today are these mission-focused credit unions. These institutions are an important part of our financial system. Our issue is not with credit unions that are meeting the needs of people of modest means, but rather with the new breed of credit unions that want to grow aggressively, serve high-income individuals and large businesses, and take over small credit unions to expand their charter. These new breed credit unions are the biggest threat to traditional credit unions, as they are fundamentally changing the nature of the business, shunning their core mission to serve those people with limited options for financial services.

It is important to look beyond the rhetoric to the reality of today's credit union landscape. For example, the reality is that over 2,000 credit unions have been absorbed by these new breed credit unions since 2001. Today there are more than 123 credit unions with over $1 billion in assets, which makes them larger than 92 percent of the tax paying banks in this country. Near where I live, Bethpage Federal Credit Union, with more than $3 billion in assets, is nearly 3 times the size of my bank, and 5 times larger than the typical community bank on Long Island. And from their advertising, I can tell you that Bethpage is very much focused on serving wealthy individuals.

During this hearing, we have heard about the need for broader authority to serve underserved areas. The reality is that there is no requirement today that credit unions demonstrate that they are meeting the needs of low-income individuals. NCUA's approval of so-called underserved areas does nothing to assure such a requirement. NCUA has declared entire cities to be underserved and allowed credit unions to open branches in high-income areas with no requirement, none at all, that they actually serve low-income neighborhoods. For example, all of Washington, D.C., has been declared underserved. Under proposals from NCUA and credit union groups, every credit union would be eligible to come into Washington, put a branch in wealthy Georgetown, and not make a single loan to a low-income person.

During this hearing, we have also heard about the need to serve small businesses. But the reality is that the new breed credit unions are hitting the congressionally mandated limits on business lending because they are making very large loans to real estate developers and others, including those businesses out of their market area.

For example, consider a $30 million luxury condo loan, which is currently in default, made by Eastern Financial Credit Union, or the loan for a luxury golf and condominium resort by Twin City Coop's Federal Credit Union. Or the construction loans by Texans Credit Union that average $10 million each. Or the millions of dollars in loans involving a land deal in Florida that caused the recent failures of credit unions in Colorado and Michigan. Are these loans that the credit union tax exemption was intended for? How many loans to low-income people could have been made instead?

Expanding business lending powers and easing credit union capital rules will only move the new breed of credit unions further away from their mandated mission, and encourage them to bulk up by acquiring small ones at an even faster pace. Fortunately, for those expansion-minded credit unions, there is a very viable option for them today—switching to a mutual savings bank charter. This charter, which some credit unions have already adopted, provides greater flexibility while still preserving the mutual member focus that credit unions find desirable.

Mr. Chairman, there remains an important role for traditional credit unions that serve people of modest means. But we see no reason for Congress to give authority to expand business lending that will only encourage a further departure from this mission.

Thank you very much.

[The prepared statement of Mr. Rock can be found on page 130 of the appendix.]

Mr. KANJORSKI. Thank you very much, Mr. Rock. And I thank the entire panel for waiting this long. Let me make first and foremost a congratulatory note to the community banks and to the average banks in America, and let it be noted for the record that our present situation of subprime loan failures is less attributable to the regulated national and State banks in this country, and more attributable to unregulated institutions in this country. And if we had had more of the formal regulated community banks or regular banks, although you are both regular banks, we probably would be in less difficulty than we are today in the credit markets. So you are fulfilling a good function and I want to make sure this committee recognizes that fact.

Now, with that being said, I think there is probably a fundamental disagreement philosophically between the chair of this committee and yourselves. And we could sit here for hours, and I would probably enjoy it, but I doubt whether we would convince each other of our mutual positions as being correct.

Although, I want you to know that prior to my arrival here in Congress and my service on this committee, I actually served as a board member of a small bank in Pennsylvania, and I think I served for about 10 years as a director in that bank. So I understand some of the problems that small banks have, certainly their competitive positions that they have. And I empathize, let it be said, with the banking community.

On the other hand, I was not preconceived to sympathize with the credit unions prior to my arrival in Congress. I had never been a member of a credit union and I knew little about what they did. I actually got here in an interesting way. I represented as an attorney the cooperatives, food cooperatives. And I will not say I fell in love with, but I became enamored with, the process of cooperatives and saw how they could be utilized to work to the benefit of people. And when I came to Congress and then studied the credit union movement, I became very appreciative of the fact that a cooperative effort in banking, removing some of the activities of competition and profiteering or profiting from commercial endeavors, actually worked to the benefit of people. I do not know how we would ever agree that all organizations in the country should be for-profit and for nothing else. I think we have a huge number of institutions that border on that cooperative area that perform great functions. Some abuse their positions. I will concede that. That is not a question. But I can tell you quite frankly, some banks abuse their positions. If we wanted to sit here and go back and forth, I do not know who would win that challenge, but some of my best friends, as they say, are now residents of Allenwood who used to be in banking institutions. May I just leave it at that—be a little humorous, but that happens. That is the—

Mr. ROCK. None of our members, I hope, Mr. Chairman.

Mr. KANJORSKI. No what?

Mr. ROCK. None of our members, I hope.

Mr. KANJORSKI. Well, I would imagine they at one time or another were your members. They are not anymore. But those are the foibles of human beings. To look at those excesses or extremes that caused those results, and then attribute it to the whole I think is somewhat of a mistake.

What I do not understand, honestly, is we worked very hard on putting a new financial structure here in place, a risk management tool. And being good businessmen, both you and your institutions; your associations being made up of good businessmen, why wouldn't you for the protection of the credit union members and for that aspect of the financial service industry and the country, why would you not be more in favor or in favor of a risk management capital system as opposed to what it is today, which does not really meet the needs and protect it against some of the abuses that you are actually asking? You heard the regulators say here, you would afford the opportunity for better Federal regulation, for better protection for the members, for better protection for society, if we put in place a risk management capital system that was not thought up by the credit unions, was not thought up by their association, was not thought up by the Congress, but actually was developed by the regulator. How can you argue against that sort of meritorious position?

Go to it. Tear me apart, gentlemen.

Mr. MENZIES. Go ahead.

Mr. ROCK. Mr. Chairman, credit unions by the nature of their structure do not have all of the same means available to them for raising capital that banks have available. Credit unions' only means of raising capital is through retained earnings. And history has shown that in times of stress when banks or credit unions are losing money, they do not have the ability to build capital through retained earnings. Therefore, it has always been thought, because that's their only method of raising capital, it has always been thought that credit unions therefore need to have higher capital requirements than banks do, because banks have other alternatives during those hard times.

The second reason—

Mr. KANJORSKI. Okay. But now let me call you on that. This risk system that is proposed by the regulators is 1 percent higher than what is required of banks.

Mr. ROCK. No. I believe it's a quarter—

Mr. KANJORSKI. It is 6 percent—

Mr. ROCK. —a quarter of a percent. Five versus five-and-a quarter is what they're proposing. A quarter of the percent.

Mr. KANJORSKI. No, I think it's 6 percent.

Mr. ROCK. No. It's 7 now. It's 7 now, Mr. Chairman.

Mr. KANJORSKI. And would go down to 6?

Mr. ROCK. Would go down to—no. Would go down to five-and-a-quarter is what they're proposing.

Mr. KANJORSKI. I thought I heard 6 in testimony, but I will trust you. Still, it is higher than what is required of banks.

Mr. ROCK. Well, by a quarter of a point. And I think the question would be, is that sufficient to protect the depositors? And historically, the answer has been no.

Mr. KANJORSKI. Well—

Mr. ROCK. Because when you're losing money, you can't build retained earnings. There are no retained earnings.

Mr. KANJORSKI. Look, when banks fail, they go to the insurance fund. When the insurance fund does not have enough money, they go to the taxpayers. We all know that, and I do not think there is anything wrong with that.

Mr. ROCK. Well, that has never happened, though, Mr. Chairman. It's theoretical.

Mr. KANJORSKI. I know. But we have supported that. Never happened, but that is the trail. But if the insurance fund for the credit unions fails, they go to the rest of the credit unions throughout the country. It does not come to the taxpayers. So they have to have an awful lot of faith in the performance of these various credit unions to risk all of their capital. I mean, it is really quite a brotherhood; 90,000 people linking together to provide security for their needs within their financial services.

Mr. ROCK. I would say two things to that, Mr. Chairman. First of all, it presumes that bank capital doesn't stand behind those obligations, and I think that's an incorrect assumption.

Mr. KANJORSKI. What bank—

Mr. ROCK. It has never happened. The collective bank capital. Yes, you look first to the insurance fund. Then you would look to the bank capital, just as you're hypothesizing for credit unions, and only then would you look to the Federal Government, which by the way, there is no requirement that the Federal Government stand behind. That's the whole too-big-to-fail argument.

Mr. KANJORSKI. And maybe you could help me out. Your position is that under present banking laws, if there were a failure of banks in the country, and the Federal insurance fund fails, they then draw on all of the other remaining banks?

Mr. ROCK. I'm saying that both of your hypotheticals are purely hypothetical. It has never happened for credit unions, and it has never happened for banks. It's not a matter of law.

Mr. KANJORSKI. Well, you know, I agree they may be hypothetical, but I would have to be honest with you and say we may get to test that system shortly. According to Mr. Bernanke the other day, he thought that there would be about 100 bank failures. Now we hope that they are not very large banks, but, you know—

Mr. ROCK. And there is a $50 billion fund standing there financed through—not through—

Mr. KANJORSKI. But there is some fear that it may be a too-large-to-fail bank that is involved, which would be incredibly disruptive.

Mr. ROCK. And that would be unfortunate.

Mr. KANJORSKI. Very unfortunate.

Mr. MENZIES. Mr. Chairman, if I could pipe in a little bit.

Mr. KANJORSKI. Yes.

Mr. MENZIES. I think the great challenge that you, sir, and this committee face is understanding what types of risk you'd really want to take with this structure called credit unions. We had the great honor of having breakfast with Mr. Bernanke this week in Florida and with Chairman Sheila Bair, and with OTS Director Reich, and it's pretty obvious that we're going through one of the most difficult economies in our history. We're talking about the housing stock falling in value from $600 billion to $1 trillion. We're talking about subprime losses that are hard to measure, that are estimated by some to equal a couple of trillion dollars. These numbers are unbelievable. And then the question is, do you take an industry whose mission is to serve the underserved—to serve the underserved—and do you give them powers that let them convert Washington, D.C., and Houston, Texas, into their marketplaces? You can go into small business lending.

Mr. KANJORSKI. Okay. Let us stop right there.

Mr. MENZIES. Okay.

Mr. KANJORSKI. I am the author of these two bills—

Mr. MENZIES. Yes, sir.

Mr. KANJORSKI. —with Mr. Royce. They do not use the definition of underserved that presently is interpreted by the regulator. The definition of underserved is greatly restricted from what its present definition is to shadow and be consistent with the New Markets Initiative definition.

And to my knowledge—I will not say that there isn't a community in America that is not in total included in the New Markets Initiative, a census tract method of being underserved, but I highly doubt it. I certainly have a congressional district that is in the lower third economically in the country, and there is no community in my district that in totality qualifies as an underserved community. So when Mr. Watts proposed that possibility of Houston and Washington, I think that is not the facts. And we are going to check into the facts, okay?

Mr. MENZIES. If in fact it's driven by economics, then, frankly, I would say that makes sense. If the underserved member is eligible because of their economic condition, not where they live, then that may well make sense if they have a net worth under some number, $100,000. If they have an income under some number, that makes a great deal of sense. But if it's geographic and Wal-Mart wants to put a store in one of these areas that's defined geographically as eligible, then should Wal-Mart be able to go borrow from a credit union or Home Depot or Lowes or somebody else?

Mr. ROCK. Mr. Chairman, I would make two points. One, and I think this was part of the point Mr. Watt was trying to make before, that would—I agree with what you have said, but that would presume that the Cities of Houston, Tucson, Philadelphia, etc., that have already been approved by NCUA, the entire city as an underserved area, that those don't get grandfathered in.

Mr. KANJORSKI. This Act is only allowing underserved areas to be served by credit unions in accordance with the definition here. It would be actually restricting what credit unions could do.

Mr. ROCK. Okay. Including the 641 previous approvals. Is that what you're saying?

Mr. KANJORSKI. I would think that is how—

Mr. ROCK. I would think so, too, but I think that's something that's not clear.

Mr. KANJORSKI. I am glad you raised the question, and we certainly will look into it.

Mr. ROCK. And the second point I would make, Mr. Kanjorski, and do agree that, as you said to Mr. Watt before, that the proposal is more restrictive, and I concur with that. But I would point out that in the City of Washington, for example, under the current proposal, almost all of Georgetown and almost the entire area along Massachusetts Avenue would qualify as an underserved area. And

I think for any of us who know those areas, those areas are hardly comprised of low-income individuals.

Mr. KANJORSKI. Now wait. Under—

Mr. ROCK. Under the new proposal.

Mr. KANJORSKI. All of Georgetown would apply?

Mr. ROCK. Almost all of Georgetown and almost all of the area along Massachusetts Avenue.

Mr. KANJORSKI. Meaning that Treasury has interpreted the New Markets Initiative statute to say that these homes in Georgetown and the residents there are underserved?

Mr. ROCK. That's the way we read the proposal. We have mapped it out, and we look at it, and that's the way we read the proposal.

Mr. KANJORSKI. I think we are going to find the old definition. We will check it out.

Mr. ROCK. No. Under the old definition, the entire City of Washington, D.C., has been approved as an underserved area.

Mr. KANJORSKI. Well, this is very good, because the evidence you are giving us we should also transmit to Ways and Means, because we are working on the reauthorization of the New Markets Initiative, and I certainly, having been one of the original drafters of that piece of legislation some 5 or 6 years ago, never intended, nor did the President at the time, ever intend that we finance those tax credits for areas like the rich sections of Georgetown. So we will certainly check into that.

Mr. ROCK. Yes.

Mr. KANJORSKI. I have taken far in excess of my time, and I am fearful that the chairman may run down here and dispossess me of the chair. So, with that, let me recognize my charming friend from Illinois.

Mrs. BIGGERT. Thank you. I hate to break into that discussion. It was, I think, lively and productive. But just a couple of questions. Mr. Menzies, in your statement you referred to a GAO study of 2003, and it says that credit union serve a more—the study found that credit unions serve a more affluent clientele than banks, and the study concluded that credit unions overall served a lower percentage of households of modest means than banks. Could you expand on that a little bit?

Mr. MENZIES. Well, you have quoted the GAO study correctly. The GAO study says that the community banks have more customers of low and modest income as a percentage of their customers than do credit unions. And that's because they're based in the community and they need to serve the entire community.

Mrs. BIGGERT. Now that is a 2003 study. Do you think that would still hold true today?

Mr. MENZIES. Well, that's a good question, and the question is, has the credit union history studied their low- to moderate-income statistics and broadcast them so that we can clearly understand that a majority of their customers are people of modest means and people who need access to credit.

Mrs. BIGGERT. Well, then, my next question is that—for both of you—is that the credit unions said that banks don't want to make small business loans, especially under $100,000. Does your bank?

Mr. MENZIES. Absolutely. We just participated, 50 ICBA banks, just participated in Chairman Bair's Small Business Loan Initiative to establish strategies to make small loans, $1,000 and under, to individuals. We make $500 and $1,000 loans all the time. We lose money on them. We lose a lot of money on them. And we lose money because we pay taxes and we have a lot of overheard associated with regulatory burden. But we do it because we have to because they're members of our community.

Mr. ROCK. Congressman, we have an entire staff of people in my bank, which is a community bank, devoted to finding and making small business loans of under $100,000. And we currently, as of the date of filing of our last call report, have $95 million of such loans outstanding. So we absolutely do.

Mrs. BIGGERT. Are the business loans under $100,000 less risky than business loans over $100,000?

Mr. MENZIES. I would say no. I would say that business loans under $100,000 inherently carry more risk, require more underwriting, require more analysis, and require a closer relationship. We have commercial lenders who have significant experience lending into small business. They need to triage whether this is an appropriate FDIC deposit-insured risk or whether we should use the SBA or SBA 504 or some other strategy to mitigate risk.

But my personal perspective would be that loans under $100,000 can be riskier than the larger loans.

Mrs. BIGGERT. You said it cost you more.

Mr. MENZIES. Absolutely it does.

Mrs. BIGGERT. Would that be true—how different would that be for a credit union to make the same loan?

Mr. MENZIES. How different would—

Mrs. BIGGERT. Well, would they have the same costs. How would the costs be different since they don't pay taxes on that?

Mr. MENZIES. I don't know the exact basis point difference in terms of regulatory burden. I do know that the credit union tax advantage gives them 50 basis points or a half a point up to sixty-some basis points of pricing advantage. That's why a 7 percent 20-year aircraft loan that I quoted was written at 5.75 for 20 years by a competing credit union. So there's a significant competitive advantage if they're not paying 35 percent to the Federal Government and 7 percent, in our case to the State, of their income.

Mrs. BIGGERT. Okay. Then Mr. Rock, you testified that in spite of the change in the credit unions that kind of metamorphose into highly competitive financial institutions that they're almost indistinguishable from banks, and yet they continue to enjoy the tax exempt status conferred when it was composed of small self-help organizations.

And if our goal is to foster a healthy competition in the financial services industry in order to benefit all the consumers, should we try and level the playing field between bank and credit unions?

Mr. ROCK. I would say yes, absolutely, among the new breed credit unions. If a credit union wants to grow to a very large size, wants to serve everyone in the community without limitation, if they want to offer all the products and services that a bank can to all the same customers, then I say I welcome the competition, but they should play by the same rules. They should be subject to the same regulations. They should pay the same income taxes and so on.

I do not think that that would be a wise policy choice for the traditional credit unions. I think the traditional credit unions that abide by the original quid pro quo, I think they serve an important function in the financial system, and I think they should be continued to allowed to do so.

Mrs. BIGGERT. Thank you. I yield back.

Mr. KANJORSKI. Thank you very much, Mrs. Biggert. We are pushing up against the votes that have been called, but I think we have enough time. Mr. Lucas of Oklahoma.

Mr. LUCAS. Thank you, Mr. Chairman. One quick question. Gentlemen, obviously you both have a great deal of experience, and when I joined this committee 13 years ago, we were still in the process of sorting out what remained of the S&L meltdown, a concept basically where short-term money was used to make long-term commitments, and when circumstances changed, an entire industry went away.

Tell me from your experience in the financial services industry in relation to how things have evolved in the last 20 years, is there still a challenge when you use short-term money to make long-term obligations?

Mr. MENZIES. We don't use short-term money to make long-term obligations. We are required by the FDIC to manage our balance sheet within an interest rate risk sensitivity that doesn't put too much earnings at risk. And the same is the case with Mr. Rock. We can't just go mismatch our balance sheet. We have a comprehensive management process to make sure we don't go make 30-year loans and put them on our books and fund them with savings accounts. It's as simple as that.

Mr. LUCAS. And do you have concerns about that being done by other people?

Mr. MENZIES. I think it is not a responsible form of financial management. I think the reason the savings and loans got into trouble is because they had been given exclusive privileges and exclusive powers, and they were funding 30-year assets with savings accounts, and the market went upside down, and the government deregulated them, and they tumble.

That is not the case with the thrifts today. The thrifts that are in business today are well capitalized and well managed, for the most part. They do a good job. But they're subject to the same types of interest rate risk management policies that I'm subject to, and I've just been through an examination, and they are serious about it.

Mr. ROCK. I would say, Mr. Lucas, yes, I think those continue to pose substantial risks. I think that 20 to 25 years ago when those events happened that we characterize as the S&L crisis, banks were not required to engage in the same level of interest rate risk simulation modeling that we are today.

And I know that our regulator, the FDIC, requires us to engage in extensive monitoring. We have special computer programs. We do it quarterly. In times of stress, we do it monthly. So, I think that has reduced it.

With regard to how the credit union regulators look at that, and whether the same requirements are demanded of them, I really don't know.

Mr. LUCAS. Fair enough. Thank you, Mr. Chairman.

Mr. KANJORSKI. Thank you very much, Mr. Lucas. I really have to apologize. We have these votes on. I would really love to sit here and trade off a lot of questions and answers, because I think we would get a lot of the needed information.

I want to assure you that this committee, and certainly this majority, are not prone to favor one institution over another. What we are trying to do is get to risk management, get to firmness in making sure that whatever occurs in our financial service industry is well examined and ideal.

We are also working on regulatory reform for banks. I am going to ask my friends in the credit union movement not to get involved in being opposed to those deregulations for banks, because we do not intend to deregulate anything that would cause greater risk to the system, but in fact deregulate those things that are determined to be unnecessary or further restrictive or limiting your ability to earn.

In that regard, I hope we come to parity here. We may not. If we do not, I don't want the two of you to get ulcers over it. If we do, I want you to realize that then we have all succeeded at our chore to get the system to work as best it can.

With that in mind, we are not going to take any further questions, because we have to make the votes. And I am going to note that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for Members to submit written questions to these witnesses, and to place their responses in the record.

I want to thank both of you for appearing here today. And we did not mean to overwhelm you with time or questions. Certainly your statements and your answers will be fully examined and taken as seriously as any of the other testimony before this hearing. And with that said, the panel is dismissed, and this hearing is adjourned.

[Whereupon, at 1:35 p.m., the hearing was adjourned.]

A P P E N D I X

March 6, 2008

OPENING STATEMENT OF
CONGRESSMAN PAUL E. KANJORSKI

COMMITTEE ON FINANCIAL SERVICES

HEARING ON THE NEED FOR CREDIT UNION
REGULATORY RELIEF AND IMPROVEMENTS

THURSDAY, MARCH 6, 2008

Mr. Chairman, I am very pleased that we meet today to examine the need for making statutory improvements and providing regulatory relief for our nation's credit unions. Nearly four years have passed since the Financial Services Committee last met to exclusively examine the many issues of concern to the credit union movement. I therefore commend Chairman Frank for convening this long overdue hearing. I am also optimistic that today's proceedings will lay the groundwork for swift action on legislation to modify the Federal Credit Union Act.

The last time we acted on comprehensive credit union legislation occurred a decade ago, when the Congress adopted H.R. 1151, the Credit Union Membership Access Act. For the last five years, we have also worked to craft and build bipartisan support for the Credit Union Regulatory Improvements Act, or CURIA. I have been a leader in both of these reform efforts.

CURIA would help to fix several problems created by the rushed drafting of H.R. 1151. These fixes include putting in place a modern risk-based capital system for credit unions, allowing credit unions of all types to expand into underserved communities, and amending conversion voting standards.

CURIA also contains a number of provisions to facilitate the ability of credit unions to make business loans. For example, CURIA would raise the current asset limit on member business loans from 12.25 percent to 20 percent, a limit comparable to the current one of thrifts for their non-real estate commercial lending.

Some have suggested that this modest change represents a "major expansion" of business lending authority. I have a different view. Prior to the enactment of H.R. 1151, we had no limits on the business lending activities of credit unions. CURIA would therefore provide minor, but needed, adjustments to the limitations on business lending currently imposed by the law.

Support for CURIA has steadily grown over time. During the 108th Congress, we had 69 supporters. In the 109th Congress, we garnered 126 supporters. To date, in the 110th Congress, we have now gained the endorsement of 147 supporters in the House.

Our legislation, moreover, no longer has just bipartisan support in the House. It now enjoys bicameral support. I am very pleased that Senator Mary Landrieu announced that she would introduce CURIA in the Senate along with Senator Joseph Lieberman. Their support clearly demonstrates that the momentum for enacting credit union statutory reforms is growing.

Although support for CURIA is building, I recognize that enacting legislation into law is often a multi-stage process. Therefore in order to achieve some progress on these matters, I recently introduced a pared back credit union bill known as the Credit Union Regulatory Relief Act. Like CURIA, Congressman Ed Royce joined me in these efforts.

H.R. 5519 contains eight non-controversial provisions found in CURIA and previously passed by the House. It also includes language to permit all credit unions to assist those living and working in underserved census tracts, help individuals with short-term financial difficulties to obtain loans, and expand member business lending activities very modestly through some narrow carve-outs and clarifications. The swift adoption of H.R. 5519 will allow us to continue to work on enacting the many other important legislative reforms contained in CURIA, but not contained in this new bill.

Before I close, I would like to strike a cautionary note. At today's hearing, we will hear not only from regulators, but also credit unions and banks. In the past, banks and credit unions have sometimes found themselves engaged in what might be termed a family feud. In reality, credit unions and banks have much in common. I hope that they realize this fact. In my view, we can work to expand the pie for both of them by advancing well-crafted reforms to their underlying statutes consistent with safety and soundness objectives.

In closing, I look forward to hearing from our witnesses and engaging in a thoughtful debate. I also I look forward to moving a credit union bill through our committee in the very near future. I yield back the balance of my time.

Rep. Randy Neugebauer
Statement for Record
Credit Union Hearing
March 6, 2007

Chairman Frank, thank you for calling today's hearing.

I had the opportunity to visit with representatives from several credit unions from my district yesterday. When someone takes the timc and expense to travel all the way to D.C. from Abilene and Big Spring, Texas, that tells me the issues we are working on here are important to them and the credit union members they work for.

I appreciate the contributions of credit unions in my district. Many are small credit unions, and they work hard to serve their members. Consumers benefit from having a wide range of financial institutions to choose from so they can find the credit union, bank or other institution that best fits their needs. We are fortunate in West Texas to have so many sound choices among financial services providers.

I support additional regulatory relief for all financial institutions. While we provided some relief in the last Congress, a number of important items were left on the table that we need to revisit. Any time we can reduce unnecessary paperwork, rules and burdensome requirements, more time and resources are freed up to allow these institutions to help their members, customers and communities prosper.

The credit unions that visited me yesterday discussed the regulatory relief items in new legislation Congressmen Kanjorski and Royce introduced this week. I appreciate their efforts to bring some new ideas to the table in addition to those in the CURIA legislation.

One aspect of CURIA I have been supportive of, however, is reforming prompt corrective action to allow credit unions to move toward a more risk-based approach. A one-size capital requirement for all credit unions does not take each credit union's risk-based profile into account. If we want financial institutions to make risk-based decisions, we must give them the ability to do so.

As the Committee moves forward from this hearing, I look forward to working on regulatory relief for credit unions, as well as for all types of financial institutions.

Congressman Ron Paul
Financial Services Committee
Hearing on "The Need for Credit Union Regulatory Relief and Improvements"
March 6, 2008

Mr. Chairman,

I applaud you for calling this hearing. The topic of credit unions is one which has been important to me and my district, but has taken on an even greater importance in recent months. With the financial crisis affecting banks resulting in a decrease in lending, credit unions can play an important role in alleviating the effects of the subprime crisis. In order to ensure that credit unions can play this important role, this committee should pass CURIA, which is sponsored by Capital Markets Subcommittee Chairman Kanjorski and Mr. Royce. I am proud to have joined them as an original cosponsor. The regulatory relief in CURIA will enable credit unions to better serve the more than 89 million Americans who are credit union members.

One important issue is the ability of credit unions to diversify their investment options. CURIA would allow federal credit unions to invest in investment grade bonds and double the amount that federal credit unions can invest in credit union service organizations.

Another aspect which is of particular interest is that of enabling credit unions to cater to underserved areas. This would enable credit unions to offer their products and services to those people who either have never been served by or who are no longer served by other financial institutions. Due to litigation by the banking industry, several credit unions in my home state of Texas have been told that they can no longer take on new customers in underserved areas, and are at risk of losing customers from further low-income areas due to the threat of future litigation. At a time when many low-income consumers are in danger of foreclosure on their homes and feeing the squeeze of inflation when they receive their paychecks, the last thing we should do is to impose new regulations such as requiring credit unions to comply with the Community Reinvestment Act. We in Congress should be doing all we can to ensure that these consumers are not unduly restricted in their borrowing or refinancing options.

Consumers are best served in the marketplace by a multiplicity of sellers. Banks and credit unions each have unique products and services that they can offer to customers, and both banks and credit unions need to realize that the financial marketplace is not a winner-take-all affair. Membership in a credit union and holding of a bank account or loan are not mutually exclusive activities. By reducing the regulatory burden facing credit unions and ensuring a level playing field, healthier market competition will ensue, allowing consumers access to the products and services they need. In a time of market turbulence, liquidity problems, and less willingness to the lend on the part of banks, credit union regulatory relief can go a long way towards helping consumers in need. I therefore urge my colleagues to pass HR 1537, the Credit Union Regulatory Improvements Act.

TESTIMONY
OF
TOM DORETY
PRESIDENT AND CHIEF EXECUTIVE OFFICER
SUNCOAST SCHOOLS FEDERAL CREDIT UNION
ON BEHALF OF THE
CREDIT UNION NATIONAL ASSOCIATION
ON
THE NEED FOR CREDIT UNION REGULATORY RELIEF AND IMPROVEMENTS
BEFORE THE
HOUSE COMMITTEE ON FINANCIAL SERVICES

MARCH 6, 2008

Chairman Frank, Ranking Member Bachus, and members of the committee, on behalf of the Credit Union National Association (CUNA), I appreciate the opportunity to appear before you and express the association's support for H.R. 1537, the Credit Union Regulatory Improvements Act (CURIA).

CUNA is the largest credit union advocacy organization, representing over 90% of our nation's approximately 8,400 state and federal credit unions and their 90 million members. I am Tom Dorety, President and CEO of Suncoast Schools Federal Credit Union in Tampa, Florida. I also serve as Chairman of the Board of Directors of the Credit Union National Association.

The nation is experiencing a credit crunch in many sectors of the economy. It is hard not to be struck by the irony of the fact that credit unions are ready, willing and able to help alleviate the problem and promote economic growth, and yet we are inhibited from doing so by outmoded laws that protect the narrow self interest of bankers

We hope this Committee can start the work of freeing us to do all we can do for our members, the American consumers.

Credit unions are member-owned financial cooperatives established to meet the financial services needs of their members. As Congress noted when it enacted the Credit Union Membership Access Act of 1998, large or small, credit unions have five features which make them unique in the financial world:

1. Credit unions are not-for-profit financial cooperatives, and therefore do not issue stock. Instead, earnings are returned to our members in the form of higher rates on deposits, lower rates on loans, and lower fees.
2. Credit unions are democratic. One member, one vote is the rule.
3. Credit unions are governed by volunteer boards of directors elected by their membership.

4. Under federal law, credit unions may not serve the general public. People qualify for membership in a credit union by virtue of their employment, organizational affiliation or community.
5. Credit unions have a social purpose. They exist to help people, not make a profit.

In order for credit unions to continue to meet the diverse financial needs of their membership, we ask Congress to enact H.R. 1537, the Credit Union Regulatory Improvements Act.

Mr. Chairman, the last major changes to the Federal Credit Union Act were made in 1998, through the enactment of the Credit Union Membership Access Act (CUMAA). Contrary to popular belief, these changes did not provide significant regulatory relief to credit unions – in fact, the opposite is the case.

CUMAA was enacted in response to a 1998 Supreme Court ruling that invalidated a 1982 National Credit Union Administration (NCUA) policy regarding multiple-group fields of membership. The bill provided a grandfather clause for then-current credit union members, and prescribed limitations that NCUA must consider prior to authorizing new multiple-group fields of membership. The law also contained "stricter regulatory, supervisory and commercial lending requirements for credit unions."[1]

As a result of CUMAA, credit unions for the first time were subjected to a statutory capital requirement, even though credit unions were, on average, far more heavily capitalized than banks. Banks operate with regulatory capital requirements, not with inflexible statutory capital requirements imposed on credit unions.

Credit unions were also subjected, for the first time, to a statutory member business lending cap. Some have mischaracterized CUMAA as giving credit unions authority to make member business loans. In fact, the law for the first time constrained business lending by credit unions. Business lending was done by many credit unions from their earliest days in the United States.

And CUMAA included language intended to clarify that all federal credit unions may apply to NCUA to add underserved areas to their field of membership. But the wording was challenged in court by banking trade groups, forcing NCUA to discontinue underserved area expansions for credit unions that would like to reach potential members who are not being served adequately.

Professor William Jackson, then of the University of North Carolina and now at the University of Alabama, noted in a 2003 study that "CUMAA imposed more limitations on credit union operations than it lifted."[2] Further, he states that the wave of deregulation of depository institutions of the last two decades was not applied to credit unions.[3] It is also noteworthy that

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[1] Congressional Research Service. "Credit Union Membership Access Act: Background and Issues," January 5, 2001. p. 1.
[2] William EE. Jackson, III. "The Future of Credit Unions: Public Policy Issues," Filene Research Institute, 2003. p 67.
[3] Ibid., p 67.

the Treasury Department found in a 2001 study that "In general, federal credit unions have more limited powers than national banks and federal savings associations."[4]

These new restrictions on credit unions have not been revisited by Congress since enactment, ten years ago. Given the time that has elapsed since the enactment of CUMAA, it is appropriate for Congress to reconsider the application of these statutory requirements.

CUNA asks Congress to provide regulatory relief in these areas. We also ask Congress to make amendments to some other sections of the Federal Credit Union Act to eliminate some regulatory burdens that were not addressed in 1998.

Member Business Lending

Credit unions support the provisions of H.R. 1537 which would increase the current limit on credit union member business loans (MBLs) from 12.25% to 20% of total assets, and permit the NCUA to increase the threshold for defining a MBL from $50,000 to $100,000. The bill would also allow, at the discretion of the NCUA Board, credit unions that fall below the net worth requirements for being "well capitalized" to make new business loans. This is especially important for adequately capitalized credit unions that have well-managed business lending programs.

Beyond what is currently in H.R. 1537, we hope that Congress also will consider eliminating the statutory business lending cap entirely, and provide NCUA with authority to permit a CU to engage in business lending above 20% of assets if safety and soundness considerations are met. If that broader approach is not approved, as an alternative, CUNA asks Congress to consider exempting MBLs made in underserved areas from the business lending cap, as proposed in H.R. 5519.

The current 12.25% member business lending cap is overly restrictive and undermines public policy to support America's small businesses. It does not take into consideration the additional capital credit unions typically hold in excess of the statutory requirement. Credit unions on average hold nearly 12% of their capital in reserve, even though 7% is the level required to be considered well capitalized. In fact, if the 1.75 multiplier was applied against the average 11.6% net worth held by credit unions today, the figure would exceed the 20% of assets MBL cap in H.R. 1537.

Quite frankly, for many credit unions, the current 12.25% MBL limit effectively bars entry into the business lending arena. Startup costs and requirements, including the need to hire experienced lenders, exceed the ability many credit unions with small portfolios to cover these costs. Expanding the limit on credit union member business lending would allow more credit unions to generate the level of income needed to support compliance with NCUA's regulatory requirements and would expand business lending access to many credit union members, thus helping local communities and the economy.

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[4] United States Department of the Treasury. "Comparing Credit Unions with Other Depository Institutions." January, 2001. p. 19.

Banking trade groups have argued that Congress should not increase the credit union member business lending limits because this type of lending is not what credit unions have historically done. This is false. Credit unions have been offering their members business loans since their inception nearly 100 years ago.

Banking trade groups also argue that credit union member business lending is a competitive threat to the bank and thrift commercial lending. If this is true, their members certainly do not think so. A recent survey by the American Bankers Association (ABA) of its own members shows that only 2% of their member banks view credit unions as their chief lending competition.[5]

Moreover, the composition of the business lending market does not suggest that credit unions are currently in a position to threaten the banking industry's dominance in the commercial lending market. At mid-year 2007, 2,026 of the 8,247 credit unions (25%) in the United States had outstanding business loans. The average size of credit union MBLs granted in 2007 was $181,000. Nationally, credit union member business loans totaled $28 billion, compared to $3.1 trillion at banking institutions. That's right: for every $100 of business loans made by banks and credit unions, credit unions total less than a dollar, or a mere 89 cents of that $100.

Over the years, credit unions' mission has been to meet the financial services needs of their members. Credit unions throughout the country have a good story to tell on how their member business lending programs have helped members who have been denied business loans from banks.

Let me provide you with several personal examples to show you how the business loans made by Suncoast Schools Federal Credit Union have helped business owners who otherwise would have had a very difficult time securing affordable commercial credit.

About a year ago, we helped a member who owns a small commercial trucking firm looking to update one of its trucks. The owner's Beacon score was significantly below our threshold of 660. Most financial institutions would have automatically declined the request due to the Beacon score, forcing the member to borrow from a finance company type organization at a significantly higher interest rate. We took the extra time to confirm that all of the negative trade lines on the member's credit report had been paid in full. Furthermore, we obtained copies of the trucking contracts that the member had to haul for Wal-mart which confirmed the stability of the borrower's cash flow. We priced the loan at 9% which was roughly 4% lower than the rates available from a finance company. The member has repaid the loan monthly according to all the contract terms.

Nearly two years ago, we helped another member who owns a florist shop. She had financed the relocation and growth of her business on her personal credit cards. Even though her Beacon score exceeded our threshold, the debt service resulting from the balances on these personal credit cards adversely impacted the member's ability to qualify for a commercial loan elsewhere. We took the time to perform a site visit to the member's shop, evaluated the business potential due to the shop's proximity to the local hospital (which was in the process of expanding its

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[5] American Bankers Journal. "Community Bank Competitiveness Survey," March 2008.

cardiac care unit), and then carefully analyzed the company's projected cash flow once the debt consolidation took place. We were able to approve a $170,000 commercial mortgage at 8.25%. The monthly cash flow savings to the member from this consolidating refinance equaled $1,413. This member is also current on her all her payments.

But we are not just helping members who would have difficulty being served by local banks. We are also helping our members save considerable amounts of money.

Another member operates a small trucking company and needed a place to store their trucks. They located and purchased a small parcel of ground in a semi-industrial section of Tampa. Due to the size of the property and relatively small dollar amount of the loan ($67,500), they were only able to obtain financing at 12.5%. The member approached Suncoast and we were able to provide mortgage financing at an interest rate of 8.25%. The savings in interest during the first five years of this loan term will amount to over $14,000.

Consider two additional examples from North Carolina. In one case, owners of a pizzeria in Raleigh were forced into bankruptcy by their first franchise company, but they paid all of their debts anyway. They opened a new store in Henderson, North Carolina, but when they tried to expand, the banks in the area would not look past the bankruptcy. Coastal Federal Credit Union helped them – and they now have two locations and 30 employees.

The second case is that of a portrait studio owner who was turned away from every bank she approached when she sought a start-up loan. The banks told her that the loan she was seeking was too small. Coastal FCU made the loan, and she has now been in business for three years.

Unfortunately, Coastal FCU is one of those credit unions that have done so much to help its business-owning members that it is now approaching its member business lending cap. It makes quality business loans to their members. It has no delinquencies on their books. It has never had a business loan go bad. Yet, located in a state with a large banking presence, many of Coastal FCU borrowers have been turned away from banks. This is a travesty in light of our current economic situation and illustrates the void in business lending that can be filled by credit unions.

The Small Business Administration concurs: Credit unions that engage in member business lending often fulfill borrowing needs that not being met by other institutions. Addressing CUNA's Government Affairs Conference in February 2007, SBA Administrator Steven Preston said, "I encourage member business lending. Small businesses need a partner they can count on and credit unions often are reaching people that others have left behind."

According to a 2001 Department of Treasury study, credit union member business lending is generally less risky than commercial lending by banks or thrifts and presents little risk to the credit union share insurance fund.

> "While commercial loans are generally riskier than consumer loans, credit union member business lending tends to be less risky than business lending by banks and thrifts. A simple stress test of the effect of credit union failures precipitated by member business lending on the National Credit Union Share Insurance Fund indicates that the insurance

> fund would remain solvent if every member business loan defaulted at a loss of 100 percent, assuming no other losses at those credit unions."[6]

FDIC and NCUA Call Report data support that claim. From 1998 to September 2007, the average net charge-off rate on business loans at credit unions was only 0.08% of loans outstanding compared to an average of 0.70% for commercial loans at banks.

The Small Business Administration's Office of Economic Research notes that bank consolidation has led to a decrease in access to capital for the nation's small businesses.[7] And, a recent Wall Street Journal Article warns:

> "A widening credit crunch doesn't bode well for the economy. Start-ups and small businesses are generally the companies that create jobs in a downturn. But tighter credit could curb business investment and hiring as companies recalculate the cost of investing in new machines, marketing campaigns or ventures. This could magnify the current slowdown in growth." [8]

Member-owned credit unions are a natural choice for business owners faced with bank consolidation- and credit crunch-related pressures. Credit unions are, by definition, locally owned and controlled with local decision-making and a strong service-oriented philosophy.

Credit union member business lending is targeted towards middle and lower income individuals. The Treasury Department study estimate that 45% of credit union member business loans went to households with incomes less than $50,000.[9] The Treasury report also confirms that credit unions that engage in business lending do so in a safe and sound manner, with extremely low loan loss rates.[10] While credit union member business lending is a negligible share of the overall commercial lending market, in segments of our economy that need help the most, additional credit union member business lending will benefit the economy significantly.

Prompt Corrective Action

Credit unions seek modernization of the statutory capital requirements Congress enacted in 1998. The Federal Credit Union Act presently specifies the amount of capital credit unions must hold in order to protect their safety and soundness and the solvency of the National Credit Union Share Insurance Fund ("Insurance Fund"), administered by NCUA with insurance coverage comparable to that provided by the Federal Deposit Insurance Corporation to banks.

By law – not regulation, as for other insured depositories – credit unions must maintain a 7% net worth or leverage ratio in order to be considered "well capitalized." In comparison, the current leverage ratio for banks to be well capitalized is only 5%. This capital requirement for credit

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[6] United States Department of Treasury, "Credit Union Member Business Lending." January 2001. 35.
[7] Small Business Administration. "Bank Consolidation and Small Business Lending: A Review of Recent Research," Office of Economic Research. March 2005. 3.
[8] "Credit Scare Spreads in U.S., Abroad," *Wall Street Journal.* January 22, 2008. A1.
[9] United States Department of Treasury. 27.
[10] Ibid. 37.

unions is inefficient in that it unnecessarily retards member service and growth, and it does not appropriately account for risk of a credit union's assets.

Congress should consider the removal of all of the prompt corrective action (PCA) stipulations from the statute and leave it to regulatory determination, similar to the system under which the banking industry operates. In lieu of that approach, CUNA supports the capital reform provisions in H.R. 1537.

Title I of H.R. 1537 would modernize the credit union system of PCA by establishing a two-tier system for federally insured credit unions involving complementary leverage and risk-based minimum capital requirements. Under the proposed system, a well capitalized credit union would have to maintain a leverage ratio of 5.25% and a minimum risk-based ratio of 10%. Because the definition of net worth would be modified to exclude credit unions' 1% deposits in the share insurance fund, the GAAP leverage requirement would actually be in the neighborhood of 6%, still a full point higher than the comparable bank requirement. The risk-based requirement would adopt a Basel-type system that would account for risk much more accurately than the current credit union PCA structure.

Although the credit union capital requirements in H.R. 1537 would be more strenuous than those currently in effect for banks, there is substantial evidence that credit union capital needs are actually lower than they are at banks. Because of their cooperative structure, credit unions have less systematic incentives to take on risk to maximize profits. This strong structural bias to risk aversion helps to explain why credit unions currently hold capital in excess of the amount necessary to be well capitalized. As a result, the reform of PCA would lead to only modest decreases in credit union capital ratios.

In a 1996 article in the Journal of Banking and Finance entitled, *The Federal Deposit Insurance System that Didn't Put a Bite on U.S. Taxpayers,* Edward Kane and Robert Hendershott note: "differences in incentive structure constrain the attractiveness of interest-rate speculation and other risk taking opportunities to managers and regulators of credit unions." More recently, in the 2001 study *Differences in Bank and Credit Union Capital Needs*, David Smith of Pepperdine University and Stephen Woodbury of Michigan State University report that, "Because credit union loan portfolios are substantially less sensitive to macroeconomic fluctuations than bank loan portfolios, credit unions need less capital to protect themselves from loan losses."

Credit unions have been affected by the recent economic conditions (although not for the same reasons as banks). However, rather than being the causes of financial problems, credit unions have suffered collateral damage from elsewhere in the financial sector.

Credit unions have made virtually none of the toxic subprime loans that some other lenders have. Regrettably, some credit union members took out these loans from other lenders. And many credit unions operate in markets with falling home prices. As a result, credit unions have experienced some increases in delinquency and loan losses. We expect average loan losses in 2008 to rise to 0.75% of loans outstanding from 0.5% in 2007. These losses pale in comparison to the 15% to 20% losses expected on subprime loans. Considering just mortgage loans, the national average delinquency rate on mortgage loans from all lenders has risen from 2.1% at the beginning of 2006 to 3.9% today. For credit unions, the comparable statistic has increased from 0.7% to about 1.5%. As a result of their conservative financial management, we expect that credit unions will come through the current economic slowdown in a very strong condition.

The capital reform proposed by H.R. 1537, supported by the National Credit Union Administration, will reinforce and strengthen the regulatory incentive for credit unions to remain very safe and sound. [11] It would also allow credit unions to do even more to serve their members.

Underserved Areas

The third major provision of H.R. 1537 clarifies the intent of Congress that all federally chartered credit unions should be allowed to apply to the NCUA to add underserved areas to their field of membership. CUNA supports this provision and believes that this provision would fulfill the Congressional intent of CUMAA.

This provision will enhance the ability of credit unions to assist underserved communities with their economic revitalization efforts by providing all federal credit unions with an equal opportunity to expand services to individuals and groups working or residing in areas that meet the income, unemployment and other distress criteria identified by the Treasury Department. The bill's definition of a qualified underserved area includes areas currently eligible as "investment areas" under the Treasury Department's Community Development Financial Institutions (CDFI) program, as well as census tracts qualifying as "low income areas" under the New Markets Tax Credit targeting formula adopted by Congress in 2000.

As Representative Kanjorski clarified during the consideration of the Senate amendments to H.R. 1151 in 1998:

> Another important provision in this bill explicitly authorizes multiple group credit unions to include underserved areas in their field of membership. This is a provision which incorporates the principles of legislation originally introduced by the gentleman from Texas (Mr. Frost).
>
> Providing service to underserved areas, which are defined in the bill and by NCUA regulations, helps all credit unions fulfill their mandate to serve persons of small means. It is integral to the spirit of the credit union movement.
>
> By including explicit language authorizing multiple group credit unions to include underserved areas in their field of membership, we are not in any way restricting the ability of the National Credit Union Administration to allow community and single group credit unions to include underserved areas in their fields of membership.
>
> Precluding community credit unions from serving underserved areas would be contrary to their reason for existence.

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[11] http://www.ncua.gov/news/press_releases/2007/MA07-0621-2.htm

> Similarly, precluding single group credit unions from serving underserved areas makes no sense and would only add paperwork and regulatory burden for both credit unions and the NCUA since virtually any single group credit union can apply to add an additional group to its field of membership, thus becoming a multiple group credit union. Single group credit unions are a subset of multiple group credit unions and it was never intended, and would make no sense, for multiple group credit unions to have this authority, and for single group credit unions not to have similar authority.[12]

The language in CUMAA related to underserved areas was included to codify and encourage use of an existing (1994) NCUA policy permitting federal credit unions "of any type" to include low-income groups within their field of membership as part of the credit unions' broader mission "to ensure that adequate credit union services are provided to all persons in the community."

Despite the clarification included in the Congressional deliberation, the ABA sued NCUA in 2005 for authorizing single sponsor and community chartered credit unions to add underserved areas to their field of membership. <u>Within days of a November 2005 hearing before the House Ways and Means Committee during which the ABA complained that credit unions do not do enough to serve people of modest means, the same group took credit unions to court to prevent them from doing so.</u>

In June 2006, as the result of the ABA lawsuit, the NCUA was forced to revise its field of membership regulations to limit the addition of financially underserved areas only to credit unions with multiple common-bond charters. The action effectively prohibits more than half of federal credit unions from extending credit union services to lower-income areas and groups that are not adequately served by other traditional financial institutions.

Mr. Chairman, as you know, these areas are called "underserved" with good reason. <u>Banks make a business decision not to operate in or provide services to underserved areas. Credit unions seek to serve the underserved. It is not just part of our Congressionally-mandated mission. It is part of our core mission.</u>

My credit union added, and opened a branch in, an underserved area in Immokalee, Florida in March 2002 -- nearly six years ago. The median income in this county is $24,315. We currently have 6,652 members, $24.6 million in deposits, $62.8 million in loans from this area. This has been a successful branch for our members. We are providing quality financial services to an area that otherwise would not have it.

Those living in underserved areas lack access to mainstream financial services. For millions of lower income families, this means their only financial services alternative is to use the high cost financial products provided by check cashers, payday lenders, finance companies and pawn shops.

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[12] United States House of Representatives. Consideration of H.R. 1151, the Credit Union Membership Access Act. 105th Congress. August 4, 1998. H7044.

In some areas, the dearth of mainstream financial service has led to violence against shop owners. When criminals know that small business owners cannot make deposits at a bank or credit union on a regular basis, they prey on those business owners.

The mountain community of Idaho City, Idaho, has been seeking a financial institution for several years after the only bank closed its branch because it was not profitable. The Idaho Credit Union League met with community leaders in Idaho City and identified a credit union – Les Bois Federal Credit Union -- willing to locate a branch there. The credit union put together a business plan and was ready to open there. The only thing that stood in their way was approval by NCUA. Les Bois FCU is a community chartered credit union. Because of the ABA lawsuit against NCUA, and the subsequent forced moratorium on underserved area expansions for community chartered credit unions, Les Bois FCU was not permitted to open a branch and serve these unbanked people.

Store owners in Idaho City have no place to deposit their daily receipts. The owner of Trudy's Restaurant must keep hers in a safe at her home. The law enforcement in this part of Idaho consists of a small county sheriff's department that covers a very large county. Trudy has been robbed five times since the bank closed. She is in the unenviable situation of having to risk her life to simply operate a small business in a mountain community. Because of the bankers' unwillingness to operate in her community, and their trade group's litigation to prevent credit unions from operating in areas like this, she risks her life and her business every time she closes her shop. Congress can and should fix this.

When NCUA was approving underserved area expansions, credit unions responded to the need for service. Between 2001 and 2006, 220 single-group and community charter credit unions received approval from NCUA to serve individuals and businesses in more than 800 areas. A survey of these credit unions conducted by CUNA in March 2006 estimated that 1.6 million members had been served in these underserved areas at a total investment to the credit unions of $1.3 billion. There are an estimated 315 credit union branch offices within underserved areas, and additional 153 branches located near these areas. Additionally, 142 shared service centers reside within or near underserved areas. As of year-end 2005, credit union members residing in underserved areas had an estimated $4 billion in outstanding loans and $3.4 billion in savings deposits with their credit unions.

Mr. Chairman, it is unfortunate that credit unions must come to Congress to ask for this clarification because we believe that we are asking Congress to enact provisions which were thought by the Congressional architects of H.R. 1151 to have been enacted ten years ago. We believe Congress authorized all federally chartered credit unions to serve underserved areas in 1998. This is what many credit unions would like to do. This is what many Americans need in order to have mainstream financial services.

Other Legislative Changes

Mr. Chairman, H.R. 1537 also contains several additional changes to the Federal Credit Union Act, many of which have been passed by the House of Representatives on at least one occasion. These provisions were also subject of hearings before the House Financial Services Committee on March 27, 2003, July 20, 2004, May 19, 2005, June 9, 2005, September 22, 2005, and October 18, 2005. In lieu of additional discussion today, I have included a summary of all the CURIA provisions at the end of this written testimony.

Credit unions also support language included in H.R. 5519 that would permit federally chartered credit unions to offer payday lending alternative services to persons within their field of membership. This provision is modeled after a similar provision permitting federal credit unions to offer remittance and check cashing services to person within their field of membership, enacted into law as part of the Financial Services Regulatory Relief Act of 2006 (PL 109-351).

Conclusion

Mr. Chairman, thank you very much for the opportunity to discuss these critically needed regulatory improvements for credit unions. I am happy to answer any questions you or the Members of the Committee may have.

Section-by-Section Summary of H.R. 1537
The Credit Union Regulatory Improvements Act

Title I: Capital Reform

Section 101. Amendments to Net Worth Categories

The Federal Credit Union Act presently specifies the amount of capital credit unions must hold in order to protect their safety and soundness and the solvency of the National Credit Union Share Insurance Fund ("Insurance Fund"). Many experts, however, have noted that this capital allocation system is inefficient and does not appropriately account for risk. Section 101 incorporates recent recommendations of the National Credit Union Administration (NCUA) to provide a two-tier capital and Prompt Corrective Action (PCA) system for federally insured credit unions involving complementary leverage and risk-based minimum capital requirements. Under the proposed system, a well capitalized credit union must maintain a leverage net worth ratio of 5.25% and a minimum risk-based ratio of 10%. This exceeds the 5% capital requirement for FDIC-insured banks, even more so when a credit unions capital deposit in the insurance fund is added.

Section 102. Amendments Relating to Risk-Based Net Worth Categories

Currently, only federally insured credit unions that are considered "complex" must meet a risk-based net worth requirement under the Federal Credit Union Act. Section 102 would instead require all credit unions to meet a risk-based net worth requirement, and it directs the Board to take into account comparable risk standards for FDIC-insured institutions when designing the risk-based requirements appropriate to credit unions.

Section 103. Treatment Based on Other Criteria

Section 103 would permit the NCUA Board to delegate to regional directors the authority to lower by one level a credit union's net worth category for reasons related to interest-rate risk not captured in the risk-based ratios, with any regional action subject to Board review.

Section 104. Definitions Related to Net Worth

Net worth, for purposes of prompt corrective action, is currently defined as a credit union's retained earnings balance under generally accepted accounting principles. Section 104 would make three important revisions to this definition. First, it clarifies that credit union net worth ratios must be calculated without a credit union's capital deposit with the Insurance Fund. Second, it provides a new definition for "risk-based net worth ratio" as the ratio of the net worth of the credit union to the risk assets of the credit union. Third, it would permit the NCUA to impose additional limitations on the secondary capital accounts used to determine net worth for low-income credit unions where necessary to address safety and soundness concerns.

Section 105. Amendments Relating to Net Worth Restoration Plans

Section 105 would provide the NCUA Board with authority to waive temporarily the requirement to implement a net worth restoration plan for a credit union that becomes undercapitalized due to disruption of its operations by a natural disaster or a terrorist act. It would further permit the Board to require any credit union that is no longer well capitalized to implement a net worth restoration plan if it determines the loss of capital is due to safety and soundness concerns and those concerns remain unresolved by the credit union.

This section would also modify the required actions of the Board in the case of critically undercapitalized credit unions in several ways. First, it would authorize the Board to issue an order to a critically undercapitalized credit union. Second, the timing of the period before appointment of a liquidating agent could be shortened. Third, the section would clarify the coordination requirement with state officials in the case of state-chartered credit unions.

Title II: Economic Growth

Section 201. Limits on Member Business Loans

Section 201 would increase the current arbitrary asset limit on credit union member business loans from the lesser of 1.75 times actual net worth or 1.75 percent times net worth for a well-capitalized credit union (12.25% of total assets) to a flat limit of 20% of the total assets of a credit union. This update would facilitate added member business lending without jeopardizing safety and soundness at participating credit unions, as the 20% cap would still be equal to or stricter than business lending caps imposed on other depository institutions.

Section 202. Definition of Member Business Loans

Section 202 would give NCUA the authority to exclude loans of $100,000 or less as *de minimus,* rather than the current $50,000 exclusion, from calculation of the 20% cap on member business loans. This change would thus facilitate the ability of credit unions to make additional loans and encourage them to make very small business loans. It also builds upon the findings in a 2001 study by the Treasury Department that found that "...credit union member business loans share many characteristics of consumer loans" and that "...these loans are generally smaller and fully collateralized, and borrower risk profiles are more easily determined."[13]

Section 203. Restrictions on Member Business Loans

Section 203 would modify language in the Federal Credit Union Act that currently prohibits a credit union from making any new member business loans if its net worth falls below 6 percent. This change would permit the NCUA to determine if such a policy is appropriate and to oversee all member business loans granted by an undercapitalized institution.

Section 204. Member business loan exclusion for loans to non-profit religious organizations

To facilitate the ability of credit unions to support the community development activities of non-profit religious institutions, Section 204 would exclude loans or loan participations by federal credit unions to non-profit religious organizations from the member business loan limits contained in the Federal Credit Union Act.

Section 205. Credit unions authorized to lease space in buildings in underserved areas

In order to enhance the ability of credit unions to assist underserved communities with their economic revitalization efforts, Section 205 would allow a federal credit union to lease space in a building or on property on which it maintains a physical presence in an underserved area to other parties on a more permanent basis. It would also permit a federal credit union to

[13] United States Department of Treasury. 36.

acquire, construct, or refurbish a building in an underserved community, then lease out excess space in that building.

Section 206. Amendments relating to credit union service to underserved areas

Section 206 would revise a provision of the 1998 Credit Union Membership Access Act that has been incorrectly interpreted as permitting only federal credit unions with multiple common bond charters to expand services to individuals and groups living or working in areas of high unemployment and below median incomes that typically are underserved by other depository institutions. The change would reestablish prior NCUA policy of permitting all federal credit unions, regardless of charter type, to expand services to eligible communities that the Treasury Department determines meet income, unemployment and other distress criteria.

Section 207. Underserved areas defined

Section 207 would expand the criteria for determining whether a community or rural area qualifies as an underserved area. The definition of a qualified underserved area includes not only areas currently eligible as "investment areas" under the Treasury Department's Community Development Financial Institutions (CDFI) program, but also census tracts qualifying as "low income areas" under the New Markets Tax Credit targeting formula adopted by Congress in 2000.

Title III: Regulatory Modernization

Section 301. Investments in securities by federal credit unions

The Federal Credit Union Act presently limits the investment authority of federal credit unions to loans, government securities, deposits in other financial institutions, and certain other limited investments. Section 301 would provide additional investment authority to allow credit unions to purchase for the federal credit union's own account certain investment grade securities such as highly rated commercial paper, and asset-backed securities. The total amount of the investment securities of any one obligor or maker could not exceed 10% of the credit union's net worth and total investments could not exceed 10% of total assets.

Section 302. Authority of NCUA to establish longer maturities for certain credit union loans

The Federal Credit Union Act was amended in 2006 to allow the NCUA Board to increase the 12-year maturity limit on non-real estate secured loans to 15 years. Section 302 would further provide the Board with additional flexibility to issue regulations providing for loan terms exceeding 15 years for specific types of loans as NCUA considers appropriate (such as for educational loans).

Section 303. Increase in 1 percent investment limit in credit union service organizations

The Federal Credit Union Act authorizes federal credit unions to invest in organizations providing services to credit unions and credit union members. Currently, an individual federal credit union may invest in aggregate no more than 1% of its unimpaired capital and surplus in these organizations, commonly known as credit union service organizations (CUSOs). A federal credit union is also limited in the amount it may loan to all CUSOs to 1% of unimpaired capital and surplus. Section 303 would increase to 2% the amount a federal credit union may invest in all CUSOs and to 2% that it may lend to CUSOs. NCUA would have authority to reduce these limits for any individual federal credit union because of safety and soundness concerns.

Section 304. Voluntary mergers involving multiple common-bond credit unions

NCUA has identified ambiguous language in the 1998 Credit Union Membership Access Act as creating uncertainty for certain voluntary credit union mergers by suggesting that groups of more than 3,000 members be required to start a new credit union rather than be incorporated as a new group within a multiple common-bond credit union. Section 304 would clarify that this numerical limitation would not apply to bar groups of more than 3,000 members that are transferred between two existing credit unions as part of a voluntary merger.

Section 305. Conversions involving certain credit unions to a community charter

In cases when a single or multiple common-bond federal credit union converts to a community credit union charter, there may be groups within the credit union's existing membership that are located outside the new community charter's geographic boundaries, but which desire to remain part of the credit union and can be adequately served by the credit union. Section 305 would require NCUA to establish the criteria whereby it may determine that a member group or other portion of a credit union's existing membership, located outside of the community, can be satisfactorily served and remain within the credit union's field of membership with the new members of group added.

Section 306. Credit union governance

Section 306 would provide federal credit union boards the flexibility to expel a member, based on just cause, who is disruptive to the operations of the credit union, including harassing personnel and creating safety concerns, without the need for a two-thirds vote of the membership present at a special meeting as required by current law. The section would also permit a federal credit union board to limit the length of service of their directors to ensure broader representation from the membership.

Section 307. Providing the National Credit Union Administration with greater flexibility in responding to market conditions

Currently, the NCUA Board may raise the usury interest rate ceiling on loans by federal credit unions above 15% whenever it determines that money market rates have increased over the preceding six-month period and prevailing interest rates threaten the safety and soundness of individual credit unions. Section 307 would give the Board greater flexibility to make such determinations based either on sustained increases in money market interest rates or prevailing market interest rate levels. The change would allow NCUA to address an on-going high interest rate environment.

Section 308. Credit union conversion voting requirements

Section 308 includes several changes to current law pertaining to credit union conversions to mutual thrift institutions. It would increase the minimum member participation requirement in any vote to approve a conversion to 30% of the credit union's membership. It would require the board of directors of a credit union considering conversion to hold a general membership meeting one month prior to sending out any notices about a conversion vote that contain a voting ballot. It would also prohibit use of raffles, contest, or any other promotions to encourage member voting in a conversion vote.

Section 309. Exemption from pre-merger notification requirement of the Clayton Act

Section 309 would give federally insured credit unions the same exemption that banks and thrift institutions already have from pre-merger notification requirements and fees for purposes of antitrust review by the Federal Trade Commission under the Clayton Act.

STATEMENT

OF

JOANN JOHNSON, CHAIRMAN
NATIONAL CREDIT UNION ADMINISTRATION

ON

"THE NEED FOR CREDIT UNION REGULATORY RELIEF"

BEFORE THE

HOUSE FINANCIAL SERVICES COMMITTEE

MARCH 6, 2008

The National Credit Union Administration (NCUA or Board) appreciates this opportunity to comment on several legislative proposals to provide regulatory relief for credit unions. H.R. 1537, the Credit Union Regulatory Improvements Act (CURIA), H.R. 1849, the Credit Union Small Business Lending Act, H.R. 3113, the Affordable Financial Services Enforcement Act, and H.R. 5519, the Credit Union Regulatory Relief Act of 2008, enhance the ability of NCUA to regulate, supervise and insure the credit union industry, incorporate a variety of improvements to the statutory regime currently in place, and provide significant benefits to consumers. NCUA supports these legislative proposals within a framework that allows for important regulatory controls.

Of particular interest to NCUA are the provisions that:

- Reform the system of Prompt Corrective Action (PCA) and establish a risk-based capital regime; and
- Clarify the ability of NCUA to allow all types of federal credit unions to adopt underserved areas.

Viewed in their totality, these legislative proposals present Congress with an opportunity to prudently modernize a variety of elements of the Federal Credit Union Act (the Act) by enhancing regulatory and supervisory oversight capabilities of the NCUA and improving the public benefits of credit unions.

NCUA's primary missions are to ensure both safety and soundness and compliance with applicable federal regulations for federally insured credit unions. It performs these important public function by examining all federally chartered credit unions (FCUs), participating in the supervision of federally insured state-chartered credit unions in coordination with state regulators, and insuring credit union member accounts. In its statutory role as the administrator for the National Credit Union Share Insurance Fund (NCUSIF), NCUA provides oversight and supervision to 8101 federally insured credit unions (as of 12/31/07), representing 98 percent of all credit unions and approximately 87 million members.[1]

The NCUA regulates and insures all FCUs and insures most state-chartered credit unions. Under this framework, NCUA is responsible for enforcing regulations in FCUs and for evaluating safety and soundness in all federally insured credit unions. NCUA is responsible for monitoring and enforcing compliance with most federal consumer laws and regulations in FCUs. In state-chartered credit unions, the appropriate state supervisory authority has regulatory oversight and enforces state consumer laws and regulations.

[1] Approximately 170 state-chartered credit unions are privately insured and are not subject to NCUA oversight.

NCUA's testimony will address each provision in the legislative proposals.

Section by Section Review of H.R. 1537 -- Credit Union Regulatory Improvements Act of 2007

Title I Capital Modernization

Prompt Corrective Action Reform and Establishment of a Risk-Based Capital Regime

In June 2007, the Board formally introduced a revised plan to enhance and modernize the system of PCA for credit unions, including significant proposed improvements to the risk-based capital system. The revised proposal reflects direct input by the Department of the Treasury and incorporates developments that have occurred with the adoption of new capital standards related to BASEL II for FDIC-insured institutions. However, it is important to note that while the Board action establishes a public record about the rationale and basis for the proposed changes, modification to the Act is necessary to authorize NCUA to adopt the changes.

NCUA is a strong advocate for reform of the PCA system for credit unions because the current statutory PCA requirements are too rigid and not tailored to each credit union's individual risk profile in order to strengthen its safety and soundness. The current system's rigidity and limited risk orientation:

- create inequities for credit unions with low-risk balance sheets;
- limit NCUA's ability to have a more relevant risk-based requirement without requiring unduly high capital levels; and
- foster accumulation of capital levels in excess of what is needed for most credit unions' safety and soundness and strategic needs.

The proposed PCA reforms result in a more fully risk-based system and are consistent with sound risk management principles. The shift in emphasis to the risk-based requirement will promote more active management of risk in relation to capital levels. It will also reduce any competitive disadvantage to credit unions of being held to an unwarranted higher capital standard than other federally insured institutions. As the federal bank and thrift regulators are in the process of modernizing capital standards under which their regulated institutions operate, it becomes even more important that capital standards for credit unions be updated. From both an industry competition and risk management perspective, it is important for the capital standards for credit unions to remain comparable and incorporate the improvements in approaches to measuring risk and allocating capital.

The new system of PCA would also provide credit unions with greater ability to manage compliance through adjustments to their assets and activities. If credit unions had more flexibility to manage their compliance with PCA, they could still maintain an appropriate protective cushion above regulatory requirements while safely returning more earnings to the members and/or expanding member services and other outreach programs.

Table 1 below compares the proposed PCA system for credit unions to that applied by federal banking regulators:

Table 1 - Proposed PCA Thresholds for Credit Unions Compared to Bank PCA Thresholds

	Credit Unions		FDIC Insured**		
PCA Category	**Leverage Ratio**	**Risk-Based Ratio**	**Tier 1 Capital to Total Assets (Leverage)**	**Tier 1 Capital to Risk Assets**	**Total Capital to Risk Assets**
Well Capitalized	5.25% or greater	10% or greater	5% or greater	6% or greater	10% or greater
Adequately Capitalized	4.25% to < 5.25%	8% to < 10%	4% to < 5% > 3% for CAMEL 1	4% to < 5%	8% to < 10%
Undercapitalized	3.25% to < 4.25%	6% to < 8%	3% to < 4% or < 3% for CAMEL 1	3% to < 4%	6% to < 8%
Significantly Undercapitalized	2% to < 3.25%	< 6%	2% to < 3%	< 3%	< 6%
Critically Undercapitalized	< 2%	NA	< 2% (tangible equity)	NA	NA

** Source: FDIC Rules and Regulations, 12 C.F.R §325.103

As illustrated in Table 2 below (Column B), the proposed leverage ratio retains the original capital requirement for "significantly undercapitalized" while raising the capital requirement for "critically undercapitalized." For the remaining categories, the actual reduction from the old to the new leverage ratio requirement is considerably less than the *prima facie* 175 basis point change in the threshold. This is due to the impact of the change in the method of calculating the net worth ratio that subtracts the NCUSIF deposit from both net worth and total assets (see Appendix 3). As Column C of Table 2 shows, the required average net worth level would only decline by 104 basis points in the top three PCA categories. The new calculation method will actually require 74 basis points more in net worth in the "critically undercapitalized" category than the existing requirement.[2]

[2] The amount of change in a credit union's leverage ratio between the current and proposed calculations is dependent upon the level of insured shares. The new calculation would result in the same leverage ratio threshold if a credit union had no insured shares. The largest reduction from the current leverage ratio to the calculated leverage ratio would occur when a credit union has all insured shares. Under the proposed calculation, over 92 percent of credit unions would

Table 2 - Current vs. Proposed Leverage Ratio Standard

PCA Category	Column A Current Requirement Net Worth / Total Assets	Column B Proposed Requirement (Net Worth – NCUSIF) / (Total Assets – NCUSIF)	Column C Net Worth Required by Column B to Total Assets [Range]
Well Capitalized	> 7%	> 5.25%	5.96%*
Adequately Capitalized	< 7%	< 5.25%	5.96%*
Undercapitalized	< 6%	< 4.25%	4.96%* [
Significantly Undercapitalized	< 4%	< 3.25%	3.97%*
Critically Undercapitalized	< 2%	< 2%	2.74%*

* Calculation based upon the average insured share to asset ratio of 75%.

NCUA supports the sections of H.R. 1537 that enhance the operational efficiency of the system of PCA for credit unions. Section 103 would allow the Board to delegate, subject to review, its authority to reclassify a credit union to a lower net worth category on safety and soundness grounds to address interest rate risk. Section 105 would give the Board additional flexibility to impose PCA in several ways:

- Allowing a temporary waiver of the requirement to file a Net Worth Restoration Plan (NWRP) in the event of a natural or man-made disaster;
- Authorizing the Board, in lieu of the present earnings retention requirement, to require a credit union that became less than "well capitalized" for safety and soundness reasons to file an NWRP if those reasons remain unresolved;
- Giving the Board discretion to order a "critically undercapitalized" credit union to take specific "other corrective action" to achieve the purposes of PCA; and
- Requiring the Board to allow a State Supervisory Authority to impose PCA on a state-chartered credit union *only when* the Board determines that "such action by the official will carry out the purpose of [PCA]."

To implement this last modification, section 105(e) requires a technical correction. To indicate where the quoted language should be inserted section 216(l)(3)(A)(ii) of the Act, the phrase "after the words 'proposed action.'" should be added to section 105(e) on page 9 at the end of line 7.

realize a reduction in the leverage ratio from 50 basis points to 90 basis points with an average reduction of 75 basis points.

Title II -- Economic Growth

As with all federally-insured financial institutions, the general deterioration in the overall credit markets over the last 18 months has affected credit union assets. As a result, NCUA began sometime ago to focus significantly more attention to active supervision and monitoring of all types of credit union lending, with a special emphasis on risk management and due diligence responsibilities.

In response to the changing environment for credit union member business lending, NCUA has devoted additional resources, special expertise and the array of supervisory remedies and restrictions it already has to address problems such as excessive rate of growth, substandard underwriting standards and criteria, over-concentration in certain categories of loans, high loan-to-value ratios, poor documentation, inexperience with MBL standards, violation of loans-to-one-borrower limits, and insufficient net worth.[3] Enacting PCA reform as proposed in Title I would add a critical supervisory tool to those NCUA already relies upon to ensure safe and sound lending.

We are confident that most credit unions involved in member business lending will be able to adjust to a statutory increase in the individual and aggregate MBL caps. Regardless of the increased caps and additional exemptions, however, NCUA is poised to continue its vigilant and aggressive approach to regulating and supervising these activities.

Section 201 -- Limits on MBLs.

Section 201 would increase the current cap on Member Business Loans (MBLs). This will allow credit unions to accommodate the expansion in member demand for these loans that has taken place over the last 10 years. Without this increase, credit unions' ability to offer this product will be limited, and in some cases eliminated, forcing members to go elsewhere to meet their MBL needs. While acknowledging the benefit to credit unions of increased member business lending, NCUA stands ready to aggressively exercise the regulatory authority it already has to regulate this type of lending. This means that we will not hesitate to impose the supervisory remedies and restrictions necessary to prevent and address problems, such as those described above, that may accompany an expansion in member business lending.

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[3] For example, recent guidance in *Letter to Credit Unions CU-07-13* emphasizes the importance of credit unions themselves assuming the responsibility to conduct its due diligence evaluation of a lending activity, even when that activity is otherwise done through a third party vendor, to ensure that the credit union fully understands the structure, practices and financial condition of the third party.

Section 202 -- Definition of MBL.

Section 202 would amend the definition of "Member Business Loans" to increase the minimum balance of such loans to one member from $50,000 to $100,000. This increase will allow member business lending to keep pace with the increase in unit costs, due to inflation and other factors, of goods and services typically financed with such loans. Compared to 10 years ago, the 25 percent of credit unions that make MBLs (as of 12/31/07) has demonstrated on the whole the ability to manage that activity safely and soundly. As with increasing the credit union MBL cap, we appreciate the benefit not only to credit unions, but to their members, of expanding the minimum size of an MBL. At the same time, we stand ready to deploy the array of supervisory remedies and restrictions NCUA already has to address problems.

Section 203 -- Restriction on MBLs.

Section 203 would grant the Board authority to make exceptions to the freeze on MBLs that applies when a credit union becomes "undercapitalized" and remains in place until it returns to "adequately capitalized." Giving the Board this flexibility acknowledges that member business lending is not always the problem that causes a credit union to become "undercapitalized." In fact, allowing member business lending to *increase* may sometimes be part of the solution that returns a credit union to "adequately capitalized."

Section 204 -- MBL Exclusion for Loans to Non-Profit Religious Organizations.

Section 204 would exempt loans to non-profit religious organizations in any amount from a credit union's MBL cap. This exemption will enhance the availability of loans to religious organizations seeking to acquire or construct a house of worship. While these loans would be excluded from the MBL cap, they remain subject to our supervision to ensure their safety and soundness.

Section 205 -- CU Leasing of Space in its Office Buildings Located in Underserved Areas.

Section 205 would permit a credit union that is housed in a building it owns located in an underserved area to lease out space not used for credit union operations. This flexibility will allow credit unions to make productive use of space not used for credit union operations while at the same time stimulating the economy of the underserved area where the space is located. However, the implementation of this shift from current policy is subject to Board regulation.

Sections 206 and 207 -- Amendments Relating to CU Service to Underserved Areas.

Sections 206 and 207 would expressly permit all types of federally chartered credit unions to adopt "underserved areas." Currently, the Act permits only federal credit unions with *multiple* common bond charters to add underserved areas into their fields of membership (FOM); it is silent about *single-group* and *community* charters from doing so. NCUA is emphatic in supporting this statutory change because it fully implements longstanding Congressional intent to give consumers in economically disadvantaged areas greater access to credit union service.

In 1998 Congress passed the Credit Union Membership Access Act (CUMAA) in order to codify the authority of NCUA to charter multiple common-bond credit unions. Pub. L. 105-219, 112 Stat. 914 (1998). CUMAA specifically authorized certain federal credit unions to add geographically based "underserved areas" to their FOMs. The concept acknowledges that geographic areas exist in the United States that exhibit certain criteria, such as a declining population base or increasing rate of unemployment, that can result in diminished access by residents and businesses to financial products and services. However, the final language of CUMAA expressly authorized only multiple common-bond credit unions to serve persons or organizations within an area that was underserved. 12 U.S.C. 1759(c)(2). CUMAA also provided a definition of an "underserved area."

To reflect CUMAA, NCUA changed its FOM regulations to substitute the term "underserved area" and its definition for the then-existing language allowing all charter types to serve low-income communities and associations. Although the "underserved" designation is not strictly a function of income level of the residents, it is expected that over time broader demographic representation among the membership will occur in FCUs that have added underserved areas.

Through outreach efforts and otherwise, NCUA continued to conscientiously carry out the intent of Congress to maximize credit union service to underserved areas. This included continuing to allow *all three* charter types to adopt them--just as NCUA had been doing before CUMAA to maximize credit union service to low-income designated areas and associations. These efforts were brought to a halt by a banking industry lawsuit challenging the authority of single group and community charter credit unions to add underserved areas. As a result of the lawsuit, NCUA amended its FOM regulation in June 2006 to limit underserved area expansions only to federally chartered credit unions serving multiple groups.

NCUA is convinced that CUMAA's omission of express authority for single-group and community credit union to serve underserved areas was an oversight. When CUMMA was enacted, Congress was duly focused on undoing the impact of the

Supreme Court's decision affecting multiple group charters.[4] As the legislative history indicates, Congress was nonetheless aware of NCUA's long-standing policy of allowing *all* federal charters to serve low-income communities and associations, which were the predecessors to underserved areas. Further, to our knowledge, no objection was made on the record to a provision in CUMAA that would have allowed *all* federal charters to adopt underserved areas. Sections 206 and 207, by extending to single-group and community charters the authority to add underserved areas, would finally correct this oversight.

In addition to maximizing credit union service to underserved, sections 206 and 207 of H.R. 1537 would achieve several other objectives without imposing additional service requirements. They would eliminate duplicative and superfluous regulatory requirements; refine the employment of census track data in making a determination about an underserved area; and codify the requirement that a branch or service facility must be established in the underserved area within two years.

Title III -- Regulatory Modernization

Section 301 -- Investments in Securities by FCUs.

Section 301 would authorize the Board, by regulation, to allow FCUs to invest in certain debt obligations (i.e., a bond, note, debenture or other non-equity "investment security")--provided they meet the statutory definition of "investment grade" securities--for their own accounts. The section imposes prudent limits of an aggregate maximum of 10% of total assets and a single obligor limit of 10% of net worth. With these constraints and further regulatory limitations set by the Board, the authority to add these types of investments provides FCUs with a safe means of further diversifying their investment portfolios. A technical correction is needed to implement this new authority. Section 301 must be amended to conform to the long-standing format of current section 107 of the Act. The present lack of conformity makes it impossible to determine where in section 107 this new authority is supposed to be located.

Section 302 -- NCUA Authority to Establish Longer Term Maturities for CU Loans.

Section 302 would give the Board the authority, by regulation, to make exceptions to the present 15-year maximum maturity on loans. This will give the Board the flexibility to allow maturities in excess of 15 years when necessary to ensure parity with other financial institutions that are permitted to offer longer maturities (e.g., student loans). Without this flexibility, credit union members will

[4] NCUA v. First National Bank & Trust Co., 522 U.S. 479 (1998).

have no choice but to rely on these institutions instead of their credit unions when they need loans with terms of longer than 15 years.

Section 303 -- Increase in Lending and Investment Limits in CUSOs.

Section 303 would increase the ceiling on both credit union loans to Credit Union Service Organizations (CUSO), and credit union investments in them, from--in each category--1% to 2% of the credit union's paid-in and unimpaired capital and surplus, provided the Board also is authorized to reduce each ceiling on a case-by-case basis when appropriate to preserve a credit union's safety and soundness. Increasing the ceiling on credit union loans to, and investments in, CUSOs will enhance their capitalization, in turn expanding the availability of the resources necessary to perform services and activities that benefit credit unions and their members. This will especially benefit small credit unions by providing the opportunity to diversify their products and services within a safe and sound regulatory framework.

Section 304 -- Voluntary Mergers Involving Multiple Common Bond CUs.

Section 304 would add an exemption from the 3000-member limit on group additions for any group transferred to a multiple group credit union by a merger approved by the Board on or after August 7, 1998---the date CUMMA was signed into law. When a credit union converts to a community charter, it is unfair to exclude certain groups from its FOM based on their size when all groups regardless of size were previously admitted legally to its FOM.

Section 305 -- Conversions of Certain CUs to a Community Charter.

Section 305 would give the Board the authority, by regulation, to determine whether a credit union that converts to a community charter can continue to add new members from its former member groups located outside the well-defined local community. This will ensure that group members outside the community (especially those who became group members *after* the conversion) will be able to obtain credit union service after the credit union converts to a community charter (i.e., a "once a group, always a group" policy).

Section 306 -- Credit Union Governance

Section 306 authorizes credit unions, through a by-law amendment, to expand their authority to expel a member, by a majority vote of the board of directors, for just cause, including disruption of a credit union's operations or nonparticipation in its affairs. In addition, the provision authorized credit unions, through a by-law amendment, to limit the number of consecutive terms a person may serve on the board of directors. Permitting these by-law amendments promotes the orderly functioning of credit unions and is consistent with the existing governance provisions of the Act.

Section 307 -- Greater Flexibility for NCUA to Respond to Market Conditions.

Section 307 would expand the Board's authority to establish a temporary interest rate ceiling higher than 15% under *either* of two events--when money market interest rates rise over the preceding 6 months *or* when prevailing interest rate levels threaten the safety and soundness of individual credit unions--instead of both, as is presently required. Untying these two conditions improves the Board's flexibility to timely respond when an exception to the 15% rate ceiling will ensure that credit unions remain both safe and sound and competitive with other financial institutions.

Section 308 – Credit Union Conversion Voting Requirements.

NCUA supports requiring a minimum of 30% membership participation in a vote to convert to a bank in order for a majority vote of those who participate to approve the proposal. We further support requiring a credit union that proposes to convert to hold a Special Meeting of the membership at least 30 days prior to issuing members their ballots, and to give notice of the Special Meeting in the notices the credit union already is required to send to its members. Finally, we support a ban on offering a voting incentive to members in any form in connection with the membership vote on a conversion proposal. Given that converting to a bank is a shift in a credit union's fundamental structure, all three measures maximize membership representation, awareness, and freedom from undue influences when members faced with such a crucial proposal.

This section requires a technical correction. Section 308 refers to the parallel U.S. Code citation for section 205(b)(2) of the Act as "12 U.S.C. 1785(b)(2)(B)", when in fact subsection (B) at the end should be omitted.

Section 309 -- Exemption from Clayton Act Pre-Merger Notice Requirement.

Section 309 would amend the Clayton Antitrust Act to exclude voluntary credit union mergers from its pre-merger notification requirement. Under this requirement, merging credit unions must file data with the Federal Trade Commission, at considerable effort and expense, so that agency can assess the merger's impact on competition in the financial services market. Excluding credit unions from the Clayton Act would relieve them of the need to comply with these burdensome notification and filing requirements.

Section by Section Review of H.R. 1849 -- Credit Union Small Business Lending Act

H.R. 1849 would implement the Credit Union Small Business Lending Act. That statute would amend sections 107 and 107A of the Act, 12 U.S.C. 1757, 1757a, and section 7(a) of the Small Business Act, 15 U.S.C. 636(a), to improve small business lending and cooperation between NCUA and the Small Business Administration (SBA), as follows:

- Section 2 excludes from the Act's definition of MBL any loan made in cooperation with the SBA under section 7(a) of the Small Business Act;
- Section 3 directs the SBA to implement an outreach program to increase credit union participation in the SBA's section 7(a) loan program and to simplify the application process for credit unions;
- Section 4 directs SBA to provide up to an 85% guaranty for loans made by a credit union up to $250,000 to a member residing in an underserved area, or where the member's business that is receiving assistance is located in an underserved area;
- Section 5 clarifies that a federal credit union making a loan secured by the insurance, guarantee, or advance commitment to purchase by the federal government or a state government (or agency of either) may make the loan under the terms and conditions specified in the law *and applicable regulations* under which the insurance, guarantee, or commitment is provided.

This bill will enhance credit unions' ability to serve their members' small business loan needs in a safe and sound manner.

Finally, a remaining obstacle to credit union participation in the SBA's Certified Development Company (CDC)/504 loan program (CDC/504 program) warrants attention. That program is a long-term financing tool for economic development within a community. It provides businesses with long-term, fixed-rate financing for major fixed assets, such as land and buildings. CDCs, which are non-profit organizations, work with the SBA and private-sector lenders to provide financing to small businesses.

Typically, a 504 project includes a loan secured with a senior lien from a private-sector lender covering up to 50 percent of the project cost, a loan secured with a junior lien from the CDC (backed by a 100 percent SBA-guaranteed debenture) covering up to 40 percent of the cost, and a contribution of at least 10 percent equity from the small business being helped.

Credit unions already participate as private-sector lenders in the CDC/504 program. However, because the credit union's underlying 504 loans are not SBA-guaranteed, credit unions must count its 504 loans toward its aggregate cap on MBLs. This discourages, and in some cases precludes, a credit union from making this type of community development loan.

Review of H.R. 3113--
Affordable Financial Services Enhancement Act

H.R. 3113 would implement the Affordable Financial Services Enhancement Act. If enacted, that law would achieve the same purpose as section 206 of H.R. 1537-- extending to single-group and community charters the authority to add and serve underserved areas. H.R. 3113 would accomplish that by amending section 109(c)(2) of the Act, 12 U.S.C. 1759(c)(2), to exclude the "field of membership category" limitation--currently limited to multiple group charters--thus allowing all credit unions, regardless of charter type, to serve underserved areas.

Section by Section Review of H.R. 5519 --
Credit Union Regulatory Relief Act of 2008

Section 2 -- Investments in Securities by FCUs.

Same as section 301 of H.R. 1537 discussed above.

Section 3 -- Increase in Investment Limit in CUSOs.

Same as section 303 of H.R. 1537 discussed above, except that: (1) the ceiling on CU loans to, and investments in, CUSOs would each be raised to from 1 percent to 3 percent of paid-in and unimpaired capital and surplus (instead of to 2 percent); and (2) the Board would not be given the authority to reduce each ceiling on a case-by-case basis when appropriate to preserve a credit union's safety and soundness.

Section 4 -- MBL Exclusion for Loans to Non-Profit Religious Organizations.

Same as section 204 of H.R. 1537 discussed above.

Section 5 -- NCUA Authority to Establish Longer Maturities for Certain CU Loans.

Same as section 302 of H.R. 1537 discussed above, except that the Board's authority to make exceptions to the present 15-year maximum maturity on loans would be subject to any provision of the Act that provides otherwise.

Section 6 -- Providing NCUA With Greater Flexibility in Responding to Market Conditions.

Same as section 307 of H.R. 1537 discussed above.

Section 7 -- <u>Conversions Involving Certain CUs to Community Charter</u>.

Same as section 305 of H.R. 1537 discussed above, except for the omission of the clarifying phrase "permitting new members to be added to such groups" (page 17, lines 4-5, of H.R. 1537). NCUA is concerned that the absence of this phrase may be misinterpreted to mean that a credit union can serve only those group members who joined prior to its conversion to a community charter--a result no different than the Act's "once a member, always a member" policy already allows.

Section 8 -- <u>Credit Union Participation in the SBA Section 504 Program</u>.

Same as section 5 of H.R. 1849 discussed above.

Section 9 -- <u>Amendments Relating to CU Service to Underserved Areas</u>.

Section 9 departs significantly from section 206 of H.R. 1537 discussed above. Both section 206 and section 9(a) would exclude the "field of membership category" limitation--currently limited to multiple group charters--for service to underserved areas (as H.R. 3113 also would) and would impose a 2-year deadline for establishing a credit union office or facility within the underserved area. If that 2-year deadline were not met, section 9(a) also would mandate termination of the approval to serve the underserved area.

But section 9(a) then goes much further, imposing minimum net worth and underserved area reporting requirements:

- To serve an underserved area, a credit union must have a net worth classification of at least "adequately classified";
- Once a credit union is approved to serve an underserved area, it must annually report to NCUA the number of its underserved members and the number of offices and facilities it maintains in its underserved area(s);
- NCUA must annually publish a report listing the underserved area applications it has approved, the number and location of underserved areas it has taken into account in approving such applications, and the total number of all credit union members within underserved areas.

While NCUA agrees that it is critically important that credit unions make every reasonable effort to fully serve their entire FOM, including underserved areas, we must reserve judgment on the specific requirements of section 9(a), which were only recently received by NCUA, pending further analysis and consideration by the NCUA Board.

Section 9(b), which modifies the Act's present definition of "underserved area," is substantially similar to section 207 of H.R. 1537 and section 4 of H.R. 1849 (which amends the Small Business Act). Each provision retains the present "investment area" criterion, but replaces the present "underserved by other depository institutions" criterion with a "low income community" criterion derived from the Internal Revenue Code.

Section 10 -- Short-Term Payday Loan Alternatives Within the FOM.

Section 10 gives the Board, in addition to its existing authority to cash money transfer instruments, 12 U.S.C. 1757(12)(B), the authority, by regulation, to "provide short-term loans as an alternative to payday loans."

Section 11 -- Credit Union Governance.

Same as section 306 of H.R. 1537 discussed above.

Section 12 -- Encouraging Small Business Development in Underserved Urban and Rural Communities.

Section 12 affects section 2 of H.R. 1849, which would exclude from the Act's MBL definition any SBA section 7(a) loan. Instead, section 12 excludes from the MBL definition a commercial, corporate, business, farm or agricultural loan to a member provided any of the following conditions is met: the member either resides or does business within an underserved area; the loan is secured by real property located within such underserved area; or the loan will be used to operate a business located within such underserved area.

Comparing the difference in scope between the two sections, section 12 excludes more than just SBA loans, but all the loans it excludes must be tied to an underserved area. Section 2 of H.R. 1849, in contrast, excludes only one category of loans--SBA section 7(a) loans--but they are excluded without regard to an underserved area. NCUA is concerned that section 12, as currently written, would unnecessarily sacrifice the exclusion for Government-guaranteed section 7(a) loans.

Section 13 -- Exemption from Pre-Merger Notification Requirement of Clayton Act.

Same as section 309 of H.R. 1537 discussed above.

Conclusion

NCUA has reviewed the various legislative proposals in the 110th Congress that address the issue of regulatory relief for credit unions. These proposals contain provisions that represent significant and positive improvements to NCUA's ability to regulate and supervise credit unions, and to carry out Congressional intent as expressed in the Federal Credit Union Act.

In particular, NCUA supports those provisions that grant greater flexibility to NCUA in the regulation of the capital structure of federally insured credit unions while at the same time allowing those credit unions to more accurately assess balance sheet risk. NCUA also supports legislation restoring the ability of credit unions to extend membership in underserved areas, in concert with longstanding Congressional interest in credit unions having a responsibility to provide financial services to consumers of modest means. NCUA supports legislation that modernizes a wide variety of credit union investment and lending options within regulatory framework that enables NCUA to perform the necessary supervision to preserve credit union safety and soundness.

NCUA appreciates this opportunity to present our views to Congress, and stands ready to answer questions regarding its perspective on these beneficial and forward looking legislative proposals.

NAFCU

Testimony of

Michael Lussier
President/CEO of Webster First Federal Credit Union

on Behalf of

The National Association of Federal Credit Unions

The Need for Credit Union Regulatory Relief and Improvements

Before the

House Financial Services Committee

United States House of Representatives

March 6, 2008

Introduction

Good morning, Chairman Frank, Ranking Member Bachus and Members of the Committee. My name is Mike Lussier and I am testifying today on behalf of the National Association of Federal Credit Unions (NAFCU). I serve as the President/CEO of Webster First Federal Credit Union, headquartered in Webster, Massachusetts. I first became President/CEO of Webster First FCU in 1990 at the age of 29 and have served in this role since then. Webster First FCU is a community credit union with approximately 32,000 members and more than $430 million in assets. Originally, Webster First FCU was founded as a Polish-ethnic credit union on January 14, 1928. We changed to a community credit union in 1956 and became a federally-chartered credit union in 1995.

In addition, I also serve as the chairman of the Political Action Committee and treasurer of the Board of Directors for the National Association of Federal Credit Unions. I am a past member of the Small Business Loan Review Board, past Director for the Credit Union League of Massachusetts Insurance Agency and past Chairman of the Massachusetts Share Insurance Corporation.

I am also the Building Committee chairman and a board member of the regional American Red Cross, and I volunteer with numerous charitable organizations such as the Webster/Dudley Rotary Club. I earned my Bachelor of Business Administration, majoring in Accounting from Bentley College and my Masters of Finance from Nichols College.

NAFCU is the only national organization exclusively representing the interests of the nation's federally chartered credit unions. NAFCU is comprised of nearly 800 federal credit unions—member-owned financial institutions across the nation—representing approximately 30 million individual credit union members. NAFCU–member credit unions collectively account for approximately 40 percent of the assets of all federally insured credit unions. NAFCU and the entire credit union community appreciate the opportunity to participate in this discussion regarding regulatory relief for America's credit unions.

Historically, credit unions have served a unique function in the delivery of necessary financial services to Americans. Established by an act of Congress in 1934, the federal credit union system was created and has been recognized as a way to promote thrift and to make financial services available to all Americans, many of whom would otherwise have limited access to financial services. Congress established credit unions as an alternative to banks and to meet a precise public need—a niche that credit unions fill today for over 90 million Americans. Every credit union is a cooperative institution organized "for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes." (12 USC 1752(1)). While nearly 75 years have passed since the *Federal Credit Union Act* (FCUA) was signed into law, two fundamental principles regarding the operation of credit unions remain every bit as important today as in 1934:

- credit unions remain totally committed to providing their members with efficient, low-cost, personal service; and,
- credit unions continue to emphasize traditional cooperative values such as democracy and volunteerism.

Credit unions are not banks. The nation's approximately 8,100 federally insured credit unions serve a different purpose and have a fundamentally different structure than banks. Credit unions exist solely for the purpose of providing financial services to their members, while banks aim to make a profit for a limited number of shareholders. As owners of cooperative financial institutions united by a common bond, all credit union members have an equal say in the operation of their credit union—"one member, one vote"—regardless of the dollar amount they have on account. These singular rights extend all the way from making basic operating decisions to electing the board of directors—something unheard of among for-profit, stock-owned banks. Unlike their counterparts at banks and thrifts, federal credit union directors generally serve without remuneration—a fact epitomizing the true "volunteer spirit" permeating the credit union community.

Credit unions have an unparalleled safety and soundness record. Credit unions—unlike banks and thrifts—have never cost the American taxpayer a single dime. Unlike the Federal Deposit Insurance Corporation (FDIC) and the Federal Savings and Loan Insurance Corporation (FSLIC), which were both started with seed money from the United States Treasury, every dollar that has ever gone into the National Credit Union Share Insurance Fund (NCUSIF) has come from the credit unions it insures. Furthermore, unlike the thrift insurance fund that unfortunately cost American taxpayers hundreds of billions of dollars, credit unions have never needed a federal bailout.

Although not the subject of this hearing, I would like to address some common misconceptions and criticisms of the credit union industry. In the past, some have stated that credit unions have changed over the years and today are really no different than banks, which pay corporate income tax. The reality is that the defining characteristics of credit unions remain unchanged. Credit unions are not-for-profit cooperatives that serve defined fields of membership, generally have volunteer boards of directors and cannot issue capital stock. They are restricted in where they can invest their members' deposits and are subject to stringent capital requirements and a cap on business lending. A key difference between banks and credit unions is that when a credit union generates earnings, it distributes those earnings to its members in the form of lower fees, higher dividends, better rates or more services, or it increases its net worth which increases the stability of the organization. When a banker claims that credit unions have it so well and do not need regulatory relief, ask them why there has only been one bank that has ever converted to a credit union.

Credit unions have grown steadily in membership and assets, but in relative terms, they are still quite small compared with banks. Federally insured credit unions have approximately $753 billion in assets as of year-end 2007. By contrast, FDIC-insured institutions held $12 trillion in assets and last year these institutions grew by an amount that exceeds the total assets of credit unions. The average size of a federal credit union is $81.7 million compared with $1.4779 billion for banks. Over 3,600 credit unions have less than $10 million in assets. The credit union share of total household financial assets is also relatively small, just 1.1 percent as of September 2007.

Furthermore, size has no bearing on a credit union's structure or adherence to the credit union philosophy of service to members and the community. While credit unions have grown, their relative size is still small compared with banks. Even the world's largest credit union, with $33 billion in assets, is dwarfed by the nation's biggest banks with hundreds of billions in assets. (JP Morgan Chase has over $1.3 trillion in assets.)

America's credit unions have always remained true to their original mission of "promoting thrift" and providing "a source of credit for provident or productive purposes." In fact, Congress acknowledged this point when it adopted the *Credit Union Membership Access Act* (CUMAA – P.L. 105-219). In the "findings" section of that law, Congress declared that, "The American credit union movement began as a cooperative effort to serve the productive and provident credit needs of individuals of modest means … [and it] continue[s] to fulfill this public purpose."

Credit unions continue to play a very important role in the lives of millions of Americans from all walks of life. As consolidation of the commercial banking sector has progressed with the resulting depersonalization in the delivery of financial services by banks, the emphasis in consumers' minds has begun to shift not only to services provided but also—and in many cases more importantly—to quality and cost. Credit unions are second to none in providing their members with quality personal service at the lowest possible cost. According to the 2005 American Banker/Gallup Consumer Survey, credit unions had the highest rated service quality of all covered financial institutions. This has held true each year since the survey was initiated.

Furthermore, while many banks and thrifts have helped to create the recent subprime mortgage debacle by placing many into predatory subprime mortgage loans, data collected under the *Home Mortgage Disclosure Act* illustrates that credit unions are not part of the problem. The difference between credit unions and banks is highlighted when one examines the 2006 HMDA data for loans to minority applicants with household incomes under $40,000. According to the 2006 HMDA data, banks charged at least 3 percent higher than the comparable Treasury yield on 34.2 percent of loans made to minority applicants with household income under $40,000. Credit unions, on the other hand, were only outside of the yield spread on 4.7 percent of their loans. This clear distinction is proof that credit unions are less likely to put minority applicants into subprime loans than banks are. Credit unions applaud these numbers as a reflection of the responsible lending practices that credit unions are engaging in, by not putting consumers in to unaffordable loans.

Looking Beyond CUMAA to Today

Credit unions have been the target of criticism by some in the banking industry for decades, and the criticisms that the bankers are lodging are nothing new. The Supreme Court's decision in 1998 in the AT&T Family Federal Credit Union field of membership case, followed by Congress' prompt passage of the *Credit Union Membership Access Act* (CUMAA) in the summer of 1998, brought the issue to a head. The fact of the matter is that when CUMAA was signed into law it overturned in eight short months a decision that had encompassed eight years of costly litigation initiated by the banks.

CUMAA was a necessary piece of legislation for credit unions at the time of its enactment because it codified a number of fundamental credit union concepts embraced by both federal and state-chartered credit unions. In addition to the previously mentioned "findings" section, these include:

- the multiple-group policy that the National Credit Union Administration (NCUA) had initiated in 1984;
- the "once a member, always a member" principle followed by virtually every credit union in the country; and

- the "family member" concept followed by many credit unions.

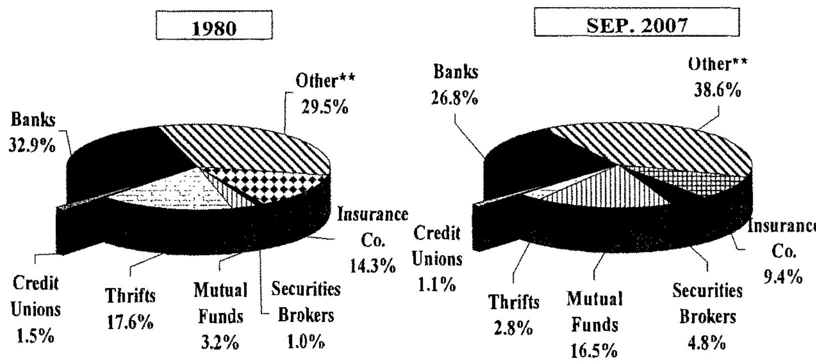
Yet CUMAA came with some provisions that were not widely supported by the credit union community. These include:

- limitations on member business loans;
- imposition of a bank-like prompt corrective action or "PCA" requirement that, given the structure of credit unions, serves in many respects as an overly restrictive constraint on growth; and
- various artificial and arbitrary limitations on growth.

It has been 10 years since the passage of CUMAA, the last major credit union legislation addressed by Congress. In that time, NAFCU and our member credit unions have recognized that there are aspects of that legislation that have worked, and some that have not, and need to be revisited. We are pleased that the NCUA and over 145 members of Congress have recognized the need for additional credit union legislation.

NAFCU is pleased to report to the Committee that credit unions today are vibrant and healthy. Membership in credit unions continues to grow with credit unions serving over 90 million Americans—more than at any time in history. Despite what you may have heard from other parties, credit unions provide little competitive threat to other financial institutions. According to data obtained from the Federal Reserve Board, during the 27 year period from 1980 to September 2007, the percentage of total household financial assets held by credit unions decreased from 1.5 percent to 1.1 percent or 0.4 percent over the course of 27 years.

DOMESTIC FINANCIAL ASSETS

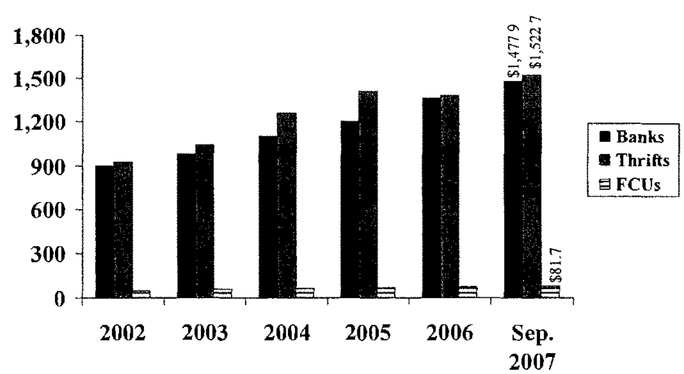


**Other includes items such as private pension funds, mortgages, asset-backed securities, finance companies, and investments in bank personal trusts.

Source: Flow of Funds Accounts of the United States, FRB

The above chart only tells part of the story. Credit unions remain small financial institutions. The chart below indicates that the average credit union has $81.7 million in assets.

AVERAGE ASSETS BY INSTITUTION (MILLIONS $)



Source: NCUA 5300 Call Reports & FDIC Quarterly Banking Profiles

As you can see from the chart, it is no surprise that a number of individual banks have total assets greater than the entire credit union community combined.

As is the case with the banks and thrifts, there has been consolidation within the credit union community in recent years. The number of credit unions has declined by more than 65 percent over the course of the past 38 years, from an all-time high of 23,866 in 1969 to 8,268 at year-end 2007. Similar to the experience of all credit unions, the number of federal credit unions has declined by just about 61 percent over that same period, from a high of 12,921 in 1969 to 5,036 today.

Regulatory Relief Proposals

Credit unions are more heavily regulated than any other consumer financial services provider. Restrictions on the operations of credit unions limit not only who can avail themselves of credit union services, but also how credit unions can raise capital. While banks and their trade associations state that about one-third of banks and thrifts have fewer than 25 employees, I must point out that over three-fourths of credit unions have fewer than 25 employees and almost two-thirds have fewer than ten employees.

NAFCU has been working with legislators on both sides of the aisle to address the need for credit union regulatory relief and improvements. In the 110th Congress, a number of initiatives have been proposed, which we applaud. NAFCU supports the efforts of H.R. 1537, the *Credit Union Regulatory Improvements Act* (CURIA); H.R. 5519, the *Credit Union Regulatory Relief Act of 2008*; H.R. 1849, the *Credit Union Small Business Lending Act*; and H.R. 3113, the *Affordable Financial Services Enhancement Act*. We believe that all of these initiatives recognize that today's credit unions exist in a very dynamic environment and that the laws and regulations dealing with credit union issues are currently in need of review and refinement. NAFCU urges the Committee to consider these proposals and to pass these bills.

Moreover, NAFCU believes that comprehensive credit union regulatory relief is needed to help credit unions further serve their members in today's sophisticated financial marketplace. NAFCU believes that CURIA, introduced last March by Representatives Paul Kanjorski (PA) and Ed Royce (CA) is a fundamental step toward comprehensive relief, as it addresses many of the regulatory burdens and restrictions on federal credit unions. We are pleased to see continued, growing support for CURIA, which is now co-sponsored by over one-third of the entire United States House of Representatives, while support continues grow. NAFCU believes this support demonstrates a clear recognition of the need to modernize credit union net worth standards, advance credit union efforts to promote economic growth and modify credit union regulatory standards. CURIA is a balanced and common-sense regulatory relief bill that addresses the important issues that America's credit unions are currently facing. Enactment of CURIA would improve the ability of credit unions to better serve their members and promote economic growth within their communities.

PCA Reform

NAFCU strongly supports reform of the credit union prompt correction action (PCA) system, which would provide a much-needed update to the capital structure of credit unions. The current capital structure for credit unions is a system that was enacted with the passage of the *Credit Union Membership Access Act of 1998*. Under the current PCA system, credit unions are classified based on their net worth ratio to one of five capital categories that range from "well capitalized" to "critically undercapitalized." However, these capital categories have proved inefficient, not taking into account the level of asset risk. Explained most simply, under the current capital system, a new one-year unsecured $10,000 loan is treated the same as a 30-year mortgage in its last month of repayment. Title I of CURIA would address this by modernizing by redefining the net worth ratio to include risk assets. This would result in a new, more appropriate measurement to determine the relative risk of a credit union's assets and improve the safety and soundness of credit unions and the National Credit Union Share Insurance Fund (NCUSIF). It is important to note that this proposal was developed in conjunction with the NCUA, which has nearly 10 years of experience in dealing with the current one-size-fits-all system established under CUMAA.

The American Bankers Association (ABA) expressed three concerns regarding a risk-based capital system for credit unions in a comment letter to the NCUA dated November 18, 2004. We believe that Title I of CURIA addresses these concerns. Specifically, the ABA said that:

(1) credit unions need a meaningful leverage ratio;
(2) there should be no substantive difference between bank and credit union leverage ratio standards; and,
(3) secondary capital would undermine the unique character of credit unions.

Specifically, Title I of CURIA would not expand the authority for NCUA to authorize secondary capital accounts. Title I also establishes meaningful leverage ratios, and we support the complimentary and risk-based standards proposed by the NCUA. Notably, Title I of CURIA closely resembles the bank-like, risk-weighted capital system. Having addressed the ABA's concerns, NAFCU believes that the current PCA reform proposal included in CURIA is well-balanced and would give the NCUA a meaningful risk-based system.

On June 9, 2005, NCUA Chairman JoAnn Johnson testified before the House Financial Services Subcommittee on Financial Institutions and Consumer Credit saying "While NCUA supports a statutorily mandated PCA system, the current statutory requirements for credit unions are too inflexible and establish a structure based primarily on a 'one-size-fits-all' approach, relying largely on a high leverage requirement of net worth to total assets. This creates inequities for credit unions with low-risk balance sheets and limits NCUA's ability to design a meaningful risk-based system." As noted earlier, Title I of

CURIA incorporates the recommendations made by the NCUA, in addressing this "one-size-fits-all" approach. For example, CURIA proposes that a well-capitalized credit union would have to maintain both a leverage net worth ratio of 5.25 percent and a risk based ratio of 10 percent. Similarly, CURIA proposes complimentary leverage and risk-based standards for the other capital categories. The proposed risk-based approach reflects a trend among all financial regulators to shift from a focus on leverage ratio to a focus on risk-assessment in determining the safety and soundness of financial institutions.

A modernized risk-based approach for credit unions would more closely emulate the capital standards for FDIC-insured banks, better enabling NCUA to detect and address potential safety and soundness concerns as soon as possible. It would allow credit unions with low-risk balance sheets to hold less capital while requiring high-risk institutions to hold more capital. This is an important feature as credit unions, unlike banks, are generally not allowed to raise capital through the sale of stock. Title I of CURIA effectively addresses the concerns with PCA reform, while at the same time incorporating the recommendations of our regulator with regard to making much-needed updates to the credit union capital structure. We urge the Committee's action on this important matter.

Limits on Member Business Loans

NAFCU supports modification of the current asset limit on member business loans at a credit union from the current formula of the lesser of 1.75 times net worth or 12.25 percent of total assets to a flat rate of 20 percent of the total assets of a credit union. This provision will facilitate member business lending without jeopardizing the safety and soundness of participating credit unions. While the current cap was first arbitrarily imposed on credit unions as part of the *Credit Union Membership Access Act* in 1998, CUMAA also directed the Treasury Department to study the need for such a cap. In 2001, the Treasury Department released its study entitled "Credit Union Member Business Lending" in which it concluded that "credit unions' business lending currently has no effect on the viability and profitability of other insured depository institutions." That same study also found that over 50 percent of credit union loans were made to businesses with assets under $100,000, and 45 percent of credit union business loans go to individuals with household incomes of less than $50,000. Furthermore, a 20 percent cap for credit union member business lending would be less than or equal to the business lending caps for other institutions. We would urge the Committee to review this study and give it the weight it deserves when considering credit union member business lending.

Webster First FCU experiences the restrictions of the present credit union member business loan cap first-hand. We are currently at our cap and as a result, are forced to turn our member-small business owners away on a weekly basis. Often times, we will extend a line of credit to a member, many of which go unused seasonally or even for a couple of years. Many of our small business owners like to have a line of credit available should they need it, even if they are not using it. Despite the fact that many of these lines of credit are not currently being used, they count toward our member business lending cap. This is a common problem that I see with federally-chartered credit unions that participate in member business lending. An increase in the member business lending cap to 20 percent of total assets would enable Webster First to do $32 million more in member business loans. At Webster First FCU, we have 100 percent of the liquidity to do this and 100 percent of the want to be able to put $32 million back into Massachusetts small businesses and the community. There are many credit unions like Webster First in Congressional Districts across the country. All we need is for Congress to enact this provision.

NAFCU also supports revising the current definition of a member business loan by giving the NCUA the authority to exclude small loans of $100,000 or less as de minimus, rather than preserving the current threshold of $50,000. This would adjust the threshold for inflation, from the $50,000 level set in 1998. These much needed updates to the limits on credit union member business loans would promote economic growth by providing additional sources of credit for small businesses.

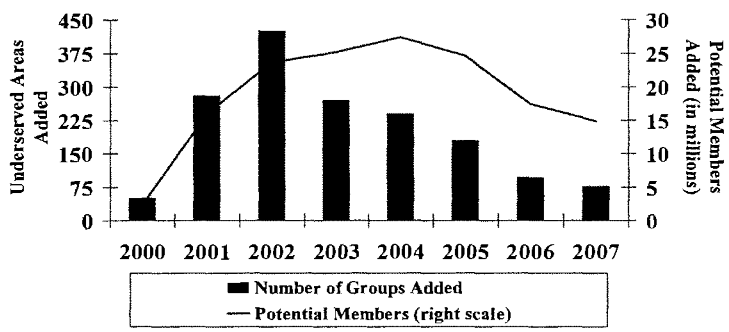
Underserved Areas

Credit unions play an important role in helping those that other financial institutions have turned their backs on and left behind. NAFCU supports making a necessary clarification to the 1998 *Credit Union Membership Access Act*, such as the one included in CURIA, the *Credit Union Regulatory Relief Act of 2008* and the *Affordable Financial Service Enhancement Act*. This would seek to clarify that credit unions are able to add underserved areas to their fields of membership, regardless of charter type. In 2005, the American Bankers Association brought litigation against NCUA arguing that under the plain language of CUMAA (American Bankers Association et al. v. NCUA, No. 2:05-cv-000904 (D. Utah, filed Nov. 1, 2006)), only multiple-common-bond credit unions could add underserved areas to their fields of membership. Up to that point, NCUA had permitted all types of credit unions to add underserved areas to their field of membership. Even though there was legislative history supporting the NCUA interpretation, the case settled out of court and as a result, NCUA modified its rules to prohibit community and single-sponsor federal credit unions from adding underserved areas to their field of membership. An underserved area under CURIA is defined as an "investment area" under the Community Development Financial Institutions Act or as a "low income community" under the New Market Tax Credit program.

NAFCU and the credit union community believe that addressing this issue through legislation would clear up the ambiguity surrounding the ability of federal credit unions to add underserved areas to their fields of membership. Regardless of charter type, these proposals would enable credit unions to be part of the solution of the unbanked problem in America, serving those who are not served by other institutions. It is disingenuous for the banking industry to falsely say credit unions are not fulfilling their mission in service to the underserved, while simultaneously working to prevent credit unions from serving those same people. Since the passage of CUMAA in 1998, federal credit unions have added over 1,500 underserved areas, bringing low-cost financial services being made available to over 150 million people. However, with the necessary clarification to

CUMAA, credit unions will be able to do even more in providing service to the underserved.

UNDERSERVED AREAS & POTENTIAL MEMBERSHIP ADDED TO FCU MEMBERSHIP



Source: NCUA Underserved Area Reports

Additionally, NAFCU supports the provision in CURIA that would enhance the ability of credit unions to assist distressed communities with their economic revitalization efforts. The proposal would allow a credit union to lease space in a building or on property in an underserved area, in which it maintains a physical presence to other parties on a more permanent basis.

Regulatory Modifications

Several provisions currently included in legislative proposals before this Committee passed the House in the 109th Congress as part of H.R. 3505, the *Financial Services Regulatory Relief Act of 2005*. Despite passing the House, they failed to be enacted and these regulatory modifications are still very much needed.

Community charter conversions involving employee group credit unions

NAFCU supports efforts that give NCUA the authority to allow credit unions to continue to serve and add members from their select employee groups (SEGs) after a credit union converts to a community charter. This provision seeks to ensure that groups within the credit union's existing membership are able to remain a part of the credit union if they wish, even though they are located outside the new community charter's geographic boundaries. Additionally, this provision would require NCUA to establish criteria to ensure that if a member chooses to remain with the credit union's field of membership, they will receive adequate service.

Member business loan exclusion for loans to non-profit religious organizations

NAFCU supports a provision that would exclude loans or loan participations by federal credit unions to non-profit religious organizations from the member business loan limit. Specifically at Webster First FCU, we have provided $4.1 million in loans to non-profit religious organizations. Accordingly, this provision would provide some much-needed relief to credit unions, such as mine that believe these non-profit religious organizations are important and greatly contribute to community growth.

Investments in securities by federal credit unions

NAFCU supports this effort to increase investment options for federal credit unions by allowing certain limited investments in securities. The current limitations in the FCUA unduly restrict federal credit unions in today's financial marketplace and have the potential to adversely impact both safety and soundness in the future. We believe that the track record of safe and sound performance by credit unions warrants expanded investment authority in accordance with regulations promulgated by the NCUA Board.

Authority of NCUA to establish longer maturities for certain credit union loans

NAFCU supports providing NCUA with the flexibility to provide for loan terms exceeding 15 years, for certain types of loans. As part of regulatory relief efforts in the 109th Congress, the NCUA was allowed to increase the 12-year limit on non-real-estate-secured loans to 15 years. However, NAFCU believes that greater flexibility is warranted for certain products, such as student loans.

Increase in investment limit in credit union service organizations

Currently, an individual federal credit union may invest in aggregate no more than one percent of its unimpaired capital and surplus in credit union service organizations, or CUSOs. We support raising the amount a credit union may invest in all CUSOs.

Credit union governance

The FCUA contains many antiquated "governance" provisions that, while perhaps appropriate in 1934, are outdated, unnecessary and inappropriate restrictions on the day-to-day operations and policies of a federal credit union. For example, credit unions are not allowed to expel disruptive or threatening members without a two-thirds vote of the membership. NAFCU supports giving credit union boards this necessary flexibility. Additionally, NAFCU supports allowing credit unions to limit the length of service of members of the board of directors to ensure broader representation.

Providing NCUA with greater flexibility in responding to market conditions

NAFCU supports the idea of giving NCUA greater flexibility to adjust interest rates depending on market conditions. Under current law, federal credit unions are the only type of insured institutions subject to federal usury limits on consumer loans. This proposal would maintain a cap, but it would also provide the NCUA with greater flexibility to modify those limits depending on market conditions.

Exemption from pre-merger notification requirement of the Clayton Act

NAFCU supports the inclusion of this language, which would exempt credit unions, just as banks and thrifts are already exempt, from the pre-merger notification requirements and fees for purposes of antitrust review by the Federal Trade Commission under the Clayton Act.

In addition to these proposals, which previously passed the House in the 109th Congress, there are several regulatory modification proposals in various bills before this Committee that we believe will enhance the federal charter.

Voluntary mergers involving multiple common bond credit unions

Current law imposes a numerical limitation of 3,000 on the size of a group that can go forward with a credit union merger before considering spinning off the group and requiring it to form a separate credit union. There is no sound reason for this restriction; NAFCU believes the 3,000 limit is arbitrary. In addition, a credit union that converts to (or merges into) a community charter should be allowed to retain all employee groups in its field of membership at the time of conversion. Current law does not allow this, penalizing not only the credit union, but also those in its field of membership. Furthermore, the retroactive effective date of August 7, 1998, (the date of enactment of CUMAA), is an important part of this section and should be maintained.

Credit union conversion voting requirements

NAFCU believes that credit unions should have the ability to convert their charters when in the best interest of the members. NAFCU supports the credit union conversion voting requirements provision of CURIA that would increase the minimum member participation requirement in any vote to approve a conversion to 30 percent of the credit union's membership. NAFCU considers this provision to be consistent with its principle that transparency is paramount in the conversion process. We believe that a minimum voting requirement is an effective way to ensure that the best interest of the membership is being pursued. Additionally, this provision would require that a general membership meeting be held one month prior to sending out notices regarding a conversion vote that contains a voting ballot. This will provide credit union members with a more meaningful opportunity to engage in a dialogue with the credit union board about the conversion process and to comment on that process and the conversion plan. Under current rules, credit union members are not necessarily informed of the board of directors' decision to convert until called upon to vote on the conversion.

Short-term payday loan alternatives within field of membership

NAFCU supports efforts to allow federal credit unions to offer short term payday loan alternatives to anyone within their fields of membership. We believe this new authority, which would be discretionary and not mandatory, will allow credit unions to help combat abuses by non-traditional financial institutions that prey on consumers, particularly those who live and work in underserved communities.

Member business loan exclusion for loans in underserved areas

NAFCU supports excluding member business loans made in underserved areas from the credit union member business lending cap. We feel that this proposal reflects an understanding that the credit union member business lending cap is often times restrictive, hindering credit unions from promoting economic growth in underserved areas. While NAFCU supports an overall modification in the member business lending cap to better facilitate economic growth in all the communities that credit unions serve, we also recognize that there continues to be an urgent need to address this matter with regard to underserved areas.

Credit union participation in SBA programs

NAFCU supports a clarification in existing law, which permits credit unions to participate in the SBA's 504 Certified Development Companies loan program. Because the terms of SBA's 504 loan program are specified in regulation and not in statute, credit unions risk non-compliance with NCUA lending rules without this clarification. A proposal to make this necessary clarification is included in both H.R. 1849, the *Credit Union Small Business Lending Act*, and H.R. 5519, the *Credit Union Regulatory Relief Act of 2008*. Additionally, NAFCU supports provisions in H.R. 1849 permitting the guaranteed and non-guaranteed portions of SBA 7(a) loans to not count against the regulatory cap for business lending, providing credit unions with greater capacity to make business loans. Furthermore, NAFCU supports the establishment of a credit union outreach program within SBA to increase credit union participation. NAFCU also believes that an 85 percent guaranty on member business loans up to $250,000 for loans made to small businesses in underserved areas will encourage more credit unions to make

SBA loans in these areas. H.R. 1849 is a pivotal step toward facilitating more SBA loans by credit unions and thus encouraging greater credit union business lending. These proposals would undoubtedly benefit the entrepreneur and small business credit union members.

We hope that the Committee will consider these issues and their importance as these various proposals moves forward in the legislative process.

Conclusion

The state of the credit union community is strong and the safety and soundness of America's credit unions is unquestionable. Nevertheless, there is a clear need for easing the regulatory burden on credit unions as we move forward and the financial services marketplace becomes more innovative. It has been 10 years since Congress has enacted major credit union legislation. Credit unions need comprehensive regulatory relief. NAFCU strongly believes that CURIA, which has over one-third of the House as cosponsors and continues to gain support, is the best vehicle to accomplish this. We also recognize that H.R. 5519, the *Credit Union Regulatory Relief Act* is an important non-controversial first step at regulatory relief and should be passed by the Committee in short order.

We continue to urge the Committee to consider the CURIA proposal, which makes much-needed refinements and improvements to the credit union regulatory structure. Moreover, NAFCU supports any regulatory relief effort that will enhance the ability of credit unions to fulfill their mission. Even though Congress has enacted major banking reforms in the 10 years since that enactment of CUMAA, we recognize that other financial institutions are also seeking regulatory relief. We firmly believe that if regulatory relief efforts are pursued by the Committee for financial institutions, such efforts must be balanced between credit unions, banks and thrifts. We hope that the Committee will consider the legislative efforts before it and included in this testimony.

These proposals will make the improvements and offer the relief needed to enable credit unions to better serve their 90 million members.

INDEPENDENT COMMUNITY
BANKERS of AMERICA

Testimony of

R. Michael Stewart Menzies, Sr.
President/CEO, Easton Bank and Trust Company

On behalf of the
Independent Community Bankers of America

Before the

Congress of the United States
House of Representatives
Committee on Financial Services

Hearing on

"The Need for Credit Union Regulatory Relief and Improvements"

March 6, 2008
Washington, D.C.

Mr. Chairman and Ranking Member Bachus, I am R. Michael Stewart Menzies, Sr., President and CEO of Easton Bank and Trust Company in Easton, Maryland. I am also the Chairman-Elect of the Independent Community Bankers of America.[1] Easton Bank is a $140 million asset community bank located in a small town on the Eastern Shore of Maryland. Our main lending focus is on small business, though 15 percent of our loans are to consumers.

ICBA appreciates this opportunity to testify on legislation (H.R. 1537) that would expand the tax-exempt credit union charter. We strongly oppose this bill, the Credit Union Regulatory Improvements Act (CURIA). Congress should not enhance the credit union charter unless it also is prepared to tax credit unions and require them to comply with the Community Reinvestment Act.

I want to make clear that community bankers strongly support locally-based non-profit organizations. I have served on a number of non-profit boards, including the local hospital board. Many of my community bank colleagues perform similar service. And, Easton Bank offers a special savings account to non-profit institutions. Our concern is that tax-exempt credit unions have strayed far from their statutory mission to serve individuals of modest means and are seeking to go even farther.

My statement makes the following key points:

- CURIA is powers enhancement, <u>not</u> regulatory relief and credit union regulation does not appear adequate to deal with the proposed increase in their powers;
- Community banks are seeking true regulatory and tax relief;
- Credit unions should not be given expanded business powers as long as they remain tax exempt.
- Credit unions should be encouraged to convert to the mutual thrift charter if they need additional authorities; and
- Tax-exempt credit unions are <u>not</u> meeting their statutory goal of serving people of modest means and pose unfair competition to community banks;

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[1] *The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 268,000 Americans, ICBA members hold more than $908 billion in assets, $726 billion in deposits, and more than $619 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

CURIA is Powers Enhancement, Not Regulatory Relief

CURIA goes far beyond eliminating unnecessary paperwork by enhancing credit unions' powers and reducing critical capital requirements.

The bill makes these substantial changes to credit unions' business lending authority:

- Increases overall business loan cap from 12.25 to 20 percent of assets;
- Exempts business loans under $100,000 from the overall cap;
- Excludes faith-based loans entirely;
- Allows undercapitalized credit unions to increase their business lending.

CURIA doubles credit unions' authority to invest in credit union service organizations. Since CUSOs have substantially more authority than credit unions themselves this indirectly increases credit unions' powers.

Credit unions' involvement in last year's Florida real estate investment scheme, dubbed "Millionaire University," illustrates just how far credit unions have strayed from their original tax-exempt mandate to serve low- and moderate-income families and into risky business loans. In this scheme a number of credit unions granted speculative out-of-market land development loans to residents from far away states. Borrowers became credit union "members" by paying a $5 membership fee. Three of those credit unions failed. What original members were served in their home states of Colorado and Michigan when these credit unions made these risky loans on Florida real estate?

While these credit unions strayed far from their home communities, their representatives in Washington have continued to ask Congress to allow them to expand into "underserved" areas, regardless of whether these areas are populated by individuals in a credit union's field of membership.

Under the guise of helping the underserved, the net effect will be to further expand credit unions' reach into the marketplace without a clear demonstration that individuals actually lack access to banking services. And, the proposed expansion does not carry any obligation that the credit unions actually serve low- and moderate-income consumers.

Credit union regulation bears a superficial resemblance to bank regulation, with minimum capital requirements and regular examinations. However, the Millionaire University fiasco and recent losses by the National Credit Union Share Insurance Fund suggests that there are substantial differences between bank and credit union supervision. NCUA has reported that NCUSIF lost $185.4 million in December, the most losses for one month or for an entire year in the fund's existence.[2]

[2]Credit Union Journal, February 22, 2008.

The Congress explicitly placed limits on the types of lending tax-exempt credit unions can do for a good reason – so credit unions can focus their efforts on serving people of modest means that share a common bond. This is not only better for local communities; it is also a much safer form of lending. Congress should conduct substantial oversight of the NCUA before it seriously considers expanding the credit union charter.

While increasing credit unions' powers and risks, CURIA allows credit unions to reduce their capital. It lowers the standard for a credit union to be considered "well-capitalized" from 7 to 5.5 percent of assets. This is particularly unwise at a time when the entire financial system is undergoing substantial stress.

Community Bankers are Seeking True Regulatory Relief

Some in the credit union industry have argued that CURIA is comparable to the community bank regulatory and tax relief bill ICBA is supporting. However, that bill, the Communities First Act (H.R. 1869), introduced by Small Business Chairwoman Nydia Velazquez, does not increase community banks' powers. It simply reduces unnecessary paperwork for community banks and their customers and begins to redress the tax inequality between community banks and their credit union competitors.

ICBA strongly urges this committee to continue the work on regulatory relief for all banking institutions that was begun in the last Congress. This is important if community banks are to remain viable competitors. Community banks have fewer personnel and other resources than larger banks to employ in their efforts to meet steadily increasing regulatory demands. We strongly urge you to continue to rebalance the account by eliminating or reducing outdated and unnecessary regulations.

For example, we urge Congress to enact the CFA provision that would eliminate the requirement that financial institutions send customers annual privacy notices when they do not share customer information and have not changed their policies. And, you could reduce the call report burden by permitting community banks to file short-form call reports for two quarters each year.

CFA also provides additional tax reforms for banks that have elected Subchapter S status. Credit union industry representatives have claimed that Sub-S provides benefits comparable to credit unions' tax exemption. This is not accurate; credit unions are tax exempt, while all Sub-S profits are taxed at the shareholder level at the top income tax rate as high as 35 percent. Community banks and their shareholders pay additional state and local taxes, for a total tax burden often exceeding 40 percent. This is true whether the bank distributes earnings to shareholders or holds them as retained earnings.

Credit Unions Should Not Get More Business Lending Authority if They Remain Tax Exempt

Credit unions are seeking to expand farther into an area that is vital to community banks, small business lending. Community bankers do not object to increased competition; many large banks and other lenders compete for small business loans. But, those lenders pay taxes, credit unions do not.

Credit unions representatives often claim that credit unions represent a small share of the financial services market. They reach this conclusion by including the assets of the entire banking system, including the nation's largest banks. However, those institutions are far less concerned about the unfair competition from tax-exempt credit unions than community banks. While total banking assets are $13 trillion, assets held by ICBA's nearly 5,000 members total $982 billion. Federally-insured credit unions hold a comparable amount, $753 billion.

At the time their tax and regulatory advantages were put in place, credit unions offered little more than basic savings accounts, certificates of deposit, and small personal loans to limited fields of membership. Congress and NCUA have substantially changed this trade-off by expanding credit unions' product line and geographic reach:

- Credit unions have substantial leeway to offer business loans and aggressively skirt the statutory 12.25 percent cap;
- Many credit unions have converted to geographically-based "community" charters, making their geographic footprint equivalent to their community bank competitors; and
- A large number of credit unions now serve so many disparate groups that individual credit unions are allowed to serve virtually anyone with a pulse.
- There is an increasing number of large, full service, credit unions over $1 billion in assets.

The Congressional Research Service has reported that through credit union service organizations, "credit unions may provide their members with a panoply of sophisticated financial services and products that rivals the offerings of banks and thrifts." The CRS report notes that "over the past 30 years, most of the distinctions between credit unions and other depository institutions have been eliminated or reduced because of deregulation; consequently, the justification for the tax exemption for credit unions has been increasingly questioned."[3]

Today's credit unions have virtually no limit to their customer base; the statutory "common bond" requirement has become meaningless because many credit

[3] Congressional Research Service. "Should Credit Unions be Taxed?" August 2005.

unions serve multiple common bonds or have expansive "community" charters. For example, NCUA gave the Los Angeles Financial Credit Union approval to serve: "Anyone who lives, worships, works in, or attends school in Los Angeles County." This encompasses a county of more than 10 million people and a geographic area larger than the states of Delaware and Rhode Island combined. Other examples abound. This hardly meets the statutory requirement that membership in community credit unions be limited to "Persons or organizations within a well-defined local community, neighborhood, or rural district."[4]

ICBA believes that these changes already justify credit union taxation and CRA coverage. Like community banks, credit unions should willingly support our nation's goals by paying their fair share of taxes. Until Congress is at least ready to require credit unions to pay taxes and comply with CRA, it should refrain from granting credit unions new powers.

Credit Unions Could Convert to Mutual Thrifts

The implicit reason for the expansions in CURIA appears to be that the current credit union charter is inadequate for the needs of some credit unions and their customers. However, ICBA believes that there is a far more appropriate alternative for them; if they need bank powers to better serve their customers, they should be encouraged to convert to a Federal savings association charter. Over 30 credit unions have taken advantage of this option, despite the substantial roadblocks that the National Credit Union Administration has put in the way of credit union-to-thrift conversions.

Why should credit unions have to convert to a new charter, rather than simply ask Congress to increase credit union powers? The answer is simple. Congress provided credit unions with a substantial tax advantage over community banks and does not require them to comply with the Community Reinvestment Act. This was part of a basic trade-off put in place decades ago: limited activities, providing credit to individuals of modest means, but valuable tax and regulatory benefits.

If some credit unions believe they need new powers, NCUA would best serve them, their members – and taxpayers – by facilitating their conversion to tax-paying mutual thrifts. Unfortunately, the agency has taken the exact opposite approach; it has erected roadblock after roadblock to conversions, even though those institutions would remain in mutual form.

The agency has imposed unrealistic disclosure requirements on credit unions seeking to convert. At one point, it even attempted to block two conversions because the required disclosures to credit union members were "incorrectly"

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[4] Federal Credit Union Act, section 109(b) (12 U.S.C. 1759(b).

folded! It only relented when it became clear that a Federal magistrate was going to rule against the agency.

Unfortunately, the pending legislation would make it more difficult for a credit union to convert. Current law requires a majority of those voting to permit a conversion. CURIA would add that at least 30 percent of members would have to participate in the vote.

This goes in the wrong direction. No other Federal financial regulatory agency imposes anything like the conversion restrictions that NCUA imposes. In fact, in all other charter conversions, the agency that an institution is leaving need only give summary approval. The only analogous situations are instances when a mutual thrift seeks to convert to stockholder form. In those cases the supervising agency seeks to ensure that the process is fair to depositors and does not unduly enrich management. The resulting numbers tell the story; hundreds of mutual institutions have converted to stockholder ownership. In contrast, only around 30 credit unions have converted to mutual thrift charters.

Credit Unions Are Not Serving Their Original Mission

As I have indicated, Congress granted credit unions' their tax exemption with the understanding that they would be serving individuals of modest means. Congress had the same rationale for credit unions' CRA exemption. The record shows that credit unions have not upheld their end of the bargain. In light of this record, there is no justification for granting credit unions additional powers and further extending the reach of their tax exempt activities.

In 2005, the Tax Foundation undertook an analysis of the credit unions' Federal Tax exemption.[5] The study calculated that the tax subsidy is worth $2 billion a year – and growing. It will be over $32 billion over the ten-year budget window. For the average credit union, this meant a return on assets ½ percentage points – 50 basis points – higher than the average bank. Only 6 basis points of the subsidy are used to lower interest rates. Another 11 "are absorbed by higher labor costs."[6] There is little or no effect on deposit rates or other costs.

Of course, these are averages that demonstrate that credit unions do not generally pass on their subsidy to their customers. However, they do have the option to use their subsidy selectively to secure business that they want. One of my customers – a retired pilot with an excellent financial record – applied for a loan to buy a private aircraft. However, his credit union offered far better terms than my bank could offer. The credit union's tax advantage helped make that possible.

[5] "Competitive Advantage: A Study of the Federal Tax Exemption for Credit Unions," by Professor John A. Tatom, Ph.D. Tax Foundation, 2005.
[6] Page 22.

A host of other studies round out the picture. A 2005 study by the National Community Reinvestment Coalition determined that banks actually do a better job of fulfilling the credit unions' mission than the credit unions. This study highlighted how banks "consistently exceed credit unions' performance in lending to women, minorities, and low and moderate-income borrowers and communities."[7] A 2003 Government Accountability Office study found that credit unions serve a more affluent clientele than banks. This GAO study concluded that "credit unions overall served a lower percentage of households of modest means than banks."[8]

Another study by the Woodstock Institute concluded that credit unions serve a higher percentage of middle- and upper-income customers than lower-income households.[9] Similarly, a study by the Virginia Commonwealth University concluded that credit unions tend to serve a higher proportion of wealthier households in their customer base.[10]

Today there are more than 120 credit unions with $1 billion or more in assets, providing sophisticated banking products and services to wealthy and middle-income members. There is no justification for their tax-exempt status and CRA exemption.

In one instance, the NCUA acted on these facts. Effective November 27, 2000, NCUA adopted a rule that required all credit unions with a community charter to adopt a Community Action Plan. The rule would have required

> that a community credit union address in either its marketing or business plan or other appropriate separate documentation, such as the strategic plan, project differentiation, etc, how it plans on serving the entire community, including how the credit union will market to the community and what products and services will be offered by the credit union to assist underserved members in the community.[11]

Unfortunately, the membership of the NCUA's board changed soon after the agency adopted the CAP requirements and the rule was repealed. In 2002, JoAnn Johnson – then a board member, now chairman – attempted to justify this

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[7] "Credit Unions: True to Their Mission?" National Community Reinvestment Coalition, May 2005. www.ncrc.org.
[8] General Accounting Office. "Credit Unions: Financial Condition Has Improved, but Opportunities Exist to Enhance Oversight and Share Insurance Management." October 2003.
[9] Woodstock Institute. "Rhetoric and Reality: An Analysis of Mainstream Credit Unions' Record of Serving Low-Income People. February 2002.
[10] School of Business, Virginia Commonwealth University. A Study on the Comparative Growth of Banks and Credit Unions in Virginia: 1985-1995." August 1997.
[11] NATIONAL CREDIT UNION ADMINISTRATION, 12 CFR Part 701, final rule, effective November 27, 2000, section 5, COMMUNITY CHARTERS, COMMUNITY ACTION PLAN (CAP) (since rescinded).

action by claiming that credit unions were already serving persons of "modest means." This is easier said than proven. During the 2005 Ways and Means Committee hearing on credit unions' tax exemption NCUA Chairman Johnson and credit union representatives had a difficult time demonstrating that they were meeting their statutory mandate of serving persons of modest means.

ICBA believes that the NCUA had the right idea when it adopted the CAP proposal in October of 2000 and took a giant step backward when it repealed the rule the following year. We strongly recommend that Congress build on the agency's work in 2000 and require credit unions to comply with CRA requirements in the same manner, and with the same asset size distinctions, as banks and thrifts.

Conclusion

ICBA strongly urges Congress to reject calls for new powers and reduced capital for the credit union industry. Credit unions should be granted no new powers as long as they remain tax exempt and are not meeting their statutory mission to serve individuals of modest means. Enhanced commercial lending authority is inconsistent with this mission.

Instead, we urge you to continue efforts to provide true regulatory burden relief for all depository institutions. This is vital if community banks are to remain competitive. And, Congress should exercise rigorous oversight of the National Credit Union Administration to determine if it is providing adequate safety and soundness regulation and not unduly restricting credit union conversions.

NASCUS

Prepared Testimony of George Reynolds
Senior Deputy Commissioner
Georgia Department of Banking and Finance
On behalf of the
National Association of State Credit Union Supervisors
Before the Financial Services Committee
United States House of Representatives
March 6, 2008

NASCUS History and Purpose

Good morning, Chairman Frank, and distinguished members of the House of Representatives Committee on Financial Services. I am George Reynolds, Senior Deputy Commissioner of Georgia Department of Banking and Finance and chairman of the National Association of State Credit Union Supervisors (NASCUS)[1]. I appear today on behalf of NASCUS, the professional association of state credit union regulators.

The mission of NASCUS is to enhance state credit union supervision and advocate for a safe and sound state credit union system. We achieve our mission by serving as an advocate for the dual chartering system, a system that recognizes the traditional and essential role of state government in the national system of depository financial institutions.

NASCUS believes H.R. 1537, the Credit Union Regulatory Improvements Act of 2007, commonly called CURIA, is important legislation. It provides regulatory modernization that enhances safety and soundness and offers additional ways for credit unions to meet the needs of consumer members. We are pleased to have this opportunity to share our state supervisory perspective regarding regulatory relief and to address the provisions in H.R. 1537 that apply to state-chartered credit unions. This testimony addresses those provisions that impact state-chartered credit unions. We appreciate your willingness to listen and understand the regulatory relief needs of the state credit union system.

As a professional state regulators association, NASCUS reviewed CURIA from a regulatory viewpoint. In determining our position on a particular provision, NASCUS considered the effect on credit union safety and soundness and state law.

[1] NASCUS is the professional association of the 48 state and territorial credit union regulatory agencies that charter and supervise the nation's 3,300 state-chartered credit unions.

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NASCUS Priorities for Regulatory Relief

NASCUS priorities for regulatory relief focus on reforms that strengthen the state system of credit union supervision and enhance the capabilities of state-chartered credit unions. The ultimate goal is to meet the financial needs of consumer members while assuring that the state system is operating in a safe and sound manner.

In this testimony, I address provisions in CURIA, as well as additional regulatory relief priorities that are vital to the future growth and safety and soundness of state-chartered credit unions. The CURIA provisions include the following:

- Proposed comprehensive capital reform for credit unions.
- Expanding the member business lending cap to 20 percent of total assets of a credit union increasing the availability of loans for consumer members.
- Amending the definition of business loans subject to the current cap of $50,000 to $100,000.
- Changes to the process for conversion of a state-chartered credit union.
- Providing an exemption from pre-merger notification requirements of the Clayton Act for credit unions.

Thinking beyond CURIA, there are several provisions from a state regulatory perspective that I believe should be considered; these provisions include:

- Advocating further capital modernization, including alternative capital.
- Allowing all state-chartered credit unions to join the Federal Home Loan Banks (FHLBs) system.
- Providing by statute that an individual with state credit union regulatory experience be included on the National Credit Union Administration (NCUA) Board.

Title I—Capital Modernization

The provisions in Title I amend the Federal Credit Union Act (FCUA) to reduce the minimum net worth ratio requirements for credit unions. The provisions also provide risk-based capital requirements for insured credit unions comparable to those imposed by the Federal Deposit Insurance Corporation (FDIC).

NASCUS supports comprehensive credit union capital reform. Credit unions need capital reform in distinct several areas. First, credit unions need to be assessed using risk-based capital standards; and second, credit unions should have access to alternative capital. From a state regulatory perspective, capital reform that addresses these areas makes logical sense for the safety and soundness of credit unions and the members they serve.

Risk-based capital

Section 102 in CURIA, Amendments Relating to Risk-Based Net Worth Categories Requirements, expands risk-based capital options to all federally insured credit unions, not just

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complex credit unions. NASCUS has long supported that risk based capital standards are appropriate; we believe it is a sound and logical approach to capital reform for credit unions.

The support for risk-based capital is widespread; the concept is supported by the federal credit union regulator, the NCUA, and by many within the credit union industry. A risk-based capital structure has proved successful for other financial institutions in this country for nearly 20 years.

The risk-based capital system of Basel I was introduced in the financial industry in 1988. The two fundamental objectives of Basel I were (1) to strengthen the soundness and stability of the international banking system; and (2) to be fair and have a high degree of consistency in its application.

Today, insured depository institutions, with the exception of credit unions, utilize risk-based capital to build and monitor capital levels. Risk-based capital enables financial institutions to measure capital adequacy and to avoid additional risk on their balance sheets. It is a system that acknowledges diversity and complexity in financial institutions. The structure provides for increased capital levels for financial institutions that choose to maintain a more complex balance sheet, while reducing the burden of capital requirements for institutions with less complex assets. This system recognizes that a one-size-fits-all capital system does not work.

The financial community continues to refine risk-based capital and acknowledges that it is a logical and important part of monitoring capital. Credit unions are the only insured depository institution currently not subject to risk-based capital standards as it was presented in the Basel Accord of 1988. A risk-based capital structure would help credit unions monitor risks in their balance sheets. It makes logical sense that credit unions should have access to risk-based capital; it is a practical and necessary step in addressing capital reform for credit unions.

Alternative capital

While risk-based capital is part of the solution for credit unions, more is needed to ensure comprehensive capital reform. NASCUS believes that CURIA's capital reform provisions would be enhanced by allowing a provision for the inclusion of alternative capital for all credit unions. Simply put, credit unions would benefit from alternatives that allow them to raise capital other than through retained earnings.

NASCUS supports complete capital reform and regulatory modernization. NASCUS regulators believe it makes sound economic sense for credit unions to access other forms of capital in addition to retained earnings to improve their safety and soundness. In fact, low-income and corporate credit unions already have access to alternative capital.

NASCUS is not the only voice advocating that credit unions should have access to alternative capital. There are others who support capital reform and alternative capital for credit unions. The Filene Research Institute released a study in November 2007, *Alternative Capital for U.S. Credit Unions? A Review and Extension of Evidence Regarding Public Policy Reform* authored by Robert F. Hoel, PhD, Professor Emeritus of Business, Colorado State University, and Filene Fellow in Residence. The report makes the case for expanded sources of credit union capital and concludes that it is in the public interest to permit credit unions greater access to alternative capital sources.

The Filene report unequivocally supports alternative capital for credit unions. It is one more voice in favor of allowing alternative capital for credit unions. Please find following a copy of the Filene Research Institute's study.

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While the majority of credit unions are not involved in the problems of the subprime real estate market, currently all financial institutions are affected by its negative impact in the residential mortgage market. During the next several years, more subprime mortgages are expected to reprice than we have experienced thus far in this uncertain market. There could be further dislocations in the home equity lending market, increased credit risk exposure, changes in appraisal values and a further decline in home values in some markets. As regulators, we are concerned about diminished asset quality, increased default rates, the impact on the secondary market and a borrower's ability to secure future loans.

Alternative capital would allow credit unions, as it does other financial institutions, to meet these challenges and potentially thrive in an uncertain market. It would provide a cushion for credit unions to recover from financial setbacks and it would add an extra layer of protection for the National Credit Union Share Insurance Fund (NCUSIF).

As regulators, we realize that alternative capital requires solid regulation and rigorous regulatory review to ensure that these products are properly structured, meet proper disclosure requirements and do not create any systemic risk. Before a credit union would be given access to alternative capital, it must demonstrate that it has the resources to properly manage alternative capital. We understand that additional dialogue with policy makers, the credit union industry and the NCUA will be necessary in order to reach consensus on alternative capital. But, NASCUS believes that the time for such dialogue is now, before capital requirements are acute and time sensitive.

Strong cooperation between state and federal regulators

NASCUS supports strong cooperation and consultation between state and federal credit union regulators as provided for in the Credit Union Membership Access Act (CUMAA). NASCUS believes that coordination between state and federal regulators is imperative to ensure effective capital reform.

Economic Growth—Title II

NASCUS supports revisions to member business lending (MBL). MBL changes can provide an opportunity for credit unions to better serve their members and they are not believed to be a risk to safety and soundness, provided that sound and proper underwriting and controls are maintained in the credit union.

Specifically, Section 201 of CURIA amends the section of the FCUA that addresses member business lending. NASCUS supports the proposed statutory increase on credit union member business lending to 20 percent of the total assets of a credit union.

In addition, Section 202 of the bill amends the current definition of a member business loan to allow NCUA to exempt loans of $100,000 or less. This amends the definition of business loans subject to the current cap of $50,000 to $100,000.

NASCUS further supports Section 204 of H.R. 1537, which revises member business lending restrictions in the FCUA, thus lifting the restrictions on member business lending to nonprofit religious organizations for federally insured, state-chartered credit unions.

While NASCUS supports these provisions, we recognize that they require proper regulatory oversight through the examination and supervision process. Further, credit unions must have a thorough understanding of member business lending and be diligent in their written policies, underwriting and controls for these provisions to be implemented in a safe and sound manner.

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Again, as I stated with alternative capital, I believe these provisions can be regulated without presenting undue safety and soundness concerns.

Regulatory Modifications—Title III

On conversions, CURIA outlines several new procedures on voting requirements. NASCUS supports full transparency and disclosure in the conversion process. Further, NASCUS believes that any legislation concerning conversion requirements of a state-chartered credit union should recognize state law. It is the role of state authority as established by state law to determine the proper procedure and disclosure for state-chartered credit union conversions.

The chartering of a state credit union is an issue determined by state law. Approval authority for a conversion is decided, likewise, by state law, which generally authorizes the state chartering authority to determine if a credit union may convert and the processes for a conversion. A conversion is a function of a credit union's original charter, separate from insurance oversight. Federal legislation should clearly recognize the rightful authority of states to determine chartering and conversion decisions for state-chartered credit unions.

In addition, NASCUS supports Section 309 of H.R. 1537 giving all federally insured credit unions the same exemptions as banks and thrift institutions from pre-merger notification requirements and fees of the Federal Trade Commission. In fact, we believe it should be expanded to include all state-chartered credit unions, regardless of their insurance.

Additional Regulatory Relief Priorities

NASCUS supports regulatory relief priorities beyond those found in H.R. 1537 and encourages this committee to add the appropriate provisions that allow for the needed changes.

Membership in FHLBs for all state-chartered credit unions

Currently, not all state-chartered credit unions have access to the same benefits. For example, not all state-chartered credit unions have access to the Federal Home Loan Bank (FHLB) System. We ask this committee to add a provision to CURIA allowing for membership by all state-chartered credit unions in the FHLB System.

We believe that all state-chartered credit unions should have access to the FHLB System, regardless of insurance type. All state-chartered credit unions are regulated and examined by state regulatory agencies to ensure they are operating in a safe and sound manner. Regulatory functions are a primary determinant of the safety and soundness of the credit union system.

State Regulatory Representation on the NCUA Board

A legislative provision providing for state-chartered financial institution regulatory experience on a federal financial agency regulatory board is not a new idea. A similar provision requiring state bank supervisory experience is included in the Federal Deposit Insurance Act. 12 U.S.C 1812(a). The Federal Deposit Insurance Act requires that a position be reserved on the FDIC Board of Directors for an individual with state bank supervisory experience.

We would appreciate your support for adding a provision to CURIA requiring that one NCUA Board member shall always have state credit union regulatory experience. NASCUS believes that requiring state regulatory experience for one of the NCUA Board members would provide value to the entire credit union system.

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About forty percent of credit unions are state-chartered. The majority of them have federal insurance provided by the NCUSIF. We believe that comprehensive experience in regulating state-chartered credit unions would provide a balanced perspective when overseeing the NCUSIF. In addition, as the NCUA promulgates regulations to further enhance safety and soundness, an individual with state-chartered credit union supervisory experience will better understand how proposed regulations will impact state-chartered, federally insured credit unions, thereby providing additional expertise to the agency.

Conclusion

NASCUS state credit union regulators believe relieving regulatory burden for credit unions is critical. Regulatory relief implemented with foresight ensures a safe and sound credit union system for the future. It also provides enhanced products and services for consumer members.

The following points review NASCUS' position on CURIA provisions and on other regulatory relief priorities for credit unions.

- NASCUS supports a risk-based capital structure for credit unions.
- NASCUS believes credit unions should be permitted to issue alternative capital.
- NASCUS supports strong cooperation and consultation between state and federal credit union regulators as provided for in the Credit Union Membership Access Act (CUMAA).
- NASCUS supports expanding member business lending provisions to 20 percent of total assets of a credit union increasing the availability of loans to consumer members.
- NASCUS supports amending the definition of business loans subject to the current cap of $50,000 to $100,000.
- NASCUS believes that the process for converting a state-chartered credit union to another financial institution charter is a matter that should be determined by state law and regulation, not dictated by federal legislation.
- NASCUS supports Section 309 that provides all federally insured credit unions the same exemption that banks and thrift institutions already have from pre-merger notification requirements and fees of the Federal Trade Commission. Additionally, we support expanding this provision to include all state-chartered credit unions.
- NASCUS believes all state-chartered credit unions should be eligible to join the FHLB system.
- NASCUS supports a statute that requires an individual with state credit union regulatory experience be included on the National Credit Union Administration (NCUA) Board.

NASCUS appreciates the opportunity to testify today and share our priorities for CURIA and for credit union regulatory relief.

We urge this Committee to be watchful of federal preemption and to protect and enhance the viability of the dual chartering system for credit unions by acting favorably on the provisions we have presented in our testimony. We welcome questions from Committee members.

Thank you.

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Testimony of Bradley E. Rock

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Committee on Financial Services

United States House of Representatives

AMERICAN BANKERS ASSOCIATION ®

Testimony of Bradley E. Rock

On Behalf of the American Bankers Association

Before the

Committee on Financial Services

United States House of Representatives

March 6, 2008

Chairman Frank and members of the Committee, my name is Bradley Rock, Chairman, President, and CEO of Bank of Smithtown, a $1.2 billion community bank located in Smithtown, New York, founded in 1910. I am also the Chairman of the American Bankers Association (ABA). ABA brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $12.7 trillion in assets and employ over 2 million men and women.

We appreciate, Mr. Chairman, the opportunity to comment on expanding the powers of credit unions. As always, these debates are filled with emotion on both sides. It is important to look beyond the rhetoric to focus on the reality of the credit union industry today. Certainly, there are many traditional credit unions that remain true to the original spirit of the credit union charter – meeting the needs of people of modest means. We must never forget that credit unions were established for this specific purpose. Serving people of small means is not a parenthetical duty; it is their legal focus and mission and is why credit unions have special federal privileges. The vast majority of credit unions continue to embody this statutory mission and we believe play an important role in our financial system.

Distinct from traditional credit unions, a new breed of credit unions has emerged that wants to serve a broad customer base, do complex business lending, and offer asset management services targeted at wealthier customers. These new-breed credit unions are virtually identical to taxpaying banks. As a practical matter, these new-breed credit unions are free to define and extend their membership as they please, allowing them to "cherry pick" the areas and individuals they will include as customers. Thus, while the rhetoric is about serving low income people, the reality is that these new-breed credit unions have a license to seek out the wealthiest areas for branching at the expense of serving people who need them the most – those of modest means.

During this hearing, we will undoubtedly hear a lot from the National Credit Union Administration (NCUA) and credit union witnesses about the need for broader authority to serve underserved areas. We strongly urge the Committee to look at the harsh reality of what NCUA has already authorized in this area. It has ***nothing*** to do with serving the low-income people and ***everything*** to do with gutting any requirement for a common bond.

The reality is this: Congress meant for credit unions to have meaningful common bonds and provided a limited exception from the common bond to serve low-income neighborhoods with inadequate banking services. Instead, the NCUA has declared entire cities and counties to be underserved and allowed credit unions to open branches in high income areas with no requirement – ***none*** – that they serve low-income neighborhoods.

For example, all of Washington, D.C. has been declared underserved, and there is no requirement that there be any service to low-income people in the District. This is not theoretical: there are numerous examples of credit unions going into ***only*** the higher income districts of so-called underserved areas.

The reality is that if NCUA broadens the so-called underserved exemption, the common bond will be basically repealed. As NCUA declares more and more cities and counties underserved, all credit unions will be able to branch almost anywhere. With no requirement to put a branch in a low-income neighborhood, every credit union would be eligible to come to Washington, D.C., put a branch on K Street, where there are several branches on every block already, ***and not make one loan to a low-income person.***

During this hearing, we will also hear about the loans to very small businesses that credit unions want to make but supposedly cannot. While the rhetoric speaks of serving the small business man or woman, the reality is that these credit unions are making ***large*** dollar loans to businesses. The truth is that these new-breed credit unions have made business lending a top priority as they seek to rapidly grow the institution – making loans that any taxpaying financial institution would want to make. The fact that some credit unions are hitting the Congressionally-mandated limits on business lending is because they are making these large loans – including those to businesses out of their market area.

Increasingly, business loans are being made to non-members. Aggressive new-breed credit unions have lending officers cold-calling on businesses and real estate developers, often outside their common bonds, who have no relationship whatsoever with the credit union. After the loan is agreed to, the credit union creates some back-channel way for the borrower to become a "member." We urge this Committee to look at these loans and ask if this is what the credit union tax-exemption is for. Loans like:

- The $30 million development loan in default for a luxury condo building by Eastern Financial Florida Credit Union.
- The loan for a luxury golf and condominium resort by Twin City Co-op Federal Credit Union.
- Construction loans averaging $10 million and all business loans averaging nearly $3 million by Texans Credit Union.
- A $10 million dollar loan commitment by the ***California*** credit union – Telesis Community Credit Union – to purchase an office tower in ***Arkansas***.
- And above all, the millions of dollars in loans involving a failed and fraudulent ***Florida*** land deal that caused the recent failures of credit unions in ***Colorado*** and ***Michigan***.

While the rhetoric is about the small mom-and-pop credit unions, the reality is that there are 123 credit unions that have over $1 billion in assets. To put that in perspective, these credit unions are larger than 92 percent of the taxpaying banks in this country. Moreover, the traditional credit unions are being squeezed out by the invasive tactics of these growth-oriented credit unions. It is no surprise that nearly 2,100 credit unions have been absorbed into larger credit unions since the beginning of 2001.

Against a backdrop where non-traditional credit unions forsake the common bond in favor of fast growth, and where energies are diverted to favoring the well-off and businesses rather than serving people of modest means, it is no surprise that ABA opposes expansion of credit union powers and easing of credit union capital rules. To allow such expansion will only move the new breed of credit unions further and further away from their mandated mission.

And while the rhetoric suggests that without these changes there are no options for these institutions to grow and better serve their customers, the reality is that a very viable option is available *today* through switching to a mutual savings bank charter – a route that some credit unions have already taken. This charter provides greater flexibility with the effective and experienced supervision of traditional banking regulators, while still preserving the mutual-member focus that credit unions find desirable.

Our statement addresses three important questions:

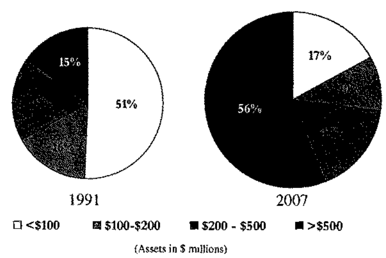
- ***Are new-breed credit unions fulfilling their mandate to serve people of modest means?***
- ***Are large business loans consistent with serving people of small means?***
- ***At what point do some credit unions cease to be the type of institution deserving of preferential treatment?***

Are new-breed credit unions fulfilling their mandate to serve people of modest means?

As the credit union industry has matured, a new breed of institution has evolved that bears little resemblance to a traditional credit union. These "morphed" credit unions that seek out large commercial customers are a far cry from traditional credit unions which have remained true to their credit union mandate to serve people of small means. With the freedom to seek new markets virtually without restriction and to offer a full range of banking and financial products, many aggressive credit unions have leveraged their tax advantage to grow rapidly. ***There are now 123 credit unions each with assets greater than $1 billion. There are 309 credit unions with assets of more than $500 million each.***

These large, aggressive institutions increasingly dominate the industry, yet many still try to hide behind the veil of a "traditional credit union." In spite of their metamorphosis into highly competitive financial institutions virtually indistinguishable from banks, these morphed credit unions continue to enjoy the tax-exempt status conferred on the industry when it was composed of small self-help organizations.

Large Credit Unions are Increasingly Dominating Industry Share
(Based on Credit Unions Total Assets)



A good example of a credit union that has grown beyond its mission to serve people of modest means is Bethpage Federal Credit Union located on Long Island in New York. Bethpage, at ***$3 billion in assets***, is nearly three times larger than my bank and nearly five times larger than the median sized community bank headquartered on Long Island. It is clear from this ad for luxury home financing that its focus is often on wealthy individuals, not people of low and moderate income.

Are you in the market for a luxury home?

If so, you should know that Bethpage now offers Jumbo Mortgage loans up to $1 million. Now, you can get those great Bethpage rates and low fees for your higher-priced home as well.

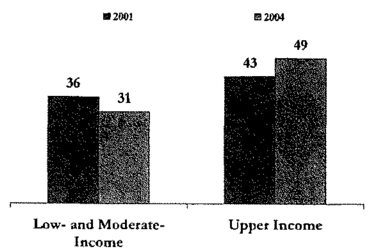
Whether you are buying a lavish estate or a modest cottage, when you finance your mortgage at Bethpage, you are now entitled to new ways to save:

- GE's Homebuyer Privileges℠ – receive discounts on home-related products and services from Home Depot, GE Appliances, and ADT Security Systems and more! Visit www.bethpagefcu.com for more details and eligibility requirement.
- Land Bound Services, LLC – receive $450 off title search (See coupon below for details).

Bethpage is not an isolated example. A recent study by the National Community Reinvestment Coalition found, "...that over a three-year time period, banks consistently outperformed credit unions in offering home loans to minorities, women, and low- and moderate-income borrowers in a majority of states."

The Government Accountability Office (GAO) confirmed this as well. It found that credit unions lag banks in serving people of modest means. Using the Federal Reserve's 2004 Survey of Consumer Finance data, GAO noted that only 31 percent of credit union customers are low- and moderate-income, while 41 percent of bank customers are low- and moderate-income. In fact, the percent of low- and moderate-income customers served by credit unions fell from 36 percent in 2001 to 31 percent in 2004.[1]

Credit Union Service to Low- and Moderate-Income Households Declined



Source: GAO and Federal Reserve Survey of Consumer Finance

The fact that credit unions lag banks in serving low- and moderate-income individuals is also confirmed in states, such as Massachusetts, where state-chartered credit unions are subject to the Community Reinvestment Act. Between 2004 and 2007, 36 percent of all Massachusetts banks received either an outstanding or high-satisfactory rating. In comparison, only 13 percent of all state-chartered credit unions received either an outstanding or high-satisfactory rating from the same regulator.

[1] *Credit Unions: Greater Transparency Needed on Who Credit Unions Serve and on Senior Executive Compensation Arrangements.* U.S. Government Accountability Office, November 2006. (GAO-07-29)

In recent years, many new-breed credit unions added "underserved" communities. While, on the surface, stretching geographic boundaries sounds like an excellent way to ensure that credit unions fulfill their mission of serving individuals of modest means, the reality is quite different. The problem begins with an extremely broad definition of what constitutes an underserved area by NCUA, so broad, in fact, that it includes ***entire cities***. In fact, in recent years NCUA has approved the cities of Houston, Washington, D.C., Philadelphia, and Tucson as underserved communities. ***More importantly, NCUA poses no requirement on credit unions to actually serve the low- and moderate-income areas within those cities.***[2] Thus, a credit union could claim all of Washington, D.C. as an underserved community and set up shop in wealthy areas and completely ignore low- and moderate-income neighborhoods.

This is more than theory: HEW Federal Credit Union added all of Washington, D.C. as an underserved community. However, neither of its two branches is in a low-income or even moderate-income neighborhood. Robins Federal Credit Union (Warner Robins, GA), with almost $1 billion in assets, added as an underserved area Clarke County, Georgia, located over 100 miles from its primary market in Macon. The branch it opened was in an upper income census tract in Athens, GA. So while the rhetoric sounds compelling, the reality is quite different and ignores the clear intent of Congress.

With no requirement or oversight that ensures credit unions claiming an underserved area actually reach out to the residents in the low-income areas, it is no surprise that expansion-minded credit unions have sought this option. In fact, the rate of approvals of so-called underserved areas has increased dramatically, ***growing from 40 to 641 approvals from 2000 to 2005,*** according to the 2006 GAO study.[3]

Moreover, it took NCUA ***eight years*** after the Credit Union Membership Access Act of 1988 (CUMAA) to issue regulations requiring credit unions adding underserved areas to establish a service facility somewhere – ***anywhere*** – in tbe underserved area. Even then, it allowed credit unions ***two years*** to establish that physical presence. Even with this lenient requirement, many credit unions objected. For example, Roger Heacock, President and CEO of Black Hills Federal Credit Union, said in a 2006 comment letter to NCUA, "We strongly disagree with this change to require a physical presence in underserved areas. This may have been necessary years ago, but

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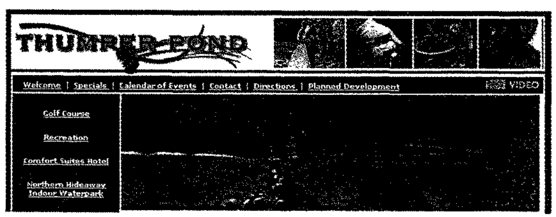
[2] The GAO found that while NCUA moved quickly to approve expansions under the underserved area authority, NCUA did not develop indicators to determine if the credit unions' services had, in fact, reached the underserved population in those expanded footprints. *Credit Unions: Financial Condition Has Improved, but Opportunities Exist to Enhance Oversight and Share Insurance Management.* U.S Government Accountability Office, October 2003 (GAO-04-91)

multiple electronic delivery channels now bring credit union services right into the home."[4] According to the U.S. Census Bureau, less than one-third of families earning less than $25,000 per year had Internet access, while almost all families earning in excess of $100,000 had Internet access. Once again, while the language suggests that underserved populations are being served, the reality can be completely different.

Are large business loans consistent with serving people of small means?

The new breed of credit unions is aggressively pursuing business customers through large commercial and real estate loans. A dramatic example of just how far these credit unions have gone is the financing of Thumper Pond. This luxury resort features a golf course, spa, waterpark, hotels, and a planned condominium community. Located in central Minnesota, the resort was financed by a large commercial loan made by Twin City Co-ops Federal Credit Union (Falcon Heights, MN). Not only is this far beyond any sensible definition of modest means, but the resort is located over 200 miles from the credit union's headquarters. Is this the kind of loan that should be tax-subsidized?

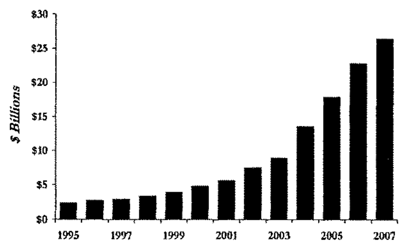


Now credit unions want to raise the cap on business lending to free up more resources to make even bigger loans. Their current tax-exempt status and lack of equivalent regulation have created huge competitive inequities in the local marketplace. Unfortunately, provisions to expand business lending, such as those in H.R. 1537, would further exacerbate these competitive inequities and raise safety and soundness concerns.

[3] Ibid.
[4] Comment letter, Roger Heacock, Black Hills Federal Credit Union, March 29, 2006

Business lending is the fastest growing line of business for credit unions. As of the end of 2007, credit unions held almost $26.4 billion in business loans, ***of which nearly $5 billion was to nonmembers.***[5] Today, business loans amount to 5 percent of all credit union loans – up from 1 percent in 2000.

NCUA: Credit Union Business Lending Soars



Source: NCUA

H.R. 1537 would increase credit unions' business lending authority to 20 percent of total assets from 12.25 percent, almost a doubling of their business lending authority. In addition, the bill excludes business loans under $100,000 from the business lending limit, up from $50,000 under current law, further masking the true amount of commercial lending engaged in by credit unions.[6] ***Taken together these changes would grant credit unions more expansive commercial lending authority than taxpaying federal savings associations,*** which are limited to a flat 20 percent of total assets limitation, without the benefit of excluding certain business loan amounts from that cap and without the significant tax benefit.

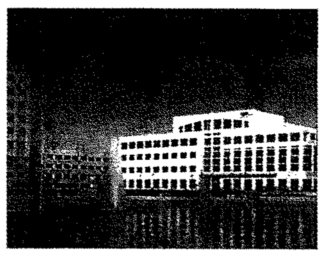
Congress put these current limits in place to assure credit unions remained focused on individuals. In fact, the Senate Report implementing the Credit Union Membership Access Act of 1998, stated that the limits "...are intended to ensure that credit unions continue to fulfill their specified mission of meeting the credit and savings needs of consumers, especially persons of modest means, through the emphasis on consumer rather than business loans."[7] How many loans

[5] Oddly, NCUA in 2003 excluded these nonmember business loans from the Congressionally-mandated cap, helping to add impetus to these types of loans.
[6] By raising the exclusion for business loans to $100,000, H.R. 1537 encourages more lending at much larger dollar volumes and it would allow even more loans to be exempt from the special regulatory requirements for business lending, such as loan-to-value limitations and using experienced business-loan officers.
[7] Senate Report 105-193, May 21, 1998, pp.9-10.

to low- and moderate-income individuals could be made instead of 20 percent of all assets being devoted to business loans in excess of $100,000? Simply put, the focus on people of small means that was clearly enunciated in the preamble to the Federal Credit Union Act would be even further diminished – but the tax exemption for credit unions would not.

There is already plenty of evidence that business lending by large credit unions is often focused on larger loans to businesses that do not deserve tax-subsidized loans:

- Chetco Federal Credit Union (Harbor, OR) has become the "800 pound gorilla" in its local market, building a $160 million business loan portfolio, with most loans in its "sweet spot" of $100,000 to $500,000; but could go as high as $5 million.[8]
- Langley Federal Credit Union (Newport News, VA) at the end of 2007 had a total of $96.8 million in ***business loans to nonmembers***, representing 17.6 percent of all the outstanding loans.

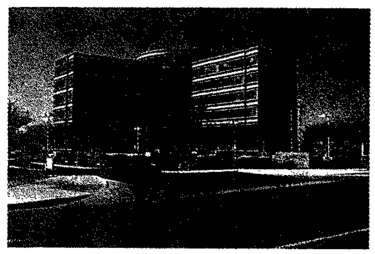


Langley Credit Union
Newport News, VA
Assets: $1.1 Billion

- The average size of a business loan made by Digital Credit Union (Marlborough, MA) in 2007 was $1 million.

[8] "Twenty Years of Experience Helps Chetco FCU's Business Lending Program Stay Innovative, Thwart Complacency" *Credit Union Times*, April 11, 2007, p. 18.

- Texans Credit Union (Richardson, TX) reported holding $350 million in construction and development loans on its books at the end of 2007. The average size of a construction loan at Texans Credit Union was $10 million. These are hardly loans to ***small*** businesses.
- Telesis Community Credit Union ***located in California*** made a commitment in 2006 to finance a $10.2 million 24-story office building ***located in Arkansas.*** The average outstanding business loan at Telesis is $680,000.
- Desert Schools FCU (Phoenix, AZ) announced it will provide commercial real estate loans up to $7 million to finance or refinance commercial property, including professional offices, retail, warehouse and industrial zoned buildings.[9]



Desert Schools FCU
Phoenix, AZ
$3 Billion

All of the above are loans for which any bank would compete. But the tax advantages enjoyed by credit unions make competition extremely difficult. A study by Virginia Commonwealth University professors Neil Murphy and Dennis O'Toole found that "...credit unions are enabled to offer a 67 basis point advantage in loan pricing and deposit pricing over banks as a direct result of the fact that credit unions do not pay state or federal taxes." The professors conclude: "In a highly competitive industry, the sixty-seven basis point government subsidy is substantial."[10] The Federal Reserve Bank of Dallas agreed with the competitive threat: "Credit unions, aided by favorable legislation and regulation, have emerged as another particularly severe threat to small banks."[11]

These are but a few examples of commercial lending by credit unions. They are not isolated cases. Many credit unions have commercial lending officers cold-calling on businesses that need million-dollar loans and are not in any way involved with the particular credit union.

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[9] "Desert Schools Finds Niche With Commercial Real Estate Loans" Credit Union Journal Daily, February 25, 2008.
[10] Murphy, Neil and O'Toole, Dennis, *A Study of the Evolution and Growth of Credit Unions in Virginia: 1997-2002*, Virginia Commonwealth University, November, 2003.
[11] "Small Banks' Competitors Loom Large," Federal Reserve Bank of Dallas Southwest Economy, January/February, 2004, p. 10.

H.R. 1537 raises serious safety and soundness issues

As credit unions have aggressively pursued business lending options, business loan delinquencies have risen. For example, Eastern Financial Florida Credit Union (Miramar, FL), which appears to be above its aggregate business loan cap, started foreclosure proceedings against a real estate developer, Merco Group Inc. of Miami, on a $30 million condo development loan for a 338-unit housing project overlooking Florida's Intercoastal Waterway. The credit union reported a loss of $45 million in 2007.

The recent examples of two credit unions failures – Huron River Area Credit Union, Ann Arbor, MI, and Norlarco Credit Union, Fort Collins, CO – demonstrate the danger of credit unions leaving their core mission and aggressively pursuing business lending outside their markets. Both credit unions far exceeded the business lending cap and were lending to speculators thousands of miles away from their market areas. Appendix 3 provides details on the extent of the problems with these two credit unions and with their regulator which was supposed to supervise the risk that business lending posed.

In fact, GAO warned about the danger of business lending by credit unions. In its 2003 study, it concluded that, "[S]ince member business loans constitute only a small percentage of credit union lending, most NCUA examiners will not have significant experience looking at this type of lending activity. In contrast, banks and thrifts offer these loans to a much greater extent than credit unions and their regulators do have experience in this area."[12] GAO was skeptical that NCUA was up to the challenge to ensuring that it is adequately prepared to monitor the expansion of credit union business lending.

In spite of the warnings and emerging evidence of problems with credit union business lending, H.R. 1537 weakens the capital regulation of credit unions. In fact, the capital provisions in H.R. 1537 are ***weaker than those applied to banks*** and do not reflect the true amount of capital on hand for credit unions to meet losses, especially during periods of financial stress. H.R. 1537 would lower the minimum capital "leverage ratio" requirement to be well capitalized from 7 percent to 5.25 percent. The current capital system was developed by Congress in 1998 because, in the

[12] *Credit Unions: Financial Condition Has Improved, but Opportunities Exist to Enhance Oversight and Share Insurance Management.* General Accounting Office, October 2003 (GAO-04-91), p. 49

words of the Treasury Department during the debate on the bill, NCUA's "...relevant statutes, regulations, and policies fall short of providing a system of prompt corrective action for credit unions. NCUA has no regulations or even formal guidelines for taking corrective action regarding a troubled credit union...."[13] Moreover, the current capital rules were specifically imposed by Congress in order that credit unions would have the same type of capital requirements that were given to commercial banks and savings institutions in the aftermath of the savings and loan crisis.

Emil Henry, former Assistant Secretary of the Treasury for Financial Institutions, reiterated in 2006 the justification for current capital requirements:

> There are also important differences in the capital structure of credit unions vis-a-vis other depository institutions. In general, credit unions can only raise equity capital by increasing retained earnings. This is an important feature that is grounded in the cooperative nature of credit unions. Thus, unlike other depository institutions, credit unions do not have access to other sources of capital to build a capital cushion when financial conditions are good.... [The] basic goal of a minimum leverage capital requirement is to encourage financial institutions to maintain sufficient capital levels so that the PCA requirements are not triggered.... Other factors that have been cited for imposing a higher leverage capital requirement surround the proper accounting for credit unions' investment in the NCUSIF [National Credit Union Share Insurance Fund] and their investments in corporate credit unions.

Also, Congress in 1998 required NCUA to establish a risk-based net worth requirement for "complex" credit unions. However, a 2004 GAO study found that only 8 percent of all federally-insured credit unions had been designated as complex by NCUA, subjecting them to a risk-based net worth requirement. ***This included none of the largest five credit unions and only one in the largest ten.***[14]

[13] *Credit Unions*, United States Department of the Treasury, 1997, p. 76
[14] *Credit Unions: Available Information Indicates No Compelling Need for Secondary Capital*, U.S. Government Accountability Office, August 2004 (GAO-04-849).

At what point do some credit unions cease to be the type of institution deserving of preferential treatment?

As the credit union industry evolves, a blurring of the line between banks and credit unions has developed. In fact, a new breed of credit union has emerged that does not fulfill the traditional mission of serving people of small means, often focusing on above median-income people and commercial businesses, both of which have many options for financing and do not need tax-subsidized help. The common bond, where people can save and lend to one another, is often forsaken for rapid growth in members. Preserving the values of the traditional credit union charter has been a long-term priority for the Congress. Credit unions that seek greater product and service authority and want greater options to raise capital to support these expanded activities can and should choose a mutual savings bank charter, with the broader authority and experienced bank supervision that comes with it. This is the reason a straightforward, fair, and predictable conversion process from a credit union charter to a mutual savings bank charter is so important.

The evolution of credit unions raises important policy questions. Are new-breed credit unions fulfilling their mandate to serve people of modest means? Do these non-traditional credit unions qualify for their special treatment, despite the fact that they no longer serve the purposes of their charter? If these credit unions are not meeting the responsibilities Congress created for their charter, why should Congress give them more authority to expand business lending and other activities through the proposed Credit Union Regulatory Improvement Act to depart even further from their mandate? At what point do some credit unions cease to be the type of institution deserving of preferential treatment?

We would respectfully suggest that the answers all point to a credible, fair, workable process whereby a credit union that wants to exercise bank powers should be able to switch to a mutual savings bank charter. Without such a process, the only response to today's new breed of credit unions is to allow them to continue to abandon people of modest means while distorting the credit union charter into something unrecognizable by the original authors of the credit union concept.

Thank you, Mr. Chairman, for the opportunity to present the views of the American Bankers Association.

Appendix 1

Largest 25 Credit Union Business Lenders

September 30, 2007

Rank	Credit Union	City	State	Total Business Loans Outstanding	Average Size Business Loan Outstanding
1	Evangelical Christian	Brea	CA	$1,071,206,000	$926,648
2	Texans CU	Richardson	TX	801,092,000	2,923,693
3	Melrose	Briarwood	NY	625,434,000	153,480
4	Patelco	San Francisco	CA	592,879,000	1,291,675
5	America First	Ogden	UT	497,515,000	999,026
6	Lockheed FCU	Burbank	CA	352,627,000	2,086,550
7	San Diego County CU	San Diego	CA	335,871,000	511,219
8	Telesis Community	Chatsworth	CA	330,593,000	683,043
9	Citizens Equity First	Peoria	IL	321,185,000	399,981
10	Kinecta	Manhattan Beach	CA	317,098,000	1,187,632
11	Premier America CU	Chatsworth	CA	309,001,000	1,437,213
12	Digital	Marlborough	MA	308,678,000	738,464
13	Progressive	New York	NY	301,912,000	130,022
14	State Employees CU	Raleigh	NC	286,740,000	76,894
15	Christian Community	Covina	CA	280,425,000	520,269
16	Royal CU	Eau Claire	WI	263,089,000	312,828
17	Eastern Financial Florida	Miramar	FL	255,879,000	1,421,550
18	Orange County Teachers FCU	Santa Ana	CA	248,699,000	322,566
19	Mountain America	W. Jordan	UT	247,903,000	511,140
20	Beacon	Wabash	IN	239,544,000	117,827
21	Whitefish CU Association	Whitefish	MT	238,091,000	333,928
22	Coastal FCU	Raleigh	NC	234,627,000	1,203,215
23	Central Minnesota	Melrose	MN	225,574,000	98,762
24	Farmers Insurance Group FCU	Los Angeles	CA	218,397,000	97,804
25	Huron River Area CU	Ann Arbor	MI	198,295,000	246,329

Appendix 2
Largest 25 Credit Unions Making Business Loans to *Non-Members*
September 30, 2007

Rank	Credit Union	City	State	Non-Member Business Loans
1	Patelco	San Francisco	CA	$569,879,000
2	Premier America CU	Chatsworth	CA	199,054,000
3	Texans CU	Richardson	TX	175,049,000
4	Orange County Teachers FCU	Santa Ana	CA	154,784,000
5	Western FCU	Manhattan Beach	CA	125,528,000
6	Credit Union of Texas	Dallas	TX	121,461,000
7	Bethpage FCU	Bethpage	NY	96,423,000
8	Langley	Newport News	VA	92,258,000
9	Safe	N. Highlands	CA	85,913,000
10	Lockheed FCU	Burbank	CA	84,644,000
11	Kinecta	Manhattan Beach	CA	84,359,000
12	Keypoint	Santa Clara	CA	80,732,000
13	Citizensfirst CU	Oshkosh	WI	79,641,000
14	Travis	Vacaville	CA	76,209,000
15	Caltech Employees FCU	La Cañada	CA	74,048,000
16	Fox Communities CU	Appleton	WI	70,481,000
17	Financial Partners	Downey	CA	68,817,000
18	Open Engineers Local #3 FCU	Livermore	CA	65,656,000
19	California Coast	San Diego	CA	64,652,000
20	America First	Ogden	UT	63,005,000
21	United Services of America FCU	San Diego	CA	62,142,000
22	Nuvision	Huntington Beach	CA	62,031,000
23	Allegacy	Winston-Salem	NC	55,254,000
24	Southland	Downey	CA	54,710,000
25	First Financial	Albuquerque	NM	53,024,000

Appendix 3

Business Lending and the Failure of Huron River Area and Norlarco Credit Unions

Due to significant losses from expansive business lending programs, two credit unions recently failed. Huron River Area Credit Union was a $268 million Ann Arbor, Michigan institution and Norlarco Credit Union was a $334 million Fort Collins, Colorado institution.

The experience of these credit unions validates the wisdom of Congress when it imposed specific business lending limits on credit unions in 1998 and raises several important policy questions. First, were these credit unions adhering to the business lending cap? Second, did their out-of-market business lending programs expose them to too much risk? Third, did the people these credit unions made loans to have the necessary affinity to qualify for credit union membership? Finally, does the experience of these credit unions suggest a lack of adequate oversight in the regulatory process?

Did These Credit Unions Adhere to the Business Loan Limit?

When Congress enacted the Credit Union Membership Access Act (CUMAA) in 1998, it specifically limited business lending authority of credit unions to 12.25 percent of assets. The intent of this restriction was to "ensure that credit unions continue to fulfill their specified mission of meeting the credit and savings needs of consumers, especially persons of modest means, through an emphasis on consumer rather than business loans."[15] Both Norlarco and Huron River far exceeded the 12.25 percent lending cap.

Business Lending by Norlarco

In the first half of 2007, the member business loan portfolio of Norlarco increased from $38 million to $78 million. However, in the call reports that credit unions are required to file with their regulator each quarter, Norlarco reported originating only $2.3 million in new business loans for that period, even though its member business loan portfolio had more than doubled. When asked by a local newspaper whether the credit union deliberately mischaracterized loans in order to remain

[15] S. Rep. No. 105-193, (1998).

under the federal lending cap, Bob Hamer, CEO of Norlarco, stated "No. There was a deliberate attempt to make as many business loans as we could."[16]

Furthermore, the $78 million in business loans that Norlarco had in June represented nearly 23 percent of the credit union's assets – nearly double the congressionally mandated limit.

Business Lending by Huron River

Huron River Area CU reported only four member business loans worth $8.6 million on its books as of December 2006. Yet after the credit union was placed into conservatorship[17] in February 2007, its financial statements were restated. The restated call reports indicate that Huron River Area CU actually had 785 member business loans worth $139 million as of December 2006. Further revisions show that by the end of June, member business loans had increased to $193 million, with $185 million in construction and development loans.

The restated call reports for December 2006 show that slightly more than 37 percent of the credit union's assets were in business loans at that time. By the middle of 2007, this figure had increased to roughly 72 percent – well above the legal business loan cap of 12.25 percent.

Did Their Business Lending Programs Expose Them to Too Much Risk?

Unlike secure lending to individuals, business lending carries inherently more risk. In fact, the delinquency rate on credit uniou business loans is more than one-and-a-half times higher than the delinquency rate on the overall portfolio of credit unions. Moreover, business loans are typically much larger than consumer loans, requiring more stringent monitoring due to their potential for greater loss. The risks associated with business lending are compounded when loans are made to out-of-market customers with no prior relationship with or connection to the credit union and in a market that is unfamiliar to the credit union. The ultimate losses experienced by both Norlarco and Huron River indicate that their business lending programs exposed them to a high level of risk which was compounded by the fact that these loans were out-of-market and were not adequately underwritten or monitored.

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[16] Robert Moore, "Norlarco Exceeds Federal Limit for Business Loans," *The Coloradoan*, September 21, 2007.

[17] In a conservatorship, the NCUA Board takes immediate possession of the business and assets of a credit union and takes on all the powers of the credit union members, directors, and officers until the Board determines that the credit union is in strong enough financial condition to continue its business, or the credit union is liquidated and its assets are sold off *See* 12 U.S.C § 1786

Out-of-Market Lending by Norlarco and Huron River

According to the financial records of Norlarco and Huron River, it appears that both credit unions were involved in making construction and land development loans in southwest Florida – well outside each of their local market areas.

NCUA records indicate that Norlarco had 1,035 loans worth $238 million in Lee County Florida. Huron River was also actively making loans in Lee County. While the dollar volume of these loans has not been made public, it is believed to be in the hundreds of millions. Huron River posted a $59 million loss during the first six months of 2007 after writing off $62 million related to potentially bad loans. The *Credit Union Journal* has reported that NCUA is holding at least $468 million in loans made by these two credit unions (and possibly a third) in Lee County, Florida.

The ability to monitor out-of-market business loans requires considerable resources, particularly when there is no physical presence in the market. It also requires considerable oversight by regulators to assure adequate compliance with federal and state law regarding underwriting standards, loan monitoring standards, and reporting accuracy.

Did the Credit Unions Adhere to the Common Bond Requirement?

The traditional philosophy underpinning credit unions is based on the idea that the deposits of members are used to provide those self-same members with loans, and the close affiliation among the members – their common bond – creates an incentive for each member to repay their obligation so that the other members do not suffer a loss. When Congress enacted CUMAA in 1998, it found that "a meaningful affinity and bond among [credit union] members . . . is essential to the fulfillment of the public mission of credit unions."[18] With regard to Norlarco and Huron River, both credit unions found ways to "qualify" borrowers who would not have had any natural affinity with either institution.

Norlarco Investors

Out-of-state investors were able to qualify for loans from Norlarco by claiming association with one of three non-profit organizations affiliated with the credit union. These include the Rocky Mountain Bird Observatory, the Boys and Girls Club of Larimer County, and Legacy Land Trust.

[18] United States. Cong. Senate. 105th Congress, H.R. 1151. The Credit Union Membership Access Act, enrolled by both the House and Senate; 28 July 1998

Such loose affiliations are often used by credit unions to meet the legal requirement for membership, but they circumvent the common bond principle. Bascially, these types of associations undermine completely the concept of a common bond, as anyone – individual or business – can join.

It is also relatively common for credit unions to simply take an applicant's word when determining eligibility. According to Bob Hamer, President and CEO of Norlarco, "We usually ask them how they believe they can be a member in their application. If they tell us, we don't assume they're lying. We don't verify that any of that is true."[19] State regulators take claims of eligibility at face value.

As a result of their involvement with the Florida land deals, many of Norlarco's members are pulling their money out of the credit union. Ron Phillips, economics professor at Colorado State University, has stated that many of his colleagues are withdrawing their money from Norlarco, the university's credit union, "Not because it's losing money, but because it's making loans in Florida . . . They are not using the money locally."[20]

Huron River Investors

It is not clear how investors qualified for loans from Huron River. Michigan law restricts credit union lending to members only and loans can be for out-of-state purposes as long as they are to members. Significantly, Huron River has been named in a lawsuit alleging real estate fraud and according to at least one report, there is no evidence indicating whether any of the more than 50 plaintiffs nationwide are members of the credit union, though at least one couple hails from Michigan.[21]

Was There Adequate Regulatory Oversight of These Credit Unions?

State supervisors have primary responsibility for examining state-chartered credit unions, but NCUA has authority to examine any state-chartered credit unions that are insured through the National Credit Union Share Insurance Fund (NCUSIF). NCUA also has the authority to place any insured credit union that encounters financial difficulties into conservatorship.[22] The overwhelming

[19] Pat Ferrier, "Non-Members Got Loans From Norlarco," *The Coloradoan*, August 28, 2007.
[20] Pat Ferrier, "Lawsuits Fly Over Norlarco's Florida Loans," *The Coloradoan*, August 23, 2007.
[21] Stefanie Murray, "Lawsuit Accuses Troubled Credit Union of Fraud," The Ann Arbor News, August 30, 2007.
[22] In the case of state-chartered, federally-insured credit unions, the NCUA must receive written approval of the reasons for conservatorship by the state regulator unless the reasons are due to serious undercapitalization of the credit union, in which case the NCUA is only required to consult with the state regulator. See 12 U.S.C. § 1786(h)(1).

majority of state-chartered credit unions have insurance through the NCUSIF and both Norlarco and Huron River are state-chartered credit unions with NCUSIF insurance.

According to a 2003 study by GAO, many state credit union regulators suffer from high examiner turnover and lack sufficient resources and expertise to ensure adequate oversight of state-chartered credit unions.[23] The report further states that in cases where state examiners lacked examiner resources or expertise, NCUA provided its own staff to ensure proper examination, and also conducted joint examinations of selected state-chartered credit unions to assess the risk they posed to NCUSIF.

State regulators in Colorado and Michigan did not catch the under-reporting of business loans and did not adequately address the risks associated with out-of-market business lending. Moreover, in the case of Norlarco, when the losses were discovered and the institution failed, the takeover of the credit union was not disclosed to the public.

The Failure of Norlarco

As previously noted, Norlarco reported originating only $2.3 million in business loans for the first half of 2007, even though its business loan portfolio had actually jumped from $38 million to $78 million. The Colorado regulator failed to catch the under-reporting of business loans by Norlarco.

Furthermore, the fact that Norlarco was in danger of failing and had been placed into conservatorship was originally kept from the public. The credit union was placed into conservatorship in May by the state regulators and was subsequently taken over by NCUA in July. However, the public did not become aware of the credit union's troubles until August 22 when *The Coloradoan*, a local newspaper in Fort Collins, broke the story.

Though Colorado law bars state regulators from disclosing the failure of a state-chartered credit union, NCUA is not under a similar obligation. The Federal Credit Union Act does not specifically require NCUA to notify credit union members, or the public at large, that their credit union has been placed into conservatorship, but nothing in the Act bars NCUA from doing so.

Reportedly, the decision not to announce the conservatorship was made jointly by NCUA and the Colorado regulator with the apparent intention of preventing a mass withdrawal of deposits from the credit union. However, the experience of the Federal Deposit Insurance Corporation

23 GAO Financial Condition Has Improved, but Opportunities Exist to Enhance Oversight and Share Insurance Management, GAO-04-91, October 2003.

(FDIC) in the late 1980s and early 1990s is that allowing word of a failure to slowly leak out is more likely to be contagious and lead to a run than informing customers about the status of their financial institution.

The Failure of Huron River

Similar to Norlarco, Huron River also under-reported the amount of business lending it was engaged in and the state regulator failed to recognize the severity of the situation. As previously noted, Huron River restated its call reports after being placed into conservatorship clarifying that it actually had $139 million in business loans as of December 2006 and not merely $8.6 million as first reported.

However, unlike Norlarco, the public was made aware that Huron River was placed into conservatorship almost immediately. Michigan law does not bar state regulators from disclosing the failure of a credit union and the decision was made to let the public know.

Considering that both Huron River and Norlarco were placed into conservatorship because of non-performing loans stemming from the same Florida development project, it would seem that the implications of placing either credit union into conservatorship would be the same. Thus, if keeping disclosure of conservatorship is truly necessary to prevent a run on member deposits, NCUA should arguably want to employ this principle across the board.

PAUL E. KANJORSKI
11TH DISTRICT, PENNSYLVANIA

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March 10, 2008

The Honorable JoAnn Johnson
Chairman
National Credit Union Administration
1775 Duke Street, Room 7011
Washington, DC 22314-3428

Dear Madam Chairman:

As a follow-up to the hearing of the House Financial Services Committee about "The Need for Credit Union Regulatory Relief and Improvements" held on March 6, 2008, I write to request that you provide additional views, information, or clarifications of the National Credit Union Administration to the portion of page 15 of your written statement describing Section 12 of H.R. 5519, the Credit Union Regulatory Relief Act of 2008. Consistent with all applicable law and regulation, I would appreciate receiving these additional views, information, or clarifications in writing no later than Friday, March 14, 2008.

Please let me know if you have questions regarding this request.

Sincerely,

Paul E. Kanjorski
Paul E. Kanjorski
Member of Congress

March 14, 2008

The Honorable Paul E. Kanjorski
U.S. House of Representatives
2188 Rayburn House Office Building
Washington, DC 20515-3811

Dear Congressman Kanjorski:

By letter dated March 10, 2008, you asked NCUA to provide additional views, information or clarifications concerning Section 12 of H.R. 5519, the Credit Union Regulatory Relief Act, to supplement our written statement of March 6, 2008. NCUA appreciates the opportunity for further comment.

Section 12 -- Encouraging Small Business Development in Underserved Urban and Rural Communities.

The Federal Credit Union Act presently excludes from the statutory cap on aggregate Member Business Loans (MBL) by a credit union loans made by two types of credit unions--those designated as "low-income" or as a Community Development Financial Institution (CDFI). 12 U.S.C. 1757(b)(2). This exclusion indirectly stimulates member business lending in "underserved areas" because most of the MBLs made by "low-income" and CDFI credit unions are made to members who reside or operate a business in an "underserved area."

Section 12 of H.R. 5519 would address member business lending to "underserved areas" directly, excluding from the MBL definition a commercial, corporate, business, farm or agricultural loan to a member when either--

- the member either resides or does business within an underserved area; or
- the loan is secured by real property located within such underserved area; or
- the loan will be used to operate a business located within such underserved area.

Section 12 extends the existing exclusion from the MBL definition directly to a range of loans associated with an "underserved area." This would allow all credit unions—not just those credit unions whose loans are excluded indirectly—to engage in member business lending to "underserved areas" without risk of that those loans will be counted against the statutory cap on MBLs by a credit union.

If NCUA can be of any further assistance to you or the House Financial Services Committee in answering questions or providing additional information, please let me know.

Sincerely,

JoAnn M. Johnson
Chairman

They Asked

CUNA Response to ABA's "Top 10 Questions"

March 5, 2008

10. If some credit unions wish to expand their lending to all types of businesses, why not have them convert to become banks as some credit unions have done?
Credit unions aren't seeking new lending authority – they simply object to a small part of the 1998 law that overturned roughly a century of making these loans without statutory limits. Why should a financial institution have to be a bank to be allowed to serve households and business?

Commercial banks have not had to abandon their bank charters to expand into new businesses like insurance, investment banking, mortgage loan brokerage, etc. And they're not proposing to abandon those charters as they attempt to expand into the real estate business.

9. How was the making of fraudulent construction loans in Florida by recently failed Colorado and Michigan credit unions consistent with the purpose of serving people of modest means?
When bankers figure out how to stop fraud they should share that secret with the rest of us. In the aggregate, credit union asset quality is considerably stronger than bank asset quality. Both credit union delinquency and chargeoff rates are lower than comparable bank benchmarks – this is true over many years and despite the fact that credit unions are more likely than banks to reach out to those of modest means.

8. Eastern Financial Credit Union was just forced to take a huge loss on a $30 million condo project. What was it doing funding a condominium development in the first place?
Banks and their mortgage banking and investment banking subsidiaries bear a large part of the responsibility for the current subprime debacle – the American public is now paying billions for banker misdeeds and our children will be paying billions for decades to come. That's not the first banker sin that we've paid for and it won't be the last. Eastern didn't cost the taxpayer one thin dime.

7. Why was Cal State 9 Credit Union issuing speculative home equity lines of credit that resulted in it being placed under conservatorship in November 2007?
In a sense every loan made by every financial institution is speculative. Lenders take risks: not all borrowers repay loans when they promise to do so. As noted above, the credit union movement's record in the aggregate is exemplary. In contrast, banks and their S&L allies have a long history of spectacular and costly missteps. In the 1990's the banking industry's bad loans not only overwhelmed capital buffers, but overwhelmed their federal insurance funds' ability to cover the losses. This ultimately stuck taxpayers with huge bills. Beyond the steps the Federal Reserve has recently taken, only time will tell what other government actions will be needed to address the subprime debacle and what the costs will be.

6. As tax-exempt institutions, shouldn't credit unions be concentrating more on fulfilling their mandate of serving people of "modest" means, rather than trying to expand loans to real estate developers?
Credit unions fulfill their mandate of serving those of modest means – and unlike banks, they do it without being told to do so. HMDA data proves this – it shows that year-after-year credit unions are much more likely than other lenders to approve loans to low & moderate income Americans. And credit unions make a greater percentage of their loans to low & moderate income Americans than do other lenders.

5. If credit unions in Massachusetts can comply with Community Reinvestment Act (CRA) requirements, why can't all credit unions?
The CRA of Massachusetts is tailored to the specific operations of Massachusetts credit unions. Plus, that's irrelevant. Credit unions can serve only their members, and they do a good job serving all their members. HMDA data shows credit unions make more loans to low and moderate income borrowers than CRA covered lenders do. CRA is just not necessary for credit unions.

4. The National Community Reinvestment Coalition (NCRC) found that credit unions are not doing as well as banks in serving low income and minority consumers. Since credit unions receive a valuable tax benefit, shouldn't they be required to measure their service to low- and moderate income consumers?
The NCRC analysis uses a flawed measure, the so-called "denial disparity ratio" to come up with the ridiculous conclusion that credit unions deny more low/mod income and minority applicants when the reverse is actually the case. In 2006 (latest data), credit unions denied only 18% of low & moderate mortgage applicants compared to a denial rate of 26.4% by CRA lenders. Of course, credit unions approved a greater proportion of low & moderate income applicants than CRA lenders did, 69.2% vs. 46.6%. As a result, a greater proportion of credit union loans (26.6%) went to low/mod income borrowers compared to only 21.8% at CRA lenders.

3. Presently there are 123 credit unions with over $1 billion in assets—making them larger than 92% of banks. At the same time, the number of small credit unions has declined by over 1,700 institutions since the beginning of 2002. Is this what Congress intended?
What Congress intended is that a strong, viable, democratically controlled, member driven, cooperatively structured credit union system provide services to American households. Size has absolutely nothing to do with it. Unlike the CEO of a bank of any size, the CEO of a large credit union – just like the CEO of a small credit union -- receives no stock options. Unlike the board members of a bank of any size, the board members of a large credit union – just like the board members of a small credit union -- generally receive no compensation. Unlike a bank of any size, a large credit union operates solely for the benefit of its members just like a smaller credit union. There are no stockholders in a credit union of any size.

Here are the facts: Today, banks hold a 94% share of financial institution assets and 99% share of financial institution business loans. These market shares have remained constant for well over a decade.

EACH of the largest three banks is bigger than the entire credit union movement.

Banking institution assets grew by $1.2 trillion in 2007 – about double the amount credit unions have grown since they began operating in the U.S. a century ago.

While the credit union movement is consolidating – so is the banking industry. The largest 100 banking institutions now control 72% of U.S. financial institution assets. These empire builders in the baking industry have increased their market share by more than 30 percentage points since 1992.

2. Federally insured credit unions have made nearly $5 billion in business loans to non-credit union members. How is funding non-member loans consistent with the purpose of credit unions?
Credit unions have NOT made $5 billion in business loans to non-credit union members. They have bought $5 billion in participations in business loans, mostly from other credit unions, made to members of those other credit unions. They do this because they are trying to satisfy member demand for these loans but they are bumping up against the arbitrary 12.25% cap and therefore must sell pieces of the loans they originate.

Small Business Administration (SBA) studies reveal that banking consolidation has been making it increasingly difficult for small businesses to obtain credit from commercial banks. In addition the banker's deep participation in the sub-prime debacle has caused them to significantly reduce credit availability in the current economic slow-down – precisely the time when many small business need credit.

1. Why should members of Congress co-sponsor H.R. 1537 if the credit union industry cannot answer these questions?
Now that we have completely answered all these questions all members of Congress should co-sponsor H.R. 1537 right away.