

**SEEKING SOLUTIONS: FINDING  
CREDIT FOR SMALL AND MID-SIZED  
BUSINESSES IN MASSACHUSETTS**

---

**FIELD HEARING**  
BEFORE THE  
**COMMITTEE ON FINANCIAL SERVICES**  
**U.S. HOUSE OF REPRESENTATIVES**  
ONE HUNDRED ELEVENTH CONGRESS  
FIRST SESSION

\_\_\_\_\_  
MARCH 23, 2009  
\_\_\_\_\_

Printed for the use of the Committee on Financial Services

**Serial No. 111-19**



U.S. GOVERNMENT PRINTING OFFICE

48-872 PDF

WASHINGTON : 2009

---

For sale by the Superintendent of Documents, U.S. Government Printing Office  
Internet: [bookstore.gpo.gov](http://bookstore.gpo.gov) Phone: toll free (866) 512-1800; DC area (202) 512-1800  
Fax: (202) 512-2104 Mail: Stop IDCC, Washington, DC 20402-0001

## HOUSE COMMITTEE ON FINANCIAL SERVICES

BARNEY FRANK, Massachusetts, *Chairman*

PAUL E. KANJORSKI, Pennsylvania	SPENCER BACHUS, Alabama
MAXINE WATERS, California	MICHAEL N. CASTLE, Delaware
CAROLYN B. MALONEY, New York	PETER T. KING, New York
LUIS V. GUTIERREZ, Illinois	EDWARD R. ROYCE, California
NYDIA M. VELAZQUEZ, New York	FRANK D. LUCAS, Oklahoma
MELVIN L. WATT, North Carolina	RON PAUL, Texas
GARY L. ACKERMAN, New York	DONALD A. MANZULLO, Illinois
BRAD SHERMAN, California	WALTER B. JONES, Jr., North Carolina
GREGORY W. MEEKS, New York	JUDY BIGGERT, Illinois
DENNIS MOORE, Kansas	GARY G. MILLER, California
MICHAEL E. CAPUANO, Massachusetts	SHELLEY MOORE CAPITO, West Virginia
RUBÉN HINOJOSA, Texas	JEB HENSARLING, Texas
WM. LACY CLAY, Missouri	SCOTT GARRETT, New Jersey
CAROLYN MCCARTHY, New York	J. GRESHAM BARRETT, South Carolina
JOE BACA, California	JIM GERLACH, Pennsylvania
STEPHEN F. LYNCH, Massachusetts	RANDY NEUGEBAUER, Texas
BRAD MILLER, North Carolina	TOM PRICE, Georgia
DAVID SCOTT, Georgia	PATRICK T. McHENRY, North Carolina
AL GREEN, Texas	JOHN CAMPBELL, California
EMANUEL CLEAVER, Missouri	ADAM PUTNAM, Florida
MELISSA L. BEAN, Illinois	MICHELE BACHMANN, Minnesota
GWEN MOORE, Wisconsin	KENNY MARCHANT, Texas
PAUL W. HODES, New Hampshire	THADDEUS G. McCOTTER, Michigan
KEITH ELLISON, Minnesota	KEVIN MCCARTHY, California
RON KLEIN, Florida	BILL POSEY, Florida
CHARLES A. WILSON, Ohio	LYNN JENKINS, Kansas
ED PERLMUTTER, Colorado	CHRISTOPHER LEE, New York
JOE DONNELLY, Indiana	ERIK PAULSEN, Minnesota
BILL FOSTER, Illinois	LEONARD LANCE, New Jersey
ANDRÉ CARSON, Indiana	
JACKIE SPEIER, California	
TRAVIS CHILDERS, Mississippi	
WALT MINNICK, Idaho	
JOHN ADLER, New Jersey	
MARY JO KILROY, Ohio	
STEVE DRIEHAUS, Ohio	
SUZANNE KOSMAS, Florida	
ALAN GRAYSON, Florida	
JIM HIMES, Connecticut	
GARY PETERS, Michigan	
DAN MAFFEI, New York	

JEANNE M. ROSLANOWICK, *Staff Director and Chief Counsel*

# CONTENTS

	Page
Hearing held on:	
March 23, 2009 .....	1
Appendix:	
March 23, 2009 .....	55

## WITNESSES

MONDAY, MARCH 23, 2009

Antonakes, Steven L., Commissioner of Banks, Division of Banks, Commonwealth of Massachusetts .....	16
Baker, Robert, President, Smaller Business Association of New England .....	29
Bland, Toney M., Deputy Comptroller, Northeastern District, Office of the Comptroller of the Currency .....	11
Clancy, Mary Ann, Senior Vice President and General Counsel, Massachusetts Credit Union League .....	38
Finn, Michael, Northeast Regional Director, Office of Thrift Supervision .....	13
Forry, Hon. Linda Dorcena, House Chairman, Committee on Community Development and Small Business .....	28
Geller, Scott, President, Middle Market Banking, Northeast Region, JPMorgan Chase & Co. ....	43
Koutoujian, Hon. Peter, House Chairman, Joint Committee on Financial Services .....	14
Mitropoulis, Iris A., President, Ventura Industries, LLC .....	40
Oddleifson, Christopher, President and Chief Executive Officer, Rockland Trust Company, and Vice Chairman, Massachusetts Bankers Association ....	31
Pelos, Perry, Executive Vice President, Wells Fargo Commercial Banking, Wells Fargo .....	39
Rosengren, Eric S., President and Chief Executive Officer, Federal Reserve Bank of Boston .....	5
Shea, Edwin T., Jr., President, Central Massachusetts Market, Bank of America .....	44
Sloane, Barry R., President and Chief Executive Officer, Century Bank .....	35
Slutz, David N., President and Chief Executive Officer, Precix .....	33
Thompson, Sandra L., Director, Division of Supervision and Consumer Protection, Federal Deposit Insurance Corporation .....	10

## APPENDIX

Prepared statements:	
Antonakes, Steven L. ....	56
Bland, Toney M. ....	69
Finn, Michael .....	78
Geller, Scott .....	84
Oddleifson, Christopher .....	88
Pelos, Perry .....	94
Rosengren, Eric S. ....	97
Shea, Edwin T., Jr. ....	121
Sloane, Barry R. ....	129
Slutz, David N. ....	133
Thompson, Sandra L. ....	138

## ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Additional information supplied by Toney M. Bland .....	149
---	-----



## SEEKING SOLUTIONS: FINDING CREDIT FOR SMALL AND MID-SIZED BUSINESSES IN MASSACHUSETTS

---

Monday, March 23, 2009

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

The committee met, pursuant to notice, at 10:02 a.m., in Gardner Auditorium, Massachusetts State House, Boston, Massachusetts, Hon. Barney Frank [chairman of the committee] presiding.

Members present: Representatives Frank; Capuano and Lynch.

Also present: Representatives Delahunt and Tierney.

The CHAIRMAN. If people will take their seats, we'll begin. This is actually a step forward for me in my career. I have been chairing the Financial Services Committee for 2½ years. My Republican friends have tried to claim that I actually was running the committee for 12 years. But this is the first time I have actually chaired a hearing in the Gardner, so I'm moving up. When I was in the State House under Speaker McGee, I never quite made the chairmanship. So getting to chair a hearing here in the Gardner is the next step in my career.

This hearing has been called in response to complaints that we have heard, those of us who are here, my congressional colleagues, and our State legislative colleagues who are represented here as well, from businesses in our districts, particularly small businesses, about their inability to get loans. Obviously, we do not get out of the economic crisis we face without businesses, particularly small businesses, being able to function. They cannot function without credit. Indeed, one of the points I have tried to make is, and I know one of the things that people wonder is, why we appear to be doing things that are to the benefit of financial institutions, and the second thing is that our country cannot function without healthy financial institutions providing credit.

The technical word for what they do is intermediation. The role of the financial institutions is to gather up large amounts of money from many people in small amounts and agglomerate it into large amounts so it can then be available in larger amounts to a few people who can use it constructively. This is a central function of our economy. And what we are trying to do is to restore the capacity of the financial institutions to do that. Their capacity has been impaired. Some of that impairment is their own fault—not entirely. Some have been damaged by the bad judgments of others. There

has been a problem in that there has been absence of rules in the system that has contributed to this.

But the point that we continue to make is that those who take the attitude that anybody who made a mistake should be allowed to suffer its consequences without help are condemning the whole society to suffer those consequences as well. We cannot get out of the economic problems we are now in without a healthy credit system, and we cannot get a healthy credit system without working with the people who are in the system.

We have tried, members here and others, to, at the same time that we offer the help, put some restrictions on that help. Indeed, while there have been some recent discussions about bonuses to AIG—and by the way, AIG was given a loan by the Federal Reserve System last September with no congressional input. The \$700 billion TARP program as it's called, the Troubled Asset Relief Program, came after that. The Federal Reserve has power under a statute dating from 1932, signed by Herbert Hoover—so its radicalism can't be blamed for this—which gives it the power to make loans. On the whole, they have exercised that power in a very constructive way. I think they made a mistake when they were new at it in September in not putting some constraints on AIG when they made the decision.

Subsequent to that, Congress got involved, and from the beginning of those discussions we, and particularly those of us here, have fought hard to put some restraints on the compensation that is paid, on the luxury entertaining, and we have also pushed for greater loans. That's the business that we are in today, talking about how do we increase the flow of loans from these institutions. But I did want to set it in that context.

We have two panels. We have a panel of regulators, and then we have a panel of lenders and borrowers. As is often the case, when those of us who hear the complaints about a lack of loans inquire as to why we don't get more loans, to some extent the banks will say it's the regulators' fault and the regulators say it's the banks' fault, and then everybody says it's awful. So the purpose isn't to lay the blame. It is to do away with any kind of obstacle.

So we are going to ask the regulators and we are going to ask the lenders to talk about how we can get them to work together so that we get a maximum flow of loans, and that's the purpose of this hearing.

I am joined by some of my congressional colleagues, two of whom serve on the Financial Services Committee, Mr. Capuano and Mr. Lynch. We also have Mr. Tierney and Mr. Delahunt.

So let me ask if any of my colleagues wish to make a statement, and I will go in order of seniority, which I think means Mr. Delahunt. That means how long he has served in Congress, not how old he is.

Mr. DELAHUNT. It is both, obviously. As I look to my left and I see Chairman Frank and I look to my right and I see Mr. Segel, your special counsel—

Mr. FRANK. He didn't get to be chairman, either.

Mr. DELAHUNT. That's true.

I have this sense of *deja vu*, because both Barney and Jim Segel and myself were members of the class of—well, we were elected in

1972 to the House of Representatives, and it's rather interesting to be here.

Let me just thank the chairman. I don't have an opening statement. I want to thank the chairman. I think this is a good hearing. I'm receiving, as I'm sure my colleagues are, a number of inquiries from particularly small businesses that have profound concerns about their inability to secure credit. It's my intention after this hearing to convene the stakeholders in my district and have a specific discussion in terms of what I can do, along with State and local officials, as well as the lenders and the appropriate regulators, to see if we can move things along. And Barney, thank you for the great work you do for the State and for the country. I will yield back.

The CHAIRMAN. My colleague, John Tierney.

Mr. TIERNEY. Thank you, Mr. Chairman. First of all, thank you for expanding your hearing out to include members who aren't on your committee. You're right in assuming that a number of people in our respective districts have made this point very clear, that they're small businesses and they're having an incredibly difficult time expanding, those who are lucky enough to have stayed in business, and some of them are barely staying alive despite having good collateral, and they're having a difficult time working with some of the financial institutions.

Mr. Chairman, I have been in this building before as a janitor in the 1970's cleaning up. The room doesn't look much different now than it did then.

But I'm not going to have a big long opening statement, other than to thank you for this hearing. I hope this gets us closer to finding out how it is we can free up some of those resources so people can keep the economy going. We'll take this information back with us as well. Thank you.

The CHAIRMAN. Next, we have two members of the committee. First, someone who is also familiar with the State House, Representative Capuano.

Mr. CAPUANO. Mr. Chairman, the only thing I can add is that usually every other time I have been in Gardner Auditorium, there have been people here with pitchforks and knives. I don't see any pitchforks. Any knives out there are hidden at the moment. I'm actually looking forward to a hearing that is educational and enlightening, and hopefully we'll be able to make things better for some of our small businesses here in Massachusetts.

The CHAIRMAN. Finally, another very diligent member of our committee, Mr. Lynch, from Boston.

Mr. LYNCH. Thank you, Mr. Chairman. I want to thank you for holding this hearing today, and I also want to thank our panelists for offering their assistance, especially Representative Tierney, Peter Koutoujian, who chairs the Banking Committee here in the House, as well as Linda Dorcena Forry, who also is here, and also an old hand, Senator Paul White, former Senator, also here today as well. Thank you for coming.

Mr. Chairman, just to give a snapshot of this situation: I have a small company in my district, New England Door. They only employ about 45 people, but they're a very profitable business in Canton, Massachusetts. They manufacture and sell garage doors. They

have a great business there. They had their line of credit terminated at the close of business on January 30, 2009, laid off all 45 employees. The business was forced to close because of the canceling of the line of credit. They're a very profitable company, and I think they offer sort of a snapshot of what's going on here in the State and across the country with the inability of good companies, solid companies, reputable, experienced companies, to access lines of credit.

I know the banks that cut that line of credit were fearful on their own account, and they didn't do it out of malice, they did it out of fear—and I must say, not necessarily irrational fear, given the economic climate. But this type of inflexibility and constriction in lending practices is just one example of many that my office has dealt with over the past 6 months.

And so we need to focus on getting that money that has been given to major lenders out into the community, out into these smaller businesses.

One of the troubling numbers that we have seen is that despite all of the money that has gone out to these banks, these larger banks, commercial and industrial lenders, the actual lending was down 7.3 percent from October through December of last year. And that's a troublesome aspect of this.

I'm very interested in hearing the testimony of the panelists today. I have to confess that I have to leave at 11:00; we have some bills on the Floor that I will have to manage down in Washington, so I'll be on the 12:00 shuttle. But I do want to again thank you all for participating in this, especially our panel of witnesses. I yield back the balance of my time.

The CHAIRMAN. All of us will be voting in Washington at 6:30 today, so we're going to move this along. But we did want to accommodate in Massachusetts this particular hearing. Let me echo what my colleague said: We are joined by two chairs from the House, Representative Koutoujian, who is chair of the House Banking Committee, and Representative Linda Darcena Forry, who has the community development side. We have been working closely with them and will continue to do that.

I will say, while Mr. Lynch referred to our former colleague, Paul White, as a Senator, he was also, in fact, a member of the House of Representatives class of 1972. So we will claim prior association with Mr. White.

With that, we will begin the testimony. What we have here are the bank regulators. There are a lot of bank regulators, Federal and State. Probably, if you were starting from scratch in creating a regulatory system, we wouldn't have so many. But we do, and we have spent a lot of our time urging them to work together, and I'm pleased to say that they do work together well, and they have been cooperative in this. So we are glad to have them, as well, of course, as our State bank commissioner, because there is what we call the dual banking system in the United States, which has both State and Federal regulators.

We will begin with a little longer statement from Eric Rosengren, who as president of the Boston Division of the Federal Reserve has a multiple set of responsibilities here, both as a regulator and as an economic policymaker. Mr. Rosengren.



**STATEMENT OF ERIC S. ROSENGREN, PRESIDENT AND CHIEF  
EXECUTIVE OFFICER, FEDERAL RESERVE BANK OF BOSTON**

Mr. ROSENGREN. Thank you very much, Chairman Frank, and thank you to the members of the committee and members of the Massachusetts delegation.

I'm going to be talking from a PowerPoint presentation, which is at the back of my testimony, so I'm going to be going through a series of charts rather than reading testimony. I think it will be helpful if you have the charts in front of you. The first chart will be Figure 1. It should be a blue chart, Federal funds effective rate, if everybody is with me.

First, I'm going to discuss some of the national programs that the Federal Reserve has been doing to try to improve business finance. And then I'm going to very briefly discuss the situation in New England.

As we're all aware, since August of 2007, financial markets have been severely disrupted. At the outset of this crisis, I and many members of the FOMC were quite concerned about how the financial crisis would spill over—

The CHAIRMAN. FOMC.

Mr. ROSENGREN. Federal Open Market Committee.

The CHAIRMAN. That sets the targets for interest rates? Just so people understand: That's the entity that sets the targets for interest rates.

Mr. ROSENGREN. That's correct. Since the outset of this crisis, we have been worried about how things would spill over to business finance. Obviously, it started in the subprime market, but spilled over to a much larger set of institutions and a larger set of problems.

Over the course of the last year-and-a-half it has been clear that the situation has gotten worse. If you look at the senior loan officer survey that the Fed conducts, it highlights the fact that it has gotten more difficult to get financing, and that got appreciably worse as we got into the fall of last year.

As we looked at the problems before getting financing, our first tool for the Federal Reserve is to move the Federal funds rate. And the chart that you have in front of you, the effective Fed funds rates, shows you how quickly the Fed funds rate went down between August of 2007 until December of last year.

I would highlight a couple of things with this chart. One is, when we bring down the Federal funds rates, it's not just to bring the rates down for banks. It's to bring short-term credit rates down that affect businesses. So the goal is that the prime rate, the LIBOR rate and other rates tied to the Fed funds rate will follow suit, not, clearly, in lockstep, but will come down as well. While they have come down, they obviously have not come down to the same degree as the Federal funds rate.

The second thing I would note is that currently the Fed funds rate is between 0 and 25 basis points. Effectively we're at zero. So our conventional way of conducting monetary policy can't be done because we have hit the bottom. The short-term rates have also come down along with the Fed funds rates. And I would note one thing in terms of Federal Reserve policy using conventional policy, and that is last year you will recollect that oil prices were quite

high, that commodity prices were quite high, and the Federal Reserve was widely criticized actually for bringing rates down as quickly as it did bring them down. I think it was a good policy that we brought the rates down as quickly as we did. We obviously didn't prevent the kind of problems that we have had, but I do think it has helped mitigate the problems to bring the rates down. I would say that many other central banks did not move with the same alacrity as the Federal Reserve.

As I have mentioned, if you turn to Figure 2, as we have gotten the Federal funds rate down to zero, we would have to move to less conventional policies. What Figure 2 does is provides the balance sheet of the Federal Reserve. This is normally something people don't spend much time on, but I think it's very important because during the course of doing the unconventional policy our balance sheet has expanded very substantially. I would highlight just a couple of the programs. We have a whole variety of programs I don't have the time to go over in any detail.

But if you look at two of the programs, if you look at the discount window lending and if you look at the central bank liquidity swaps, so it's the blue and the green, those are two of the areas that we have expanded the most. Now, what is the purpose of those two programs? The purpose of those two programs is to help with interbank lending. So one way of looking at those is they are ways of auctioning dollars to banks in the United States and dollars to foreign banks abroad that are active in the interbank rate, and the goal is to try to bring the interbank rate down. In particular, a rate called LIBOR, the London Interbank Offered Rate, is a rate that banks trade between each other. And so the purpose of these two programs was to bring that rate down.

And if you turn to Figure 3, which compares the LIBOR rate to the Federal funds rate, you can see that the LIBOR rate has come down quite substantially. It was very, very elevated during the end of the third quarter. It's now trading much closer to the Fed funds rate. This is a very important rate for businesses. The LIBOR rate is used as a base rate for a variety of lenders. LIBOR is used for a base rate when you have a subprime mortgage and you have a reset. LIBOR is used in many credit cards. In fact, my credit cards are tied to LIBOR. And many business loans are tied to LIBOR. So when you're bringing the LIBOR rate down, you're reducing the cost of funding for many of our businesses. So the purpose of these programs, while it was directed to the interbank rate, was really to get borrowing costs down for a wide variety of businesses, in that small, medium, and large businesses are all frequently borrowing at the LIBOR rate.

If you turn to Figure 4, as well as the interbank rate, we have had a variety of programs that have been designed to impact the general market conditions. General market conditions have been seriously impacted, particularly as we got into the fall. This just highlights two of those programs. One is the commercial paper funding facility, which provides an ability of organizations that are having trouble issuing commercial paper into the general market to issue it directly to the Federal Reserve. And the other is the AMLF program conducted out of the Federal Reserve Bank of Boston, which was intended to provide stability to asset-backed com-

mercial paper and to money market funds. I will describe that a little bit more in a minute.

For large businesses, large businesses frequently do borrow in the commercial paper market. It's an important source of short-term financing. But it's not just large businesses that benefit from commercial paper. Organizations like GE and many other organizations fund themselves in the commercial paper market and then lend to small and medium-sized businesses. So everything from inventories to floor plan financing to other types of financing are indirectly financed by organizations like a company like GE getting access to the commercial paper market. The commercial paper market and money market funds were badly disrupted. We created these programs to provide funding in the commercial paper market to try to make up for the fact that it was very difficult for issuers to issue directly into the market at that time.

You can see in the next chart, which looks at the asset-backed commercial paper, that, as with the LIBOR rate, the asset-backed commercial paper rates have come down quite dramatically, as have commercial paper rates more generally. So both those types of rates are now trading much closer to where the Fed funds rate is currently trading. This has an impact on businesses both directly and indirectly to the extent that they're dependent on the commercial paper market.

So again, these are programs to stabilize more general financial markets, but the purpose really is to get the cost of financing down to businesses small, medium and large.

If you turn to Figure 6, it highlights what was happening with our money market funds at the end of the third quarter of last year. Money market funds were very badly disrupted. Why do we care about money market funds? We care about money market funds because—most people think of money market funds on the deposit side, where they're finding their own funds. But on the other side of their balance sheet is a variety of short-term financing. In particular, they're buying a lot of the commercial paper market issued by firms. So if money market funds are stabilized, it helps to stabilize the commercial paper market.

The purpose of our AMLF program was to try to stabilize the money market funds. There were other programs that went into place as well, like the insurance fund. You can see that while there were very dramatic declines in money market funds in terms of funds flowing out of the money market funds in the third quarter, over the last 4 or 5 months, it has been quite stable. That's good news for commercial paper. It is good news for CD's. It is good news for the types of assets that these types of organizations are participating in.

Just this last week we started a new program, the term asset-backed securities loan facility, it's just in the process of starting up. It's intended to help with the securitization market. There has been virtually no securitization going on since the fall of last year. The securitization market is important because a lot of short-term credit was actually financed through issuing securities more generally. If you can't issue those securities, there is not an easy way for financial institutions to unload some of the short-term credit that they're getting. That affects student loans. That affects small

business loans. That affects credit card loans. So a wide variety of loans are impacted if we're not able to get the securitization market back up and running. So this program is designed to do that.

I think it's a little preliminary to know exactly how well that's going to work out. I'm optimistic it will work out and that it will be a successful program, but we're just at the initial stages. That's one reason I don't have a chart on it. It was just this last week.

Figure 7 highlights what has been happening in the mortgage market. Last week we had an FOMC meeting, and there was a very substantial announcement come out of that FOMC meeting. At the Federal Open Market Committee meeting, we agreed to purchase an additional \$750 billion in mortgage-backed securities on top of the \$500 billion that we had already purchased. We announced \$500 billion in November of last year. You can see that prior to that announcement, mortgage rates were trading around 6 percent. Since that announcement, they have been trading much closer to 5 percent. The hope is with this announcement that mortgage rates will fall even further.

Now, that not only helps homeowners who are able to refinance, it also helps small businesses. The reason for that is many small businesses actually depend on their home equity lines, on their regular mortgage loans. And so to the extent that people are able to refinance or get financing through their home, to the extent that we're able to stabilize housing markets, that's good news for many small businesses, because that's usually the first place that people turn when they're starting from scratch to start a business. The reason for that is financing costs on your home are usually much lower than costs from other types of sources. So while it's primarily focused on housing, it does have collateral benefits that are very important for small businesses.

Turning to Figure 8, getting more to the banking system: What this chart shows is, it separates out organizations nationally that are CAMELS Rating 1 and 2, the strongest institutions, from institutions that are CAMELS 3, 4, and 5, those institutions are weakest. It breaks up into four categories: Total assets; total loans; commercial/ industrial loans; and commercial and real estate loans.

What you can see is those institutions that are healthiest have tended to continue to expand lending. Those institutions that are most troubled have tended to decrease lending. It highlights the importance of trying to get our banking system restored to health.

6. Yes, Chairman Frank?

The CHAIRMAN. Just to reinforce the reason we're here, if people look at that chart, the largest drop has been in commercial and industrial loans. That's just a reinforcement of the point that has brought us here, that is, people trying to do business who—the decrease in commercial and industrial loans is by far the greatest. And that, of course, really underlines the need for this hearing. Please go ahead.

Mr. ROSENGREN. It highlights the importance of trying to get our banking system as well as our securitization system—

The CHAIRMAN. But it also, there is a disproportionate hit here on commercial and industrial loans, businesses, small businesses. There is no point in trying to sugarcoat this. Commercial real estate, not as bad. Total loans, not as bad. The heaviest hit here are

the commercial and industrial loans, and that is why we have to address this issue.

Mr. ROSENGREN. And just turning to the last chart, Figure 8: What this provides is the CAMELS 3, 4, and 5 nationally and in New England. So you can see nationally over the last year there has been a dramatic increase in our most troubled banks. It has gone from roughly 6.3 percent to over 13 percent, our CAMELS 3, 4, and 5 nationally. You can see in New England it's roughly 5 percent.

The CHAIRMAN. Have you explained what CAMELS means to people who are not in the banking business?

Mr. ROSENGREN. It's a way of measuring the financial strength of banking institutions, so it's Capital, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to interest rates.

The CHAIRMAN. CAMELS is an acronym for these things?

Mr. ROSENGREN. It's an acronym for how we rate banks.

You can see that in New England, we don't have as many troubled institutions as other parts of the country. This is one time where New England hasn't been as badly impacted in a recession as some other regions. Obviously, places like Miami, San Diego, Arizona, and Las Vegas are areas where they had many more construction loans and many more problems as a result in their banking system. While we have more healthy banks, obviously we have some banks that are having difficulty, and obviously if the economy gets worse, it's going to be a problem for even some of the institutions that are currently healthy.

So in conclusion, I would just highlight a couple of things. Initially, the Federal Reserve used conventional monetary policy to lower interest rates. The purpose of that is to lower interest rates not only for households and other types of financing, but also for small, medium, and large businesses. As we got to the floor on the Federal funds rate, we have had to turn to alternative policies. Those alternative policies have looked at a variety of different ways that we can bring interest rate spreads down. Most of those programs are designed to try to provide financing that will be important for businesses. Most of these programs will hopefully help the situation in terms of reducing the cost to businesses and hopefully providing greater availability than we would have in the absence of those programs. Thank you.

[The prepared statement of Mr. Rosengren can be found on page 97 of the appendix.]

The CHAIRMAN. Thank you. We will get to questions. But I do want to emphasize: Having interest rates go down is a good thing, but not to people who can't get loans. And that figure you gave showed the commercial/industrial loans have been hurt most; there has been the biggest drop. That's the focal point of this hearing. We need to figure out how we can allow these job-generating businesses to get the advantage of these lower interest rates.

Next, and I appreciate her coming here, because we were on the same plane yesterday, is Sandra Thompson, who is the Director of the Division of Supervision and Consumer Protection of the Federal Deposit Insurance Corporation.

**STATEMENT OF SANDRA L. THOMPSON, DIRECTOR, DIVISION  
OF SUPERVISION AND CONSUMER PROTECTION, FEDERAL  
DEPOSIT INSURANCE CORPORATION**

Ms. THOMPSON. Chairman Frank and members of the committee, I appreciate the opportunity to testify on behalf of the FDIC regarding the availability of credit to small and medium-sized businesses in Massachusetts.

The FDIC is acutely aware of the—

The CHAIRMAN. Ms. Thompson, can you move the microphone?.

Ms. THOMPSON. The FDIC is clearly aware of the challenges faced by banks and their customers during these difficult economic times. Liquidity in the marketplace has been adversely affected since the credit disruption began in mid-2007. Lack of liquidity and the slowing economy are having a profound effect on the availability of loans nationwide for both businesses and consumers.

The focus again is on the ability of borrowers to repay their loans, which means determining that loans are affordable and sustainable over the long term. Few would argue that we should return to the loose lending standards of recent years that have resulted in so much damage to the financial system.

While prudent underwriting may mean that some borrowers who received credit in past years will have more difficulty receiving it going forward, it should not mean that creditworthy borrowers are negatively impacted.

Unfortunately, in returning back to basic lending standards, there is a risk that some lenders will become overly risk-averse. As bank supervisors, we have a responsibility to assure our institutions, regularly and clearly, that appropriately underwritten loans are encouraged. The financial data for banks in Massachusetts and the Northeast in general reflect a lower risk profile, fewer delinquencies, and nominal asset losses, in large part due to more prudent underwriting standards. The institutions here that did not take undue risks have nonetheless been affected by the national credit disruption as liquidity has become scarce.

With regard to the supervisory role, in the period leading up to the credit market disruption, regulators should have been more aggressive in their supervisory approach to certain concentrations of credit risk that put us where we are today. The FDIC understands the critical role that credit availability plays as the lifeblood of the national economy, especially for small businesses. A number of discussions have taken place with the FDIC supervisory management team to underscore the FDIC's proper role and to raise sensitivity to issues of credit availability. FDIC senior management has reiterated that examiners should be encouraging banks to continue making good loans and work with customers who are facing financial difficulties. Prudent, responsible lending is good business, and it benefits everyone.

Community banks are uniquely equipped to meet the credit needs of their local markets. They have a proven tradition of doing so through good times and bad. And most community banks here in Massachusetts have largely avoided the undue concentrations and reckless lending practices that led to the present issues in the financial sector.

Massachusetts community institutions continued to grow their loan portfolios in 2008, although at a slower pace than at the peak of the expansion. Surveys of small businesses were conducted by the National Federation of Independent Businesses last fall and early this year. Most of them reported that finance and interest rates were not the problem, that the economy and poor sales were the biggest problem. Most of the institutions here in Massachusetts have a solid capital and solid funding base, and they will be in a good position to help finance the recovery. The FDIC believes that banks should be encouraged to make good loans, lenders should work with borrowers who are experiencing difficulties during this challenging period whenever possible, they should avoid unnecessary foreclosures, and they should continue to ensure that the credit needs of their communities are fulfilled.

Thank you for the opportunity to testify today, and I would be happy to answer any questions.

[The prepared statement of Ms. Thompson can be found on page 138 of the appendix.]

The CHAIRMAN. Thank you, Ms. Thompson. Next, we have Toney Bland, the Deputy Comptroller for the Northeast District of the Office of the Comptroller of the Currency.

**STATEMENT OF TONEY M. BLAND, DEPUTY COMPTROLLER,  
NORTHEASTERN DISTRICT, OFFICE OF THE COMPTROLLER  
OF THE CURRENCY**

Mr. BLAND. Chairman Frank, members of the committee, and members of the Massachusetts delegation: Thank you for this opportunity to talk to you today about the OCC's role in ensuring availability of credit for small and mid-sized businesses in Massachusetts. I have been a national bank examiner for 28 years, and I have served in a variety of positions in the field and in our Washington, D.C., headquarters before taking my current responsibility as Deputy for the OCC's Northeastern District. In that capacity, I am responsible for the oversight of nationally chartered community banks in the District of Columbia and 14 States, including the Commonwealth of Massachusetts. The OCC has long recognized the importance of small and mid-sized businesses to the overall health and vitality of our economy, and we believe the Administration's small business and community lending initiative will have a positive impact on the ability and willingness of commercial banks to lend to that important sector.

Like much of the United States, Massachusetts is coping with serious economic challenges. Consumer-loan delinquency rates are rising as home prices and labor markets decline, and commercial real estate is also suffering. Many Massachusetts firms have responded to the downturn by scaling back their operations. The vast majority of these small businesses are still fully viable. They continue to produce goods and services, and they still need access to credit.

As bank regulators we recognize the important role that credit availability plays in the viability of these companies, and we have encouraged banks on an interagency basis to meet the credit needs of their small and mid-sized business customers. Yet in times of recession, bankers may be more cautious about the level of credit risk

they assume and more selective in the loans they choose to make, especially if they find their capital or access to funding constrained. This is one reason why we stress the need for strong risk-management systems, capital and liquidity planning.

Fortunately, most banks have such systems in place and remain well-positioned to meet their customers' demand for credit. Indeed, our examiners indicate that most community national banks in Massachusetts expect to see modest growth in their small business loan portfolios this year. Various Federal and State programs, including the Small Business Administration loan-guarantee program, can be especially valuable in this environment in helping bankers meet the credit needs of small and mid-sized businesses.

In evaluating the underwriting and quality of small business loans, the OCC views government guarantees or support provided to these programs as effective mitigants of credit risk. In fact, our guide to examiners specifically states that those portions of credit having a government guarantee should usually be accorded a pass rate. National banks with strong encouragement of the OCC are active participants in these programs. The OCC also encourages lending to small and mid-sized businesses through our evaluation of the bank performance under the Community Reinvestment Act, or CRA, our extensive community affairs activities, and our formal outreach programs.

I know that some people believe that CRA contributed to the current credit problems. We at the OCC disagree. CRA encourages each insured financial institution to help meet the credit needs of the community in which it operates, but it does not ask banks to make bad loans. In fact, CRA lending has been a profitable business for most banks and a business that has had very significant benefits for communities across the country. The OCC's CRA examination process ensures that a national bank's lending to small and mid-sized businesses is carefully assessed and subject to public scrutiny and that these activities have a direct influence on the institution's CRA rating. This creates an additional incentive for banks to lend to creditworthy small business borrowers.

The OCC's community affairs department provides important information and resources to examiners, bankers, industry associations, and community groups. Ten OCC community affairs offices are located in major metropolitan areas across the country, including Boston, and these individuals actively promote existing programs and innovative ideas for advancing small business lending.

We also have a number of activities and publications specifically aimed at increasing awareness of programs that promote lending to small businesses. For example, the OCC and other bank regulatory agencies regularly convene seminars for Massachusetts financial institutions, focusing on prudent lending and promoting bank involvement in Community Reinvestment Act activities, including small business lending. My written testimony contains more information on these and many other OCC efforts to advance small and mid-sized business lending.

Let me close by emphasizing that the OCC will continue to support and encourage lending to small and mid-sized businesses in Massachusetts and throughout the country. Thank you. I look forward to your questions.



[The prepared statement of Mr. Bland can be found on page 69 of the appendix.]

The CHAIRMAN. Next, Mr. Michael Finn, who is the Northeast Regional Director for the Office of Thrift Supervision.

**STATEMENT OF MICHAEL FINN, NORTHEAST REGIONAL  
DIRECTOR, OFFICE OF THRIFT SUPERVISION**

Mr. FINN. Good morning, Chairman Frank, and members of the committee. I appreciate the opportunity to appear on behalf of the OTS this morning to discuss ways to expand credit to small and medium-sized businesses in Massachusetts and throughout the country.

I would like to begin today by thanking you, Mr. Chairman, for your leadership during the House passage of bills supported by OTS in two consecutive Congresses that allowed thrifts to expand lending to small business, which is fully consistent with the thrift charter and consumer and community lending. We stand ready to work with you again this year and to see these important changes enacted into law.

OTS supervises 19 savings institutions with home offices in the State of Massachusetts. They range in size from \$25 million in total assets to \$2.5 billion. At the end of 2008, these institutions collectively held about \$10.5 billion in assets.

For OTS-regulated thrifts, total loan originations and purchases declined 11 percent from 2007 to 2008. However, in several categories of loans, including small business loans, the numbers actually increased during that period from 2007 to 2008.

Nevertheless, the current law limits the ability of thrift institutions to extend credit to small businesses, and many thrifts are unable to achieve efficiencies of scale that might make small business lending profitable.

The Home Owner's Loan Act, which places a cap on commercial loans at 20 percent of the savings institution's assets, states any commercial loans beyond 10 percent must be in small business. The legislative proposal that OTS supports would lift the cap on small business loans entirely and increase the cap on other commercial lending from 10 percent to 20 percent.

We are also working on a new proposal within OTS to provide additional flexibility for savings institutions by redefining small business loans to replace the current dollar limit, which is set at \$2 million, with a standard that will reflect more changes in economic conditions, either based on geography or institution size. OTS will also propose a change that would increase the permissible community development investments for OTS-sponsored institutions.

These changes would be consistent with the spirit of the thrift charter as a consumer and community lender and would make credit available to more neighborhoods and businesses. The changes would also diversify the thrift business model to make institutions more resilient when a slump hits one single sector of the economy, such as we have seen in the housing market.

Thank you again, Mr. Chairman, for inviting me here today. I look forward to responding to your questions.

[The prepared statement of Mr. Finn can be found on page 78 of the appendix.]

The CHAIRMAN. Next our colleague in government, the House Chair of the Banking Committee, Peter Koutoujian.

**STATEMENT OF THE HONORABLE PETER KOUTOUJIAN,  
HOUSE CHAIRMAN, JOINT COMMITTEE ON FINANCIAL SERVICES**

Mr. KOUTOUJIAN. I was hoping my testimony would start with a bang, but—

Chairman Frank, Congressman Capuano, and Congressman Lynch, and a special thanks as well to Congressmen Tierney and Delahunt, who are not even a part of the committee but care enough to learn what is going on, especially here in Massachusetts, thank you very much.

I'm going to speak and the overarching arc of my speech will be regarding the strength and soundness of Massachusetts State-chartered banks, the challenge of finding ways to help small businesses obtain loans, and some closing comments and approaches as well.

I have sort of derived this information through myself and my staff's investigation of not only statistical information bearing on Massachusetts but also in speaking with the banking and the business community as well.

Topic 1, strengthen soundness of Massachusetts State-chartered banks: The banking industry facing economic challenges is due in part to these issues surrounding subprime mortgage loans. Though in Massachusetts we are not immune from the ailments encountered, these State-chartered institutions are faring better than their counterparts in other States. The reasons? There was a limited involvement in some of the subprime market. There was an exercise of due diligence and safety and soundness procedures in issuing loans that in some cases might have been greater than in other places.

As of September of 2008, the Massachusetts bank outstanding loans were approximately at \$173.8 billion, and as of December of 2008, State-chartered institutions' reserves to noncurrent loans and loans in arrears and leases was 96.45 percent and the United States was at about 68 percent. I think this shows that we have a strong and stable reserve system here in Massachusetts. Also, the noncurrent loans and leases to total loans and leases was .97 percent and the United States was 2.64 percent, almost 3 times as much.

And then the State-chartered institutions' net charge-offs to loans and leases or losses was .16 percent and the United States was 1.1 percent—again, a significant difference.

The results of these statistics show that Massachusetts State-chartered institutions fare better than the U.S. average; and also in speaking with local representatives of some of the banks, we are hearing that most State-chartered community institutions have few if any foreclosures, as some have indicated.

With regard to savings, we know that much of our sort of economic concerns are as a result of people saving more. Massachusetts State-chartered banks have seen an increase in savings de-

posits due in part to consumers moving money from riskier investments to more stable investments, such as money market and CD accounts, possibly—no hard statistical data—possibly as much as 6 percent. While FDIC covers deposits up to \$250,000, State-chartered banks and credit union deposits are covered in full, which could also be a reason that people are pulling their money out of other institutions and placing it into the State-chartered, bringing that number up to 6 percent.

Finding a way to help small business obtain credit is part of, I think, our greater challenge here. There is a desire by banks to resume lending to business, but current economics make credit decisions more difficult and complex for commercial lenders. There is a key factor—a key factor in a lender's decision is the borrower's ability to pay back the loan. Such determination is made by evaluating the strengths of the borrower's business plan as well as the overall market for the product. In this economy, where markets are contracting and consumer spending is down, the complexity of this determination becomes more difficult. Another factor affecting credit availability for small to mid-sized businesses in Massachusetts is the decline in value of real estate or capital equipment, which may prevent a business from accessing a lower cost of debt for refinancing. Current economic conditions have forced a lot of nonbank lenders as well to pull out, a major source of credit for business in the last decade. And larger banks, a major source of funding to mid-market companies, have curtailed lending to address bankwide risk concerns. Some other feedback from the business community is that they have said that they have been receiving feedback—excuse me, that they had been receiving feedback of businesses being denied loans, as well as a feeling among some businesses that applying for a loan is simply not worth it due to the belief in a lack of loan availability, based on many media reports. Another business community representative recognizes that lending has been tough, especially in certain sectors such as construction, but is receiving some feedback that there has been a small increase in lending in the last few weeks and is hoping that the trend will continue.

According to the Associated Industries of Massachusetts, the business confidence index fell to an all-time low in February, to 33.3 points, 3 points below December's previous record. It's also AIM's, or Associated Industries of Massachusetts's, feeling that many companies are simply not applying for loans. Companies are in a pullback mode, trying to preserve their resources and ride out what they perceive to be an economic downturn. This is much like consumers who are now also contracting their own spending and enhancing their own savings.

I think also the fact that the most recent data in Massachusetts shows the jobless rate climbing to 7.8 percent, creating more unemployment, perhaps less opportunities for companies to market and sell services and wares, is also something of great concern to them.

I think that, as I close my testimony, there are items that our committee is willing to work and desirous to work with the banking community and the business community to identify if there is anything legislatively and, something we're hoping to learn today, if

there is anything legislatively hindering what they're hoping to do, restrictive statutes or regulation.

I also think, Mr. Chairman, that we have to be considerate—and I don't know what the answer is to this yet, but I'm interested in exploring this. We need to be careful, I think, with regard to Federal banking regulation and the fact that the State has no say whatsoever in that. So while we may be hindering by too much regulation on one side, perhaps we're not helping by having some say in what's going on with regard to Federal banks.

I think also we can silo—I hate this new word—information that we need to expand. It's not just about banking. It's sort of like “shovel-ready.” For me, it is a new word we have to use too much now. But we need to be thinking about business banking and many other markets and opportunities. I think that we need to work together, as Congressman Frank said recently, the Federal, the State, and the regulators, all working together to help all the industries here in Massachusetts. Thank you very much.

The CHAIRMAN. Thank you. Commissioner Antonakes.

**STATEMENT OF STEVEN L. ANTONAKES, COMMISSIONER OF BANKS, DIVISION OF BANKS, COMMONWEALTH OF MASSACHUSETTS**

Mr. ANTONAKES. Good morning, Chairman Frank, and Congressmen Lynch, Capuano, Delahunt, and Tierney. My name is Stephen Antonakes, and I serve as the commissioner of banks for the Commonwealth of Massachusetts. I commend you, Mr. Chairman, for scheduling this timely hearing on the credit needs of small and mid-sized businesses. The ongoing success of our businesses and their access to credit is critically important to both the Massachusetts and our national economy.

The two primary points of my testimony are that local financial institutions continue to lend and that the Patrick Administration is working to encourage public/private collaboration to assist businesses during these times. Certainly the well-chronicled difficulties being experienced by some of our large nationwide money-center banks have resulted in the restriction of credit.

However, the experience of community banks and credit unions has been strikingly different. I have just completed a series of roundtable discussions across the Commonwealth and have heard from hundreds of bank and credit union officers on their perspectives of what is happening on Main Street. Many Massachusetts State-chartered institutions report increased lending as a result of reduced competition from some of their largest bank competitors. This is yet another example of how our diversified and decentralized system of banking continues to serve our Nation well.

This contention is supported by our analysis of FDIC call report data, which shows that Massachusetts State-chartered community banks' balances for commercial real estate loans and commercial/industrial loans increased 14½ percent from 2007 to 2008 and nearly 26.9 percent from 2006 to 2008. The Massachusetts community banking system and credit union movement remain fundamentally sound and continue to serve as sources of strength.

I also note that the opportunity for the U.S. Treasury to provide TARP funds to Massachusetts banks has been significantly re-

stricted. More than 5 months after the largest banks were provided TARP funds, no term sheet has been released for mutual banks. Massachusetts has the largest percentage of mutual banks in the country. Accordingly, TARP funds are still not an option for the majority of community banks operating in the Commonwealth. This has had the effect of unnecessarily restricting increased lending opportunities that might otherwise be available through the use of TARP funds.

Finally, events beyond the control of community banks have and will continue to affect their ability to lend in the future. The conservatorship of Fannie Mae and Freddie Mac as well as proposed significant deposit insurance assessment increases will significantly impact the earnings of State-chartered community banks and in the case of the ongoing issues in the corporate credit union system State-chartered credit unions as well. It is important to note that these actions will not threaten the capital base of any Massachusetts State-chartered bank or credit union. However, the availability of credit to consumers and businesses alike will be reduced across-the-board as a result of these increased operating costs.

In sum, the ability of local institutions to continue to lend will not be impacted by their bad acts but by the bad acts and aggressive risk-taking of others.

Massachusetts has also had a proud history of attempting to leverage partnerships to increase opportunities for small businesses to flourish. The Massachusetts Small Business Capital Access Program, or CAP program, involved an initial \$5 million State appropriation in the early 1990's to provide a cash collateral guarantee or credit enhancement to small business loans. Today, over 100 banks participate in the CAP program.

Since the banks utilize their own underwriting criteria and directly provide the funding, the loans are simpler to originate than loans made through SBA. Participating banks also receive credit under the Massachusetts Community Reinvestment Act. In 15 years, a total of \$10 million in State funding has been leveraged into \$241 million in loans to over 3,800 small businesses, with an average loan amount of \$51,000 and loans as small as \$1,000. CAP program loans have helped create or retain 26,000 Massachusetts jobs and brought in over \$100 million in payroll taxes to the Commonwealth.

The Massachusetts Banking Partners small business loan program provides greater access to reasonably priced credit and banking services to small businesses as well as access to vital business assistance. The program recognizes that many startup and small business owners need help with recordkeeping, general management, and preparing a business plan and financial statements. The Banking Partners program matches small business owners receiving technical assistance and training with small business assistance providers with participating banks.

In addition, the Patrick Administration is currently working to develop additional programs to further assist small and mid-sized businesses having difficulty accessing credit. As we continue to work our way through the current economic downturn, small and medium-sized businesses will face increasing challenges. I thank

you for the opportunity to testify today. I would be happy to answer any of the committee's questions. Thank you.

[The prepared statement of Mr. Antonakes can be found on page 56 of the appendix.]

The CHAIRMAN. To begin, Mr. Antonakes, two of the issues that you mentioned that are relevant: First, we are working closely with the FDIC and the Chair, Sheila Bair, to reduce that increased assessment. If the legislation passes the House and, suitably amended, passes the Senate, and the lending authority of the FDIC is sufficiently increased, that increased assessment will be cut by two thirds. Instead of going from 6.3 percent to 20 percent, it will go from 6.3 percent to 10 percent. And we have the Chairwoman's word on that. That's pending. We are very optimistic that will happen. So that is going to happen.

Secondly, your mentioning the problem of Massachusetts suffering disproportionately when there is not a means of getting Federal TARP money to mutual banks: A letter will be on the Secretary of the Treasury's desk tomorrow signed, I believe, by all the members of the Massachusetts delegation, including those of us on the committee, insisting that be done very promptly. Apparently, I'm informed by my staff that—we have expressed an interest in this—they are having difficulties finding what type of collateral to take since mutual banks don't have stock. We will find something. I will be talking to the Secretary of the Treasury today. I guarantee we will get very prompt action and the funds will be made available to the mutual banks.

Now let me ask you—I apologize, I should have structured this differently. I should have begun with the businesses, because here's the problem, frankly: When we get to you, then we wonder why we're here, because everything is good. But everything isn't good. It doesn't mean people are bad, but there are problems. We hear from a lot of businesses that they are not able to get loans. I have a business in the New Bedford area, a very important functioning business, that is having problems getting their credit extended. So we know there are problems here.

What I should have done is had the businesses come first and hear their complaints, and then the banks would explain in the second panel what they're trying to do but, and then you would have come last, because you would have heard businesses complaining, and the banks, frankly, saying that, yes, part of the problem is the regulators. And you have a dual mandate. You have as members of the Federal Government the mandate of getting the economy going, but you also have the safety and soundness mandate. People sometimes overlearn lessons.

So I'm going to ask the bank regulators, the three Federal bank regulators, less so the Federal Reserve—and this does come from both the large banks and the community banks—I want you to respond to the charge we get that while you are for lending in general, some of the people who work for you are sometimes not for lending in particular. We can't make loans in general. I mean, we do have those numbers that Mr. Rosengren showed us that commercial and industrial loans have been disproportionately hit, and we have people who come and show us balance sheets—we're not experts—that seem to us to justify loans. So what are you doing

to make sure that your examiners don't err on the side of safety and toughen up too much? Ms. Thompson, let's begin with you.

Ms. THOMPSON. I would admit that we do hear complaints all the time about this very issue. The FDIC as insurer, we insure the deposits of over 8,300 institutions. But we are the primary Federal regulator for just over 5,000 institutions, and most of the institutions we supervise are community banks. What we're finding, and particularly in Massachusetts, is that as some of the larger banks are pulling out, some of the community banks, especially the ones here in the Commonwealth, are regaining access to borrowers that they may have lost for competitive reasons prior to the credit issues in the economy.

Two things: One, we supervise over 133 institutions here in Massachusetts, and we have noted that their lending has increased. And we have specifically told our examiners that they are to strike a balance. We want to encourage institutions to make loans, to make responsible loans. There are 30 institutions in Massachusetts that have applied for TARP funds. As mentioned before, 18 of them are mutual, three are C corp., and 9 are public. And it's interesting to note that when the TARP was first implemented in October, it was for the publicly held companies, and we have been working diligently with the OTS to try to come up with a term sheet to help get the mutuals in play for the TARP money.

There have been some allocations—I think there have been 12—10 that have been given, 10 awarded to—

The CHAIRMAN. Ms. Thompson, two things: First, I want to see that term sheet. It doesn't have to be perfect. The term sheet people can understand the terms under which mutual banks will be able to get TARP funding. The Secretary is going to be coming back for some more help. I don't know how he would expect myself, Mr. Capuano, Mr. Lynch on the committee and the others to be responding to requests for more authority if a significant chunk of the banks in our State can't get it. So please understand that is not now a nice thing to happen; it's a prerequisite for further cooperation.

Secondly, let me ask you, and I'll ask all the others as well: We get complaints from banks, I will get a complaint from a constituent—it's delegated. I'm not a lending officer. I don't want to be. But I have a responsibility to ask: I was told, "Yes, we would like to do that, but we're worried about the regulator." I want from you and staff a way I can get those complaints with sufficient anonymity. Because you understand a banker doesn't want to sign his name to a complaint about a regulator, human nature being what it is. But we really need a complaint process. I appreciate you're trying. You have a lot of people under you.

Here's the deal: I think a lot of people—and it's not their fault—who work for you figure they are more likely to get in trouble if they approved a loan that went bad than if they denied a loan that didn't happen and that should have happened. I appreciate that. I do want to move on. Do you have anything further to say?

Ms. THOMPSON. I offer our ombudsman, to the extent people want to work out a complaint—

The CHAIRMAN. Ms. Thompson, we have heard—as I look at the complaints, many of them have been from the larger institutions,

where the Fed obviously would have a role. What is the Federal Reserve doing to see that there is not overrestriction, in our concern for safety and soundness.

Mr. ROSENGREN. I would agree with your observation that I think a disproportionate number of the problems are at our larger institutions. As the chart that I showed for New England, we have a lot of community banks that are actually well capitalized and are able to provide lending, but they can only do it up to the capacity of their capital. So for many small businesses, I think there is access to our community banks. And in terms of the advisory councils that I—

The CHAIRMAN. Don't tell me the good stuff. Talk about the bad stuff.

Mr. ROSENGREN. In terms of the bad stuff, for the larger institutions, they do have more capital issues than our smaller institutions. Some of the issue has to be that we have to get them restored to health. That's part of the purpose of some of the TARP funding. We also need to get some of their bad assets off their balance sheets. Secretary Geithner was talking about that this morning, on ways to try to remove bad assets. I think both of those are critical to getting the large banks in a position where they feel comfortable lending to medium and large businesses.

The CHAIRMAN. If in fact the plan the Secretary is announcing, with getting private capital and public capital together to try and bail the banks out with some of the things that went bad, but in a way that promises that there will be some public return if things get better—if that were to work in a couple of months, could we look for an increase in lending? I think these people need to know that if in fact there is this program of buying the toxic assets—which is a very bad term. I think the opposite of a toxic asset is a nurturing liability, if we're inventing terms. But if we are able to help the banks divest of some of the bad decisions that are weighing on them or the bad results, could we count on that leading in part to increased lending?

Mr. ROSENGREN. I think it will improve the situation. It won't happen overnight. It takes time for both the bad assets and it takes time for the good bank that's left to start thinking about future prospects of the problems in the portfolio.

The CHAIRMAN. Please advise the good banks that will be left that they should start thinking about it now. Seriously. If it is sequential, it's going to be a problem. They know what's coming. They should start looking at these things now, start the conversations now, because I will tell you, if in fact we go ahead with this—and as I understand it, the Secretary is not asking for further congressional help to implement this—but if this goes forward, and I think it is necessary—but if it doesn't pretty soon start to produce some results, then the anger is going to be such that we're going to lose some capacity to do these things. Mr. Bland.

Mr. BLAND. Chairman Frank, back to your original question about our examiners. As Ms. Thompson said, it is a balancing act. One of the things we have to do is periodically check in with our examiners and make sure that they understand the environment we're in and what are the right calls to make. We do that constantly, with meetings and also instructions that go out to them.



We realize that, from the past, we make sure that we're making calls that are consistent not only within Massachusetts but around the country. And that is one of the big things we learned especially from the 1980's that is very important, to have some oversight and some quality control around decisions that we make.

The other thing I want to mention is, in terms of improvement, I think the Administration's proposal on small business lending will be very important. I think we should see some traction starting fairly soon. On June 30th, the regulatory agencies will start tracking the Small Business Administration's small lending activity. That should be important.

The CHAIRMAN. The reason being that if the banks then make loans that qualify there, they get a guarantee that should make it easier for them—

Mr. BLAND. Up to 90 percent. My last point is, in terms of customers who would like to anonymously lodge complaints or inquiries into situations with their banks, we have a customer assistance group that allows them to call in—

The CHAIRMAN. By "customer," you mean the banks you regulate?

Mr. BLAND. Banks we regulate, but also a customer of a bank.

The CHAIRMAN. I appreciate it. Mr. Finn.

Mr. FINN. Chairman Frank, I appreciate your attention on mutual institutions. As you know, OTS has a very large mutual bank population, and it has been a difficult issue.

But beyond that, in talking about our approach towards supervision, just this past week, I was up here in Boston meeting with my Boston staff and on Friday with the rest of our regional staff. We're trying to send clear, steady messages to staff to be prudent regulators, to identify concentrations in risk early, so that institutions can deal with them in a capable way. If you wait too long, it becomes a problem where you need very severe actions to bring about the right change.

So we are closely looking at risk. But we also talked about the availability for creditworthy borrowers. The Agency put out a statement back in, I think it was November of 2008, and while that didn't have binding rules, it's a message that needs to be reinforced to regulators.

The CHAIRMAN. The regulators together, we have heard some acronyms here. You've been spared one of the most unpleasant-sounding ones, I think, which is what these people when they get together call the FFIEC, the Federal Financial Institutions Examination Council. We have most of the members of the FFIEC here today.

But there have been some statements. Let me say this, and then I'm going to move on to my colleagues: We're part of the problem, we the politicians. We tend to be somewhat too harsh and go after the mistakes. As an example, AIG, a lot of problems with the bonuses they should not have been granted, and the retention bonuses I think were frankly a form of extortion—although I do want to say, the people who got those, we're not talking about Madoffs here, we're not talking about criminals. I think some of the vitriol needs to be toned down. Bad policy doesn't mean they are horrible people. We need to be able to control the policy.

But in fairness to the Federal Reserve and Secretary Paulson, who was there under the Bush Administration as well, some of the people who have been very critical of the decision to deal with the debtors of AIG were equally critical of the decision not to deal with the debtors of Lehman Brothers. Lehman Brothers was allowed to go under and the debtors got no help. AIG, the debtors got help. There were people equally critical of both. What we need to do is get a system so we can avoid both of those extremes.

I want to say this: Please convey to your examiners, all of you who have examiners—I am chairman of the committee. I talk to all of the members of this committee. I know in the past they have been afraid that if there were failures they would be attacked for laxity. I will work very hard to say, look, we are asking for there to be more balance. I understand, if there is more balance, that means more good loans being made and inevitably it means more bad loans being made. There is no way I can tell you to have your people approve only good loans. We hope to get the percentage fairly high.

I will tell you that I will urge my colleagues to understand that. We urge you to take a little bit of a risk now on the side of more loans because we think credit is too tight. As you get it more relaxed, yes, we won't get it perfect. But I think that is what we need to do. And I will tell you that to the extent that we in Congress are involved, our reactions will reflect that.

Let me go next to my colleagues on the committee. Mr. Capuano.

Mr. CAPUANO. Thank you, Mr. Chairman. I would like to start, because it was a new issue to me, with what Commissioner Antonakes mentioned on the mutuals. I hadn't heard that before. And Mr. Frank's comment that they have no stock is an issue. Do you have any suggestions? I'm not trying to put you on the spot. If you want to do it later, or just let me or the chairman know, suggesting items for collateral that we might be able to support.

Mr. ANTONAKES. I would be happy to follow up with you, Congressman. But I think, as the chairman indicated, there is always a way to get it done. We would favor different ways of looking at things, be it subordinated debt through the holding company. Some kind of a deposit at the mutual bank has been discussed as well. And even, you know, perhaps rather than a cash infusion and perhaps, you know, as the Secretary of the Treasury's statement today, we'll work on it, the means of moving some troubled assets off of bank balance sheets, not just the five largest banks in the country, but even a few community banks. There are a very small number that are struggling. The ability to move just one or two bad loans off the balance sheet could immediately restore them.

The CHAIRMAN. The lack of a means for applying for TARP funds doesn't carry over with the assets.

Mr. ANTONAKES. Correct.

The CHAIRMAN. The fact that they're not eligible for the funds yet would not intrude—wouldn't mean they couldn't participate in that other program.

Mr. ANTONAKES. Yes, Mr. Chairman. I'm just hoping the program on—that allows us to move the assets out is flexible enough to deal with small asset issues versus large asset issues.

Mr. CAPUANO. Mr. Commissioner, I'm happy to look at the suggestions, but you have to understand you're talking to someone who hates what is about to happen this week. I think what the Federal Reserve and the Treasury are doing this week is horrendous. I think it is incredibly dangerous to take almost all the risk and put it on the taxpayers' backs. Why do you think the market is going up today? Because the market sees a killing. I don't blame them. I would be doing the same thing. They see a killing, a massive shift of taxpayer money to private enterprise. I hate it. I will take it up with both Secretary Geithner and Chairman Bernanke this week as they come before the committee. I know I am a voice crying in the wilderness. I get it. But I respectfully disagree with taking those assets off. I also know that I'm in the minority.

I do believe there are other ways to do it. I think there are plenty of ways to leave those assets on the books of the people who took the bad gambles, which for the most part are not our community banks. Very few community banks took these humongously bad gambles. Most of them were made by the big guys, and everything is rolling downhill. I think there is a way to do it, to leave the risks on the back of the people who took that risk, as opposed to taxpayers. That's a different issue. We'll be dealing with that next week.

I guess I do want to follow up on what the Chairman had to say, what Chairman Koutoujian had to say: I agree that a lot of it has been people backing off. It has also been exactly what Chairman Frank said, which is everybody in the whole system, both the regulators and the bankers and community bankers, are afraid to make not a bad loan but anything other than a perfectly excellent loan to a guaranteed payer. Again, I really think that the most important thing is to comment to the regulators that you have to talk to your own people. Again, I understand there is a balance. I understand that. I think it's perfectly fine if the instruction goes out to loosen it up again, to make sure that Congress knows that, you know, there is a little bit of extra risk.

I can only analogize it to 2004, when the convention was here in Boston. It was a couple of years after the 9/11 attack. Every single security agency in Washington was up here trying to protect us. I understand that. Every one of them wanted to close down every road for 14 square miles. And we had no—because nobody wanted to be the guy who said, "Open up Route 93," in case, God forbid, there was a problem. I understand that. I respect that. It's exactly what's going on in the banking industry right now.

The balance is, when you make these commentaries, when you enlighten your regulators, that you also document it and let us know. I think the chairman is 100 percent right: We understand that if things open up a little bit better, that some additional loans might go bad. That is better for the economy. It is better for everybody if one or two go bad. Nobody wants to go back to the bad old days of just throw it out the door. But there is some balance. And I am not trying to ask you to put your own reputations or your people's reputations on the line. If it's done in an open and transparent way and a thoughtful way, I think that there will be plenty of Members of Congress who will stand up and do the right thing.

With that, Mr. Chairman, I yield back the balance of my time.

The CHAIRMAN. Mr. Delahunt.

Mr. DELAHUNT. I'm going to ask Mr. Bland to focus on the Community Reinvestment Act, and if you have data that would indicate delinquencies and defaults from institutions that operate under the—operate within the Community Reinvestment Act. Because I think there is a perception out there that the CRA in no small measure is responsible. And my understanding of the data is that is entirely inaccurate. I think it's important that we lay out for the record once and for all the impact of the CRA. So reflect on that for a minute, but let me just take another minute to reflect on I think what you're hearing from the chairman as well as Mr. Capuano. I just think it's very natural for people to err on the side of caution when there is a crisis like the one that we have now. I remember vividly back in the late 1980's or actually in the early 1990's the term "performing/nonperforming loans," and actually institutions that I believe—lending institutions, banks, that could have survived did not because of fear of lack of discretion maybe, lack of flexibility.

And I think the message that you're hearing from members of the panel is to go back to your personnel and tell them to exercise judgment. Don't become so concerned that what we have is the ability to lend but a reluctance to lend because of the mood of the moment. That is really defeating in terms of what we as an institution, in terms of Congress, and the Administration is attempting to do. Exercise judgment. Don't be too reluctant.

Now is a good time to be in the market. There are a lot of good buys out there. One only has to see what the Chinese are doing worldwide. I read recently a quote from one of the Chinese leadership that said this is a once-in-a-century opportunity, so therefore the Chinese, who I believe have in excess of a trillion dollars, are all over the globe now buying. Again, I'm not suggesting that we all run out and be rash, but at the same time, let's strike that balance. It's important that we do. Mr. Bland, will you speak to the issue of the CRA?

Mr. BLAND. Representative Delahunt, I don't have the specific numbers in front of me, but I would be happy to get those for you. But I can safely say with all confidence that the CRA loans, the loans made under CRA, have not fared worse than loans outside of CRA.

Mr. DELAHUNT. Say that again, and say it a little more loudly so everybody can hear.

Mr. BLAND. I can say with 100 percent confidence that loans under CRA have not performed any worse than loans outside of the CRA.

Mr. DELAHUNT. Let me suggest to you, from what I have been able to gather, is that in fact they're doing better than loans outside of the CRA. So I would like you to get that information and provide it to me and start to focus your public comments, or whoever you report to, on the realities that exist out in the marketplace. With that I yield back.

The CHAIRMAN. And to make the question complete: What we're looking for is a comparison not just of CRA loans versus non-CRA loans in the banking system, but CRA loans versus all loans—because I believe statistics are pretty clear that the great majority of

loans that got us in trouble were made out of the banks, not credit unions, that the credit unions and banks were not making these loans. We need to remind people CRA only covers the banks. So it's loans made by mortgage finance companies and others where I think there is a disproportionate part of the problem. That's the comparison we could get, not just in the banking system and CRA, but in the banking system and other loans, many of which were outside the system. Mr. Tierney.

Mr. TIERNEY. I don't want to recover a lot of ground we have already covered. I think the questions were right on point. But am I correct in saying that all of your organizations have authority to step in and take some sort of corrective action if in fact people are having bad lending practices? But if they're not lending enough, if they fall down on the balance, where you don't think they're lending enough, there is not much more than jawboning that you can do? Is that a fair assessment? Is there something else you can do where you see a bank making decisions that are somewhat on the side of so overly cautious that it belies reasonable judgment? Mr. Finn?

Mr. FINN. Yes, Mr. Tierney. We do have the CRA Act, which if they're not doing enough lending within their designated community, they would get rated either less than satisfactory or needs to improve. And we can require certain corrective actions when they receive an adverse rating like that.

It also impacts their ability to get approval on certain applications as well. So it does come with a cost. There is some mechanism when institutions are not out lending in the community—

Mr. TIERNEY. And you are monitoring that?

Mr. FINN. We do monitor that.

Mr. TIERNEY. You have found nobody on the other side of that so far?

Mr. FINN. We do occasionally have institutions that obtain that rating. Typically in the thrift industry, and I think across much of the banking system, we have a large portfolio of small institutions, typically the only loans that they make are in the community. So it's not an issue. But from time to time we do come across institutions that don't make loans, and again, we would rate them adversely.

Mr. TIERNEY. Any other tools? Ms. Thompson.

Ms. THOMPSON. The CRA is a good tool. In fact, we just recently—

Mr. TIERNEY. Would you say that again?

Ms. THOMPSON. CRA is the best tool that we have to monitor the banks' lending efforts and initiatives. I would like to mention that on behalf of the FDIC—

Mr. TIERNEY. Can you speak right into the microphone?

Ms. THOMPSON. On behalf of the FDIC, you do have my commitment and also the Chairman's that we are telling our examiners to make sure that they strike a balance, that banks are—we're going to encourage banks to make good loans, and we are encouraging them to modify loans and work with borrowers to avoid unnecessary foreclosures. This is a good time where judgment comes into play. Many of the people who work for us have been through the 1980's and the 1990's, so they are capable of making good judg-

ments about financial institutions and lending. As we go back to basics, we want to make sure that the fundamentals of lending are still in play.

The CHAIRMAN. Mr. Capuano has a question or further comment.

Mr. CAPUANO. Thank you, Mr. Chairman. Number one, the CRA is an annual rating. You don't get to do it every month or a couple of days. It's a tool, but it's a weak tool at best. Number two is that actually some of the things we had hoped, many of us had hoped that would happen through the TARP legislation, is that as we're giving taxpayer dollars to some of these institutions, that they would then be required to put some of it out in loans. In my opinion, most of that has failed.

There are two other comments I wanted to make. Again following up on Chairman Koutoujian's comments—yes, I think there has been some retrenchment on some loans, but I think a lot of that is tied to a lot of smaller businesses actually supply larger businesses. If the larger business can't get a loan to do something, then the smaller business can't get a loan either, either because their potential or the purchaser of whatever it is they make isn't there, or they don't have the stability that the loan is perfect.

And the last comment I wanted to make is, for, again, particularly for the smaller, more community-oriented or statewide banks: One of the problems I'm hearing is from the FDIC. Right now they're struggling to deal with the increased fees to get the FDIC to pay for something they didn't do. I understand fully well the FDIC has certain capitalization requirements of their own. I get it. You know that we're working on trying to increase access to capital.

But I want to make sure that if that—actually under any circumstances would be nice, but particularly if Congress is able to increase the access to capital for the FDIC, that you then go back and either repeal or reduce or reverse or even rebate some of these fees going on, and only because it is exactly the opposite of what should be happening. The banks that have been the least guilty of engaging in risky behavior are now paying to stabilize the FDIC, for understandable reasons, in order to support the activity by the most risky behaviors. It's completely the wrong way to go.

I understand it's the only tool you have at the moment. I get it. But I also think it's critically important. That's millions of dollars on the books of some of our more local banks that would then have it available to loan out.

The CHAIRMAN. Mr. Tierney.

Mr. TIERNEY. Thank you. Just closing on that, I think the next time that anybody contemplates waiving those fees for any lengthy period of time, maybe we would rethink that and understand that that is an assurance against the day, it might be something like the experience we're experiencing today.

My last question would be: I hear stories over and over again that regardless of the SBA's programs, banks continue to not be anxious to lend utilizing the SBA. Are you hearing the same thing and making those observations? If you are, what needs to be done either through legislation or through regulation by the SBA or in some other way, so that more banks utilize the resources of the SBA and then be able to pass that on to borrowers?

Ms. THOMPSON. I think the announcement by the President last week of increasing the guarantee from 80 percent to 90 percent for an SBA loan and also the Treasury's purchase of assets backed by the SBA, will do a lot to increase SBA lending.

Mr. ROSENGREN. I agree with her observation. SBA lending is not very substantial in New England. It's much more substantial in other parts of the country. We have had meetings with community bankers to try to encourage them. I'm a little skeptical that it's the amount of the guarantee. I think it's the paperwork. It's viewed as a very onerous system, both by the borrower and the bank.

The CHAIRMAN. Let me note, because we do have the vendors of the Small Business Association on the next panel along with the bankers.

Mr. TIERNEY. I'm hearing what it is—is that it on that? These are things I want to ask the next panel.

Mr. ROSENGREN. I think it is a good thing to ask the next panel. But we have had the same observation, that many banks have been reluctant to do the program. I don't know that the staffing of the program has been as great as the funding for providing the loans. So I think it may be an opportunity to look at whether they have enough staff to push it out to financial organizations and also ask—I know they have tried to streamline the programs. I know they have made improvements in the program. But what we talk to bankers, there are probably more improvements that need to be done to really make it a streamlined program that they're actively using.

Mr. KOUTOUJIAN. If I may add, Congressman, you may want to ask some later panels. The SBA typically guarantees about \$20 billion in loans annually, and new lending this year is on track to fall below \$10 billion at this point.

The CHAIRMAN. We will have on the next panel the president of the Smaller Business Association, and representatives of the borrowers. We will hear directly from them and from some community bankers.

I thank the panel. We hope to be able to follow up on the supervision, and we will be pursuing the mutual term sheet.

The next panel will come forward. As they do, let me note that, through my error, we forgot to add the credit unions, who will be represented, as well as State Representative Linda Dorcena Forry, who is the chair of the Community Development Committee in the House. We will take 2 minutes to change.

[Discussion off the record]

The CHAIRMAN. Our next panel includes both representatives of the banking industry and of the borrowers. We are going to resume the hearing, if people will please either take a seat or leave. If you want to stand up, it's okay as long as you don't talk.

We'll begin with Representative Dorcena Forry. Representative? I know you guys get criticized for excess, but spring for a couple of microphones here.

**STATEMENT OF THE HONORABLE LINDA DORCENA FORRY,  
HOUSE CHAIRMAN, COMMITTEE ON COMMUNITY DEVELOP-  
MENT AND SMALL BUSINESS**

Ms. DORCENA FORRY. The press would probably kill us for that. I want to thank you, Chairman Frank, and Congressmen Capuano, Delahunt, and Tierney for holding this hearing today. My name is Linda Dorcena Forry. I'm a State Representative for the 12th District, newly named chair for community and small business. I think it's great that we have the two panels this morning. To hear the panel of regulators and how they are going to try to ensure the adequate extension of credit to small businesses is very important. I look forward to hearing from the lenders and borrowers as well. I'm here with two staff members, John and Lou, who are each analysts. I cannot stay for the whole thing, but they will be here taking notes.

As we have heard this morning, small businesses are the economic engines in our communities, not just in Massachusetts, but throughout this country. It is important and really a timely discussion that we're having today on how are we going to help these businesses on Main Street remain viable. Expanding credit to small businesses and mid-sized businesses is what's going to help us move out of this economic situation, this economic meltdown.

In the wake of the crisis, our banks have become risk-averse. However, despite the lack of available credit, our local businesses cannot afford risk-aversion. They have invested everything into keeping their businesses afloat, at times tapping into their home equity to make capital investments, purchase new inventory, or even to make payroll.

And even businesses that have not been as actively affected have found themselves losing their lines of credit. I'm not speaking merely about average business owners. I'm referring to colleagues, my colleagues, in State Government, in the Legislature, who are still investing in their businesses. I have a colleague who had a line of credit, a \$50,000 line of credit, for several years, always paid on time, never used it, paid the rate that you need to pay every month to make sure he sustained his credit. Recently, he received a letter from his lender telling him that the line of credit is no longer available to him. This is the time, you know, that he may need to have access to that line of credit even more.

So I think that it is important that we are here, and this is a good thing. But we have to ensure that the TARP funds trickle through the banking system and into our communities. Stimulus money should not only go to purchase bad loans from failing institutions while letting them tighten their underwriting criteria to the other extreme. If we are going to bail out the banks, then they need to continue to support small businesses with access to credit. I say this recognizing that this can be done while still making their underwriting criteria more reasonable than it has been in the past. They can be reasonable lenders without abandoning our small businesses. I think that's why this discussion is important today. I thank you all for holding this hearing.

The CHAIRMAN. Thank you, Representative Forry. You and Representative Koutoujian, being here at the State level, you hear even more than we do the complaints from regular people. We want you



to get together so we can work together to resolve them. I'm going to go next to Mr. Robert Baker, who is president of the Smaller Business Association. Obviously, there is a great deal of interest in this.

**STATEMENT OF ROBERT BAKER, PRESIDENT, SMALLER  
BUSINESS ASSOCIATION OF NEW ENGLAND**

Mr. BAKER. Mr. Chairman, I'm president of the Smaller Business Association of New England. We have about 700 businesses. We represent about 700 businesses, small businesses, including banks, accounting firms, but mostly manufacturing and high-tech companies throughout New England. I was a banker for 8 years. I also ran a quasi-public loan fund for the Commonwealth called the Economic Stabilization Trust. So I have a pretty good perspective about what happens in a credit committee and how public money can play a role to supplement, enhance, and help companies on the margin receive financing.

As a trade association, one of our core competencies is to actively aggressively seek capital for small businesses' sustainability and growth through bank and nonbank services. In Massachusetts, we are blessed. We have a number of quasi-public entities, private entities that have public purposes, the Massachusetts Community Development Corporation, the Economic Stabilization Trust, the Property and Casualty Initiative, the Business Development Corporation of New England, the Massachusetts Capital Resource Company. They are numerous, which makes a big difference to us in Massachusetts, as opposed to other States.

So at any one time, I'm engaged in identifying comprehensive capital solutions for probably 8 to 12 companies. My observations are really grounded on my transactional experience with these companies. You know, a great deal of conversation has been generated, and I'm probably a better public lender than I was a private lender. Understand that I think intervention in credit markets is good, and I think the banks are pretty supportive of that. We haven't found any resistance. You know, it's not a straight up-or-down decision, but when you bring to them a collateral enhancement or an infusion of new money from a quasi-public lender, they're pretty receptive in this State. So I will say that.

However, you know, small businesses, the banks are driven somewhat by the economic performance of these companies. Unfortunately, I think our high-tech sector is doing pretty well, but our traditional manufacturing has been doing, you know, more poorly than it has in the past. And I think this has somewhat contributed to poor earnings. And when you have poor earnings, the regulators do come in and classify those loans as nonperforming loans.

The question is, how do the banks deal with that? What we found is the banks have been very patient about dealing with those small, middle-market credits and giving them an opportunity to identify additional financing rather than forcing them to liquidate.

The options to the businesses which they're utilizing right now, rather than risk of closing, is they're seeking—there are a fair amount of out-of-State factoring companies, finance companies, not regulated by the banking sector. But businesses have to pay a premium because the risk profile is greater, I would say 18 to 24 per-

cent. I think that's minimizing it. So what happens, if a company loses money and they come to us and we look at a factor that looks at the receivables and inventory and we finance the balance sheet rather than the performance of an operating company.

You know, I think that's a better alternative than the company going out of business. We had a company, let's say, a knife-sharpening company in Medford. Two years ago they lost money. They were asked to leave the bank or move over to the managed asset portfolio. That bank exercised a fair amount of patience. In sequential order what we did for this company was the following: We found them a finance company, and yes, they charged 18 to 24 percent, since March or June of 2007. However, the company, that has 50 to 60 jobs, did stay in business. Sequentially we found the Massachusetts Community Development Corporation to pay out another of the bank's loans. And this week the company will return to private banking, thus paying off finally the real estate loan of that bank and paying off the expensive line of credit.

Those situations I don't think are unusual, of what's happening day to day. I think the biggest challenge is overcoming the stigma of losing money, and then it's very difficult to regain your footing without a couple of years of earnings to get back into traditional banking. I think that's the hurdle that people are facing today.

I was appointed by Governor Patrick to the Economic Stabilization Trust. There are only five of us. We make working capital available to manufacturers both on the upside and the downside. Companies may have had a bad year but have 3 months of break-even or profitability. We make loans between \$100,000 and \$750,000. You know, unfortunately, the two quasi-public corporations that do the most risk lending in Massachusetts are probably the least capitalized. So I think that's something we would like to propose to the State Legislature in terms of going forward.

The CHAIRMAN. But you're not before the Legislature. Federal issues would be—

Mr. BAKER. Excuse me. I know. Anyway, the SBA package I think would be helpful. It gives the banks a chance to—it incents them by raising the guarantee from 75 to 90 percent. It drops all the fees. A pretty interesting component: it makes business stabilization loans, so that a company can get \$35,000 from a bank to defer principal and interest payments for about 6 months, if it lasts that long, so they won't go on the nonperforming list. So I think that's—

Finally, there is a 504 modification, so if you bought a piece of real estate 10 years ago, you had a million-dollar loan, the bank's share was 50 percent of that, you've paid down your balance to \$250,000, you could actually recast that now, probably get a lower interest rate, and put the money back in the company. So there are some tools. Thank you very much.

The CHAIRMAN. Thank you. Next, Christopher Oddleifson is the president and CEO of Rockland Trust, and someone I know from experience has been a very creative participant in some of the Federal programs we have had planned out with the community agencies. Mr. Oddleifson, let's get you the microphone.

**STATEMENT OF CHRISTOPHER ODDLEIFSON, PRESIDENT AND  
CHIEF EXECUTIVE OFFICER, ROCKLAND TRUST COMPANY,  
AND VICE CHAIRMAN, MASSACHUSETTS BANKERS ASSOCIA-  
TION**

Mr. ODDLEIFSON. Good morning, Chairman Frank, and Congressmen Delahunt, Capuano, and Tierney. I'm Chris Oddleifson, President and CEO of Rockland Trust Company. I'm also the vice chairman of the Massachusetts Bankers Association, on whose behalf I'm testifying. I appreciate being here. Thank you.

As we have heard this morning, community banks in Massachusetts are in fact lending to creditworthy businesses. In fact, one of the ironies of this environment is that it has turned out to be a tremendous opportunity for community banks because of the retreat of a lot of these other lenders, the finance companies, the institutional investors, insurance companies, and larger out-of-State lenders. There is a breach that has been opened, and community banks have stepped in. We're seeing a sharp increase in demand, and we're seeing an increase in our portfolios. I'll share some statistics in a moment.

As you've heard this morning, Massachusetts banks are well-capitalized. We're well-positioned to lend. We didn't get into any of that crazy stuff that got all the smart guys in trouble. And we don't have significant foreclosure problems. We on the whole have managed our risk well, which as you also have heard this morning includes sometimes saying no to businesses we have less confidence in their ability to repay the loan. Loan-loss reserves are far more than the national average, almost twice the percentage on hand that we had in the last massive crisis, in the late 1980's and early 1990's.

As evidence that the local banks are lending, looking at sort of the community banks, commercial loan balances in Massachusetts have increased from \$5 billion in the end of 2007 to \$5.7 billion in 2008. I have heard from my colleagues throughout the State that in fact they're seeing unprecedented demand. That is good news for us. I mean, it helps our business. But it's in the context of bad news overall.

Let me give you sort of a specific anecdotal example of how community banks are provided credit by just citing a couple of statistics from the bank I lead, Rockland Trust Company. We have \$3.6 billion in assets. We have offices and locations throughout eastern Massachusetts and Cape Cod. A year-to-year comparison between 2007 and 2008: In 2007, we originated \$318 million of commercial loans. In 2008, we originated just over \$400 million. That is a 26 percent increase. As I say, many of those opportunities were as a result of lenders leaving, and allowed us to actually build some fine relationships with great local companies in our trade area. I would say that while our first quarter numbers aren't public, we are seeing in 2009 good, continuing, robust lending activity.

The Massachusetts Bankers Association would like to encourage the community—I think we have talked about this this morning—to help responsible lenders expand their capacity and be careful not to make it too loose, where we have some of the egregious practices sort of come back on in. But the balance that we have talked about this morning I think is very, very important.

To further revitalize the commercial credit market here in Massachusetts, the Massachusetts Bankers Association, along with our member institutions, have been working with the Patrick Administration over the last several months on initiatives such as Soft Second, which has a little bit of a guarantee to a commercial loan to incent the commercial lender to extend credit. In addition, the Association is hosting a commercial lending summit that will bring together bankers and Federal and State government officials and academics to discuss the State's climate and look for ways to work this issue.

I would like to take the opportunity to make a couple of comments on related topics. First, the issue of perception: Quite simply, a better distinction needs to be made between the banks that caused this problem and the banks that are part of the solution, the traditional local banking community; and the Massachusetts Bankers Association is certainly working hard on this, and we appreciate the chairman's comments on this issue. But the misperception continues that all banks are having problems; and especially those banks that took Capital Asset Program funds, part of the TARP funds, those banks are especially problematic. There are a number of banks which took those funds from an offensive point of view, to expand credit, not from a defensive point of view, and that is completely lost on many. To the extent we can solve that, we'll increase public confidence, we'll make consumers believe that the loans are available, and I think it will assist the overall economic recovery.

The second point I would like to sort of mention is, we certainly applaud the committee's work on mark-to-market accounting issues. As you know, many of the losses suffered by local banks are largely accounting rules, and inflexible rules have led to a loss in earnings and capital, which inhibits their ability to loan. This is sort of the performing/nonperforming loan all over again and performing/ nonperforming securities. One great example is the Federal Home Loan Bank of Boston, which is a critical partner to local lenders, extending credit to the communities, had to take a \$340 million writedown, and their economic loss is only anticipated to be \$22 million. Take out \$340 million of capital but you only expect to lose \$22 million. That is astounding. I think it's the performing/nonperforming issue.

The current proposals released by FASB are a good first step, but they don't go far enough to really sort of addressing this issue.

The CHAIRMAN. By FASB, we have a Federal Accounting Standards Board, which we are talking to about changing this form of accounting.

Mr. ODDLEIFSON. In conclusion, Massachusetts community banks are currently experiencing good loan demand. We're actually growing our balance sheet. We're doing it in prudent and responsible ways. We want to be a part of the solution and solve the problems that we believe for the most part others created.

[The prepared statement of Mr. Oddleifson can be found on page 88 of the appendix.]

The CHAIRMAN. Thank you, Mr. Oddleifson. I very confidently misidentified the FASB, which is the Financial Accounting Stand-

ards Board, not the Federal. Next time I explain something, I'll try to get it right.

Next I want to call Mr. David Slutz, who is the president and chief executive officer of the Precix Corporation, which I should note is active in the district I represent. We have had conversations, and I am troubled that we haven't been able to make more progress. This is an example, in my judgment, of where we have a business suffering unduly because of this. Mr. Slutz.

**STATEMENT OF DAVID N. SLUTZ, PRESIDENT AND CHIEF  
EXECUTIVE OFFICER, PRECIX**

Mr. SLUTZ. Thank you, Chairman Frank, and members of the committees, for providing me the opportunity to speak this morning. What I would like to do this morning is actually talk about our company briefly—we are a small manufacturer based in New Bedford—to provide an overview of our borrowing situation with our current lender and offer some recommendations that we think would help the situation, many of which have already been mentioned before, but from my perspective, I'll mention those again.

My name is actually David "Slutz." My wife prefers "Sloots" over "Sluts," but that's okay. I have been called that for many, many years now. I'm the president and CEO of Acushnet Rubber Company. We're doing business as Precix. We were part of that golf ball company that was the Acushnet Rubber Company until 1994.

One of my key roles in my position is lender relations, and over the past years, I have dealt with lenders of various sizes and negotiated the day-to-day relationships. Acushnet in New Bedford has been around since 1910. We are a manufacturer of o-rings and custom seals for customers within the automotive, aerospace, and chemical processing industries. The automotive piece is primarily why I'm here today, because, as we know, the build rates have gone from \$16 million to less than \$8 million, and with those build rates, our sales levels have gone down accordingly.

In New Bedford, we have 225 associates. Our average tenure is 24.8 years. I have worked for three elastomer companies, and I can honestly say that we have some of the best, if not the best, work force with whom I have ever worked. Our products go in every car manufactured in North America, every aircraft, over half of the automobiles and aircraft built in Europe, and 25 percent in Asia. Twenty percent of our business goes overseas. For a small company in New Bedford, we touch an awful lot of vehicles.

Like most in the supply chain in automotive, the last 6 to 9 months have been, for lack of a better phrase, just plain miserable. Our sales have dropped by half, through no fault of our own. We have taken \$4.2 million in operating expense out of the business. Our work force is down by 25 percent. Those of us who remain, including myself and my senior staff, are all going through rolling layoffs. We actually get paid for a week and then are off for a week. So we're trying to preserve as much employment as we possibly can. They can't write a textbook for what we're going through at this point in time.

All of our stakeholders have had a hand in getting us through this difficult time. Our employees have sacrificed pay and reduced hours this year. Our equity sponsor is accepting zero return, and

our vendors have are allowing us to stretch payables. The only stakeholder not really participating has been our senior secured lender.

Our relationship with our current bank began in late 2007. Our loan is pretty simple. It's a long-term debt, also a short-term revolver. Since inception, we have paid down the long-term debt by more than \$625,000. We have made all our payments on time and had clean audits. Quite frankly, we're a good and boring customer.

In November of 2008, we saw the downturn getting worse, and we notified our lender of our tightening credit situation. Built into our current loan is a 350 holdback, \$350,000. We're not talking about a large sum of money. We simply asked the bank to allow us access to the pre-existing 350 holdback, and at that point, they flatly said no. On top of that, they have actually been imposing additional restrictions and making our lives more miserable.

It's important to understand that my company is not one that was going through a leveraged buyout. We're not overly leveraged by any means. We're simply caught up in the revenue decline because of automotive. We have provided the bank with a reasonable business plan and recovery scenario going forward, because the good news on automotive is what comes down will eventually come back up. And the good news is over the past couple of weeks, we had started to see our business slowly start to increase, so we're slightly optimistic.

Despite being over-secured by over \$3 million in excess collateral, the bank denied our request and now is seeking to reduce my borrowing availability and raise my operating costs through increased interest rates and the imposition of consultants and additional reporting requirements, the specifics of which are located in my written testimony.

From our vantage point, they're not helping us, by any means. Rather they're working to push us under. They're living to the letter of the law of our 2007 loan agreement. That was written when the world was a different place. This is an institution which I will not be naming specifically, but is a TARP recipient.

So in summary, I would like to point out, our Nation's economy has gone through some very difficult and challenging times. Our employees via downsizing, rolling layoffs, vendors taking extended payment terms, management deferring payments, and the owners forgoing dividends, have all contributed to the cause. The only stakeholder not working with us to get to the other side is our lender, who without Federal aid probably would not be here today. Our note then and now has been fully collateralized, yet they will not release the \$350,000 holdback or work with us in any way. Instead of helping us, it seems like they're trying to push us under and put 225 people out of work.

So my message to the committee is this: It's imperative that if the banks that are recipients of the TARP funds truly want to support economic stabilization and recovery with more than just words, they should be willing to provide reasonable and prudent assistance to companies such as ours; companies that are not over-leveraged. We have strong collateral support; we're simply going through a tight cash time. They should be ready, willing, and able to provide temporary working capital and credit availability in situ-

ations where: (A) there is tangible collateral support; (B) there is a reasonable, detailed operating forecast showing the amount and duration of the temporary financing need; and (C) the needed incremental credit availability is small relative to the current loan balance, like in our case; leverage is not at excessive levels; and there are domestic jobs with good benefits at risk.

So instead of quoting loan agreements that were crafted in a world that has changed since 2007, the lenders should be businesspeople first and, to quote a major banking executive who testified in Washington, D.C., “Americans first and bankers second.”

I am certain there are other small to medium-sized manufacturers like us that are experiencing a similar set of circumstances. So if economic stabilization and recovery is to occur, it is imperative that banks take a more measured and reasonable approach to providing temporary support to companies like Precix using the guidelines I have suggested.

Thank you for your time and the opportunity to speak to you to inform you about this aspect of business lending for medium-sized companies.

[The prepared statement of Mr. Slutz can be found on page 133 of the appendix.]

The CHAIRMAN. Thank you. Next, we’re going to call on Mr. Barry Sloane, who is the president and chief executive officer of Century Bank, not the lender in question.

**STATEMENT OF BARRY R. SLOANE, PRESIDENT AND CHIEF  
EXECUTIVE OFFICER, CENTURY BANK**

Mr. SLOANE. Right, Mr. Chairman. Thank you. Good morning. Thanks for the privilege of appearing before your committee, gentlemen. I would like to share our perspectives on the current state of the credit crisis. I am joined today by my three sons, Marshall, Jack, and Charles, who I think, after 2 hours of a congressional hearing, can’t wait to go back to school.

Just a word of note on Century Bank: Century was founded 40 years ago by my father, Marshall, on a corner of Mystic Avenue in Somerville in a temporary office trailer. He is today our chairman, and as we approach our May 1st anniversary, we are proud to be the largest family-controlled bank in New England.

My brother Jonathan and I are the co-CEO’s of an institution with \$2 billion of assets, 22 branches in Massachusetts, 400 employees, and now a member of an exclusive club, an increasingly exclusive club, those community banks who are increasingly profitable. Our earnings were up 15 percent last year, with growing local deposits of 12 percent, and we did not need, nor accept, the TARP capital from the Treasury.

Century was founded under the concept in 1969 that there was a powerful case for a community-based lender to business, a premise that is remarkably even more compelling today. We proudly service over 6,000 business clients, and since 2004, we have made over 1,500 small business loans, many in partnership with the SBA. Our total loan portfolio is over \$900 million and has grown in an upward slope since the early 1990’s, increasing 15 percent last year. We are safe, we are sound, and with abundant li-

quidity to expand our loan portfolio. We are ready and able to lend to the business community.

Why have we done well and others have not? In our view, there are three simple reasons: First, we have a culture based on risk management. We are lenders. We live and breathe our loan portfolio through a highly centralized process. Second, we lend only in our local market. Market intelligence is critical to a successful loan policy. And third, we seek and nurture long-term relationships with all of our borrowers. A single transaction without relationship continuity is discouraged.

So how can we make a contribution to today's dialogue to seek solutions to enhanced business credit availability? In our view, there are two pathways: One, to make the banks stronger so they can make more loans; and two, to make the small business community healthier so they can become stronger borrowers. Let's take a look at the banks first.

In our view, far too much emphasis has been placed on bank capital, and not enough on earnings. The TARP program provided capital to banks with marginal or adequate capital ratios but at a high price. It became an instant drag on net earnings, or profits. Net profits build branches, hire lenders, feed the loan-loss reserve, and expand the capabilities of the institution in its local market.

How could the Congress help the profitability of the independent banks, improve their efficiency and their relative competitiveness? Here is our five-point agenda: First, simplify the regulatory structure. It's obvious from the previous panel, with all due respect to the professionalism and dedication of the regulators presenting, that this is the opportunity to reform and merge the five bank safety-and-soundness regulators into one Federal system. We at Century are regulated by three agencies. It is an inefficient structure. And please, do not burden the independent banks of the United States with the proposed systemic risk regulator. We always thought there was such a thing, and it was called the Secretary of the Treasury. We are worried about a proposal that, based on my recent reading, takes some 300 pages to just explain the question.

Second, please change the FDIC premium structure. Convert the premium charge from a bank expense to a user fee that is disclosed, transparent, and much more economically efficient. The pending 2009 FDIC special assessment will have a significant negative earnings impact on the independent banks. Why should the banks that practiced sound lending have their earnings negatively impacted by the irresponsible behavior of others? The 2009 assessment will effect a contraction of the lending of sound banks through the shrinkage of earnings. The FDIC premium should be paid by the depositor as a discrete tax paid on the health of the fund and not a charge to individual banks.

Third, reinstate the Glass-Steagall barriers between commercial and investment banking. Admit the failure of that experiment and acknowledge that commercial bankers are risk-based asset managers and investment bankers are fee-based originators. They are two very different genetic animals and are poisonous together. The short-term high fees of the broker/ trader will devour the good judgment of the banker/ lender. Get the brokers out of the banking business, and please stop this wild proliferation of bank charters



to institutions that neither have the temperament, geographic focus, nor long-term relationship culture to be known as a bank. Level the competitive landscape so that once again community banks can make loans at fair prices to their local customers and stop losing business to the "Street." You in Congress control the competitive equation. Put the emphasis back on community connectedness and away from globalism.

Now let's talk a little bit about the health of the small and medium-sized business community. These entrepreneurs are experiencing two reinforcing negative impacts: The dramatic fall in real asset values; and the staggering collapse of their cash flows from double-digit sales declines. This vortex has especially impacted the firms that are in the automotive, housing, and consumer discretionary sectors, where sales have fallen 20 to 50 percent. There is no way for a small business to survive a market cycle with such a severe fall in cash flow if they have any meaningful level of debt.

The SBA does a fine job. Few people realize that the SBA has until recently recouped all of its loan defaults from the guarantee fees charged borrowers. There was no subsidy from the taxpayers. We are a so-called preferred lender and use the SBA credit enhancement frequently. The recent changes in the 7a program, especially increasing the guarantee to 90 percent, is a good thing for small business, as is the elimination of new guarantee fees. However, you must keep in mind that a loan we don't like at a 75 percent guarantee, we won't like any better at 90 percent. It probably fails due to inadequate asset valuations and/or cash flow. We're not inclined to make a loan because we lose less money. It's either a good credit or not. Higher 7a guarantees do not transform a marginal applicant into a good credit.

The combination of this recession and the credit crisis have been a tsunami for small business. Frequently, I sit through urgent meetings with business owners of, in many cases, multi-generational family businesses that are floundering on the shoals of this crisis. This is the Hurricane Katrina for small business. They don't need more debt. That's the last thing they need. They need equity. They need help, and they need it soon. This is figuratively more a challenge for FEMA than it is for the SBA. Lifetimes of resourcefulness and initiative in small business are melting away with each GDP contraction.

In summary, if this government has the capital to keep Bank of America's planes in the air, Citi's corporate retreat staffed to serve lunch, and even pay the AIG bonuses, then it must find the capital to help mitigate so many of the family business tragedies playing out every day in bank conference rooms across the Nation. I don't have to tell all of you in Congress of the importance of small and mid-sized businesses in the economy and the employment health of the Nation. They need their own TARP program. Let the banks administer it. Make it an equity investment. Take the pressure off these business owners who are watching their dreams evaporate day by day. My dad, my brother, my sister, and I, sincerely hope to see it. Thank you.

[The prepared statement of Mr. Sloane can be found on page 129 of the appendix.]

The CHAIRMAN. Thank you. Mary Ann Clancy, from the Credit Union League.

**STATEMENT OF MARY ANN CLANCY, SENIOR VICE PRESIDENT  
AND GENERAL COUNSEL, MASSACHUSETTS CREDIT UNION  
LEAGUE**

Ms. CLANCY. Thank you, Mr. Chairman. Mr. Chairman, Congressman Capuano, Congressman Delahunt, Congressman Tierney, for the record, my name is Mary Ann Clancy. I serve as senior vice president and general counsel of the Massachusetts Credit Union League, our State trade association, serving just over 200 State and federally chartered credit unions, about 2.4 million consumers as credit union members.

I am very humbled and honored to be included on this panel today and with the opportunity to provide some assistance. I have a few oral comments and would like the Chair and the committee's permission to submit a written statement at the conclusion of this.

The CHAIRMAN. Certainly.

Ms. CLANCY. As you all know, the credit union model is a not-for-profit financial cooperative model for the delivery of financial services to both consumers in Massachusetts and across the country. There is no other like it. We provide access to credit and savings services to all of our members, including small businesses. We celebrate our 100th anniversary of credit unions in the birthplace of credit unions here in Massachusetts this year, and in light of the current economic challenges, we believe that this is an important model, with built-in ethical and member service standards that's important to preserve.

Credit unions are healthy, but they are not immune to the current challenges in the financial services arena. We do, however, throughout this time, remain focused on providing access to credit at every opportunity. From a historical perspective, small business lending, or member business lending, as we call it in Massachusetts, is not new. It started in 1926, with a loan to a variety store in Fall River and a cemetery in Dorchester. Our history underscores the hallmark of this lending. We loan where others have vacated or are unwilling to loan, and we loan based on the capacity to repay over time. Over time, credit unions have become an increasing resource for member businesses as well as consumers. The average size of a member business loan in Massachusetts is about \$250,000. Nationally, it is about \$213,000. We are slightly higher because of the commonality of multi-family properties that are investment properties, that many consumers come to us to buy the old home in the neighborhood, so to speak.

Most recently and due to changes in the marketplace, we are seeing requests for about \$500,000 up to \$1 million. We are regulated by the Division of Banks and the National Credit Union Administration in this area for State-chartered credit unions and by the National Credit Union Administration for federally chartered credit unions. However, regardless of our charter, we do face a cap of 12.25 percent of assets. That was in place over 10 years ago, and many of our credit unions are approaching that limit.

About one third of the credit unions offer member business loans. It's about 6 percent of our total loans outstanding. It is a growing

part of our portfolio. And we keep a majority of our loans in the portfolio, which allows us to stay in the game during these tough economic times. Our loan charge-off rates for member business loans is about .32 percent.

The heart of our lending is for sole proprietors and small businesses. We don't do big commercial loans or dealer floor plan financing. But we do estimate based on a national perspective that about \$10 billion in new funds for member business loans without an impact to the Federal or State government would result if we were able to eliminate the 12.25 percent cap. We view this as an important economic boost. We also view it, particularly as the labor markets continue to deteriorate, other people try to jump in and start their own small businesses, as a way to try to reach these people and to serve them.

Thank you for the opportunity to provide these comments today, and also in particular to bring this focus, to bring this light here in Massachusetts, and keep us on the forefront perhaps of possible solutions.

The CHAIRMAN. Thank you. Next, Mr. Pelos is the executive vice-president of Wells Fargo Commercial Banking.

**STATEMENT OF PERRY PELOS, EXECUTIVE VICE PRESIDENT,  
WELLS FARGO COMMERCIAL BANKING, WELLS FARGO**

Mr. PELOS. Thank you very much. For a guy from Minnesota, I appreciate you guys ordering the weather particularly for me. It feels like home. Chairman Frank and members of the committee, my name is Perry Pelos. I'm an executive vice president and group head of Wells Fargo's commercial banking group, and it is an honor for me to be here to speak to all of you today. I worked for almost a quarter of a century at Wells Fargo, the entire time in either commercial or corporate banking.

First, allow me to describe our commercial banking customers. We serve middle-market businesses with annual sales of between \$20- and \$750 million. We serve over 12,000 of these businesses around the country. In New England we have full-service relationships, including loans and lines of credit, with companies in energy, agriculture, manufacturing, transportation, and high tech, and although our market share at the moment is smaller, much smaller, in Massachusetts relative to our industry peers, we view the State and this region as a big opportunity for growth for us.

Wells Fargo has remained open for business while many other banks have pulled back or exited from commercial lending. Now, as always, we want to do what's right for our customers, and we have never stopped lending. We have been able to increase our lending to creditworthy customers over the past year-and-a-half. That is partly because we were building capital and actually shrinking our balance sheet in 2005 and 2006, when credit spreads were unrealistically low and not priced for underlying risk.

Here's how we have increased our loans specifically: In the last 18 months, we have made \$63 billion in commercial loans and commercial real estate loans. Our middle market portfolio in the Northeast grew 11 percent from year end 2007 to year end 2008. I would add that our middle-market portfolio in my business in commercial banking grew 55 percent in Massachusetts last year.

Our commitments to government and education in Massachusetts and five other Northeast States are \$543 million, and in 2008, we achieved double-digit growth in asset-based middle-market commercial real estate and specialized financial services, which includes capital markets and relationships with Fortune 500 companies. At the end of the fourth quarter of 2008, we had \$68 billion in commercial real estate and construction loans, up 6 percent from the third quarter.

To address the committee's question about the effect of Federal laws and regulations on credit availability, we urge an approach more consistent with past economic downturns. We believe the chairman's efforts with respect to mark-to-market accounting will allow the entire financial-services industry to continue supporting the credit needs of our customers more effectively. In January of this year, we made \$14 billion in commitments to commercial banking customers, and half of these dollar commitments were to new commercial banking customers. Overall, we extended \$51 billion in loan commitments in January, and that brings the total credit extended to our customers to \$144 billion in the last 4 months. That is nearly 6 times the \$25 billion capital investment made by the U.S. Treasury in the fall of last year. Our integration of Wachovia into Wells Fargo is proceeding better than expected. In New England Wachovia's commercial banking portfolio is about \$6 billion in loan commitments, including government and education, in year end 2008. We're committed to the financial success of all of these New England companies and institutions, and we look forward to long-term relationships with all of them.

After the Wachovia acquisition, we stepped into open lines of credit for some businesses whose access had been shut down, especially cities and not-for-profit hospitals, which until very recently have been part of my group. When the debt markets for these borrowers were compromised last fall, Wells Fargo substantially increased its support and level of commitment to this area. As we continue to integrate the Wachovia businesses and manage through a very difficult economic time, we'll continue to work with our customers. Mr. Chairman and members of the committee, thanks for listening and I'm pleased to answer any questions you have.

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

The CHAIRMAN. Next, another borrower, Ms. Iris Mitropoulis, who is president of Ventura Industries.

**STATEMENT OF IRIS A. MITROPOULIS, PRESIDENT, VENTURA INDUSTRIES, LLC**

Ms. MITROPOULIS. Thank you for holding this hearing today and for giving me the opportunity to be here and participate. My name is Iris Mitropoulis. I am president of Ventura Industries, a Massachusetts company I formed in 1996 to acquire manufacturers of custom machinery. In 1998, I purchased Kingsbury Corporation, located in Keene, New Hampshire, with funds provided by BankBoston and CIT Group Equipment Financing. For the last 5 years, Ventura Industries has been in the top 100 women-led businesses in Massachusetts. I also serve on the government relations committee of AMT, the Association for Manufacturing Technology.

AMT is a trade association whose membership, mostly small businesses, represents more than 400 manufacturing technology providers located throughout the United States, almost the entire universe of machine tool builders who manufacture in our country. We are the companies who build machines that make things. Seventeen of AMT's members are located in Massachusetts.

My industry is really the foundation upon which all other American manufacturing rests. We provide the manufacturing technology essential to a wide array of industries, from cutting, grinding, forming, and assembly machines to inspection and measuring machines and automated manufacturing systems. There can be no cars, airplanes, washing machines, air conditioners, or medical devices without our member companies. There can be no green initiatives without companies like ours, which design the machines and systems needed to produce the parts that go into green engines. Furthermore, our member companies are a critical part of our defense industrial base.

As crucial and necessary a part of our American manufacturing sector as we are, however, our credit needs are not presently addressed in the stimulus and aid packages. We are not surviving the current economic chaos, in significant part because lack of credit is endangering the continued existence of virtually all of our member companies.

The recent meltdown in the financial services sector has basically frozen credit to companies like mine. For the last 20 years, I have been the CEO or owner of small businesses that belong to the AMT. I have raised over \$100 million for these businesses, and I have never seen a time when it is more difficult to raise credit.

My company does not produce commodity machines. My company is an engineering firm that designs and manufactures custom machines to solve the customers' manufacturing needs. New programs and productivity improvement are the two drivers. Recent customers, for example, are United Defense, now part of BAE, for machines to manufacturer tank track links.

My company has been on a 2-week shutdown because all new programs evaporated last fall and we have been unable to obtain a loan even though we have a history of profitability until recently and collateral to offer. We actually were unable to send a serviceman to Precix because of that. Today, I think one of our service people is there.

The shutdown we are currently on is jeopardizing the launch of a major new transmission program for one of the Big Three. We are making assembly machines that will assemble a key component to that transmission.

Two weeks ago, I met with the director of the New Hampshire Business Finance Authority and the New Hampshire District Director of the Small Business Administration to see if they had any programs that could assist my company during this credit market turmoil. The Business Finance Authority already had a 90 percent guarantee program, and the SBA district director was anticipating that certain SBA programs would see their guarantee increased to 90 percent. Even with 90 percent guarantees, I was most discouraged to hear both say that they do not expect to see an increase in lending anytime soon. The only loans they saw closing were

loans to prom queens. Unfortunately, given the extreme downturn in the economy and business, most small businesses will not in the near term be able to meet normal credit standards. We do not qualify at present as prom queens.

I also met last week with staff of the New Hampshire Economic Development Authority. While sympathetic to our plight, they were frustrated that even with funds coming into the State from the Financial Stability Act, there were no programs available to them to assist companies such as Kingsbury, a company founded in 1894 that employs 100 highly skilled engineers, machinists, and electrical and assembly technicians and is one of the few remaining U.S. custom builders of highly engineered mid- to high-production metal cutting and assembly systems, a company that purchased over \$15 million of goods from New England suppliers in the last 5 years, \$7 million of that in Massachusetts.

I appreciate that this is a hugely complex issue legislators are dealing with, and I do not presume to know the correct answer. As a small business owner who has run up against obstacles recently to obtain financing, I see two areas that may help critically needed funds flow to AMT members and others. With respect to funds going to States under the Financial Stability Act, if the States were allowed to reallocate and create new uses for some portion of those funds, they may be able to use their discretion to save companies and jobs that are vital to their State economy. In the case of the SBA, since the SBA's programs are intended to lend to small businesses that can't otherwise get credit, I suggest that SBA preferred lenders be allowed to make loans without regard to traditional evaluation of repayment ability if a loan is needed in order to save jobs and other credit considerations have been met. Even if this modification were allowed until September 30, 2009, it would be a tremendous boost for small businesses.

In closing, I would like to point out that AMT used to be known as the National Machine Tool Builders Association—that is, until there were too few of us left to support an association. Membership has broadened to include manufacturers of other forms of manufacturing technology. Since the economic crisis began last fall, two to three AMT members per month have failed. There is no evidence that this number is abating, and very well may increase if something is not done.

Due to the financial pressures of my company, I did not attend the last AMT government relations committee meeting in February. When I called the committee chair a few days later to ask about the meeting, he responded, "It was the scariest meeting I have ever attended in my entire life. You are all in the same boat. You all need credit, and it's not available."

As I stated earlier, I do not pretend to know the answers. I have a green crystal ball on my desk but I can't see through it to predict the future. All I know is that our industry needs access to credit yesterday. America cannot afford to lose the few remaining machine tool companies in the United States today and still be a world leader. Thank you for allowing us to testify.

The CHAIRMAN. Thank you. Mr. Scott Geller, from JPMorgan Chase.

**STATEMENT OF SCOTT GELLER, PRESIDENT, MIDDLE MARKET BANKING, NORTHEAST REGION, JPMORGAN CHASE & CO.**

Mr. GELLER. Good afternoon, Mr. Chairman, and members of the committee. My name is Scott Geller, and I am the president of Middle Market Banking for the Northeast Region of JPMorgan Chase, and I'm also responsible for our Financial Institutions Group nationwide within our commercial bank.

I'm pleased to represent our company at today's field hearing. We at JPMorgan Chase are working hard to restore confidence in the U.S. financial system. Although the economic environment continues to be difficult, we have endeavored to responsibly deploy the TARP funds as Congress intended: To restore stability and provide liquidity to the financial system; to ensure credit flows to businesses and consumers; and to stabilize the housing sector by modifying as many mortgages as possible.

Each month, JPMorgan Chase provides to the Treasury Department a snapshot of the intermediation activity in which we have engaged as a result of our participation in TARP. Although we have seen an increase in mortgage originations as a result of lower interest rates, demand for credit in most other areas remains low. It's important to note that during a recession, it is normal to see generally flat to lower applications for loans across-the-board. However, we are open for lending. During January we extended almost \$50 billion of new lines of credit and loans. We have also committed to extend an incremental \$5 billion in lending to government and the not-for-profit sector over the next year.

JPMorgan Chase also continues to implement our mortgage modification plan to keep as many homeowners in their homes as possible. This effort covers more than \$1.4 trillion of mortgages, having been expanded to include not only loans that we own ourselves, but also investor-owned mortgages that we service. To date, we have modified over 330,000 mortgages, and we plan to double this number by the end of 2010. I'm proud to say that the re-default rates we are seeing are significantly better than some of the numbers that have been published by the regulators.

In addition to the numbers we have provided detailing our lending activities, I would like to talk about New England specifically. As you are aware, branches are important to our middle-market clients, and we would generally not expect a bank to do much business in areas where it doesn't have a footprint. Although our commercial bank has an office in Boston, we do not have any branches in Massachusetts or in New England. As a result, our focus has been on larger commercial and industrial clients, governments, nonprofits, health-care, and other companies that are less branch-dependent. Keeping this in mind, let me address some of the issues we are facing and some of the successes we're seeing in Massachusetts and nearby.

Overall, demand for commercial lending is down across the United States, as small and mid-sized companies are rationally responding to the difficult economy by carefully managing their liquidity and spending less. The impact of the recession is being felt as businesses across-the-board see lower sales and are therefore reluctant to take on additional debt. The reduced pace of business ac-

tivity has resulted in less demand for both working capital loans and fixed asset spending.

Although small, our business in New England actually grew by approximately 14 percent year over year, primarily because of health care and higher education. We have \$140 million in new or increased business in our pipeline, including a major transaction with a hospital here in Massachusetts. We have lending relationships with 108 New England companies, and 16 of these relationships were added in the past year, an increase of more than 10 percent. We also serve as a correspondent bank for 12 other financial institutions in New England.

Banks are a vital part of the overall lending picture, but it's important to note that the capital markets are very different today than they have been historically. Going into the current recession, banks accounted for only 20 percent of the lending activity that took place in our economy. Fifty years ago, this number was closer to 60 percent. The difference is made up by money market funds, securitizations, and bond funds, just to name a few. The erosion of this nonbank lending will continue to be a factor in the recovery almost regardless of what traditional banks can do on their own.

Lending is our business, but it comes with a duty to lend responsibly. All of us at JPMorgan Chase are trying to meet the needs of creditworthy borrowers in a safe way, and we look forward to continuing to work with this committee to find solutions to get our financial services industry and our economy back on track. Thank you again for the opportunity to appear today, and I'll be happy to answer any questions.

[The prepared statement of Mr. Geller can be found on page 84 of the appendix.]

The CHAIRMAN. And finally, Mr. Edwin Shea, who is the Central Massachusetts market president of Bank of America.

**STATEMENT OF EDWIN T. SHEA, JR., PRESIDENT, CENTRAL MASSACHUSETTS MARKET, BANK OF AMERICA**

Mr. SHEA. Most importantly, I run our business banking group from Boston out through central Massachusetts for Bank of America.

Good afternoon, Chairman Frank, Representative Capuano, and Representative Tierney. I appreciate the opportunity to share our views on the current state of lending to small and medium-sized businesses. For over 200 years, Bank of America has been serving business clients and weathered many economic cycles with them. Today we have relationships with more than 4½ million businesses across the country and serve these clients with a wide range of products and services. Our testimony today will focus on small and medium-sized businesses, with annual revenues up to approximately \$20 million.

In my daily interactions with clients, I hear about their declining sales, difficulty collecting receivables, and more stringent terms from suppliers. Consequently, the bank itself is feeling this downturn in our small-business loan portfolio, with a steady rise in delinquencies and companies reporting a weaker financial condition. We also see that the recession is having a disproportionate impact on businesses at the smaller end of the spectrum, those with reve-



nues less than \$500,000. Larger, more established businesses are faring better but are also responding to the slower economic climate by lowering capital expenditures, reducing inventories, and laying off employees.

In light of these challenges, we continue to take actions to help small business. We are actively marketing our full suite of services and credit products, and we are working more intensely than ever to restructure loans for distressed clients wherever possible. For our small business customers, we have increased the use of our fixed payment programs, where we significantly reduce the interest rate and monthly payments.

For example, in 2008, we assisted over 40,000 of these customers, representing \$550 million, by modifying payment structures to improve their cash flow. Another way we are helping small business is through our commitment to community development financial institutions. These organizations play important roles as conduits to provide credit to small businesses and community organizations. We are a leading financial-service investor in CDFIs, with more than \$450 million in direct lending investments in 2008.

In Massachusetts, we have built strong relationships with a number of CFDIs, such as Boston Community Capital and ACCION USA. In 2009 we do expect to see a decrease in new loan commitments to the smaller businesses in the segment. This is due to several factors. The first is a decreased demand for loans overall. Applications for new loans have been declining for well over a year. The primary reason for this trend appears to be an overall reluctance of business owners to take on new debt during a time of economic weakness.

The second factor is that more loan applicants are experiencing deteriorating financial conditions. We have seen a noticeable increase in applications from clients that have hit a time of serious financial stress in their business and personal finances. In these circumstances, we may not be able to approve them within our prudent lending guidelines.

The third factor is underwriting standards. During the period of 2005 to 2007, Bank of America expanded its focus on small business lending, particularly for the smallest businesses as a segment. Our underwriting guidelines at the time reflected a positive economic outlook as well as the experience of prior years, generally a period of economic strength, with relatively low delinquency and loss levels for very small firms.

As we began approving and booking more loans, however, we started to see a deterioration in these small businesses' ability to pay us back. The economic downturn has exacerbated this problem and has led us to return to more prudent, sustainable underwriting standards to ensure acceptable credit quality for new loans.

From our perspectives, these three factors are creating a contraction in new credit that we are seeing in our own client base. Given this current outlook, government assistance and loan programs have made a difference to our clients. Bank of America received a \$45 billion preferred stock investment through the TARP program, and we are lending significantly more with that investment than we would be without it. Also, the recent actions by the Obama Administration will create new opportunities for lending to new busi-

nesses, through reducing fees and increasing guarantees on SBA loans. Bank of America is a longtime participant in SBA loan programs. We are currently the No. 1 lender in loan volume in the 504 program and actively participate in the 7a express program.

In summary, Bank of America remains committed to small and medium-sized businesses. We continue to market our services, including credit products, to this segment, while adjusting our business model to meet the needs of our clients during this economic downturn. We are making every effort to approve as many clients as we can during this time within prudent lending guidelines, and we will continue to extend credit to this very important segment. Thank you for the opportunity today.

[The prepared statement of Mr. Shea can be found on page 121 of the appendix.]

The CHAIRMAN. Let me begin. There are six representatives, six bankers, on the panel. One of our concerns was whether or not regulators were exerting pressure for standards that might deter some of your activity. I would ask each of you, have you encountered that? Is that a factor? Have you made fewer loans than you might otherwise have made in any number because of the regulators? Mr. Pelos?

Mr. PELOS. Are they still in the room? I guess there are two ways to answer that. The first is, I don't think that anything the regulators have done specifically has caused us to lend less. Those are the things that are already being done.

But I do think, with this whole stress-test concept that's out there, it's causing a lot of stress in a lot of places. Because part of it is that none of us has the answers to that. So if you set a standard that will allow the financial services industry to get through a very, very severe recession as your standard for the stress test, you might cause that to happen by causing people to hoard capital to get them through a really, really bad recession, and it may be a self-fulfilling prophecy.

The CHAIRMAN. You have not encountered that yet in specific issues with regulators, but you are concerned that the stress test would have an impact?

Mr. PELOS. Yes, but we don't know—

The CHAIRMAN. Let me say this: The regulators understand that we have a certain role here to play. I'm not suggesting that anyone would be penalized by anything they said here. I know we're joshing. But that's not going to happen. We need to get honest answers. That's a relevant point to us. We have to make sure the stress test doesn't become a source of that. Mr. Sloane?

Mr. SLOANE. Mr. Chairman, I would not blame the regulators for the condition we're in.

The CHAIRMAN. I didn't ask you to blame them. I asked a much different question. Have they in your experience been too tough either in general or in specific cases?

Mr. SLOANE. No. I think they are expecting us to live up to the loan policy of the institution. If valuations have fallen and cash flows have collapsed, the loans will become less attractive to all concerned.

The CHAIRMAN. You said you have a 300-page proposal on systemic risk. I'm not aware of one.

Mr. SLOANE. It's the one from the Congress.

The CHAIRMAN. We haven't put out any 300-page proposal.

Mr. SLOANE. There are three proposals. Congressman Capuano sent them out for his roundtable. There is one from the Treasury Department.

The CHAIRMAN. Is that Mr. Paulson's from a year ago? Don't worry about that one.

Mr. SLOANE. There is a third which is about 200 pages long. And isn't there a congressional task force on the systemic risk regulation? Which one is it?

The CHAIRMAN. Oh, that's the TARP oversight panel. Let me say, Mr. Paulson's plan, which had the credit unions and the State-chartered banks and everybody in an uproar, don't pay attention to that. Mr. Paulson did some good work, but there is no 300-page or other page—you got a proposal from the congressional oversight panel, which is useful to look at. But those are private citizens. Mr. Oddleifson?

Mr. ODDLEIFSON. The short answer is no, but I would add that our last exam was a year ago, and they have in the past had very, very thorough, very granular looks at a number of specific loans very carefully, down to the utmost detail. Their focus is on ability to repay. I suspect with the deteriorating environment around us, that threshold will be tougher to overcome.

The CHAIRMAN. Mr. Shea.

Mr. SHEA. That isn't my area of expertise. My area is business banking space in Boston out to central Massachusetts. I can tell you that in our space, we're trying to make every good loan we can.

The CHAIRMAN. And you're not running into any resistance from the regulators?

Mr. SHEA. Not from my experience, my area of expertise, no. We are trying to make every good loan and win every new client relationship we can.

The CHAIRMAN. Mr. Geller?

Mr. GELLER. Chairman Frank, nothing specifically. The regulators continue to scrutinize us. They always have. But they haven't really changed anything, nor have I noticed anything.

The CHAIRMAN. I think the thing about the stress test is a relevant one. Let me ask Mr. Shea—I was struggling—I didn't expect you to tell us that Bank of America expects to increase the loan limit. There were two issues, one was the lack of demand, and obviously no one's expecting you to subpoena borrowers, so we realize that.

But there were two others that sort of have an overlap which troubles me. One is the weakness of the individual potential borrower. But the second, which is the troubling one, is the weakness in the economic climate, which would appear logically to have to mean other than the individual borrower. That's Mr. Slutz's problem. You get dinged if you are in trouble yourself, but you get dinged if you're not in trouble because the economy is. That is the part about self-fulfilling prophecies that I worry about. If you enumerate those two separate issues, it seems to me we're getting to Mr. Slutz's issues, which is a question of, I'm okay and I can show you that I'm okay, but a loan, a credit that I was supposed to have

access to a couple of years ago, I can't get now because there is trouble in the economy generally. How do we deal with that?

Mr. SHEA. A couple of things. First, I stated there were three major contributing factors.

The CHAIRMAN. Right. One was the lack of demand. I understand that.

Mr. SHEA. Lack of demand, deteriorating financial condition, and we're taking a harder look from an underwriting perspective.

The CHAIRMAN. Two and three were, it seemed to me, the individual borrower, but then the general economic atmosphere. The underwriting standards—in other words, you're being tougher. Even if the borrower is in the same condition as the borrower was in a couple of years ago, it will be harder for that borrower to get a loan.

Mr. SHEA. One of the things we look at in lending credit is the conditions you're lending into. The current environment has changed. We're in a recession. There are more delinquencies. It's a greater risk profile to lend into, and we need to be more prudent when we make credit decisions.

The CHAIRMAN. That's what troubles me. We're saying, again, that a company—to some extent, the frustration for the company is, how do they deal with that? How do they show you they're in good shape? This notion that the environment as a whole—

I guess the question is: You said that the \$45 billion in advance in the TARP—and we should be clear: In fairness to Bank of America, part of that was because Bank of America, at the urging of the Federal Treasury and the Federal Reserve, agreed to take Merrill Lynch—I'm not asking you to take on—when I think Bank of America would have been just as happy to kiss it good-bye. But they were urged strongly not to do that, and the TARP money—and in fairness, that ought to be taken into account.

But you say that the \$45 billion is helping you lend more, and I think it has. But that doesn't affect the underwriting standards. I guess the question is, without the \$45 billion, would you have been up against some limitation given your capital? How has the \$45 billion helped you to lend more? Has it affected or not affected the underwriting standards? So is it you have more capital and you can lend more?

Mr. SHEA. I'm not prepared to discuss the impacts of TARP.

The CHAIRMAN. But you said that the \$45 billion helps you lend more.

Mr. SHEA. It shores up the bank's capital, and we can therefore make more loans. My area of expertise is the business banking space, companies that generally—

The CHAIRMAN. I understand, but I need to know how—I don't think it's an unfair question—how does the fact that the \$45 billion is available help you to make more loans? Is it that you have more capital, you were against a limitation? If you can't, I'm going to ask somebody in the bank to explain that, because that's obviously a very critical question. But it doesn't help us with the tightening of underwriting standards.

Mr. SHEA. I can get back to you with a better answer, Congressman.

The CHAIRMAN. Mr. Pelos, let me ask you, and then also Mr. Geller: It is the larger banks that we are talking about. Have your underwriting standards tightened? Is that part of the reason why an individual institution which would be in the same economic position, a business, that it was in a couple of years ago—would they find it harder to get a loan today?

Mr. PELOS. I would provide this: Everything we do is custom-made, so there aren't many programs in the commercial banking space. So I think in general I would say that our underwriting standards have remained the same for all this crisis. That's why we're getting more loans, even though commercial lending—

The CHAIRMAN. So a business that had some arrangement with you a couple years ago shouldn't find any difference?

Mr. PELOS. No, to me, let's say we have a company that we have an agreement with, and we say, "As long as you don't lose money, the agreement stands." That would probably be the same agreement we have today. The problem is, that company may be losing money today. So the risk profile of the borrower is different. We would underwrite the way we would have underwritten a—

The CHAIRMAN. If the company wasn't losing money and there was no significant deterioration of the company, the prior agreement should still be available for them.

Mr. PELOS. If the company's financial characteristics were the same 2 years ago as they are today, we would probably underwrite it the same way. If the financial characteristics of the company were different, we would underwrite it the same.

The CHAIRMAN. Let me ask Mr. Geller.

Mr. GELLER. I think each company needs to stand on its own merits. To the extent that a company continues to make money and is in the same financial condition that it was in 2 years ago, then we would look to lend to that company. To the extent that the financial condition has deteriorated, obviously you have to relook at that and underwrite it accordingly.

The CHAIRMAN. So with you, it would be the focus on the company, the underwriting standards would not have tightened.

Mr. GELLER. Again, each individual borrower needs to stand on its own.

The CHAIRMAN. There does appear to be a distinction, Mr. Shea said, that in addition—it seemed to me that both of you were citing one factor where they were citing two, and that is something I'm going to want to pursue further. Mr. Pelos?

Mr. PELOS. Again, we have 12,000 customers, and every deal we do is custom-made. I'm sure within that band of 12,000, you are going to find a couple hundred where that may not necessarily be the case. But in general, our underwriting standards are simple.

The CHAIRMAN. Because this is our problem. The Federal Government—some of this TARP money is being advanced. We don't want the banks getting into serious trouble. But I think it is reasonable to say, recipients of TARP money, it ought to make some difference in your own risk profile, that people ought to be a little bit less risk-averse after taking TARP money than before; and I'm not sure that has always been the case, and that is what we need to pursue. Mr. Capuano.

Mr. CAPUANO. Thank you, Mr. Chairman. It's like two different worlds. I'm hearing from all the bankers that, "Everything is fine, we're comfortable." I'm hearing from all the businesses, "We can't get any money." I understand that we all come from different positions. But there has to be something in the middle. Are you not hearing each other? Did you not just hear what the other side said? Have you not witnessed it? Have you not had businesses come to you and say, "We cannot get a loan."

It just seems like we're in this vortex of, "Well, we have to tighten up our standards. Okay, but we're not doing it because we're being told to by regulators." Okay. So are you just doing it because you want to? And, "We're doing it because businesses aren't selling." Why aren't businesses selling? Every business, every economist I have talked to says the major problem with this economy is the lack of availability of credit—every single one of them, no exceptions. They may have differences of opinion on how to settle it. But the problem has been identified by everybody as the same problem. We have some businesses here—I can't imagine you haven't heard it from others—"We don't have access to credit." Yet everybody is telling me, "Fine, we have credit." Ms. Mitropoulis, how much do you need?

Ms. MITROPOULIS. \$2 million.

Mr. CAPUANO. Who has \$2 million? A million-and-a-half? Mr. Slutz, how much do you want?

Mr. SLUTZ. I'll take \$700,000.

Mr. CAPUANO. Half of what she wanted. Do you see the problem?

The CHAIRMAN. It's actually a third.

Mr. CAPUANO. Well, she went down. Do you see the problem? There is some disconnect here. Now for me personally, I voted for TARP, and I still support the concept of it, because I'm trying to bridge that disconnect. The truth is, I don't really care if a few banks go down. I don't like it, I don't want it, but that's not why I voted for TARP. I did not vote for TARP to strengthen your bank or your bank or anybody else's bank. I voted for it and I still support it because I want to take that money and give it to the businesses so they can get back to buying and making things and getting this economy going. I don't mean to be disrespectful. It's not the banks that keep the economy going. You're just the grease. We tried to provide some additional grease, and yet you're not doing it.

I know that not everybody can. I know all that. I understand different people have different roles in the economy. I get it. But you're telling me there is not a single bank in Massachusetts of any level of any size that can provide capital to one of our best companies in the State, an internationally known company?

Do you understand the disconnect I'm having? I don't quite get it. What are we supposed to do? How do we get you together? If it's not the regulators who are tightening it up, who is it? Do I have to talk to you to say, "Look, talk to your loan officers and calm them down." I understand your standards have to go up. Do they have to go up all the way? Is there no middle ground? Because if not, then everything we have done thus far, everything we might do, is a waste of time. We are dooming ourselves unless everybody, not just the regulators—apparently not the regulators at all, ac-

according to this panel—takes a half a step back and reopens their wallet. Who has an idea for me. What am I supposed to do? What else can Congress do to loosen this up, to get money back into the economy—I'm not asking you to throw money away—into good manufacturing businesses that actually produce things or build things? What can I do? Anybody?

The CHAIRMAN. Let me parse the question, to the extent that I have heard suggestions: We are working hard to get the FDIC's assessment cut very substantially below what it had been, and we are working hard to get the mark-to-market rule made much more flexible and the consequences more flexible. I think we will be successful in both of those. Those are two of the suggestions we are working on.

Mr. BAKER. Take the current situation over here. It may be at what cost. There may be other options for some companies that have failed in the bank's mind to meet standards, so they may have to pay a premium, or then they'd have to ask for supplementary capital. That's available in Massachusetts. Every situation is different. But, I mean, there are situations where, as I have talked about, near your backyard, Medford, where companies slip out of favor with a bank.

The other issue is how patient is the bank going to be, how flexible? Is it going to be a liquidation situation, or is it going to be, "Let's work through it; let's rehab this credit; let's give the company time?" This gentleman has taken out \$4½ million in cost. If he's cash-flow-neutral or cash-flow-positive, there may be another way to go about it than a strict vanilla situation from a conventional lender.

Mr. CAPUANO. That's a fair answer.

Mr. BAKER. It is customized. It's a case-by-case situation, because all loans are risk-rated at institutions. You know, when it's a criticized asset, you sometimes have to deal with it.

The CHAIRMAN. Here's the point we're trying to get to: With \$350-plus billion in TARP funds already advanced and more coming and some other flexibility, has that had an effect on the risk profile the banks are willing to take, or not? That is one of our key questions we have going forward. If the answer is no, it's not conducive to further congressional support.

If I could, Mr. Slutz, you gave—are you cash-positive now? Are you making money?

Mr. SLUTZ. Over the past several months, no.

The CHAIRMAN. What is your projection?

Mr. SLUTZ. The projection is the build rates in automotive, basically you get above 12 million vehicles per year, we all get healthier.

The CHAIRMAN. Your collateral hasn't deteriorated?

Mr. SLUTZ. Not at all.

Mr. CAPUANO. One of the things we heard a week or two ago, maybe 2 weeks ago now, we had all the major banks in, and they were complaining about some of the regulations, some of the requirements both on the TARP money and additional requirements that people like me would like to put on. When asked, "Why don't you give it back," they said, "We can't." "What do you mean, you can't?" You can't because if you do, you then have to fill that hole

with your own capital. So you can, but you choose not to. It's similar to this.

So they can look at each individual circumstance and understand that this is a long-term, good business that has actual assets—I understand fully well, I want to make it very clear, I'm not asking any bank ever to invest or to loan a penny to naked, vacant paper. That's how we got into the problem we have. We're talking manufacturing here. We're talking, not here, but in other places, housing. We're talking things that have real, hard assets. To not be able to look at those individually and understand that, you know what? Your loans, your economy? Where do you think the banks are going to go if there is nobody left to loan to? How does this work? You have to make loans to substantial businesses.

And if there is any way you could find to suggest to me how we could help encourage that—and again, I'm not looking to throw money away, as has been done. It was a horrendous thing that was done through business—which, again, to me is where Government comes in. How do we help you get to the point where you make thoughtful loans to substantial businesses that have hard, fixed assets?

If you have any ideas, please let us know, because I for one am struggling how to get this done. If not today, tomorrow is fine, next week's fine. I'm not trying to put anybody on the spot. I'm trying to emphasize where my problem is, trying to get this money loose.

The CHAIRMAN. Mr. Oddleifson.

Mr. ODDLEIFSON. Mr. Sloane and I will sort of put ourselves out there first. One thing, one program that we're involved with that actually has—we have some money out in more recent situations is a program which encourages lending in what's called hot zones, economically distressed areas. We have extended the kind of allocations from the Department of Treasury, and that's worked quite well.

I will tell you that they are more risky, because we are working out a couple of them right now. We did put ourselves out there for a tax benefit, but they were getting a chunk of it back through credit loans. And I believe in the stimulus package there is some additional allocation above and beyond what was there originally.

Mr. SLOANE. I would just add, Congressman, that it would be my pleasure to review both of these situations. We don't know either client. But on behalf of our loan committee, I would be happy to review them both to see if there is anything we can add.

Mr. CAPUANO. Swap business cards. I want to add, there is no finder's fee.

Mr. SLOANE. But to your earlier point: It's not so much that conditions tightened or loan conditions tightened. It's the gravity of the depth of a business cycle will make that happen automatically, so that the valuation of real property, the value of receivables—imagine being in the automotive industry, being a tertiary player there, and having the Big Three receivables or even their parts manufacturers. There are a whole series of automatic discounts that happen in cases like this, and that oftentimes is how you evolve a situation here.

The CHAIRMAN. Mr. Tierney.



Mr. TIERNEY. I appreciate that offer, Mr. Sloane, and I suspect that it goes back to a point where it used to be that as part of assessing the loan, you had the character of the borrowers. We hear all the time the too-big-to-fail thing. Some of our banks are too big to deal with their borrowers. They don't know them under circumstances intimately enough to add that to the mix. That certainly is a part of this, and it may be why one of your bank or banks would be able to look at this. You can look at the situation. You know the local situations.

I'm stunned that nobody wants to go beyond what the line says. It's easy to run the formula down and kick somebody out the door. That has to be part of that. I'm talking about small businesses in particular, it has to be part of assessing the character, the community, the situation you're in—looking for other things, as Mr. Baker said, but also making a judgment call as to whether or not the outside situation may be getting worse, whether this particular borrower is going to be good for it, is going to at least try as hard as you could expect to make it. I think that might be part of the answer. That might work. I think it does.

The only other thing I would add: Mr. Sloane, you've made the comment during the course of your remarks that got my attention on that. I think you said that you thought the deposit fees on guarantees for deposits ought to be paid by the depositor. I have a real adverse reaction to that. My understanding is the purpose of those guarantees is so that lenders—so banks, rather, will be able to entice borrowers to have confidence and put money in their bank. It's for the benefit of the bank. Why do you want to tag consumers with yet another fee? They have to pay to go to the ATM, which is supposed to save us money. It's not saying us a dime. They have to pay everything all the way down. This is something uniquely for the health of the banks and for the banks to get deposits, and yet you want to turn it around.

Mr. SLOANE. Sure. That is a very thoughtful analysis. I appreciate that, Congressman. I think my view here is that there is an inequality that is evolving between those institutions with a high-quality balance sheet and those with a low-quality balance sheet, and that the premiums necessary to fund the entire deposit insurance process are being placed across the whole industry. My view is that the FDIC premium ought not to penalize the successful institution and its earnings, and it ought to be clearly assessed as a user fee, because it ultimately gets passed through to the depositor in one form or another. It is an expense of our business. The way it is functioning now, you have a large percentage of institutions that have done poorly, and those premiums necessary to restock the fund are falling on everybody's balance sheet.

Mr. TIERNEY. Maybe we should make some differentiation.

The CHAIRMAN. May I say, there is an effort to require you to be more risk-based, and the FDIC is doing that. But the point is this, you couldn't do that if it was an individual charge. You can only do that through institutions. That is, the FDIC can allocate that institutionally, and in addition to lowering it in general, we have asked them to look at making it somewhat more risk-based. That does so.

Mr. TIERNEY. Thank you, Mr. Chairman.

The CHAIRMAN. I thank the witnesses. We are going to be pursuing this. Again, I appreciate the fact that to get the economy fully functioning—I think we’re making some progress. Things are better than they would have been, although that’s not encouraging to people when they’re still in a negative situation. But the kinds of efforts going forward that we continue to need require a good deal of public support. One of the things I would urge on the banks is this: The programs we are talking about are, A, trying to improve the whole economy. But the institutions you represent are inevitably the direct beneficiaries. And you benefit both in that way and you benefit from the whole going forward.

We are at risk of that kind of activity stopping, and when we ask you to think about your lending standards, factor that in. It’s not simply your own bottom line, but your interest as an institution in this economy, in our being able to go forward. And if we aren’t able to get a better response out of the larger banks in particular, I think you are going to find that when we talk to you and you urge us to do this or that or when you complain about restrictions on your compensation or your travel—Mr. Sloane, you referred to, oh, we can afford this or that. In fact, we have been putting some very tough restrictions on that, to the point where both the New York Times and the Washington Post in the last couple of weeks, there were complaints from the banks saying we’re not doing this, that we’re being too tough on them.

But I do have to say to bankers: If I were there and if I believed that it was important that this government has the capacity to continue to do the kinds of things that we need to get the credit system functioning again, I would factor it into my lending decisions, because continued tightness, a drop in loans going forward because of underwriting standards tightening up, that will have negative consequences in the ability of the government to respond in ways that you’d like us to.

The hearing is adjourned.

[Whereupon, the hearing was adjourned.]

# **A P P E N D I X**

March 23, 2009

56

TESTIMONY OF

STEVEN L. ANTONAKES

COMMISSIONER OF BANKS  
COMMONWEALTH OF MASSACHUSETTS

On

SEEKING SOLUTIONS:  
FINDING CREDIT FOR SMALL AND MID-SIZE BUSINESSES IN MASSACHUSETTS

Before the  
COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

March 23, 2009, 10:00 a.m.

State House, Boston, Massachusetts

Good morning, Chairman Frank, Congressmen Capuano and Lynch. My name is Steven L. Antonakes and I serve as the Commissioner of Banks for the Commonwealth of Massachusetts. The Division of Banks is the primary regulator of nearly 250 state-chartered banks and credit unions with total combined assets in excess of \$350 billion. The Division is also charged with the licensing and examination of over 1,000 non-bank mortgage lenders and brokers, over 4,000 individuals engaged in mortgage lending and brokering, as well as an additional 3,500 non-bank financial entities, including check cashers, money transmitters, finance companies, and debt collectors.

I commend you, Mr. Chairman for scheduling this timely hearing on the credit needs of small and mid-sized businesses during these difficult economic times. The ongoing success of our private-sector businesses is critically important to the Massachusetts economy. According to the United States Small Business Administration ("SBA"), there were an estimated 26.8 million small businesses in the United States in the year 2006. These small businesses created nearly 80% of the new jobs in the last 10 years and employ over 50% of the nation's private sector workforce.

Small businesses continue to play an instrumental role in the Commonwealth's economy as well. As of 2006, there were nearly 600,000 small businesses in Massachusetts employing over 2.8 million people. Our smallest businesses, those employing 20 individuals or less, employ 25 percent of the Massachusetts workforce. The continued emergence of new small businesses as well as the healthy growth of existing small businesses is critical to our economy and is also a significant source of new jobs.

Access to credit is essential to fuel the growth which will produce new jobs. Job creation will play a critical role in allowing our Commonwealth and our nation to emerge from our current economic downturn. Similarly, any significant curtailing of business credit will further hinder our overall economic recovery. Restrictions in financing could result in small businesses needing to increasingly rely on more expensive credit card financing, savings, or non-traditional forms of financing. This would significantly increase operating costs and curtail expansion opportunities.

During my testimony today, I would like to address two issues. First, the experience and challenges of Massachusetts state-chartered community banks in the current environment to continue to help to meet local business credit needs. Second, a series of Massachusetts initiatives designed to establish strategic partnerships between businesses, lenders, and Massachusetts government as a means of embracing and nurturing businesses in the Commonwealth. Finally, I will conclude with some thoughts on how future regulatory restructuring can continue to promote the diversity of our financial services industry.

#### **Challenges for Community Banks**

Media reports have continuously focused on diminished consumer and business credit opportunities. Certainly the well chronicled difficulties being experienced by some of our large nationwide money center banks have resulted in the deleveraging of large balance sheets and therefore, the restriction of credit. However, the experience of community banks and credit unions has been strikingly different. I have just completed a series of roundtable discussions across the Commonwealth and have heard from hundreds

of bank and credit union officers on their perspectives of what is happening on Main Street. Many Massachusetts state-chartered institutions report increased lending as a result of reduced competition from some of their largest bank competitors. This is yet another example of how our diversified and decentralized system of banking continues to serve our nation well. This contention is supported by our analysis of FDIC Call Report Data which shows that Massachusetts state-chartered community banks' balances for commercial real estate loans and commercial loans to businesses increased 14.5 percent from 2007 to 2008 and nearly 26.9 percent from 2006 to 2008. Please See Exhibit A, *Massachusetts State-Chartered Community Banks' Business Loan Balances 2006 – 2008*. While years of consolidation among some of our nation's largest financial institutions has had the effect of increasing systemic risk to our banking system, the community banking system and credit union movement remain fundamentally sound and continue to serve as sources of strength during our existing economic difficulties by providing credit to consumer and business customers and positively impacting the local communities where they are based.

Despite their ability and willingness to lend, some community bankers are frustrated that business loan demand has diminished due to the same media reports that credit is unattainable. Moreover, some businesses are likely delaying expansion opportunities given poor economic forecasts. While some community banks have tightened underwriting criteria, many others report that businesses seeking credit have significantly weaker financial positions than before our economic decline took hold. These banks would argue that they have not tightened underwriting standards, but rather they have maintained them.

Many community banks in stock form are also frustrated by the broad application of criticism stemming from the bad acts of some of the largest financial institutions and former Wall Street firms. Acceptance of TARP funds, in the eyes of many, has now become untenable given many banks' experience of having to defend the need for so-called government "bailout" funds despite running well capitalized and well managed institutions. The opportunity for the U.S. Treasury to deploy TARP funds to Massachusetts banks has also been significantly restricted. Massachusetts has the largest percentage of mutual banks in the country. Mutuality is quite likely the reason Massachusetts remains so well banked today despite years of bank consolidation. More than five months after the first banks were provided TARP funds, the United States Treasury Department has still not released a term sheet for mutual banks. Accordingly, TARP funds are still not an option for the majority of community banks operating in the Commonwealth. This has certainly had the effect of unnecessarily restricting increased lending opportunities that might otherwise be available through the use of TARP funds.

Finally, events beyond the control of community banks have and will continue to affect the ability of community banks to lend in the future. The conservatorship of Fannie Mae and Freddie Mac as well as proposed significant deposit insurance assessment increases will significantly impact the earnings of state-chartered community banks and, in the case of the recapitalization of the corporate credit union system, state-chartered credit unions as well. The initially proposed 20 basis points special assessment by the FDIC will cost 36 Massachusetts state-chartered banks over one million dollars each and an additional 73 state-chartered banks over half a million dollars in increased premium payments. The NCUA's planned capital restoration plan for the corporate



credit union system could eliminate up to two years of earnings for most state-chartered credit unions. It is important to note that these actions will not threaten the capital base of any Massachusetts state-chartered bank or credit union. However, the availability of credit to consumers and businesses alike will most certainly be reduced across the board as a result of these increased operating costs. In sum, the ability of local institutions to continue to lend is not being impacted by their bad acts, but by the bad acts and aggressive risk taking of others.

#### **Massachusetts Innovations to Support the Financing of Small Business**

Massachusetts has a proud history of attempting to leverage partnerships to increase opportunities for small businesses to flourish. Access to credit and other banking services remains paramount to the success of small businesses. Massachusetts banks have historically played a significant and vital role in providing such financial services to numerous small businesses located throughout their communities. Nevertheless, it is estimated that nearly 10 percent of the nation's population at this time remains unbanked. Accordingly, many of our smallest and emerging new businesses are likely to be owned and operated by individuals that are indeed unbanked.

Individuals without traditional banking relationships are predominantly low income and minorities. As a result of being outside the financial mainstream, unbanked individuals are typically dependent upon non-traditional, more expensive providers of both credit and other money management services. In the case of small businesses, the reliance on these higher cost financial services directly impacts profitability and

prospects for growth. Massachusetts has developed two programs designed to make financing easier for our smallest businesses.

Massachusetts Small Business Capital Access Program (“CAP Program”)

In the early 1990s, Massachusetts was also facing a credit crunch. The ongoing recession and the New England banking crisis resulted in a substantial reduction in credit availability especially for small and new businesses. Recognizing that most new jobs are created by small businesses and that the creation of new jobs would be vital to the Commonwealth’s ability to emerge from the economic downturn at the time, Massachusetts policymakers sought new innovative solutions to encourage increased small business lending. The result was the highly successful Massachusetts Small Business Capital Access Program, or CAP Program.

In an effort to encourage bank lending, \$5 million in state funding was initially appropriated to provide a cash collateral guarantee or credit enhancement to small business loans made under the CAP Program. This allowed banks to originate loans they might not otherwise have been able to make.

Today, over 100 banks participate in the CAP Program. Since banks utilize their own underwriting criteria and directly provide the funding, the loans are simpler to originate than loans made through the SBA. Banks also receive credit under the Massachusetts Community Reinvestment Act for participating in the CAP Program.

The CAP Program is designed to assist small businesses with annual revenues of \$5 million or less to obtain financing from participating banks. CAP Program loans may be used to start or expand businesses, or to provide permanent working capital to ensure continued profitable operations. Typical uses are equipment purchases, start-up costs, and

real estate acquisitions. The CAP Program can also be used for working capital lines of credit.

In 15 years, a total of \$10 million in state funding has been leveraged into \$241 million in loans to 3,828 small businesses. With an average loan amount of \$51,000 and loans as small as \$1,000, CAP Program loans have helped create or retain 26,000 Massachusetts jobs and brought in over \$100 million in payroll taxes to the Commonwealth. The CAP Program has also been instrumental in providing financing to small businesses in inner city neighborhoods with more than \$20 million in loans to 275 businesses in Boston's Roxbury and Dorchester neighborhoods. Finally, \$34 million in CAP Program loans have gone to start up businesses. An additional \$22 million in loans have been provided to firms with annual revenues of less than \$100,000.

Massachusetts Banking Partners Small Business Loan Program ("Banking Partners")

The charge of the Massachusetts Banking Partners Small Business Loan Program, or Banking Partners program, is also to provide greater access to reasonably priced credit and banking services to small businesses as well as access to vital business assistance services. The program recognizes that many start-up and small business owners need help with recordkeeping, general management, and in preparing a business plan and financial statements. Specifically intended for very small businesses located in low- or moderate-income census tracts needing small dollar loans, the Banking Partners Program matches small business owners receiving technical assistance and training from small business assistance providers with participating banks.

These participating banks accept referrals of small business applicants who are receiving services from not-for-profit small business assistance providers. In exchange,

participating banks offer small business loans at a rate below the lender's typical market rate; make smaller dollar loans than those generally available; and consider financing for early-stage businesses. Banks participating in the Banking Partners program also receive consideration under the Massachusetts Community Reinvestment Act.

### **Systemic Supervision and Regulatory Restructuring**

In the weeks ahead as Congress evaluates our regulatory structure, I urge you to examine the linkages between the capital markets, the traditional banking sector, and other financial services providers. Our top priority for reform must be a better understanding of systemic risks. The federal government must facilitate the transparency of financial markets to create a financial system in which stakeholders can understand and manage their risks. Congress should establish clear expectations about which regulatory authority or authorities are responsible for assessing risk and for using the necessary regulatory tools to address and mitigate risk.

Congress, the Obama Administration, and federal regulators must also consider how the federal government itself may inadvertently contribute to systemic risk—either by promoting greater industry consolidation or through policies that increase risk to the system. Perhaps we should contemplate that there are some institutions whose size and complexity make their risks too large to effectively manage or regulate. Congress should aggressively address the sources of systemic risk to our financial system.

State bank regulators have long believed capital and leverage ratios are essential tools for managing risk. Federal regulation needs to prevent capital arbitrage among institutions that pose systemic risks, and should require systemic risk institutions to hold more capital to offset the grave risks their collapse would pose to our financial system. Perhaps most

importantly, Congress must strive to prevent unintended consequences from doing irreparable harm to the community banking system in the United States. Federal policy to prevent the collapse of those institutions considered too big to fail should ultimately strengthen our system, not exacerbate the weaknesses of the system. Throughout the current recession, community banks have largely remained healthy and continue to provide much needed capital in the communities where they operate. The largest banks have received amazing sums of capital to remain solvent, while the community banks have continued to lend in this difficult environment with the added challenge of having to compete with federally subsidized entities.

Congress should consider creating a bifurcated system of supervision that is tailored to the size, scope, and complexity of financial institutions. The largest, most systemic institutions should be subject to much more stringent oversight that is comprehensive enough to account for the complexity of the institution. Community banks and credit unions, which operate in a much smaller market than the money center banks, should be subject to regulations that are tailored to the size and sophistication of the institutions. In financial supervision, one size should no longer fit all.

The Treasury Department and the Federal Reserve should be required to provide a plan for how to unwind the various programs established to provide liquidity and prevent systemic failure. Unfortunately, the attempts to avert crisis through liquidity programs have focused predominantly upon the needs of the nation's largest institutions, without consideration for the unintended consequences for our diverse financial industry as a whole, particularly community banks. Put simply, the government is now in the business of picking winners and losers. In the extreme, these decisions determine survival, but they also affect the overall competitive landscape and relative health and profitability of institutions. The

federal government should develop a plan that promotes fair and equal competition, rather than sacrificing the diversity of our financial industry to save those deemed too big to fail.

### **Conclusion**

Again, Mr. Chairman I thank you for calling today's hearing. As we continue to work our way through our current economic difficulties, small and medium-sized businesses will also face increasing challenges. It is these businesses, however, that can play a significant role in our economic recovery by adding new and sustainable jobs. I appreciate your efforts and the recent actions by the Obama Administration to strengthen SBA lending programs. But the federal government cannot do it alone. Innovative collaborations between state governments, non-profit entities, and local banks as I have described have also proven to be extremely effective in nurturing and supporting our small businesses and creating new and long lasting jobs.

Our highly diverse financial system has been the envy of the world, allowing our markets to be flexible and responsive, and has survived booms and busts. Thanks to our decentralized regulatory system, our financial institutions are competitive internationally and locally. However regulators and legislators address the current market failings, it should be in a way that preserves the diversity of financial institutions and supervision that has made our economy nimble, resilient, and dynamic.

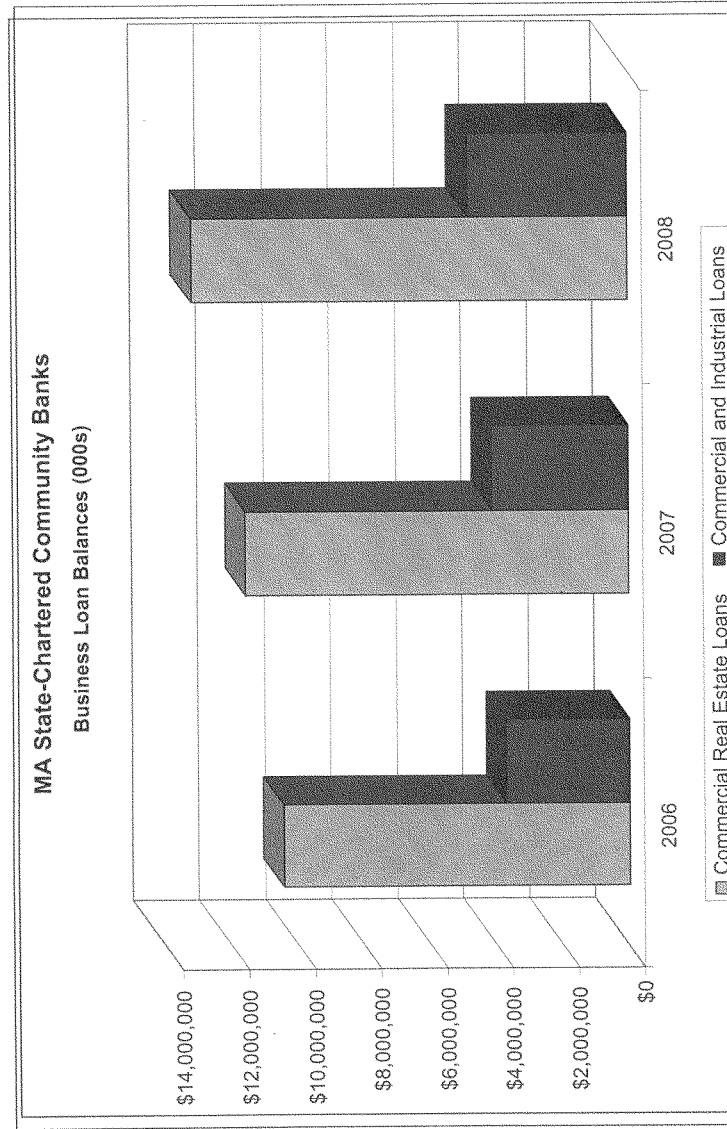
There is a need for improved coordination and cooperation among functional regulators. The Conference of State Bank Supervisors ("CSBS") has been actively engaged in efforts to enhance coordination as we work to develop a federalist system of supervision that ensures safety, soundness, and consumer protection, but still provides economic growth and innovation. As Congress reviews proposals to restructure our financial regulatory system,

there are several principles that must be adhered to. Ultimately, CSBS believes the structure of the regulatory system should:

1. Usher in a new era of cooperative federalism, recognizing the rights of states to protect consumers and reaffirming the state role in chartering and supervising financial institutions.
2. Foster supervision that is tailored to the size, scope and complexity of the institution and the risk they pose to the financial system.
3. Assure the promulgation and enforcement of consumer protection standards that are applicable to both state and nationally chartered financial institutions and are enforceable by locally responsive state officials against all such institutions.
4. Encourage a diverse universe of financial institutions as a method of reducing risk to the system, encouraging competition, furthering innovation, ensuring access to financial markets and promoting efficient allocation of credit.
5. Support community and regional banks, which provide relationship lending and fuel local economic development.
6. Require financial institutions that are recipients of governmental assistance or pose systemic risk to be subject to enhanced safety and soundness and consumer protection oversight.

I thank you for the opportunity to testify and would be happy to answer any of the Committee's questions.

EXHIBIT A



SOURCE: FDIC Call Reports



For Release Upon Delivery  
10:00 a.m., March 23, 2009

**TESTIMONY OF**  
**TONEY M. BLAND**  
**DEPUTY COMPTROLLER, NORTHEASTERN DISTRICT**  
**OFFICE OF THE COMPTROLLER OF THE CURRENCY**  
**before the**  
**COMMITTEE ON FINANCIAL SERVICES**  
**UNITED STATES HOUSE OF REPRESENTATIVES**

**March 23, 2009**

Statement Required by 12 U.S.C. § 250:

The views expressed herein are those of the Office of the Comptroller of the Currency and do not necessarily represent the views of the President.

**Introduction**

Chairman Frank, Ranking Member Bachus, and members of the Committee, my name is Toney Bland and I am the Deputy Comptroller for the Office of the Comptroller of the Currency's Northeastern District. I appreciate the opportunity to appear before the Committee to discuss the availability of credit for small and midsize businesses in Massachusetts. In addition to responding to the Committee's inquiry, I am also here to listen and hear other viewpoints on this important topic.

I have been a National Bank Examiner with the OCC for twenty-eight years, and have served in a variety of positions in the field and in our Washington D.C. Headquarters. For almost my entire career, I have been involved in the direct supervision of community and midsize national banks. In my present capacity, I am responsible for the oversight of nationally chartered community banks in the District of Columbia and fourteen states, including Massachusetts. To put our regulatory role in Massachusetts in perspective, OCC supervises a relatively small portion of the banks headquartered in the state. There are ten nationally chartered community banks headquartered in Massachusetts, holding aggregate assets of roughly \$2.3 billion. In addition, however, several large national banks supervised by the OCC do a significant volume of business in Massachusetts, but are headquartered in other states. By comparison, 165 thrifts and state chartered banks with assets of over \$450 billion are headquartered in Massachusetts.

**Lending to Creditworthy Small and Midsize Businesses**

The OCC fully recognizes the importance of small and midsize businesses to the overall health and vitality of Massachusetts and the U.S. economy. As Secretary of the Treasury Geithner stated last week when he announced another component of the administration's Financial Stability Plan – the Small Business and Community Lending Initiative, "Small businesses are the engine of America's dynamism." The OCC fully supports the Administration's initiatives to expand credit availability and begin the process of financial recovery. We believe these initiatives will have a positive impact on banks' ability and willingness to lend.

The OCC's core mission is to ensure that national banks remain safe and sound and meet the credit needs of their communities and customers. In carrying out our mission, we strive to ensure that banks have the systems and capital in place to support their lending activities. A critical part of our job is determining when potential risk exposures or weaknesses in risk management practices require corrective action by bankers. Knowing when to make these calls requires judgment and a balanced supervisory approach. Taking action too quickly or harshly can impede economic growth and access to credit; waiting too long or not requiring appropriate controls can lead to excessive risks that could impair a bank's ongoing ability to lend and its overall financial condition. The OCC strives to get this balance right through strong, thoughtful and consistent supervision and clear two-way communication with the banks we supervise.

Senior Deputy Comptroller for Bank Supervision Policy and Chief National Bank Examiner, Timothy W. Long, will testify before this Committee later this week on the OCC's national role in ensuring that banks remain safe and sound and meet the credit

needs of their communities and customers. Mr. Long will describe how, across the OCC, we strive to get this balance right.

However, the subject of today's hearing is more specific – the availability of credit to small and midsize businesses here in Massachusetts. To put my remarks into context, it is important to point out that, just like much of the United States, Massachusetts is presently facing serious economic challenges. The Massachusetts economy entered into recession in June of last year as deterioration in the state's housing market and the contracting national economy suppressed employment and industrial production. There have been significant employment reductions in Massachusetts in construction, wholesale and retail trade, information technology and the financial services sector. Payrolls are even taking a hit in Massachusetts' significant education sector which historically has been one of the most stable and consistent sources of growth for the region. Although still below the national level, the state's overall unemployment rate increased to 7.8% in February, up from 7.4% in January. The area is also witnessing worsening local commercial property conditions, with increasing vacancies expected across most property types. And finally, consumer loan delinquency rates in the state are increasing due to declining home prices and the deteriorating labor market. This widespread contraction of economic activity is expected to continue over the coming year.

Many Massachusetts firms have responded to current conditions by running at less than full capacity and, as a result, may experience pressure on profits for some time. We recognize that the vast majority of these small businesses are still fully viable, continue to produce goods and services and still need access to credit. Not surprisingly,

however, the uncertainty surrounding the future of economic conditions in Massachusetts is in some instances restraining loan demand from these small and midsize business borrowers. Likewise, it is not uncommon or unexpected that during recessionary times, banks may be more cautious in the level of credit risk they assume and more selective in the loans they choose to make. However, despite these difficult circumstances, examiners are observing increased levels of lending in OCC supervised community banks in Massachusetts. And, in fact, all of these national banks have strategic plans for growth in 2009.

According to the Small Business Administration (SBA) Office of Advocacy, Massachusetts's 595,959 small businesses (those with fewer than 500 employees) represent 98.0% of the state's employers and 48.3% of its private-sector employment. These companies provide economic opportunities to diverse groups of people and bring innovative products and services to the marketplace. As bank regulators, we recognize the important role that credit availability plays in the viability of these small companies. We share the goal of ensuring banks meet the credit needs of their small and midsize business customers, and have taken steps to see that this happens. Through the *Interagency Statement on Meeting the Needs of Creditworthy Borrowers* issued in November of 2008, all the federal regulatory agencies reiterated our view that, at this critical time, it is important that all banking organizations meet the needs of creditworthy borrowers. The OCC is reinforcing the message of the interagency statement with national banks through our examination process. In addition, our ability to monitor small business lending will be enhanced by steps we are taking to obtain more frequent

reporting of small business lending data. Bank regulators are currently in the process of revising the quarterly Report of Condition to provide this information.

One way banks can reduce the credit risk in loans to small and midsize businesses in this environment is to utilize federal and state programs that are designed to make credit more accessible and reduce lenders' credit exposure. The SBA loan guarantee program is one of the best known of these programs. In evaluating the underwriting and quality of small business loans, OCC views government guarantees or support provided through other programs positively as effective mitigants of credit risk. In fact, guidance provided to our examiners in the *Comptroller's Handbook for Rating Credit Risk* specifically states that those portions of credits having a government guarantee are usually assigned a "pass" rating. This standard is applied uniformly by our examiners in Massachusetts and across the country.

National banks actively participate in government guarantee programs for small business lending. For example, according to the SBA's Website, nine of the ten nationally chartered community banks in Massachusetts have originated SBA guaranteed loans, and seven large national banks doing business in Massachusetts are designated as SBA Preferred Lenders.

#### **Community Reinvestment Act**

Beyond our safety and soundness examination activities, OCC encourages lending to small and midsize businesses in a variety of other ways. Among these are our evaluations of national banks' performance under the Community Reinvestment Act (CRA), our extensive Community Affairs activities and our formal outreach programs.

The CRA encourages each insured financial institution to help meet the credit needs of the community in which it operates. The number and dollar volume of loans to small businesses, particularly those with annual revenues of less than \$1 million, are important considerations in the OCC's evaluation of how well an institution is meeting local credit needs and in the assignment of its public CRA rating. OCC's CRA examination process ensures that a national bank's lending to small and midsize businesses is carefully assessed and subject to public scrutiny, and that these activities have a direct influence on the institution's CRA rating. The bank's knowledge that it will receive positive CRA consideration creates additional incentive to responsibly lend to creditworthy small business borrowers.

#### **Community Affairs and Outreach Activities**

OCC's Community Affairs Department is instrumental in providing information and resources to our examiners, bankers, industry associations and community groups. This OCC function is comprised of staff located in our Washington, D.C. headquarters, as well as Community Affairs Officers located in ten major metropolitan areas across the country, including Boston. These individuals play an active role in agency initiatives to promote existing programs and innovative ideas for advancing small business lending.

The OCC's community affairs activities and publications are specifically developed to increase examiner, banker and community group awareness of programs that promote lending to small businesses. Recent newsletters, informational publications, conferences and teleseminars have highlighted various aspects of small bank lending opportunities and incentives:

- OCC and the other bank regulatory agencies regularly convene seminars for financial institutions to promote bank involvement in CRA activities, including small business lending. During January and February 2009, OCC, the other bank regulatory agencies and SBA held eleven seminars in various locations in the Northeast focused exclusively on small business issues. The OCC has additional programs planned throughout the rest of this year.
- In October 2008, the OCC released the Fall 2008 edition of the *Community Development Investments* newsletter which illustrated various ways multi-bank community development corporations have collaborated to provide financing to small businesses. This newsletter highlighted recently enacted legislative changes to the “Part 24” public welfare investment authority of national banks which will encourage increased bank investment in community development finance activities. We are particularly appreciative of Chairman Frank’s strong leadership in connection with the passage of this important legislation.
- Over the past three years, the OCC has developed two *Community Development Insights* reports which serve as primers for banks considering participation in the SBA 7(a) or 504 Certified Development Corporation loan programs. After the release of these reports, OCC held national informational telephone seminars which drew a combined 3,000 listeners. We intend to update both of these reports in the next few months to reflect the changes included in the American Recovery and Reinvestment Act of 2009. Following release of the updated reports, we plan to hold an additional telephone seminar highlighting



the changes. We will also publicize the SBA program changes through our ongoing CRA outreach to bankers at training seminars and conferences.

- OCC's public Website also houses a wealth of information on small business lending on its Small Business Resource Guide Webpage.

And finally, OCC management and examiners regularly conduct outreach meetings and participate in industry and interagency forums with bank directors, chief executive officers, and senior credit officers to promote sound lending, including loans to small and midsize businesses.

### **Conclusion**

The OCC recognizes the important roles that credit availability and prudent lending to small businesses play in our nation's economy, and we share the Committee's goal of ensuring that banks continue to meet the credit needs of their customers. We recognize that banks are operating in an economic environment that continues to pose significant challenges to them and their customers. However, we have and will continue to support and encourage lending to small and midsize businesses – in Massachusetts and across the country – through our supervisory activities, the CRA process, guidance to bankers, small business related programs and publications and ongoing outreach efforts.

Embargoed until  
March 23, 2009, at 10:00 am



Statement of

Michael Finn, Northeast Regional Director  
Office of Thrift Supervision

regarding

**Seeking Solutions: Finding Credit for Small and Medium-Sized  
Businesses in Massachusetts**

before the

Committee on Financial Services  
United States House of Representatives

Field Hearing  
March 23, 2009

Office of Thrift Supervision  
Department of the Treasury

1700 G Street, N.W.  
Washington, DC 20552  
202-906-6288

Statement required by 12 U.S.C. 250: The views expressed herein are those of the  
Office of Thrift Supervision and do not necessarily represent those of the President.

**Testimony on Seeking Solutions: Finding Credit for Small and Medium-sized Businesses in Massachusetts**

**Before the Committee on Financial Services  
United States House of Representatives  
March 23, 2009**

**Statement of Michael Finn, Northeast Regional Director  
Office of Thrift Supervision**

**I. Introduction**

Good Morning Chairman Frank and members of the Committee. We appreciate the opportunity to provide the Committee with the Office of Thrift Supervision's (OTS) views on expanding credit for small and medium-size businesses in Massachusetts and throughout the U.S.

First, I would like to thank Chairman Frank for his leadership on this issue. A statutory change sponsored by Chairman Frank and supported by OTS passed the House of Representatives in the 109<sup>th</sup> and 110<sup>th</sup> Congress would have increased credit for small-to medium-sized businesses by lifting the limitations on small business lending under which savings associations operate. We appreciate Chairman Frank's resolve and stand ready to work with him to see the changes enacted.

This hearing is very timely. Small business owners have noted the constriction of credit and regulators are working with banks to provide borrowers credit in a safe and sound manner.

This morning, I will discuss factors that OTS believes impede the extension of credit to the small businesses that are the backbone of communities across the

country. I also will describe legislative and regulatory changes that we believe would alleviate these obstacles.

## **II. Thrift Industry Lending**

OTS supervises 19 savings institutions with home offices in Massachusetts that range in asset size from \$25 million to \$2.5 billion. As of year-end 2008, these institutions held total assets of \$10.5 billion. All of these thrifts are well capitalized and have Outstanding or Satisfactory ratings on their most recent CRA examinations. There are also several OTS-supervised institutions headquartered outside of Massachusetts that have a presence in the state.

The institutions that OTS supervises are community-oriented banks that provide credit to meet the needs of families, business and neighborhoods. Small manufacturers and service companies drive employment in communities. Taxes paid by the businesses and employees support infrastructure, schools, social services and other activities in the community.

OTS-supervised savings associations have made diligent efforts to serve the needs of these businesses and have been successful in some regards. For the institutions that we supervise, total loan originations and purchases declined about 11 percent from 2007 to 2008. However consumer and commercial business loans, and nonresidential and multifamily mortgages increased during this period.

Nevertheless, thrift institutions' ability to extend credit to small businesses is limited by law. These caps make the small business lending line of business difficult even for lenders that have not reached the statutory limits and that want to serve that segment of their communities. OTS-regulated institutions do not want to be subject to sanctions for violating regulations by inadvertently exceeding the statutory limits on

small business lending. Also, due to the statutory limits, many thrifts are unable to achieve efficiencies of scale that would make small business lending profitable.

There are legislative actions that OTS believes would increase the availability of credit and facilitate small business lending. OTS also is proposing regulatory changes that would provide more flexibility. I will describe these actions and recommendations in detail.

### **III. Legislative Recommendations**

OTS has advocated and supported legislation to remove the cap on small business lending for thrift institutions. Due to the Chairman's leadership, a statutory change to lift the limitations under which savings associations operate passed the House of Representatives or the Financial Services Committee in the past three Congresses.

The Home Owner's Loan Act (HOLA) currently caps the aggregate amount of loans for commercial purposes at 20 percent of a savings institution's assets. Any commercial loans in excess of 10 percent must be small business loans.

The legislative proposal that OTS supports would remove the cap entirely on small business lending and increase the cap on other commercial lending from 10 percent to 20 percent. The existing 20 percent of assets ceiling imposed on small business lending limits the alternatives for thrifts wishing to diversify their lending operations and credit risk. Smaller lenders operating under these caps are particularly constrained in small business loans they may make to their communities.

### **IV. Regulatory Proposal**

OTS also is exploring regulatory avenues to provide additional flexibility. Currently, we are working on a proposed regulatory change that would amend the definition of "small business loan" to increase flexibility for savings associations wishing to make these loans.

The OTS periodically reviews its rules and regulations regarding lending and investment to ensure that they fully implement statutory authority and requirements, protect consumers, and enable savings associations the flexibility to engage in lending that provides necessary credit to consumers and communities in a safe and sound manner. OTS has modified its lending and investment rule over time as federal savings associations, their markets, their competition, and the economy have changed. This evolving environment makes it appropriate for OTS to again re-examine and update its rules.

OTS is now proposing two specific amendments to its lending and investment regulations. First, the definitions for “small business loans” and “loans to small businesses” would be amended to replace the current dollar limit with a standard that will adapt to and reflect different economic conditions. Second, *de minimis* community development provisions would be amended to increase the amounts that could be invested.

HOLA provides that the Director of OTS has the authority to define “small business loans.” OTS currently defines a “small business loans and loans to small businesses” either to include (1) a loan of any size to a small business as defined by the SBA, or (2) a loan that does not exceed \$2 million (including a group of loans to one borrower) that is for commercial, corporate, business, or agricultural purposes.

OTS is proposing to revise the definition to remove the dollar limit for a small business loan. Instead, the rule would provide that the standards for what qualifies as a small business loan are established by the OTS Director in Thrift Bulletins published from time to time. This change would provide greater flexibility for OTS to adjust the maximum size of a small business loan and possibly vary the limit by thrift size or geography.

Another regulatory change that OTS believes will make a difference is a proposal to increase the *de minimis* community development investments permissible for savings associations. Savings associations are authorized to make *de minimis* community development investments by regulation and OTS is proposing to increase the permissible investment to the greater of three percent of total capital from one percent of total capital or \$500,000 from \$250,000.

This regulatory amendment would provide savings associations with additional flexibility to assist their communities through community development investments.

#### **V. Closing**

We believe these legislative and regulatory changes would go a long way towards unfreezing credit markets in Massachusetts and throughout the country so that savings banks have great ability to lend to small-and medium-size businesses.

We appreciate the Committee's support and stand ready to work with the Committee

JPMORGAN CHASE & CO.

Statement of

Scott Geller

before the

House Financial Services Committee

United States House of Representatives

“Seeking Solutions: Finding Credit for Small and Mid-Size  
Businesses in Massachusetts”

March 23, 2009



Good morning, Chairman Frank, Congressman Capuano and Congressman Lynch. My name is Scott Geller and I am President of Middle Market Banking for the Northeast region at JPMorgan Chase and I am also responsible for our Financial Institutions Group nationwide within our Commercial Bank. I am pleased to represent our company at today's field hearing.

We at JPMorgan Chase are working hard to restore confidence to the U.S. financial system. Although the economic environment continues to be difficult, we have endeavored to responsibly deploy the TARP funds as Congress intended: to restore stability and provide liquidity to the financial system; to ensure credit flows to businesses and consumers; and to stabilize the housing sector by responsibly modifying as many mortgages as possible.

Each month, JPMorgan Chase provides to the Treasury Department a "snapshot" of the intermediation activity in which we have engaged as a result of our participation in the TARP. Although we have seen an increase in mortgage originations as a result of lower interest rates, demand for credit in most other areas remains low.

It is important to note that during a recession, it is normal to see generally flat to lower applications for loans across the board. However, we are lending. During January, we extended almost \$50 billion in new lines of credit and loans, including:

- More than \$16 billion to individual consumers including mortgages, student loans, auto loans, home equity lines, and credit card loans;
- More than \$30 billion in new and renewed commitments to mid-sized businesses and large corporations; and
- More than \$12 billion in purchases of mortgage-backed and other asset-backed securities.

We have also committed to extend an incremental \$5 billion in lending to the government and non-profit sector over the next year.

JPMorgan Chase also continues to implement our mortgage modification plan to keep as many homeowners in their homes as possible. This effort covers more than \$1.4 trillion of mortgages, having been expanded to include not only loans that we own ourselves but also investor-owned mortgages that we service. To date, we have modified over 330,000 mortgages and we plan to double this number by 2010. I am proud to say that the re-default rates we are seeing are significantly better than some of the numbers we have seen published by the regulators.

In addition to the numbers we have provided detailing our nationwide lending activities, I would like to talk about New England specifically. As you are aware, branches are

important to our middle market clients and you would generally not expect a bank to do much business in areas where it doesn't have a footprint. Although our commercial bank has an office in Boston, we do not have any branches in New England. As a result, our focus here has been on larger C&I clients, governments, non-profits, healthcare, and other companies that are less branch dependent. Keeping this in mind, let me address some of the issues we are facing and successes we are seeing in Massachusetts and nearby.

Overall, demand for commercial lending is down across the United States, as small- and mid-sized companies are rationally responding to the difficult economy by carefully managing their liquidity and spending less. The impact of the recession is being felt as businesses across the board see lower sales and are therefore reluctant to take on additional debt. The reduced pace of business activity has resulted in less demand both for working capital loans and fixed asset spending.

Although small, our book of business in New England actually grew by approximately 14 percent year over year, primarily because of healthcare and higher education. We have \$140 million in new or increased business in our pipeline, including a major transaction with a hospital here in Massachusetts. We have lending relationships with 108 New England companies and 16 of these relationships were added in the past year, an increase of more than ten percent. We also serve as a correspondent bank for twelve other financial institutions in New England.

Banks are a vital part of the overall lending picture, but it is important to note that the capital markets are very different today than they have been historically. Going into the current recession, banks accounted for only 20% of the lending activity that took place in our economy. Fifty years ago this number was as high as 60%. The difference was made up by money market funds, securitizations, and bond funds just to name a few. The erosion of this non-bank lending will continue to be a factor in the recovery almost regardless of what traditional banks can do on their own.

The depth and severity of the recession has obviously taken a toll on our business. Although we were profitable during 2008, our earnings were down 64% from the prior year. Our challenge over the next several months will be to continue serving our valued clients while managing our own credit and risk profile. The best way to do this in our view is to keep our lending standards prudent and to maintain a fortress balance sheet.

Our Tier 1 capital ratio at year-end was 10.9%, up from 8.4% at the beginning of 2008. Without the TARP funds this number would have been 8.9%. We have significantly increased loan loss reserves (up \$14 billion to \$24 billion).

In light of the ongoing uncertainty, we announced on February 23<sup>rd</sup> that we were cutting our quarterly common stock dividend to \$0.05 cents from \$0.38 cents per share. Taking this precautionary step will allow us to preserve an additional \$5 billion in common

equity per year. We took this step out of an abundance of caution to keep our balance sheet strong and to enhance our ability to continue the judicious extension of credit mindful of the market and credit risks that we all face. It is important to note that this action was not taken in direct response to TARP but was rather what we believed to be the most prudent course of action during this time of crisis.

Lending is our business, but it comes with a duty to lend responsibly. All of us at JPMorgan Chase are trying to meet the needs of creditworthy borrowers in a safe way, and we look forward to continuing to work with this Committee to find solutions to get our financial services industry, and our economy, back on track. Thank you again for the opportunity to appear today and I would be happy to answer your questions.

## Massachusetts Bankers Association

**Statement of Christopher Oddleifson, President & CEO, Rockland Trust Company  
on behalf of the Massachusetts Bankers Association  
House Financial Services Committee Field Hearing  
Gardner Auditorium, State House  
Monday, March 23, 2009**

### Introduction

Chairman Frank, members of the Committee, my name is Chris Oddleifson and I am the President and Chief Executive Officer of Rockland Trust Company. I also serve as Vice Chairman of the Massachusetts Bankers Association, which represents nearly 200 commercial, savings and cooperative banks and federal savings associations located throughout the Commonwealth and New England. I appreciate the opportunity to testify at today's hearing regarding credit availability for small- and medium-sized businesses in Massachusetts.

Community banks here in Massachusetts are making loans to creditworthy businesses. While these are certainly difficult economic times, I am pleased to confirm that the current environment has proven to be a time of tremendous opportunity for community banks because of how well-positioned they are to address the unmet needs of business borrowers. Many community banks are seeing a sharp increase in loan demand from businesses and, as those opportunities are carefully underwritten, approved, and closed, experiencing significant loan growth. In Massachusetts, both loans and deposits grew last year while loan delinquencies (up a bit in the 4<sup>th</sup> quarter) remained less than 1 percent. In contrast, the national average approached 3 percent.

The banking industry in Massachusetts is well-capitalized, and holds higher levels of reserves than the national average. Even as the nation continues to struggle through the ongoing recession, Massachusetts banks are well positioned to be an active part of the solution to the state's economic problems. Our banks did not engage in subprime lending or offer exotic mortgages, they did not, and do not, have significant foreclosure problems and managed risk well, including denying certain loans when it was appropriate. With the relative slow growth throughout the state, we did not see as much of the speculative building and lending that has caused significant problems in other areas of the country such as the southeast and the southwest.

Massachusetts institutions also have strong capital and reserves on hand. In fact, loan-loss reserves are far more than the national average and almost twice the percentage on hand during the last major downturn in the late 1980s and early 1990s. While some Massachusetts banks reported losses in 2008, these were not shortfalls in their core businesses but extraordinary items on their balance sheets, such as the losses in Fannie Mae and Freddie Mac preferred stock.

With the recent "flight to quality" and increases in deposits at local banks, there is plenty of money to lend to qualified residential and business borrowers. Local banks continue to lend in a safe and sound manner to local businesses throughout the state. In fact, commercial loans balances at Massachusetts community banks increased from \$5 billion in 2007 to \$5.7 billion in 2008 and we have heard from bankers throughout the state that loan demand is up sharply in recent months. Therefore, given loan availability here in Massachusetts, we suspect that business

Massachusetts Bankers Association, Inc  
73 Tremont Street, Suite 306  
Boston, Massachusetts 02108-3906  
Tel: 617-523-7595/Fax: 617-523-6373  
<http://www.massbankers.org>

House Financial Services Committee  
Monday, March 23, 2009  
Page 2

that are having difficulty seeking credit may be experiencing a deterioration in their business model or earnings due to the economic downturn.

However, banks, both large and small, account for only a portion of the commercial credit market in the United States. Finance companies, various investment funds, institutional investors and insurance companies have all played a major role in commercial lending in recent years. Unfortunately, problems in the secondary market have led many of these large institutions to reduce or even discontinue their commercial lending activities.

While there are many underlying reasons why community banks are now seeing a surge in loan demand, a primary reason for the current increase in their lending is the decrease in credit made available by these other entities. Business borrowers who formerly found a home with larger out-of-state institutions are more and more frequently turning to their local banker. While community banks, due to the size of the loans they can make, cannot completely fill the void left by the departure of larger lenders, community banks have done a great deal to fulfill the business lending needs based upon the increased flow of loan applications they are seeing.

To provide you with a specific, anecdotal example of what Massachusetts community banks are doing to expand the flow of credit to business borrowers, let me tell you about our bank. I am the President of Rockland Trust Company, a commercial bank, which currently has approximately \$3.6 billion in assets. Rockland Trust offers a full range of banking services through its 60 full service branches and 10 commercial lending centers located throughout Southeastern Massachusetts and on Cape Cod, and can make loans of up to approximately \$55 million.

A year to year comparison between 2007 and 2008 of Rockland Trust's commercial loan closings gives some indication of just how much the demand for credit has increased: during 2007 Rockland Trust closed \$318 million in commercial loans, while in 2008 Rockland Trust closed \$401 million in commercial loans. During the fourth quarter of 2008 alone, Rockland Trust's commercial loan balances grew by \$76 million, or 26% on an annualized basis. This fourth quarter growth represented approximately half of Rockland Trust's organic commercial loan growth experienced in 2008. Thus far in 2009 Rockland Trust continues to experience significant commercial loan application activity.

While there may be excess capacity among traditional banks, some businesses are less creditworthy than they were 12-18 months ago due to the recession. As I mentioned earlier, community banks have not tightened their underwriting criteria, however some of the lenders that had been offering credit with more favorable terms may not be in the market any longer. We would encourage the Committee to focus on policies that help responsible lenders expand their capacity to lend instead of loosening the credit markets only to have some of the more egregious practices of the last several years return.

The Association, along with our member institutions, has also been working with the Patrick Administration over the last several months on initiatives to further revitalize the commercial credit market here in Massachusetts. We have been working with the Governor's Secretary of Housing and Economic Development Greg Bialecki on a proposal to create a "soft-second" type of program for commercial loans that will provide a small government guarantee on

House Financial Services Committee  
Monday, March 23, 2009  
Page 3

a portion of the total loan amount. The program, which is similar in structure to the state's successful Soft Second program for residential mortgage loans, would help encourage lending to businesses that may be suffering from the effects of the current recession.

In addition, the Association is hosting a Commercial Lending Summit on April 7 that will bring together bankers, state and federal government officials, quasi-public agencies, and academics to discuss the state's economic climate and potential opportunities for local banks to expand their commercial lending business. Representatives from the Patrick Administration as well as the Small Business Administration, MassDevelopment, and others will also provide an overview of the state's plans for use of the economic stimulus funds to help spur job creation and economic growth.

#### **Other Issues Affecting the Flow of Credit**

The Association would also like to offer our comments on several legislative and regulatory issues that could have an impact on the lending capacity of all institutions in Massachusetts. First, from a perception standpoint, a better distinction needs to be made between Wall Street investment banks and the traditional retail banking community. MBA is working very hard on this problem, and we appreciate the Chairman's past comments on this issue. However, the misconception that all banks are having problems dampens public confidence, makes consumers believe that loans are not available, and hampers the economic recovery.

Second, the recently announced increases in FDIC deposit insurance premiums along with the 20 basis point special assessment will impose significant costs on the banking industry and result in capital being removed from the system at a time when policymakers are asking banks to lend more in their local communities. While the banking industry has always and continues to stand behind the FDIC fund, both the timing and the amount of these new assessments may have a serious impact on lending. We would encourage the Committee to work with the FDIC to determine ways in which the impact of the special assessment can be minimized and spread over time. We appreciate your work in passing legislation recently that would increase the FDIC's line of credit with the Department of the Treasury, and we urge you to work with your colleagues in the Senate to ensure this legislation is signed into law soon.

The Association also applauds the Committee's work on mark-to-market accounting issues, in particular the hearing on March 12. As you know, many of the losses suffered by local banks are largely accounting losses. Inflexible rules have led to an erosion of earnings and capital at many institutions which, in turn, inhibit their ability to lend. For example, the Federal Home Loan Bank (FHLB) of Boston recently was forced to write down more than \$339 million in other-than-temporary-impairment (OTTI) charges on its mortgage-backed securities portfolio, when the actual anticipated loss is only expected to be approximately \$22 million. This has led the FHLB to suspend the dividend on its stock – much of which is held by community banks.

The Association appreciates the recent announcement by the Financial Accounting Standards Board (FASB) that it will act within the next three weeks to finalize changes to the mark-to-market accounting rules. However, the current proposals released by FASB, while a very good first step, do not go far enough – particularly with regards to the regulatory and capital impact of these accounting losses. We believe that further changes to the rules may be needed,

House Financial Services Committee  
Monday, March 23, 2009  
Page 4

and that action in this area will provide significant benefit without any cost to the federal government. We encourage the Committee to continue with your strong oversight of this process.

Finally, the Association remains concerned about the potential impact of changes to the bankruptcy laws that would allow cram-downs on all residential mortgages. While this doesn't specifically impact commercial lending, it will certainly increase losses in the mortgage backed securities market which many banks hold and also discourage banks from making credit available to certain borrowers in the future. We hope this legislation can be narrowed to apply only to those that received high cost or non-traditional mortgage loans originated during a set period of time.

#### **Conclusion**

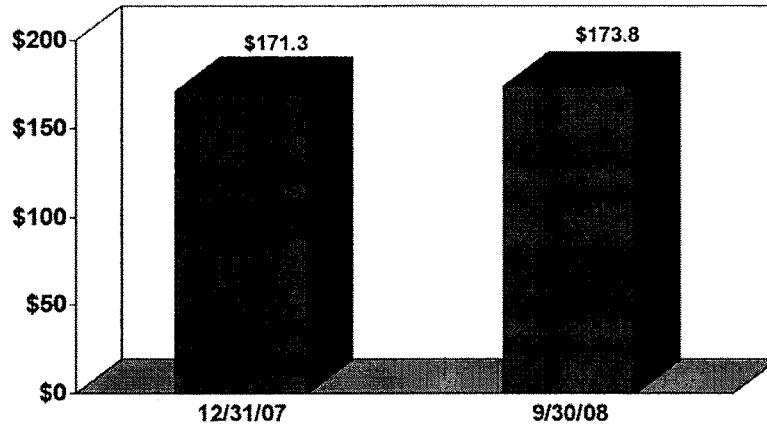
Massachusetts community banks are currently experiencing increased loan demand and, in accordance with prudent underwriting and decision-making, are actively working to address the unmet needs of credit-worthy businesses. To the extent that there is any "credit crisis" here locally in Massachusetts, community banks are very much a part of the solution and are not the ones causing any of the problems.

I hope this information is helpful. Thank you for considering our views.

## Massachusetts Banks

### Loans

Amounts in Billions

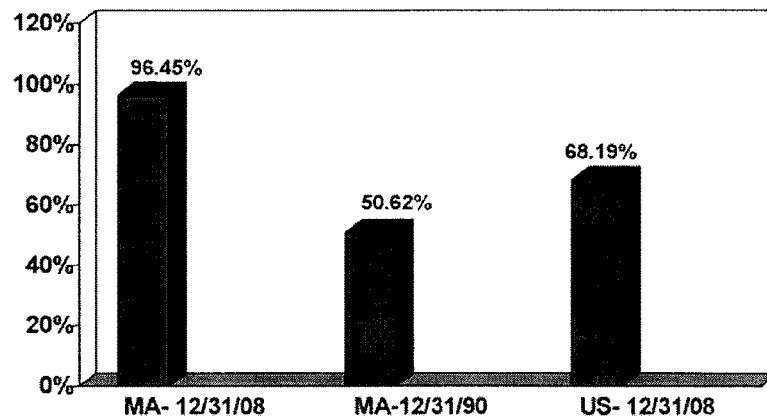


1

## State Chartered Institutions

### Reserves to Noncurrent Loans and Leases

Percent

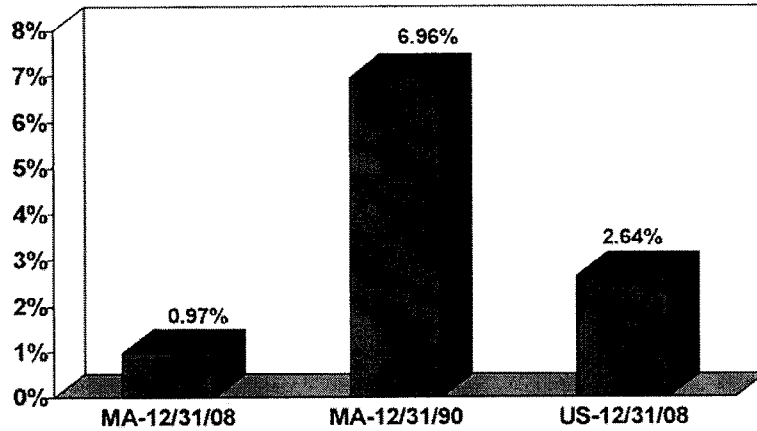


2



## State Chartered Institutions

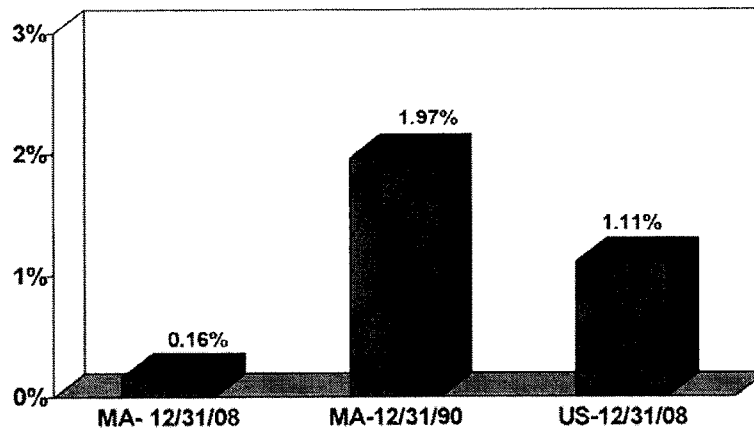
Noncurrent Loans and Leases to Total Loans and Leases  
Percent



3

## State Chartered Institutions

Net Charge-offs to Loans and Leases  
Percent



4

Testimony of

Perry Pelos  
Wells Fargo & Company

before the

House Financial Services Committee  
US House of Representatives  
Boston, Massachusetts

March 23, 2009

Chairman Frank, Ranking Member Bachus, members of the committee: My name is Perry Pelos. I am Executive Vice President and Group Head of Wells Fargo's Commercial Banking Group. It's an honor for me to speak to you today.

I've worked almost a quarter century at Wells Fargo – the entire time in Commercial Banking and Corporate Banking. I attended Northwestern University, where I earned a bachelor's degree in economics and an MBA in finance and accounting.

First, allow me to describe our Commercial Banking customers. We serve middle-market businesses with annual sales between \$20 million to \$750 million. Wells Fargo serves 12,000 of these businesses nationwide. In New England, we have full service relationships — including loans and lines of credit — with companies in energy, agriculture, manufacturing, transportation, and high-tech. Although our market share at the moment is smaller in Massachusetts, relative to our industry peers, Wells Fargo views the state and region as an opportunity for growth.

Wells Fargo has remained open for business when many other banks have pulled back or exited from commercial lending. Now, as always, we want to do what's right for our customers. We've never stopped lending.

Wells Fargo has been able to increase our lending to creditworthy customers over the past year and half. That's partly because we were building capital and shrinking our balance sheet in 2005 and 2006 when credit spreads were unrealistically low and not priced for their underlying risk.

Here's how we've increased our loans:

- In the last 18 months, we made \$63 billion in commercial loans and commercial real estate loans.
- Our middle-market portfolio in the Northeast grew 11 percent from year-end 2007 to year-end 2008.
- Our commitments to government and education in Massachusetts and five other Northeast states are \$543 million.
- In 2008, we achieved double-digit growth in asset-based lending, middle market lending, commercial real estate, and

specialized financial services – which includes capital markets and relationships with Fortune 500 companies.

- At the end of fourth quarter 2008, we had \$68 billion in commercial real estate and construction loans, up 6 percent from the third quarter.

To address the Committee's question about the effect of federal laws or regulations on credit availability, Wells Fargo urges an approach more consistent with past economic downturns. We believe the Chairman's efforts with respect to mark-to-mark accounting will allow the entire financial services industry to continue supporting the credit needs of our customers.

In January of this year, we made \$14 billion in commitments to commercial banking customers. Half of these dollar commitments were to new customers. Overall, Wells Fargo extended \$51 billion in loans and loan commitments in January. That brings the total credit extended to our customers to \$144 billion in the last four months. That's nearly six times the \$25 billion capital investment made by the U.S. Treasury in Wells Fargo last fall.

Our integration of Wachovia into Wells Fargo is proceeding even better than we expected. In New England, Wachovia's commercial banking portfolio was \$6 billion in loan commitments, including government and education, at year-end 2008. Wells Fargo is committed to the financial success of each of those New England companies and institutions, and we look forward to long-term relationships with them all.

After the Wachovia acquisition, Wells Fargo stepped in to open lines of credit for some businesses whose access had been shut down, especially cities and non-for-profit hospitals. When the debt markets for these borrowers were compromised last fall, Wells Fargo substantially increased its support and level of commitment to this area.

As Wells Fargo continues to integrate the Wachovia businesses and manage through a difficult economic time, we will continue to work with our customers.

Mr. Chairman and members of the committee, thank you for listening. I'm pleased to answer any questions.



Written Testimony of  
Eric S. Rosengren  
President & Chief Executive Officer  
Federal Reserve Bank of Boston

Field hearing of the  
Committee on Financial Services of the  
U.S. House of Representatives:  
*“Seeking Solutions –  
Finding Credit for Small and  
Mid-Size Businesses in Massachusetts”*

Monday, March 23, 2009  
Massachusetts State House  
Boston, Massachusetts

---

*Note: The figures (charts) mentioned in this testimony are attached below the text.*

---

Chairman Frank and members of the Committee, it is my pleasure to appear before you today to discuss the availability of credit for businesses amid the current economic and financial turmoil, and the steps the Federal Reserve is taking to help make credit available to small and medium-sized businesses.

In my testimony today I plan to first share some national context, and some perspective on the Federal Reserve System's responses to date. I plan to then comment, more briefly, on the situation in Massachusetts.

#### **The National Context**

Since August of 2007, financial markets have been severely disrupted. The functioning of financial markets and the functioning of institutions that serve as financial intermediaries have tremendous downstream impacts on businesses, state and local governments, and households. As a result, these disruptions are of great concern to the Federal Reserve as we pursue our policy goals of maximum sustainable employment, stable prices, and moderate long-term interest rates.

While credit availability has been a concern since the outset of the financial crisis, the credit situation became more severe as problems expanded beyond a few large financial institutions focused on subprime-mortgage securitizations to a broader group of financial institutions. The Federal Reserve's *Senior Loan Officer Opinion Survey on Bank Lending*

*Practices* has been showing substantial tightening of credit, which dovetails with the perspectives voiced since last summer by many advisory groups we engage at the Boston Fed. Other entities such as Associated Industries of Massachusetts are finding when they survey companies that credit conditions are tightening – and that the tightening may affect companies directly, or indirectly through suppliers and customers who face credit constraints.

The Federal Open Market Committee (FOMC) remains focused on ensuring adequate financing for businesses of all sizes. Last week’s official FOMC statement indicated, among other things, that “weaker sales prospects and difficulties in obtaining credit have led businesses to cut back on inventories and fixed investment.” Earlier this month, the Federal Reserve’s *Beige Book* report suggested that “The availability of credit generally remained tight. Lenders continued to impose strict standards for all types of loans, with scattered reports of further tightening and particular scrutiny focused on construction projects and commercial real estate transactions.”

Credit availability issues remain a significant focus at the Federal Reserve and are a significant factor in how we are addressing the current economic and financial problems. The Federal Reserve has acted proactively and creatively to address these concerns – first by aggressively easing conventional monetary policy (the federal funds rate) and, since the fall, using less-conventional monetary policy tools to mitigate continuing problems with the cost and availability of financing for businesses and households.

**Figure 1** shows how the Federal Reserve acted to address problems in financial markets, and concerns that market disruptions would impact the cost and availability of finance, by rapidly moving the target federal funds rate to only a little above zero. As the Federal Reserve

lowered the target federal funds rate, most short-term market interest rates fell – although not commensurate with the decline in the federal funds rate.

It is important to note that many small and medium-sized businesses have loans tied to the prime rate, or to the London Interbank Offered Rate or Libor, which decreased significantly as we moved the federal funds rate from 5.25 percent in July 2007 to between zero and one-quarter of one percent at the end of December. While a year ago many observers were critical of these rapid rate cuts, it is fortunate that the Federal Reserve *did* move so quickly. While the reduction in interest rates did not prevent the economy's weakening, it helped cushion the economy against some of the shocks experienced over the past year.

With the federal funds rate approaching the zero bound, the Federal Reserve has turned to some alternative approaches to monetary policy, which have rapidly increased the Fed's balance sheet. Many of the new programs are intended to improve the availability of credit in the marketplace and reduce the cost, which had not fallen commensurate with the decline in the federal funds rate. I would like to briefly discuss these Federal Reserve programs.

**Figure 2** shows the composition of the Fed's balance sheet. The largest expansion of the balance sheet occurred in the fall, as a series of actions were taken in response to the increasingly fragile state of financial markets. Our actions were designed to improve the functioning of interbank lending. Borrowers and businesses whose rates are tied to interbank rates like Libor benefit as interbank lending markets see more normal spreads and declining rates.

Allow me to mention two programs that have been critical to the improvements in interbank lending markets and the related reduction in market interest rates – the Federal Reserve's Term Auction Facility or TAF, and a network of liquidity swap lines we have arranged



with other central banks. The TAF is designed to help ensure that banks can obtain the funds they need to provide credit to their customers. It involves an auction-model variant of discount-window lending to financial institutions (backed by collateral subject to significant “haircuts,” to mitigate risk to the Federal Reserve). Central bank liquidity swaps are loans made to foreign central banks so that they can provide dollar funding to their banks in much the same manner as our TAF.

These two programs were designed to stabilize and improve the functioning of the interbank dollar-lending market – indeed, to ease conditions in global dollar markets that were spilling over into our own funding markets. As shown in **Figure 3**, the Libor rate is now much more aligned with the federal funds rate. The reduction in the Libor rate helps a variety of borrowers. Most subprime mortgages have reset rates tied to Libor, many credit card rates are tied to Libor, and the rates on many business loans are tied to Libor. The actions we have taken are reducing the cost of financing for borrowers and businesses whose rates are tied to Libor and thus influenced by the functioning of interbank dollar lending markets.

I would like to mention another area of substantial growth in the Fed’s balance sheet – specifically, the Federal Reserve liquidity facilities designed to provide market support and improve conditions in short-term credit markets (see **Figure 4**). Some, like the Commercial Paper Funding Facility (CPFF), provide an alternative funding source to the market when interest rate spreads become very elevated.

In general, the various programs that have expanded the Federal Reserve’s balance sheet should be less attractive to market participants as financial conditions improve. **Figure 5** shows

that of late, the rate on asset-backed commercial paper has fallen dramatically, and many issuers can receive better terms by issuing commercial paper directly to the market.

**Figure 6** shows that the prime money market funds have tended of late to have a net inflow of funds, which has helped stabilize short-term credit markets because money market funds are a key investor in these markets. Correspondingly, money market funds have reduced their reliance on the Fed liquidity facility that was designed to help them – the asset-backed commercial paper money-market mutual fund liquidity facility, or AMLF. This experience provides a clear example of how improved market conditions provide incentives for financial firms to reduce reliance on our facilities. We expect this to be the case for many of our facilities as the economy and financial markets gradually improve. Stabilized short-term credit markets mean that businesses that borrow with commercial paper are able to obtain less costly, more dependable sources of financing. In addition, many issuers of commercial paper used the funding to provide loans to businesses to finance receivables, to provide floor plan financing, and to provide other types of essential short-term credit.

Two new programs should provide additional help to markets. First, the Term Asset-Backed Securities Loan Facility (TALF) is designed to facilitate the renewed issuance of consumer and small business asset-backed securities – essentially providing a financing vehicle for credit instruments that have been disrupted by poor functioning in securitization markets. This facility, which is just starting up, should help make credit more available for student loans, consumer credit, commercial real estate, and small business loans; leading to lower borrowing rates and improved access in the market for consumer and small business credit. The facility will do this by lending against triple-A rated asset-backed securities collateralized by recently originated student loans, auto loans, credit card loans, loans guaranteed by the U.S. Small

Business Administration, mortgage servicing advances, loans or leases relating to business equipment, leases of vehicle fleets, or floorplan loans. A second program involves the large-scale purchases of mortgage-backed and agency securities. As shown in **Figure 7**, conventional mortgage rates that had been around 6 percent have declined since the announcement of this program.

Last Wednesday the Federal Open Market Committee announced that to provide greater support to mortgage lending and housing markets, the Federal Reserve would further increase its balance sheet by purchasing up to an additional \$750 billion of agency mortgage-backed securities (bringing its total purchases of these securities up to \$1.25 trillion this year), and to increase its purchases of agency debt this year by up to \$100 billion (to a total of up to \$200 billion). An important effect of this program is that it provides lower cost loans to homeowners, but it should be recognized that the program also bears significant benefits for many small businesses, which often rely on home equity loans as a critical source of initial financing. I should also mention that in order to improve conditions in private credit markets, the Committee on Wednesday decided to purchase up to \$300 billion of longer-term Treasury securities over the next six months. This action is expected to ease credit conditions in a wide variety of markets that tie their cost of finance to Treasury yields.

#### **The Situation in Massachusetts**

While my goal today has been to provide some national context and perspective, I would like to add a few comments about the situation in Massachusetts and New England. **Figure 8** shows that lending patterns in the United States differ depending on the financial condition of the

banks. Banks with the lowest supervisory ratings have reduced their lending while banks in better health show positive asset-growth percentages. Empirical research suggests that during previous banking crises this behavior was, to an important degree, explained by differences in the ability to *supply* credit, not just differences in the *demand* for credit. As you know, extending credit means expanding the asset side of the balance sheet for a bank, and banks must maintain a reasonable capital-to-assets ratio. This underlines the importance of steps to bolster or resolve poorly capitalized banks, in order to address broader problems of credit availability.

**Figure 9** shows that the share of commercial and savings banks with the lowest supervisory ratings is quite a bit smaller in New England than it is nationally – and furthermore, that share has remained constant in New England while doubling for the nation overall in a year's time. Considering the aforementioned dynamic, the good news locally is that a greater share of New England banks are in good health and thus more able to supply credit to businesses. Of course, most anecdotal indications are that even among healthy banks willing to lend to creditworthy borrowers, standards have probably tightened in response to the riskier environment (that is, over concern related to the impact of the slowing economy on even creditworthy borrowers).

### **Concluding Observations**

In conclusion, I would offer just a few summary thoughts. Over the last year and a half or so, the Federal Reserve has been proactive and innovative in trying to address problems in financial markets and the broader economy. While traditional monetary policy had focused on lowering the federal funds rate to spur interest-sensitive economic activity, now that this rate has

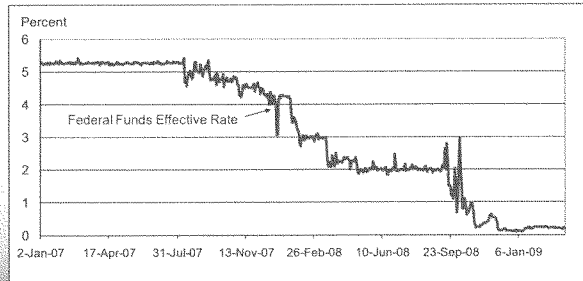
approached the zero-bound floor, the Federal Reserve has focused on more direct means of lowering the cost of credit in the marketplace, which had not fallen commensurate with the decline in the federal funds rate. Federal Reserve programs have intended to offset disruptions to interbank lending, short-term credit financing, the ability of money market mutual funds to meet investor redemption requests, and housing finance – and these program should have beneficial effects on the cost and availability of credit for businesses.

Thank you for inviting me to testify today. If I can answer any questions I would be very pleased to do so.

<b>Figures</b>
----------------

Figure 1  
Federal Funds Effective Rate

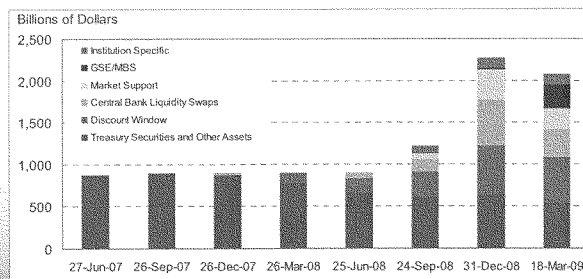
January 2, 2007 - March 18, 2009



Source: Federal Reserve Board / Haver Analytics

Figure 2  
Composition of Federal Reserve System Assets

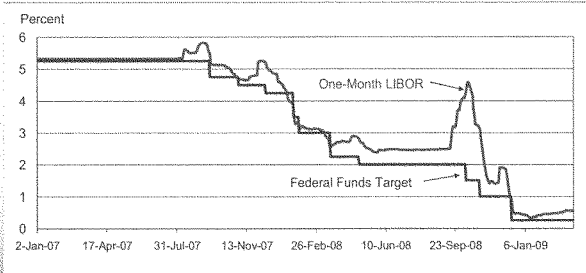
June 27, 2007 - March 18, 2009



Source: Federal Reserve Statistical Release H-4.1

Figure 3  
One-Month London Interbank Offered Rate (LIBOR) and the Federal Funds Target Rate

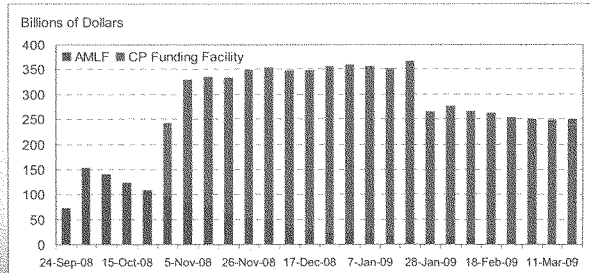
January 2, 2007 - March 18, 2009



Source: Federal Reserve Board, Financial Times / News Analytics

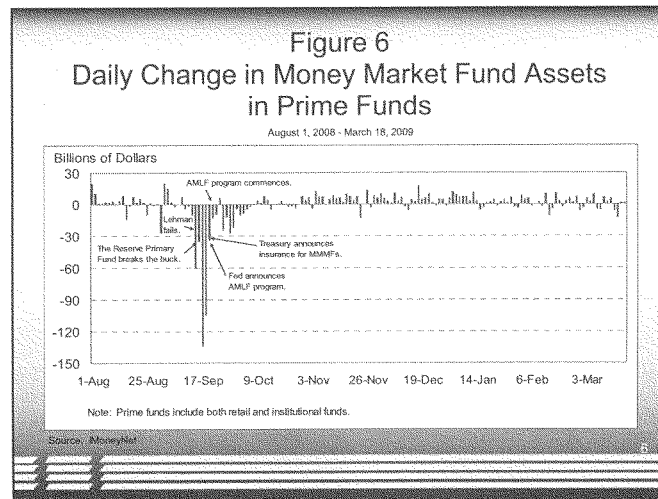
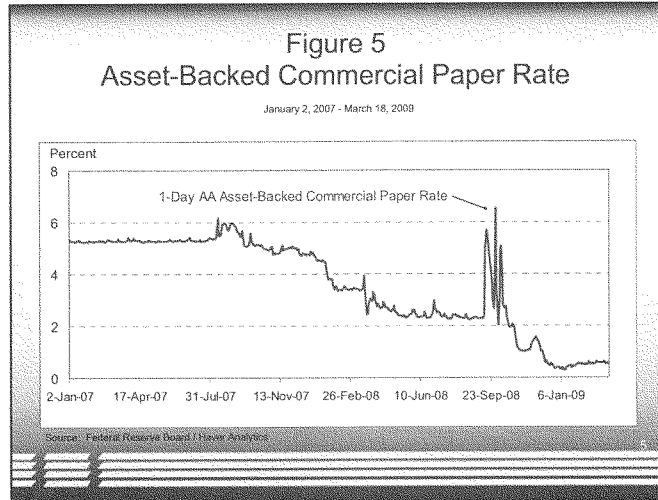
Figure 4  
Federal Reserve System Assets held by Market Support Facilities

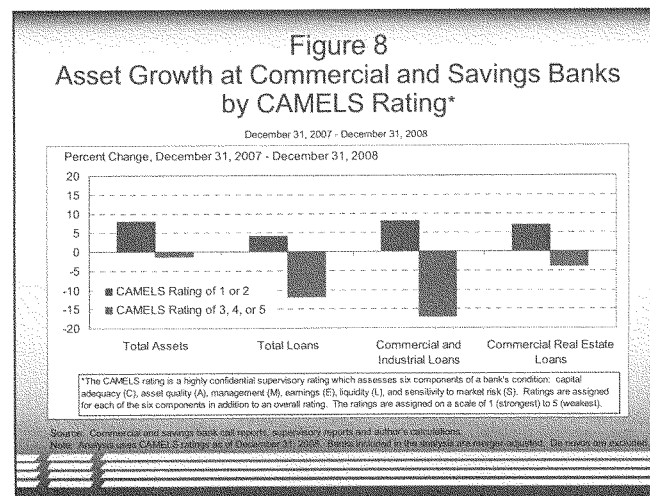
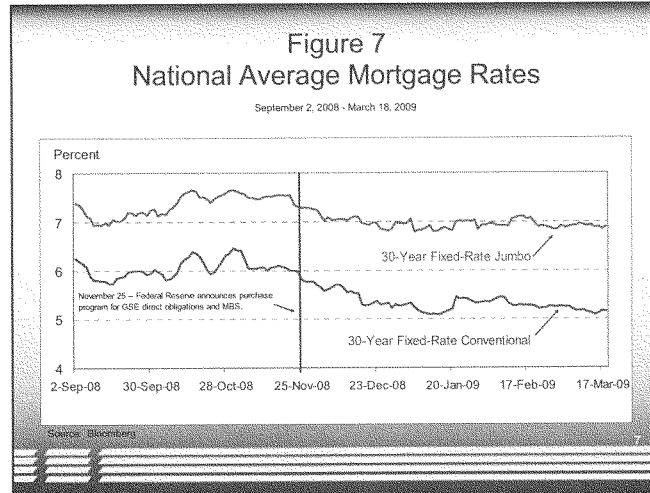
September 24, 2008 - March 18, 2009



Source: Federal Reserve Statistical Release H-4.1







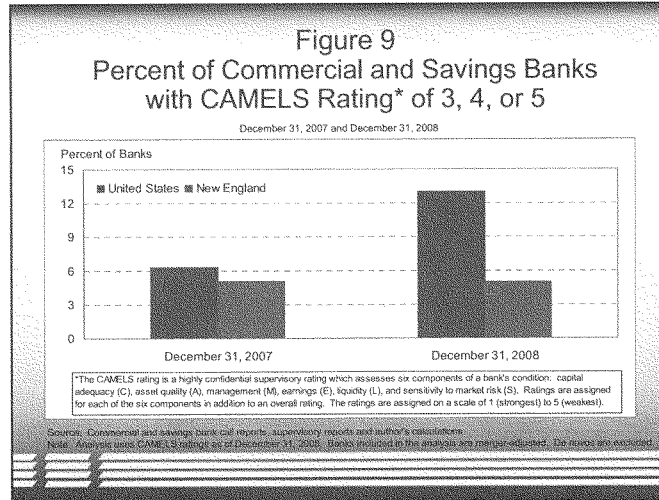
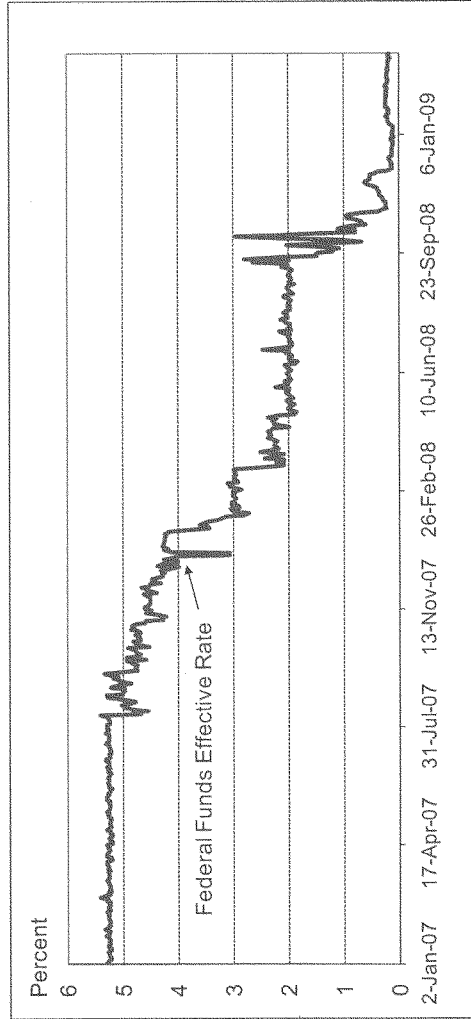


Figure 1  
Federal Funds Effective Rate

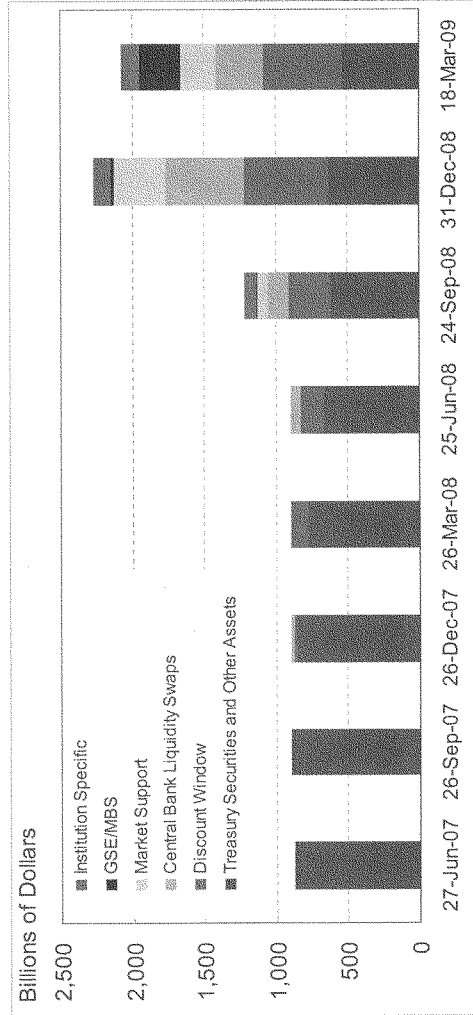
January 2, 2007 - March 18, 2009



Source: Federal Reserve Board / Haver Analytics

**Figure 2**  
**Composition of Federal Reserve System Assets**

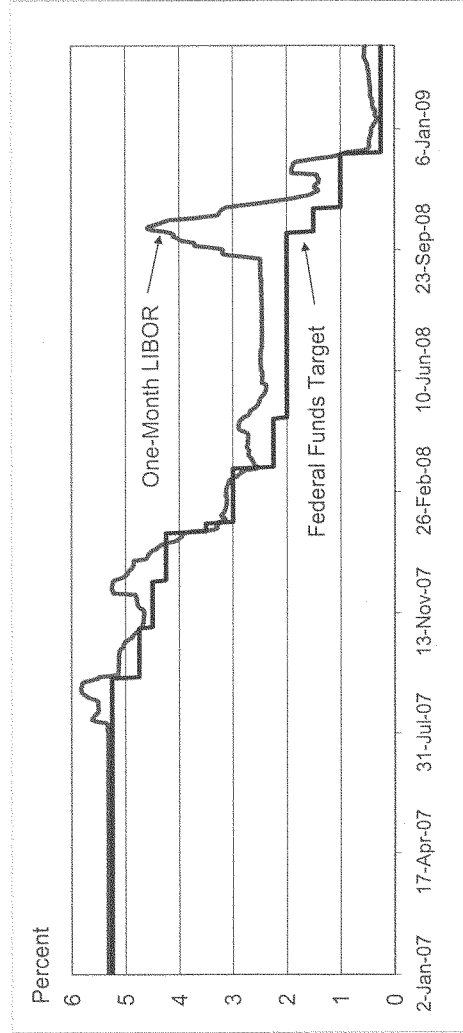
June 27, 2007 - March 18, 2009



Source: Federal Reserve Statistical Release H.4.1

**Figure 3**  
**One-Month London Interbank Offered Rate**  
**(LIBOR) and the Federal Funds Target Rate**

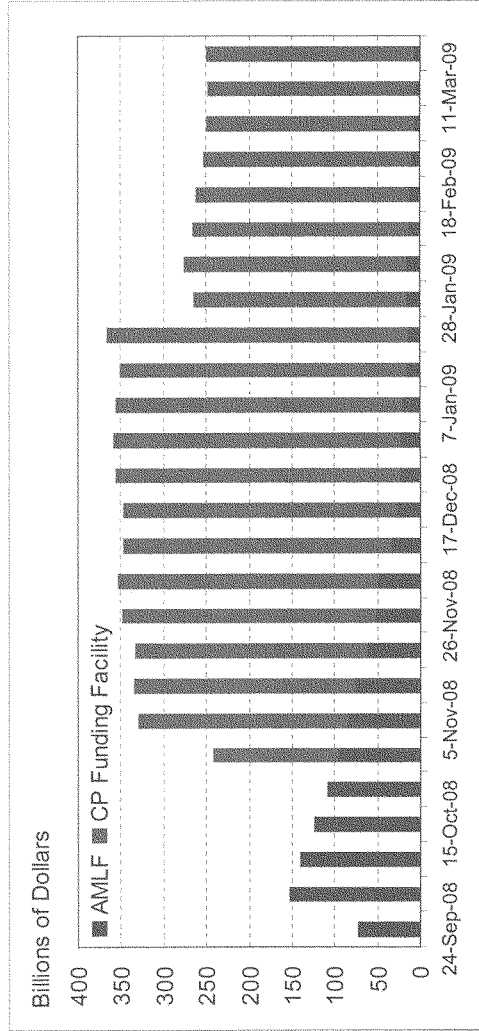
January 2, 2007 - March 18, 2009



Source: Federal Reserve Board, Financial Times / Haver Analytics

**Figure 4**  
**Federal Reserve System Assets**  
**held by Market Support Facilities**

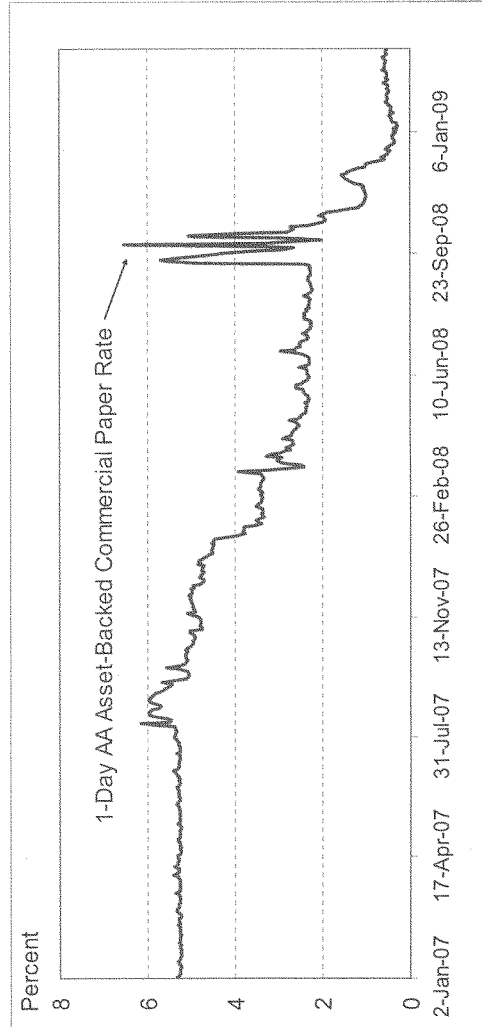
September 24, 2008 - March 18, 2009



Source: Federal Reserve Statistical Release H.4.1

Figure 5  
Asset-Backed Commercial Paper Rate

January 2, 2007 - March 18, 2009

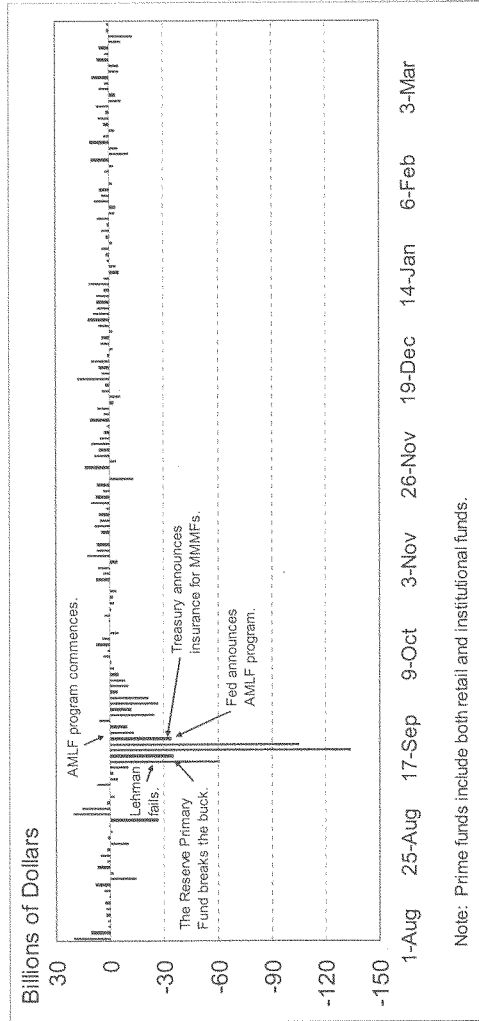


Source: Federal Reserve Board / Haver Analytics



**Figure 6**  
**Daily Change in Money Market Fund Assets**  
**in Prime Funds**

August 1, 2008 – March 18, 2009

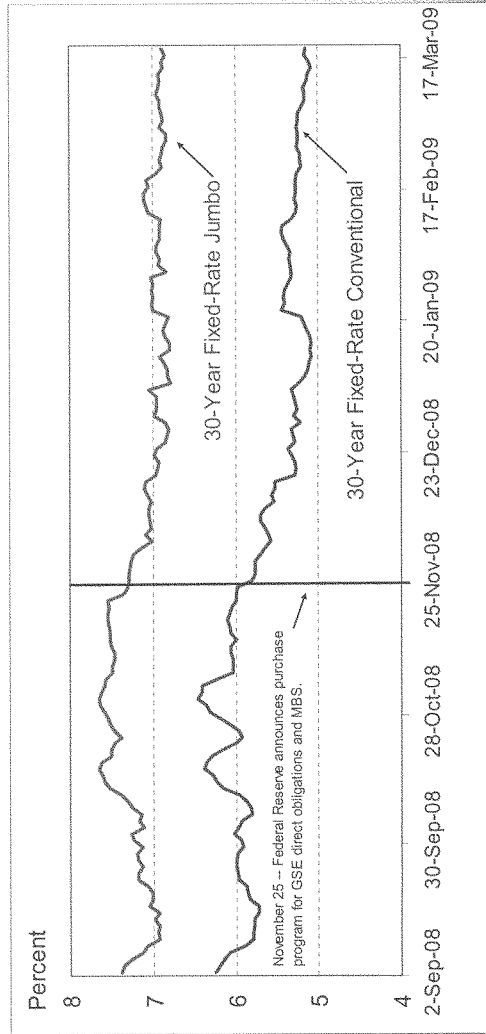


Source: iMoneyNet

# Figure 7

## National Average Mortgage Rates

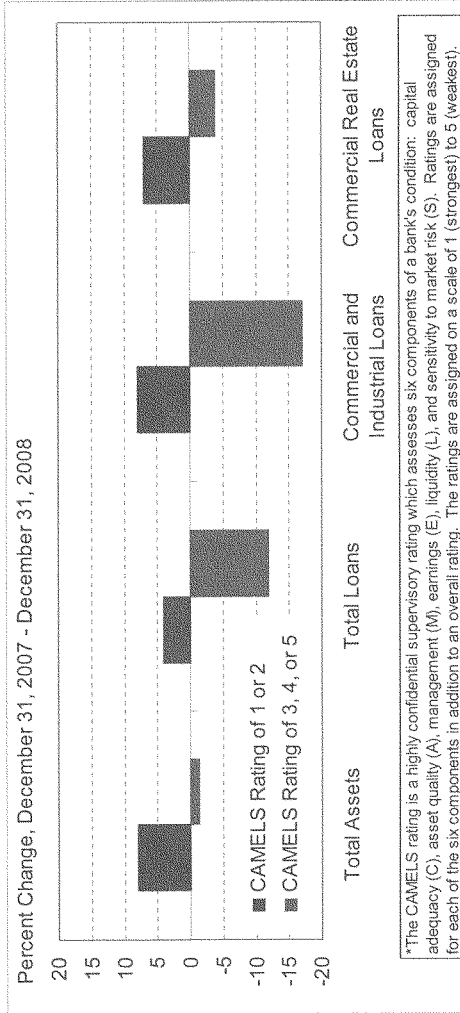
September 2, 2008 - March 18, 2009



Source: Bloomberg

**Figure 8**  
**Asset Growth at Commercial and Savings Banks**  
**by CAMELS Rating\***

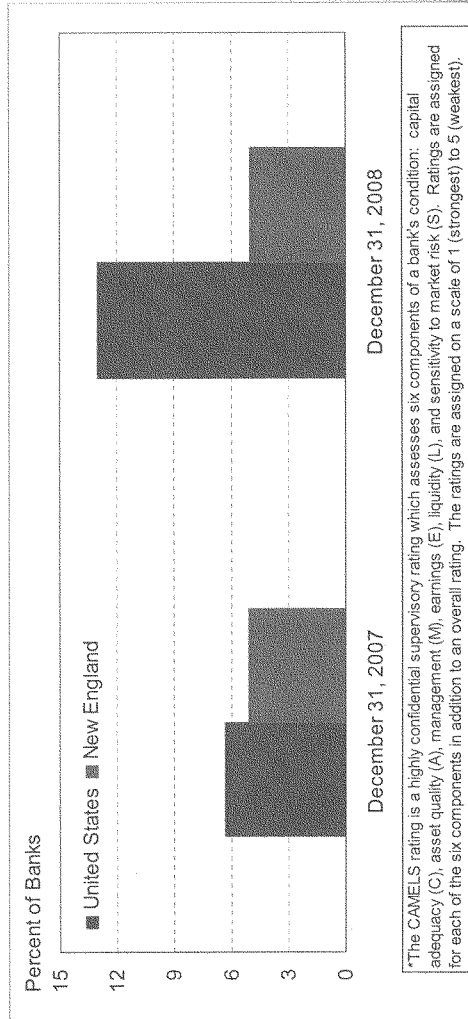
December 31, 2007 - December 31, 2008



Source: Commercial and savings bank call reports, supervisory reports and author's calculations.  
 Note: Analysis uses CAMELS ratings as of December 31, 2008. Banks included in the analysis are merger-adjusted. De novos are excluded.

**Figure 9**  
**Percent of Commercial and Savings Banks**  
**with CAMELS Rating\* of 3, 4, or 5**

December 31, 2007 and December 31, 2008



Source: Commercial and savings bank call reports, supervisory reports, and author's calculations.

Note: Analysis uses CAMELS ratings as of December 31, 2008. Banks included in the analysis are merger-adjusted. De novos are excluded.

**Testimony of Edwin T. Shea, Jr.  
Business Banking / Regional Market Executive  
Central Massachusetts Market President  
Bank of America**

**Before the House Financial Services Committee  
Field Hearing On  
Finding Credit for Small and Medium-Sized Businesses**

**Gardner Auditorium  
Massachusetts State House  
Boston, Massachusetts**

**March 23, 2009**

**Introduction**

Good morning, Chairman Frank and Members of the Committee. My name is Ed Shea and I am the Business Banking Market Executive for the Boston / MetroWest Market and the Central Massachusetts Market President for Bank of America. I appreciate the opportunity to share our views on the current state of lending to small and medium-sized businesses. The issues being discussed today are of great importance to our local, state, regional and national economy.

Bank of America has a broad, strong and longstanding commitment to serving small and medium-sized businesses. We and our predecessor banks have been serving business clients for well over 200 years. During that time, we have weathered many economic cycles with our clients. Today, we have relationships with more than 4.5 million small and medium-sized businesses across the country and serve these clients with a wide range of products and services, including deposit products, treasury management solutions, loan products, investments and advisory services, as well as a full suite of online banking capabilities. Bank of America provides products and services to all types of businesses, from home-based businesses through Fortune 500 corporations. Our testimony today will focus on our Small Business Banking and Business Banking client segments, representing small and medium-sized businesses with annual revenues of up to approximately \$20 million.

**Current Business Environment**

We are keenly aware of the challenges our business clients are facing during this economic cycle and the ways in which they are adapting to these changes. A recent survey by the National Federation of Independent Business (NFIB), a leading association of small businesses, provides perspective on some of the impacts small businesses are feeling:

- In February, the NFIB index of small business optimism fell to its second lowest data point in the 35 year history of the survey.
- Expectations for growth in sales and profits continue to fall, causing small businesses to cut prices as they focus on liquidating inventory and trimming labor costs. Expectations for future hiring are also at historically low levels, with lower sentiments coming only during the 1974-75 and 1980-82 recessions.

- Reports of capital investments made in the prior six months were flat while plans for capital outlays in the next six months were up slightly. However, since 2006, small businesses have trended toward consistent decreases in actual and planned capital expenditures.
- Small business sales and earnings are lower. The number of small business owners reporting higher sales in the past three months on a seasonally adjusted basis was down a net 28 percent -- one of the worst readings in survey history.

Separately, a recent report by VISA on business failures and bankruptcies found that bankruptcies are expected to increase 30 to 40 percent in 2009, with a corresponding increase in business closures.

Our own experience with small business clients tells a similar story. In our daily interactions with clients we are seeing first-hand the effects of economic weakness, including loss of customers, greater difficulty in collecting receivables, suppliers who require higher up-front payments and layoffs of long-time employees. Business owners tell us they are delaying or cancelling investments, as well as hiring and expansion plans until times are better. They are eliminating non-essential expenditures and looking for ways to preserve cash.

An example of the hardships our clients are facing can be illustrated by a recent conversation we had with a client who has been in the auto repair business since 1973. This business owner told us that he has seen many ups and downs over the years, but has never experienced anything in his business like he is going through now. His revenues are off almost 50 percent year-over-year and he has been forced to make hard decisions to reduce expenses to off-set lost revenue and keep his business open. Over the past several months, he has laid-off two of his six technicians and is considering eliminating certain employee benefits. Unfortunately, we are hearing these types of stories on a frequent basis in our daily conversations with clients.

Not surprisingly, our small business loan portfolio is also seeing the effects of the downturn. Over the past year, we have seen a steady rise in delinquencies on business loan accounts. More clients are calling to let us know they are facing cash shortfalls and will not be able to make upcoming loan payments. Clients who have made payments consistently for months and years have now fallen behind. Whereas in the past we would expect most delinquent clients to catch up over several months, we are now seeing more who simply cannot pay at all. As a result, our credit losses more than doubled from 2007 to 2008.

In our client interactions and in our data, we see that the recession is having a disproportionate impact on businesses at the smaller end of the small business spectrum – those with revenues less than \$500,000. These smaller businesses often serve small geographic or niche markets. They are more often newer businesses with fewer financial resources to fall back on when times get tough. They are sole proprietors or partnerships whose personal income and assets are largely tied up in the businesses. These smaller clients are, in many cases, living “paycheck-to-paycheck” and simply do not have the resources to weather the storm.

Larger, more established businesses are faring better but are also showing signs of financial difficulty, as evidenced by lower capital expenditures, reduction in inventories and lay-offs. The key difference is that these larger businesses tend to have stronger balance sheets, more stable and predictable cash flow and greater access to working capital to manage the contraction of their businesses. As a result, businesses in this segment are not facing the same level of stress as smaller businesses.

#### **Bank of America’s Commitment to Serving Small Businesses**

In light of these challenges, we continue to take actions to help small businesses. We continue to actively market our full suite of credit products. And we are working more intensively than ever to restructure loans for clients who are in financial distress. Specifically, in an effort to provide relief to clients struggling to make their small business credit card payments, we have increased the use of our fixed payment programs where we significantly reduce the interest rate and monthly payments. In 2008, we assisted over 40,000 clients with balances in aggregate of approximately \$550 million by modifying payment structures to improve their monthly cash flow.

Another way we are helping small businesses is through our commitment to Community Development Financial Institutions. CDFIs play important roles as conduits to provide credit to families, small businesses, multi-cultural organizations, community facilities and non-profits serving low-to-moderate income communities that might not qualify under more traditional credit criteria. Bank of America, inclusive of Merrill Lynch, is the leading financial services investor in CDFIs with more than \$450 million in direct lending and investments in 2008.



In Massachusetts, we have built strong relationships with a number of CDFIs, such as Boston Community Capital, ACCION USA, New Bedford EDC, Western MA Enterprise Fund and others. Bank of America also has been innovative in support of CDFIs through its Program Related Investments (PRIs). This program provides low-cost loans and investments at below-market rates. These investments, nearly \$100 million in 2008, provide long-term capital to CDFIs, ensuring the funds assist underserved and economically distressed individuals and communities. Approximately 21 percent of our nearly \$450 million PRI portfolio is invested in small business and microenterprises. Bank of America will continue to demonstrate further leadership and support of CDFIs through grants, loans and investments by leveraging the PRI program together with other resources of our Community Development Banking and Small Business Banking divisions.

In addition to our CDFI commitment, we remain committed to our 10-year \$1.5 trillion community development goal. Small business lending and investment is one of the categories that we will report on annually, further underscoring our commitment to and focus on this segment. Our target over the next 10 years is to make at least \$250 billion – or 17 percent of the total goal – in loans and investments to small businesses. This includes:

- Small business loans up to \$1 million (up to \$5 million for those in low- and moderate-income areas);
- Government-guaranteed loans;
- Investments directly in minority-owned businesses; and
- Investments in CDFIs serving small businesses and venture capital funds for minority-owned and inner-city businesses.

Specifically, with respect to small business credit, we continue to actively lend money to businesses every day to finance a wide variety of business projects, investments and working capital needs. In spite of the large increase in small business lending losses within our existing portfolio, Bank of America's overall amount of outstanding loans to businesses is relatively stable.

#### **Current Credit Outlook**

However, in contrast to the relative stability in our existing loan portfolio, we do expect to see a decrease in new loan commitments in 2009 to the smaller businesses in the segment. This is due to several factors:

- 1) Decreased demand for loans overall. Applications for new loans have been declining for well over a year. The primary reason for this trend appears to be an overall reluctance of business owners to take on new debt during a time of economic weakness. Many business owners have shelved investment and expansion plans until the economy improves. In fact, when we proactively call clients to offer business loans, this is the story we often hear.
  
- 2) Deteriorating financial condition of loan applicants. We have seen a noticeable increase in applications from clients who have strong past credit history and performance, but have hit a time of serious financial stress in their business and personal finances. Many clients who were deriving good income from their businesses a year ago have since faced a cash crunch. Often, their business income is down significantly from the previous year, and the business is facing a monthly cash shortfall or a large reduction in the owner's take-home pay. In their personal finances, these business owners are sometimes facing increasing expenses that exacerbate the cash crunch. When we underwrite loans for smaller businesses, we look at creditworthiness and current cash flow of both the business owner and the business itself to determine the ability to repay. So when business owners come to us in situations of financial stress – even if their credit scores are still good – we are often not able to approve them within our prudent lending guidelines.
  
- 3) Underwriting standards. During the period of 2005 – 2007, Bank of America expanded its focus on small business lending, particularly for the smallest businesses of the segment. Our underwriting guidelines at the time reflected a positive economic outlook as well as the experience of prior years, generally a period of economic strength with relatively low delinquency and loss levels for very small firms. However, as we began approving and booking more loans, we started to see a deterioration in these small businesses' ability to pay us back. The economic downturn exacerbated this problem and has led us to return to more prudent and sustainable underwriting standards to ensure acceptable credit quality for new loans. This is necessary for the future health of our loan book and our ability to continue to invest in new products and services for the small business segment.

From our perspective, these three factors are creating the contraction in new credit that we are seeing in our own client base.

Government assistance in loan programs has made a difference to our clients. Bank of America received a \$45 billion preferred stock investment through the TARP program. While we cannot determine whether the next loan we make is funded by that money, we are lending significantly more with that investment than we would be without it.

Bank of America is a long-time participant in SBA loan programs. We are currently the #1 lender (in loan volume) in the SBA's 504 program and were the #1 lender (in units) for 10 years in a row in the SBA 7(a) Express program until last year. (In early 2008, a change in product strategy and underwriting standards began reducing the overall number of applications that were eligible for consideration under the SBA 7(a) Express program, but we remain an active participant in this program). Both the 504 and 7(a) Express programs allow us to provide credit to clients to supplement our conventional small business lending.

However, it is important to note that both programs together comprise only around 5 percent of our total loans outstanding to small businesses. This is because we use our conventional products and underwriting programs to approve the vast majority of clients who demonstrate the creditworthiness and cash flow to repay the loan. Regardless of the guaranty percentage, we need to have confidence in the client's ability to repay before extending credit.

In our view, the recent actions by the Obama Administration to assist small businesses will create new opportunities for lending to small businesses. In particular the 90 percent guaranty on traditional 7(a) loans is a positive development. However, we would encourage the SBA to go one step further and simplify the paperwork and documentation requirements in the 7(a) program. Bank of America has not participated in the traditional 7(a) program for several years because the heavy paperwork burden created dissatisfaction for our customers and significantly increased our origination costs. Bank of America currently works with a third-party non-bank to extend this program to clients who would benefit.

Regarding the 504 program, we would recommend expanding its scope to include refinancing of existing owner-occupied real estate debt. Currently, the SBA only allows for new expansion, purchase and construction, but does not allow debt to be refinanced. Expanding the program to include refinancing would allow businesses to reduce interest rates and payments and use the savings to retain jobs and increase investment in their businesses.

**Conclusion**

In summary, Bank of America remains committed to small and medium-sized businesses and considers this a very important segment to serve. We continue to market our credit products to the segment and adjust our business model to meet the needs of our clients during this economic downturn. For example, we have increased staffing in many parts of our loan origination process so we can spend more time consulting with clients to find the right credit solutions for their businesses. We are making every effort to approve as many clients as we can during this time, within prudent lending guidelines. While we expect to see many of our small business clients struggle through the next several quarters, Bank of America will continue to extend credit to this very important business segment.

Thank you for the opportunity to share our views today. I look forward to responding to any questions from the Committee.

Testimony before the Committee on Financial Services  
3/23/09  
Boston, MA

Barry R. Sloane  
Co-CEO  
Century Bank  
Medford, MA

Good Morning Ladies and Gentlemen.

Thank you for the privilege of appearing before your Committee to share my perspectives on the current state of the credit crisis for small and medium sized businesses.

First a word of background on Century Bank.

Century was founded 40 years ago by my father, Marshall, on a corner of Mystic Avenue in Somerville in a temporary office trailer.

He is today our Chairman, and as we approach our May 1 anniversary are proud to be the largest family controlled bank in New England.

My brother Jonathan and I are Co-CEO's of an institution of \$2 billion of assets, 22 branches in Eastern Massachusetts, 400 employees; and a member of a now exclusive club: community banks who are increasingly profitable (earnings up 15% in 2008), with growing local deposits (up 12% in 2008), that did not need or accept the TARP capital from the Treasury.

Century was founded on the concept in 1969 that there was a powerful case for a community based lender to business in Middlesex County; a premise that remarkably is even more compelling today.

We are in business to serve the needs of consumers, local business, local governments, and not-for-profit institutions in Massachusetts, Rhode Island and New Hampshire. We proudly service over 6,000 business clients, and since 2004 alone we have made over 1,500 small business loans, many in partnership with the SBA. Our total loan portfolio is over \$900 million and has grown on an upward slope since the early 1990's; increasing over 15% in 2008.

We are sound, safe, and with abundant liquidity to expand our loan portfolio. We are ready and able to lend to the business community.

Why have we done well and others not? There are three simple reasons:

First, we have a culture based on risk management. We are lenders; we live and breathe our loan portfolio through a highly centralized management process.

Second, we lend only in our local market. Market intelligence is critical to a successful loan policy.

Third, we seek and nurture long-term relationships with all of our borrowers. A single transaction without relationship continuity is discouraged.

So how can we make a contribution today to the dialogue of “seeking solutions” to enhance business credit availability?

There are two pathways. One, to make banks stronger so they can make more loans. Two, to make small business healthier so they become stronger borrowers.

Let’s take the banks first.

Far too much emphasis has been placed on bank capital, not enough on earnings. The TARP program provided capital to banks with marginal or adequate capital ratios, but at a high price, becoming an instant drag on net earnings (profits). Net profits build branches, hire lenders, feed the loan loss reserve, and expand the capabilities of the institution in its local market.

How can you in Congress help the profitability of independent banks? Improve their efficiency and relative competitiveness.

- 1) Simplify the regulatory structure. Seize this reform opportunity to merge the 5 bank safety and soundness regulators into one federal system. We are regulated by three different agencies, it is inefficient. Please do not burden the independent banks with the process of a proposed “systemic risk regulator.” We always thought there was one; it was called the Secretary of the Treasury. We are worried about a proposal that based on my recent reading, takes some 300 pages to just explain the question.
- 2) Change the FDIC premium structure. Convert the premium charge from a bank expense to a user fee that is disclosed, transparent, and much more economically efficient. The pending 2009 FDIC special assessment will have a significant negative earnings impact on independent banks. Why should banks that practiced sound lending have their earnings negatively impacted by the irresponsible behavior of others. The 2009 assessment will effect a contraction on the lending of sound banks through the shrinkage of earnings. The FDIC premium should be paid by the depositor as a discrete “tax” based on the health of the fund; not a charge to individual bank earnings.
- 3) Reinstate the Glass-Steagall barriers between commercial and investment banking. Admit the failure of that experiment and acknowledge that commercial bankers are risk based asset managers, and investment bankers are fee based originators. They are two different genetic animals...and are poisonous together. The short-term high fees of the broker/trader will devour the good judgment of the banker/lender. Get the brokers out of the banking

- business, and please stop this wild proliferation of bank charters to institutions that have neither the temperament, geographic focus, nor long-term relationship culture to be known as a “bank.” Level the competitive landscape so that once again community banks can make loans at a fair price to their local customers and stop losing business to “The Street.” You in the Congress control the competitive equation, put the emphasis back in community connectedness and away from globalism.
- 4) Please do not recapitalize and re-empower the GSE’s (Government Sponsored Enterprises) to repeat the securitized lending mistakes of the last decade. Sub-prime loans would never have been made in such size if the GSE’s had not facilitated the transactions. The oversight and control of those agencies is in your hands. Put the loans back on the bank balance sheets where their approval will again be thoughtful and they will be supervised.
  - 5) Finally, the Government, in our view, has done far too much to forgive the short-sighted irresponsible mistakes of the giants. Why should they be rescued? Let them reorganize fundamentally in an orderly way...break them up...restore a decent competitive balance in American banking...create a far more distributed pattern of deposits. The “giants” will forget the lessons of this crisis, and using “other people’s money” do it all over again in the future.

Now let’s talk about the health of the small and medium sized business community. These entrepreneurs are experiencing two reinforcing negative impacts, the dramatic fall in real asset values, and the staggering collapse of their cash flow from double digit sales declines.

This vortex has especially impacted firms that are in the automotive, housing, and consumer discretionary sectors, where sales have fallen 20-50%. There is no way for a small business to survive a market cycle with such a severe fall in cash flow if they have any meaningful level of debt.

The SBA does a fine job. Few people realize that the SBA has, until recently, recouped all of its loan defaults from the guarantee fees charged borrowers; there was no subsidy from the taxpayers. We are a so-called “Preferred Lender” and use the SBA credit enhancement as a frequent tool in our portfolio lending process. The recent changes increasing the “7A” program federal guarantee level to 90% is a good thing for small business; as is the elimination of new guarantee fees.

However, you must keep in mind that a loan we don’t like at a 75% guarantee, we won’t like any better at 90%. It probably fails due to inadequate asset valuations and cash flow. We’re not inclined to make a loan because we could lose less money. It’s either a good credit or not. Higher 7A guarantees do not transform a marginal applicant into a good credit.

The combination of this recession and the credit crisis are a tsunami for small business. Frequently, I sit through urgent meetings with business owners of, in many cases, multi-generational family businesses that are floundering on the shoals of this crisis. This is the

Katrina for small business, they don't need more debt, that's the last thing they need, they need equity, and they need help...soon. This is figuratively a challenge for FEMA, not just the SBA. Lifetimes of resourcefulness and initiative in small business are melting away with each GDP contraction.

If this government has the capital to keep Bank of America's planes in the air, Citi's corporate retreat staffed to serve lunch, and even pay AIG's bonuses...then it must find the capital to help mitigate so many of the family business tragedies playing out everyday in bank conference rooms across the nation. I know I don't have to tell you in Congress of the importance of small and mid-sized business in the economic and employment health of the nation. They need their own TARP program, let the banks administer it, make it an equity investment, take the pressure off these business owners who are watching their dreams evaporate day by day.

In a Trillion Dollar Stimulus program, ONE billion dollars could rescue until the recovery 10,000 small businesses at \$100,000 each. If we can underwrite the corporate planes and bonuses, then we have the capacity to support small business, but do we have the will?

My Dad, my brother, my sister, and I, sincerely hope so.

Thank you for your consideration.





David N. Slutz  
President & Chief Executive Officer

March 20, 2009

---

**Testimony for the U.S. House of Representatives Committee on Financial Services  
Monday, March 23, 2009**

---

Chairman Frank, Congressman Lynch, members of the Committee, thank you for providing me the opportunity to appear before you today to discuss business credit from a medium sized business perspective. I would also like to thank State Representative Koczera, State Senator Montigny, Mayor Lang (City of New Bedford) and Matt Morrissey of the New Bedford Economic Development Council for their interest, support and guidance through these challenging times.

What I propose to do in the remarks that follow is to:

- Briefly describe our company, associates and products;
- Present an overview of borrowing from a borrowers perspective and present our history with our current lender; and
- Explain our current situation and lack of support we are receiving form our senior secured lender and offer recommendations.

**Who am I**

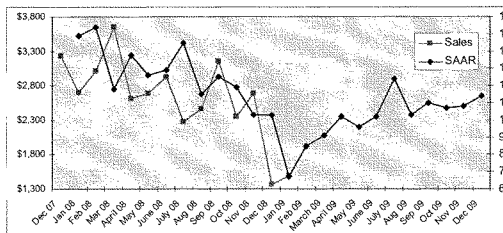
My name is David Slutz, President and CEO of the Acushnet Rubber Company and I am here today to speak about credit availability for working capital and capital investments from a borrower's perspective. One of my key roles in my position is lender relations. Over the past nine years I have dealt directly with several lenders of various sizes in various locations.

### Who is Acushnet Rubber Company d/b/a Precix®?

My company, the Acushnet Rubber company d/b/a Precix was founded in 1910 and is headquartered in New Bedford, MA. Up until 1994 we were part of the Acushnet company, the parent of Titleist. Yes, our founder, Skipper Young, an MIT grad, did invent and bring to market the Titleist golf ball and, no, I did not bring any samples with me.

Two-hundred and twenty-five associates convert raw ingredients into finished o-rings and seals for customers within the automotive, aerospace and chemical processing industries. I have worked for three elastomer companies and I can honestly say that we have some of the best, if not the best, craftspeople in the business. When business is brisk, as it was just one year ago, we manufacture and ship more than 20 million parts per week. Our products are in every automobile and aircraft built in North America, over ½ of those in Europe and a growing share in Asia. If full 20% of our production is exported.

Like most in the automotive supply chain the past six – nine months has been challenging. In February of 2008 we were shipping \$151K/per day. Today our daily sales runs in the \$80K/day range. Needless to say the economic malaise that arose in the 3<sup>rd</sup> and 4<sup>th</sup> quarter last year has hit us and everyone else in our industry very hard. Build rates have gone from more than 16M to less than 8M. Our overall sales trend with automotive build rates as the graphic shows. The good news is that what goes down will come back up so as the build rate recovers so will our base business.



Our belt tightening started last April and was in full gear by summer – all told we have taken \$4.2M in operating expense out of the business. Today our employment is down by 25% with the remaining employees, including myself and the entire senior management team, on rolling layoff. We are working hard to preserve employment while keeping costs in check in order to get to the other side.

All of our stakeholders have had a hand in us getting through this difficult time: our employees have sacrificed pay via reduced ours; our equity sponsor is accepting zero return and our vendors are allowing us to stretch payables. The only stakeholder that has not participated in this survival mode is our Senior Secured lender.

### Lending into the Middle Market

The common conversation around the proverbial water cooler as of late is all around securing credit. It seems that the old running saying that banks are only there when you don't need them is as true as ever. Just this week I attended the State of the City Message in New Bedford and was sitting with several developers and members of the New Bedford Economic Development Council. The talk quickly turned to lack of lending and I can tell you first hand that the examples given were not fly-by-night projects – these were real projects backed by solid companies with solid track records. One example given featured a regional bank, the other a much larger institution. And in general terms

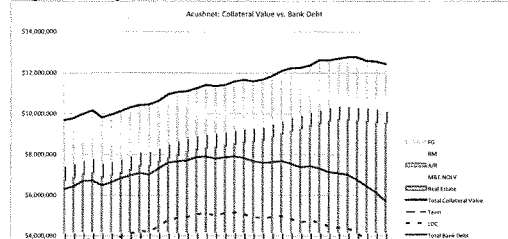
access to capital is a frequent conversation the Economic Development folks have with existing and new potential businesses looking to locate in Southeastern Massachusetts.

The general feeling is that every project is suspect and the world is being painted one color and that color is being tainted by the seemingly never-ending barrages of negative news. It is as if no one wants to make the first move for fear of being wrong and that the stench of 2008 is clouding everyone's judgment.

### Lending/Lender Details

Our relationship with our current lender began in late 2007. We have a fairly straight forward lending arrangement that has both a long-term and short-term component. This is an asset-based loan with machinery & equipment, real estate and inventory as collateral. Since inception we have paid down the long-term debt by more than \$625,000; made our payments 100% on time; had clean audits and have been perfectly transparent on any details asked of us. Our systems/accounting can be described as non aggressive (i.e. boring) and I would consider us a very good customer.

We proactively notified our lender in November 2008 that our forecasts indicated tightened



borrowing availability and cash flow heading into 2009. At this time we did forecast a breakeven/small loss for 2009 (after several years of solid profitability) asked for release of a \$350K holdback reserve under the current line of credit commitment.

We needed and still need this reserve released for borrowing availability while we continue searching for

alternative sources of capital.

It is important to understand that we are not a company that borrowed excessively or are the product of a highly leveraged buyout transaction. In fact we are just the opposite. In spite of an industry driven decline in revenue we still maintain a significant amount of tangible collateral value in excess of our loan amounts (see graph) and maintain positive interest coverage ratios.

Despite being over-secured by more than \$3 million of excess collateral the bank flatly denied our request and is actually seeking to reduce our borrowing availability and add operating costs to the company through increased interest rates and the imposition of consultants and additional reporting requirements. Since our November request the following have transpired:

- Ordered new collateral appraisals that cost \$23,000. Due to current economic conditions machinery, equipment, real estate and inventory all came in lower. They are attempting reduce our borrowing base by this so-called collateral shortfall even though the loan still has excess collateral backing it up. This would push availability down by \$488,000 and effectively push us into negative territory;
- Forcing us to recalculate ineligible inventory on a weekly not monthly basis. Needless to say due to slow sales more inventory is becoming slow and/or obsolete and therefore ineligible for borrowing purposes. This is squeezing our availability by \$30 - \$50,000/week;

- Issued a default notice in December due to our breaking of the fixed charge coverage ratio. Our interest rate is schedule to increase by 2%;
- Imposing a third party audit of our cash flow and business plan that will cost at least \$23,000 – this is in addition to our normal quarterly audits that run \$10,000/audit.

From our vantage point they are not helping by any means, rather they are working to push us under. They are living to the letter of the 2007 loan agreement and general bank guidelines as if nothing has changed between now and then. Again, this is an institution that has been given billions in TARP funds.

### Summary

Our nation's economy has and continues to go through some challenging and unprecedented times. Our employees via downsizing and rolling layoffs; vendors by provided extended terms; management by deferred pay and owners who have forgone dividends continue to be supportive and make sacrifices to help us get to the other side – the only stakeholder that is not working with us is our lender – a lender who may not have made it to this point without billions in federal assistance. Assistance was extended to the institution via the taxpayer financed TARP program but no such assistance is being extended to my and countless other companies.

Our note then and now is fully collateralized but they will not release the \$350K holdback or work with us in any way. Instead of helping they quite honestly seem focused on pushing us under and putting 225 hard-working New Bedfordites out of work.

My message to the committee is this: it is imperative that if banks that are the recipients of TARP money truly want to support economic stabilization and recovery with more than just words they should be willing to provide reasonable and prudent assistance to companies such as ours – companies that are not overleveraged, that have strong collateral support, that are simply going through a tight cash flow time due to overriding economic conditions. They should be ready, willing and able to provide temporary working capital credit availability relief in situations where:

- There is tangible collateral support;
- There is a reasonable detailed operating forecast showing the amount and duration of the temporary financing need;
- The needed incremental credit availability is small relative to current loan balances;
- Leverage is not already at excessive levels;
- There are domestic jobs with benefits at stake.

What we and countless other companies like mine need is lenders that are flexible and willing to work to the other side. If a note is fully collateralized why would you not open a pre-existing line in a loan agreement? If the trough is temporary, as they all are, why would you not work with the borrower to get to the other side? Obviously there is more value for all stakeholders when auto builds rebound and consumers are spending again. Instead of quoting loan agreements that were

crafted before the world changed in 2008 we need lenders to be business people and to quote a banking executive who testified in Washington "Americans first, bankers second."

I am certain there are other small to medium sized manufacturers like us that are experiencing the same set of circumstances. If economic stabilization and recovery is to occur it is imperative that banks take more measured and reasonable approaches to provide temporary support to companies like Precix using the guidelines I have suggested.

Thank you again for your time and for the opportunity to inform the committee about one aspect of the lack of credit availability in the current economic environment.

138

**EMBARGOED UNTIL DELIVERY**

**STATEMENT OF**

**SANDRA L. THOMPSON  
DIRECTOR  
DIVISION OF SUPERVISION AND CONSUMER PROTECTION  
FEDERAL DEPOSIT INSURANCE CORPORATION**

**on**

**CREDIT AVAILABILITY FOR SMALL BUSINESSES  
IN MASSACHUSETTS**

**before the**

**FINANCIAL SERVICES COMMITTEE  
U.S. HOUSE OF REPRESENTATIVES**

**March 23, 2009  
Boston, Massachusetts**

Chairman Frank and members of the Committee, I appreciate the opportunity to testify on behalf of the Federal Deposit Insurance Corporation (FDIC) regarding the availability of credit to small- and medium-sized businesses in Massachusetts. As federal insurer for all banks and thrifts, and primary federal supervisor for just over 5,000 state chartered banks, including 133 headquartered in Massachusetts, the FDIC is very aware of the challenges faced by financial institutions and their customers during these difficult economic times. Liquidity in the marketplace has been adversely affected since the credit disruption began in mid-2007 as the securitization market virtually ceased operating and investors became extremely risk averse. Lack of liquidity in the financial markets is, in turn, an obstacle to granting credit, and the slowing economy is having a profound affect on the availability of loans nationwide for both businesses and consumers

After the lending excesses and poor underwriting of recent years, lenders – especially banks – once again are applying traditional standards in evaluating applications for credit. The focus again is on the ability of borrowers to repay their loans, which mean determining that loans are affordable and sustainable over the long term. Few would argue that we should return to the loose lending standards of recent years that have resulted in so much damage to the financial system.

While prudent underwriting may mean that some borrowers who received credit in past years will have more difficulty receiving credit going forward, it should not mean that creditworthy borrowers are negatively impacted. Unfortunately, in returning to more prudent standards, there is a risk that some lenders will become overly risk averse. As

bank supervisors, we have a responsibility to assure our institutions, regularly and clearly, that appropriately underwritten loans are encouraged. The financial data for banks in Massachusetts and the northeast in general, reflect a lower risk profile, fewer delinquencies and nominal asset losses due to more prudent underwriting standards.

In today's economy, deposit insurance is more valuable than ever. While many sources of bank funding have dried up, deposits have not. Well-managed banks, especially community banks that rely on insured deposit funding, should be able to weather the financial storm. They will be a key source of lending to help the economy recover.

In my testimony, I will briefly describe the conditions currently creating obstacles to credit availability and credit conditions generally in Massachusetts. I also will discuss the efforts the FDIC is making to encourage prudent lending by the institutions we supervise.

#### **Obstacles to Credit Availability**

The institutions in the northeast and Massachusetts that did not take undue risks have nonetheless been affected by the national credit disruption as liquidity has become scarce. Earlier in this decade, credit was abundant for all types of borrowers including large firms, small businesses, and households. Borrowers enjoyed relatively low cost financing which stimulated economic growth and a housing boom. However, we now



know that too much of this lending was poorly underwritten. Conditions in the financial markets masked substantial credit risks that were inherent in the lending practices, resulting in loans that were not sustainable. This, in turn, resulted in significant losses when economic conditions did not match overly optimistic expectations. The emergence of significant volumes of problem real estate loans led to a dramatic shift in credit market liquidity since mid-2007 that changed the landscape for lenders and borrowers alike.

The contraction in credit availability can be generally explained by a convergence of two significant factors.

The first factor is the virtual shut-down in recent months of the private securitization market. Securitizations play a significant role in credit creation since they provide banks and other lenders with a vehicle to originate and package loans for sale to secondary market investors. It was the securitization market that fueled much of the growth in residential and commercial real estate lending in the earlier part of this decade, so the impact of this tightening is felt particularly in these sectors.

Private-label securitization played an increasingly important role in bank funding through 2007, but declined precipitously in 2008. Although federal agencies are taking steps to reduce credit spreads and re-start the securitized credit markets, such as the Federal Reserve's Term Asset-Backed Securities Facility (TALF), the impact of these efforts may not be evident until later in the year.

The second factor in the contraction of credit is that the financial services companies that make or arrange loans have become decidedly more risk averse as they seek to preserve capital and reduce credit losses resulting in a significant negative effect on the availability of credit. Bankers are understandably concerned about credit quality as delinquencies, credit losses, and repossessed assets have risen substantially since the beginning of 2008. Recent measures of credit quality have weakened to levels not seen since the 1990-1991 recession.

Perhaps the best way to compare lending patterns in Massachusetts to the rest of the nation is to focus on *community institutions*, or banks and thrifts with assets of \$1 billion or less, which tend to lend mostly in their local areas.

At Massachusetts community institutions, asset quality is deteriorating from the strong levels of recent years, albeit at a slower rate than the rest of the nation. As of December 31, 2008 the ratio of noncurrent loans to total loans was 1.30 percent, up from 0.71 percent one year earlier.<sup>1</sup> This compares to a noncurrent loan rate of 2.31 percent for all U.S. community banks. Net charge-offs for Massachusetts community institutions totaled a negligible 0.14 percent in the fourth quarter of 2008 compared to 0.08 percent the prior year.

Construction and development (C&D) loan portfolios in Massachusetts community institutions reported the highest noncurrent rate of any loan type at 5.77 percent as of year end 2008, up from 3.22 percent one year earlier. However, concern

---

<sup>1</sup> *Noncurrent loans* are 90 days or more past due or in nonaccrual status.

over the noncurrent loan rate is mitigated to some extent by the fact that Massachusetts community institutions hold concentrations of C&D loans that are approximately half the level held by community institutions in the nation as a whole.

By contrast, community institutions in Massachusetts are more heavily concentrated in one-to-four family residential loans, which comprise 54 percent of loan portfolios in the state versus 27 percent for the U.S. as a whole. Notwithstanding these concentrations and the general deterioration in mortgage credit quality in the state since 2005, credit losses on mortgage loans at Massachusetts community institutions remain relatively low. All other noncurrent loan rates also remain at or below national levels, and real estate owned was half of the national level as of yearend 2008. So while problem loans have clearly risen in the Commonwealth; they remain well below national levels.

Massachusetts community institutions continued to grow their loan portfolios in 2008, although at a slower pace than at the peak of the expansion. On a merger-adjusted basis, community institutions in the Commonwealth saw total loans and leases grow by 8.4 percent in 2008 – up from 4.7 percent in 2007, but still well below the double-digit increases on 2004 and 2005. Among the largest loan categories, the fastest growth was in commercial and industrial (C&I) loans, which grew by 14.8 percent, followed by real estate loans, which grew by 8.3 percent. Meanwhile, consumer loans fell slightly during the year. By comparison, community institutions nationwide grew their loan portfolios by 9 percent last year on a merger-adjusted basis, led by real estate loans, which grew by

10.1 percent. However, among these institutions, commercial loans grew twice as fast in Massachusetts than they did in the nation as a whole.

With respect to small business lending, available data do not clearly distinguish recent trends in the availability of small business credit in Massachusetts compared to the nation as a whole. Surveys of small businesses conducted by the National Federation of Independent Business (NFIB) last fall and early this year show that while small business loans have clearly become harder to obtain, deteriorating business conditions appear to represent an even larger problem.

In the January NFIB survey, the percent of respondents who said that loans were “harder” to get in the last three months outnumbered those who said loans were “easier” to get by 13 percentage points, the highest margin since 1981. However, at the same time, the percent of respondents who said that sales were “lower” in the last three months outnumbered those who said sales were “higher” by a whopping 31 percentage points, the highest margin in the 35-year history of the survey.

As of January, the percent of respondents citing “finance and interest rates” as their single most important business problem stood at just 4 percent, the same level as a year ago. By comparison, a 28 percent plurality of respondents cited “poor sales” as their biggest business problem, up from 15 percent a year ago.

**Supervisory Response to Tight Credit Conditions**

In the period leading up to the credit market disruption, regulators should have been more aggressive in their supervisory approach to certain concentrations of credit risk that put us where we are today. While the banking supervisors issued a number of warnings to the industry and provided guidance for enhancing risk management, in hindsight, the agencies should have been more vigilant about some institutions' outsized risk exposures and underwriting practices.

Bankers are well aware of these current credit conditions. They observe first hand the challenges that their borrowers face every day. This environment has caused some lenders to seek refuge in more liquid, low-risk investments, such as U.S. Treasury securities, rather than taking on additional lending risks. Moreover, banks with large concentrations of credit in the real estate sector in many cases are seeking to reduce those exposures.

The FDIC is committed to ensuring that our examiners understand their proper role and carry out their responsibilities in an objective and even handed manner. The examination process focuses on assessing banks' own risk management process and identifying any weaknesses for consideration and correction by bank management.

For the past several years, the FDIC and the other banking agencies expressed growing concern about the relaxed underwriting standards and non-traditional mortgage

products that were increasingly evident in the marketplace. As long as real estate values continued to rise, the true nature of some of these poorly underwritten and poorly structured loans was masked. While a significant portion of the risky lending was done outside the regulated banking industry, its impact on the market has affected all participants.

The FDIC understands the critical role that credit availability plays as the lifeblood of the national economy, especially for small businesses. A number of discussions have taken place with the FDIC's examination management team to underscore the FDIC's proper role, and to raise sensitivity to issues of credit availability. FDIC senior management has reiterated that examiners should be encouraging banks to continue making prudent loans and working with customers facing financial difficulties.

Many members of the FDIC's supervisory staff served through the 1980s and 1990s as regulators and understand the importance of avoiding any actions that could induce a credit crunch. Our examiners are keenly aware that credit extended by community banks is critical to local economies across the country. Most FDIC examiners live in the communities of the banks they examine, and are very familiar with the local markets and economic trends.

The FDIC understands the tight credit conditions in the market and is contributing to a number of efforts to improve the current situation. Over the past year, we have issued several guidance papers to the institutions we regulate to encourage banks to

maintain the availability of credit. Moreover, examination professionals have received specific instruction on properly applying this guidance within the context of FDIC supervised institutions.

In November 2008, we joined the other federal banking agencies in issuing the *Interagency Statement on Meeting the Needs of Creditworthy Borrowers*. The statement reinforces the FDIC's view that the continued origination and refinancing of loans to creditworthy borrowers is essential to the vitality of our domestic economy. The statement encourages banks to continue making loans in their markets, work with borrowers who may be encountering difficulty during this challenging period, and pursue initiatives such as loan modifications to prevent unnecessary foreclosure.

In light of the present challenges facing banks and their customers, the FDIC hosted a roundtable discussion two weeks ago to focus on how regulators and financial institutions can work together to improve credit availability. The banking industry's national trade associations and individual banks shared their concerns and insights with the four federal banking agencies. We wanted to learn what some of the obstacles might be for bankers to continue lending to creditworthy borrowers in their communities. This session was instructive to all parties in attendance. One of the important points that came out of the session was the need for ongoing dialog between bankers and their regulators as they work jointly toward a solution to the current financial crisis. Chairman Bair announced this past Friday that the FDIC will establish an advisory committee on issues unique to community banking.

**Conclusion**

Prudent, responsible lending is good business and benefits everyone. Community banks are uniquely equipped to meet the credit needs of their local markets, and have a proven tradition of doing so, through good times and bad. Most community banks in the northeast have largely avoided the undue concentrations and reckless lending practices that led to the present crisis. Most of them have a solid capital and funding base and will be in a good position to help finance the recovery.

Banks should be encouraged to make good loans, work with borrowers that are experiencing difficulties during this challenging period whenever possible, avoid unnecessary foreclosures, and continue to ensure that the credit needs of their communities are fulfilled.

Thank you for the opportunity to testify today, and I would be happy to take any questions.





---

Comptroller of the Currency  
Administrator of National Banks

---

Washington, DC 20219

June 12, 2009

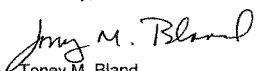
The Honorable Barney Frank  
Chairman  
Committee on Financial Services  
United States House of Representatives  
Washington, DC 20515

Dear Chairman Frank:

Enclosed please find my response to a request for additional information that you and Representative Delahunt made during the March 23, 2009 hearing on "Finding Credit for Small and Midsize Businesses in Massachusetts." During the hearing, Representative Delahunt asked that I provide additional data on the performance of loans issued pursuant to the Community Reinvestment Act (CRA). You then expanded that request for information that would compare the performance of CRA loans against all other loans.

I hope the enclosed response for the record is informative. If you have questions or need additional information, please contact John Hardage, Director for Congressional Liaison, at 202-874-1881.

Sincerely,

  
Toney M. Bland  
Deputy Comptroller  
Northeastern District  
Office of the Comptroller of the Currency

cc: Honorable William Delahunt

Enclosure

During the March 23, 2009 House Financial Services Committee field hearing in Boston, MA on "Finding Credit for Small and Midsize Businesses in MA," Rep. Delahunt suggested that loans made under the Community Reinvestment Act (CRA) were faring better than loans outside of the CRA. Rep. Delahunt then requested that the OCC provide information on the performance of CRA loans. Chairman Frank subsequently expanded that request to provide a comparison of CRA loans versus all loans, referencing statistics "that the great majority of loans that got us in trouble were made out of the banks."

The CRA was enacted in 1977 to encourage banks and thrifts to increase their lending and services to low- and moderate-income persons and communities, consistent with safe and sound banking practices. The CRA applies to banks and savings associations, the deposits of which are insured by the Federal Deposit Insurance Corporation. In contrast, the CRA does not apply to mortgage banks or brokers, entities which are regulated by states.

While it is true that the subprime mortgage crisis is the foundation for the economic turmoil we are facing today, evidence shows that the insured depositories, which are subject to CRA, were not the main providers of products, such as 2-28 adjustable-rate subprime mortgages, that have led to so many problems. Indeed, over one-half of the subprime mortgages initiated during the last several years – and the ones with the most questionable underwriting standards – were originated through mortgage brokers for securitization by nonbanks, including major investment banks.

A number of recent studies support the notion that CRA is not to blame for the mortgage crisis. One study, by the Federal Reserve Bank of San Francisco entitled "Lending in Low- and Moderate-Income Neighborhoods in California: The Performance of CRA Lending During the Subprime Meltdown,"<sup>1</sup> is particularly instructive. While this study focuses on CRA lending in California, it finds that loans made by institutions subject to CRA were about 30% less likely to go into foreclosure (after adjusting for other factors that affect the likelihood of foreclosure such as credit score) than loans from mortgage companies not subject to CRA. Even more significantly, loans made within the banks' CRA assessment areas had even lower foreclosure rates, only about half as likely to go into foreclosure as loans from independent mortgage companies. While additional research is needed to determine if the findings in California are applicable to other mortgage markets, the study notes that "the size and diversity of California lend it weight as a valid case study for the performance of CRA lending more generally." Further, the authors note, after carefully explaining their methodology and findings, that their research "should help to quell if not fully lay to rest the arguments that the CRA caused the current subprime lending boom by requiring banks to lend irresponsibly in low- and moderate-income areas."

In his article "The Community Reinvestment Act and the Recent Mortgage Crisis,"<sup>2</sup> former Federal Reserve Governor Randall Kroszner discusses findings of another analysis by the Federal Reserve of mortgage-related data and its potential contribution to the subprime crisis. The article includes the finding that only six percent of all the higher-priced loans were issued by CRA-covered lenders to lower-income borrowers or

<sup>1</sup>[http://www.richmondfed.org/conferences\\_and\\_events/research/2008/pdf/lending\\_in\\_low\\_and\\_moderate\\_income\\_neighborhoods.pdf](http://www.richmondfed.org/conferences_and_events/research/2008/pdf/lending_in_low_and_moderate_income_neighborhoods.pdf)

<sup>2</sup> [http://www.frbfsf.org/publications/community/cra/cra\\_recent\\_mortgage\\_crisis.pdf](http://www.frbfsf.org/publications/community/cra/cra_recent_mortgage_crisis.pdf)

neighborhoods in their CRA assessment areas. Governor Kroszner later concludes that "First, only a small portion of subprime mortgage originations are related to the CRA. Second, CRA-related loans appear to perform comparably to other types of subprime loans. Taken together . . . we believe that the available evidence runs counter to the contention that the CRA contributed in any substantive way to the current mortgage crisis."

Finally, a report was released just last month by a multi-state collaboration of organizations entitled "American Dream III: Promoting Responsible Lending to Lower-Income Communities and Communities of Color."<sup>3</sup> This study examined seven metropolitan areas and found that financial institutions covered by the CRA had a much larger presence in the overall lending market than in the higher-cost lending market. "Conversely, lenders not covered by the CRA made the vast majority of higher-cost loans in all metropolitan areas examined." Again, this is further evidence that national banks and other entities covered by the CRA were not making the subprime loans.

These studies provide strong support that the CRA did not exacerbate the financial crisis.

---

<sup>3</sup> A copy of the report can be accessed at <http://www.woodstockinst.org/>