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TESTIMONY OF
RONALD COVEY
PRESIDENT AND CHIEF EXECUTIVE OFFICER
ST. MARY'S BANK CREDIT UNION
ON BEHALF OF
THE CREDIT UNION NATIONAL ASSOCIATION

BEFORE THE COMMITTEE ON FINANCIAL SERVICES AND
THE COMMITTEE ON SMALL BUSINESS
UNITED STATES HOUSE OF REPRESENTATIVES

HEARING ON
"CONDITION OF SMALL BUSINESS AND COMMERCIAL REAL ESTATE
LENDING IN LOCAL MARKETS"

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Chairman Frank, Chairwoman Velazquez, Ranking Member Bachus, Ranking Member Graves, Members of the Financial Services Committee and Small Business Committee: Thank you very much for the opportunity to testify today regarding the condition of small business and commercial real estate lending in local markets. My name is Ronald Covey, and I am President and Chief Executive Officer of St. Mary's Bank Credit Union[1] in Manchester, New Hampshire. I am testifying on behalf of the Credit Union National Association (CUNA)[2].

St. Mary's Bank Credit Union – a member-owned, not-for-profit financial cooperative – was the first credit union established in the United States. We are proud of

[1] St. Mary's Bank Credit Union was founded in 1908 as La Caisse Populaire Ste. Marie, to serve the Franco-American population living in Manchester, NH. The French name loosely translates to The People's Bank. In 1925, the credit union's charter was amended to use both the French and English versions of the name. In recent years, the credit union has only used St. Mary's Bank. St. Mary's Bank Credit Union serves 75,000 members; its total assets were $660 million as of September 2009.

[2] CUNA is the nation's largest credit union advocacy organization representing nearly 90% of America's 7,800 state and federally chartered credit unions and their 92 million members.

our heritage. For just over a century, we've been helping New Hampshire residents with a wide range of affordable products and services, including checking accounts, personal loans, real estate loans, business financial services, and savvy financial planning.

My testimony today focuses on the history of credit union business lending at St. Mary’s Bank Credit Union and nationally, the safety and soundness of credit union business lending relative to similar loans made by banks, the demand for small business lending that we are seeing in New Hampshire and nationally, and our reaction to the President’s proposal to create a $30 billion Small Business Lending Fund. Additionally, I will discuss our support for legislation, H.R. 3380, which would permit credit unions to inject as much as $10 billion into small businesses this year, helping them create over 100,000 jobs, at zero cost to the taxpayer and without increasing the size of government.

Business Lending is a Part of the Core Credit Union Mission and St. Mary’s Bank Credit Union Has Been Fulfilling That Mission For Over a Century

The idea behind credit unions is very simple: people pool their savings together and make loans to neighbors and coworkers in order to help each other achieve a better standard of living. Following this basic principle of “people helping people,” we improve communities and generate opportunities for those most in need. We have always considered supporting local business as one of the key factors in creating healthy communities. That is why we have always taken, and continue to take, the initiative in helping business owners.

Credit union involvement in business lending dates back to the first days of the credit union movement. The earliest credit unions were founded so that people could borrow money to buy goods at lower cost and sell them for a profit.

The founders of the American credit union movement very specifically noted the important role credit unions should play in providing access to credit for small businesses. As Alphonse Desjardin said in 1908, as he encouraged the founding fathers of St. Mary's Bank Credit Union to organize the United States' first credit union:

> "There are not only the manual laborers, whether of industry or of the land, who need credit and who, very often, are forced to suffer the extortions of the Shylocks of usury: There is also a very interesting class of small merchants, of humble industrialists, of modest entrepreneurs whose financial status does not permit them to have access to the large banks where their well enough known fellow businessmen go to stock up in order to enjoy the benefit of a checking account. To all of them as well, the cooperative offers financial assistance that is most precious."[3]

Business lending is part of the credit union DNA. St. Mary's Bank Credit Union has a track record of granting member business loans that dates back to our early years. St. Mary Bank Credit Union even provided vital loans during the Great Depression, when economic conditions forced many other financial institutions to close. According to the minutes of our Credit Committees during this time, St. Mary's Bank Credit Union granted business loans for apartment buildings, commercial real estate, working capital, time notes, and equipment loans. The businesses ranged from lumber yards, convenience stores, and heating oil companies to hardware stores and retail outlets.

Member business lending has continued at St. Mary's Bank Credit Union through our current recession. We still provide business loans for working capital (lines of credit)

[3] *L'Avenir National* (Manchester, N.H.), Vol. XXI, No. 67, 28 November 1908, p. 4-5.

inventory, accounts receivable, equipment loans, seasonal loans, commercial real estate loans, and energy loans. St. Mary's Bank Credit Union is an approved Small Business Administration lender and participates in the Business Express program, SBA 7(a) Loan Program, and SBA 504 Program. We also utilize several New Hampshire state programs through the Business Finance Authority of New Hampshire.

St. Mary's Bank Credit Union member business loans today provide:

- Critical financing for multi-family residential housing, much of which is in low-income areas;
- Working capital and equipment loans for small manufacturing companies and sub-contractors that provide jobs and economic stability in our market;
- Commercial real estate loans and rehab loans for business growth and expansion; and
- Working capital and equipment loans for entrepreneurs, small service, and professional organizations.

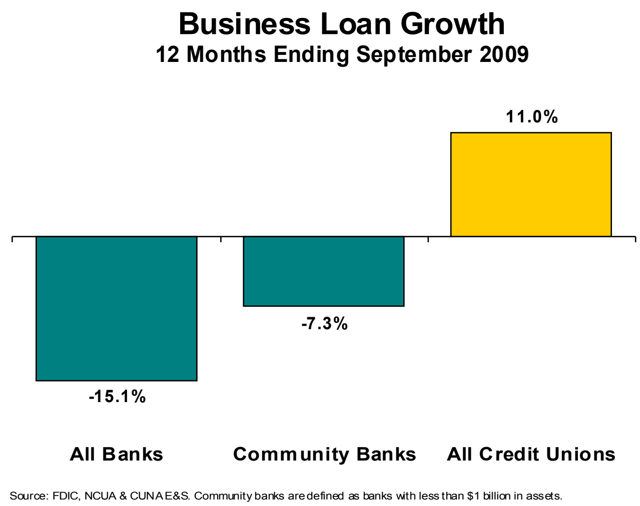
St. Mary's Bank Credit Union's average business loan size is under $200,000. We have 959 business loans, totaling approximately $75 million and 2,201 business members. Our potential is much greater!

Business Lending Demand Exists

St. Mary's Bank Credit Union's aggregate limit for net member business loans is $85.3 million based on the 12.25 percent of total assets cap in the Federal Credit Union Act. At the current time, we have a new business pipeline of $7.6 million and an additional $7.5 million in business loan requests that, if approved, would exceed our aggregate limit by $4.8 million. We will attempt to place the additional requests that exceed our cap at other financial institutions; failing that, business members will have to wait until other business loans are paid down. Either way, these business members will likely experience a delay in receiving funds that could drastically affect their business activities, their financial wellbeing, and their employees – a delay that we are hoping to prevent by being here today.

Let me emphasize this point: I do not see a scarcity of creditworthy business borrowers. I have the funds to lend, and nearly $5 million of loan requests that may go unfilled because of a statutory cap that was enacted twelve years ago without any economic or safety and soundness rationale. Given the demand we see, it is difficult to understand why we should not be able to put money back into the community, into the hands of hard working business owners, so they can employ more people and create more opportunities. That would simply be following through on the credit union mission.

On a national level, we know there is demand for business loans because credit union business lending actually grew in 2009 while bank business lending contracted. If there was a scarcity of demand for business loans, all lenders would have seen contraction, not growth, in business lending.



We also know that there is demand for business lending because our members tell us there is. I have with me several hundred letters from business owners from across the country who have received loans from credit unions, some after having been rejected by banks – big banks and community banks. These individuals have experienced first-hand the value in credit unions providing business loans; they see it as part of our mission.

We are simply asking for the opportunity to fulfill our potential as a business lender to our members. We have the resources to continue promoting business growth in our communities. We want to serve their needs. It would be disheartening to have to tell a qualified borrower that we cannot make a loan because of an agenda put forth by banks like the one that closed his line of credit or declined her original application. Limiting our cap to 12.25% of total assets does a great disservice to business owners everywhere, and stymies the kind of economic stimulation and job growth this country truly needs right now.

Credit Unions Stand Apart from Other Financial Institutions

Mr. Chairman, it is important to note that we would not be here talking about this issue if all financial institutions had behaved like credit unions. Credit unions did not contribute to the sub-prime meltdown or the subsequent credit market crisis.

Credit unions truly are Main Street financial institutions – small, local, and community-focused. The average credit union has roughly $110 million in total assets whereas the average banking institution is fifteen times larger with $1.7 BILLION in total assets. (The median size credit union has just $15 million in total assets and the median size bank is about ten times larger with $150 million in total assets).

Credit unions are careful lenders. And, as not-for-profit membership cooperatives the overriding operating objective at credit unions is to maximize member service. Incentives at credit unions are aligned in a way that ensures little or no harm is done to the member-owners. As we have seen, the incentives outside of the credit union sector are aligned in a way that can (and often does) cause harm to consumers. In the case of toxic mortgages such as sub-prime mortgages, entities operating outside of the cooperative sector focused on maximizing loan originations (specifically fee income from those originations) even though many of the loans originated were not in the borrower's best interest.

Credit Unions Lend to Their Business-Owning Members Safely and Soundly

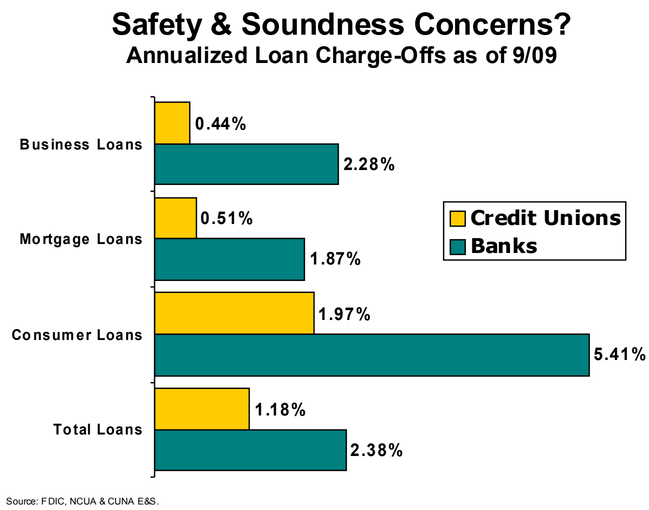
Some have suggested that an increase in credit union business lending could increase the exposure to the National Credit Union Share Insurance Fund (NCUSIF). However, the facts suggest that concern is misplaced.

First, as described below, our business loan loss rate is lower than that of banks, and lower even than our own losses on mortgages and consumer loans. Second, increasing the business lending cap gives well-capitalized credit unions a way to further diversify their portfolios, ultimately lowering overall risk. Third, the NCUA has full authority to supervise business lending by credit unions, and current rules severely limit business lending by credit unions which are not adequately capitalized. In fact, just this week, the Chairman of the NCUA Board wrote Treasury Secretary Geithner reiterating the agency's commitment to strong regulation of member business loans.[4] Increased business lending by credit unions would not be risk free, but it would certainly be very low risk.

Like most other credit unions, St. Mary's Bank Credit Union has a strong track record for sound business loan underwriting and performance. Our average business loan delinquency rate over the last 24 months was around 0.5%. Our net business loan charge-offs rate over the same 24-month time period has averaged about 0.32%

Credit unions, in general, have lower charge-off rates and lower delinquency rates on business loans than banks.

[4] A copy of this letter is attached to this testimony.



Considering all loans, in the first three quarters of 2009 the credit union loan loss rate was about half that of banks (1.18% vs. 2.38%). For business loans in particular, the credit union loan loss rate was only one fifth of the same rate at banks (0.44% vs. 2.28%). Among the three major categories of credit union lending (residential mortgage, consumer, and business), business lending has the lowest loss rate.

The President's Proposal to Create a $30 Billion Small Business Lending Fund Does Not Address the Chief Impediment Facing Credit Union Member Business Lending

During his State of the Union Address, the President proposed giving community banks access to $30 billion in TARP funds with the intention that those funds, which would count as capital for the banks, would be used to encourage additional lending to small businesses. Credit unions have not sought to be included in this program; however, even if credit unions were envisioned to be eligible to participate, current statutory restrictions related to credit union capital would prohibit using these funds and counting them as capital.

However, while we strongly support Congress considering capital reform for credit unions, the chief impediment to credit unions increasing the availability of small business credit is **NOT** a lack of capital. The chief impediment is the statutory cap on credit union business lending in the Federal Credit Union Act. This cap, which is essentially 12.25% of the total assets of a credit union, was enacted in 1998 as part of the Credit Union Membership Access Act (CUMAA). CUMAA was designed to permit multiple common bond credit unions to continue to serve their members in the wake of a ruling by the Supreme Court in a case, brought by the American Bankers Association, which overturned an NCUA interpretation of the Federal Credit Union Act. It is important to note that for the 90 years credit unions were in existence prior to the enactment of the cap, there was no statutory limit on the amount of business lending credit unions could do, and the business lending market share held by credit unions at the time of the cap was extraordinarily small.

There was no economic or safety and soundness rationale for the cap when it was enacted, and none exists today. At the time of CUMAA's enactment, the rationale for the cap, as stated by the Senate Banking Committee, was "to ensure that credit unions continue to fulfill their specified mission of meeting the credit and savings needs of consumers… through an emphasis on consumer loans rather than business loans."[5] Of course, credit unions have been and continue to be clearly focused on meeting the lending needs of consumers. Raising the cap would have a negligible effect on credit union lending to consumers. Any increase in business lending would for the most part replace investments rather than consumer loans. The average credit union has a total loan to

[5] Senate Report 105-193. p. 9

asset ratio of about 65%. Excluding the 5% held in fixed and other assets, that leaves about 30% of assets in cash and investments. If all of the additional business lending capacity were used, that would still leave about 18% of assets in cash and investments without any reduction in consumer lending. Even for the minority of credit unions with much higher loan to asset ratios, raising the cap would very likely not decrease consumer lending, or at least not by much. Just because a credit union could make more business loans does not mean it would forsake existing consumer loan demands to meet new business loan demand.

Small businesses need credit unions today because banks that have been serving them, in some cases for years, are pulling back access to credit. The Congressional Oversight Panel's February 2010 oversight report concludes that as many as 3,000 banks could be forced to curtail business lending. These actions leave many creditworthy business owners high and dry, unable to get the funds they need to operate and expand. It is frustrating to both the credit unions as well as the small business owners that additional resources would be available at credit unions but for a statutory cap on business lending which was enacted twelve years ago as a concession to the bank lobby on a bill designed to permit credit unions to continue to serve their members.

Representatives Kanjorski and Royce have introduced legislation (H.R. 3380) which, if enacted, would increase the credit union member business lending cap from the current level of 12.25% of total assets to 25% of total assets. It would also increase the de minimus amount of a credit union business loan from $50,000 to $250,000. This legislation would add an addition $100 million of business lending capacity to my credit union. We could fill our outstanding loan requests and be there to help our community even more.

CUNA estimates that if H.R. 3380 were enacted into law, credit unions could lend an additional $10 billion to small businesses in the first year, helping small businesses create as many as 108,000 new jobs.[6] **H.R. 3380 is a job creation bill that would not cost the taxpayers a dime and would not increase the size of government.**

Some have suggested that increasing the credit union business lending cap is politically controversial. However, voters disagree. According to a recent survey by Voter Consumer Research[7], 62% of consumers identify jobs and the economy as the most important issues facing our country. When respondents were presented with a proposal

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[6] CUNA conservatively estimates that credit unions would increase member business loans (MBLs) by about $10 billion in the first year following expansion of MBL authority.

The estimated $10 billion, first year increase in lending is derived using three key assumptions:

1. We assume that "grandfathered" credit unions (i.e., the approximately 150 credit unions that are currently above the 12.25% cap) do not increase their lending when the cap is raised.
2. We assume that credit unions that are not currently engaged in MBL activity would enter the market in an amount, on average, equal to 1% of total assets under the new authority. Our conservative estimate assumes that 40% of the increased level of activity would occur in the first year.
3. We assume that all other MBL credit unions lend in an amount equal to their current "use" rate. Our conservative estimate assumes that 40% of the increased level of activity would occur in the first year.

We assume that the new loans would largely be loans that would not otherwise be made by banks. We further assume that the $10 billion increase in lending would be a "new normal" - that the 1st year-addition would represent a permanent addition to loan volume in credit union portfolios. In this regard, the increase in lending can be viewed as American Recovery and Reinvestment Act (ARRA)-like stimulus similar to direct spending. Thus, we assume that the additional lending would produce jobs at a rate that is similar to the estimates published by the Council of Economic Advisors (CEA) in its May 2009 estimates of job creation. See: http://www.whitehouse.gov/administration/eop/cea/Estimate-of-Job-Creation/

Using these assumptions and rounding, each $92,000 in additional MBL lending on the part of the nation's credit unions will create one additional job. Therefore, expanded credit union MBL authority will result in an estimated first-year increase of 108,000 new jobs nationally.

[7] The survey of 1,000 registered voters, 42% of whom identified themselves as credit union members, was conducted by Voter Consumer Research from January 24-28, 2010.

that would let credit unions pump $10 billion into small businesses and create over 100,000 jobs as well as leading banking arguments that the cap should not be removed because credit unions do not pay taxes and it would give them an unfair advantage, 63% of those surveyed responded favorably to the credit union proposal, while only 27% opposed. When respondents are reminded that bankers—after receiving taxpayer bailout money—are paying themselves bonuses and not making small business loans, nearly 70% side with credit unions and only 20% side with banks.

A growing list of small business associations and think tanks support lifting the cap on credit union business lending, including the following[8]:

Americans for Tax Reform
Competitive Enterprise Institute
Ford Motor Minority Dealer Association
League of United Latin American Citizens
Manufactured Housing Institute
National Association of Mortgage Brokers
National Cooperative Business Association
National Cooperative Grocers Association
National Association of Realtors
National Farmers Union
National Small Business Association
NCB Capital Impact
National Association of Professional Insurance Agents
National Association of the Self-Employed
National Association of Manufacturers
National Council of Textile Organizations
Council of Insurance Agents and Brokers
Center on Risk, Regulation, & Markets at the Heartland Institute

H.R. 3380 is a common sense bill that will help small businesses and support communities, and I encourage Congress to enact this legislation as soon as possible.

[8] A copy of an open-letter that these group have sent to Congress is attached to this testimony.

Before concluding, I do want to make a comment regarding the concerns raised by some that credit unions should not have additional business lending authority because they are tax-exempt organizations. This concern ignores both the history of credit unions having and using unlimited statutory business lending authority for the first 90 years of their existence at the same time they have had a tax exemption. As Congress has reaffirmed several times over the last seventy years, most recently in 1998, the tax status is a function of the structure of credit unions as not-for-profit, democratically-controlled, member-owned, financial cooperatives. The tax status has nothing to do with the powers of credit unions, and everything to do with how credit unions are organized.

The credit union structure is unchanged over the past 100 years and we continue to fulfill our mission of serving especially those of modest means. For example, according to Home Mortgage Disclosure Act data, minorities and lower income Americans are much more likely to have their home mortgage loan applications approved at credit unions than at other lenders.[9]

In the business lending arena, the Treasury's 2001 comprehensive analysis of credit union business lending showed that 25 percent of member business loans were made to members with household income of less than $30,000 -- and that these loans totaled 13 percent of the outstanding member business lending balances. Another 20 percent of the loans (with 15 percent of the outstanding loan balance) went to households with incomes reported to be between $30,000 and $50,000.

[9] Since 2005, credit unions have approved an average of 68% of applications from low/mod income borrowers, whereas other lenders approved an average of only 51% of these applications. Moreover, since 2005, an average of 26% of total credit union mortgage originations were to low/mod income borrowers while low/mod income originations represented only 23% of total originations at other lenders.

The irony is that bankers have repeatedly criticized credit unions for not doing more to serve the underserved, while at the same time repeatedly used the courts and persuading Congress to keep credit unions from being able to do more. The time is now to set aside the banker rhetoric. We urge Congress to permit credit unions to do what they were established to do – serve their members, including those who own small businesses. We have the willingness to help. We have the capacity to help. But, we need Congress to act.

Mr. Chairman, thank you very much for the opportunity to testify today. I am happy to answer any questions the members of the Committee may have.

National Credit Union Administration

Office of the Chairman

February 24, 2010

The Honorable Timothy F. Geithner, Secretary
United States Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Dear Secretary Geithner:

I am writing as a follow-up to the recent discussions our agencies have had about credit union member business loan limitations.

The Federal Credit Union Act limits the amount of member business loans (MBLs) the great majority of credit unions can grant to the lesser of 1.75 percent of net worth or 12.25 percent of assets. Congress presently contemplates legislation that would raise or eliminate that statutory limitation by enabling credit unions to grant more MBLs. Should the legislative process result in an increase to or elimination of the current MBL limitations, I assure you NCUA would remain vigilant in carrying out our supervisory responsibilities.

NCUA has long exercised caution in monitoring MBLs from the standpoint of safety and soundness. We routinely issue guidance to ensure the credit union community and agency staff understand the risks associated with MBLs. For example, last month, the agency released NCUA Letter to Credit Unions 10-CU-02 ("Current Risks in Business Lending and Sound Risk Management Practices"). This guidance reminds credit union officials of the importance of ensuring that risk management practices must continue to evolve as the size and complexity of MBL portfolios increase. NCUA also plans to provide extensive MBL training to our field staff in the coming months.

NCUA recognizes that successful MBL programs depend upon credit unions limiting products to only those consistent with the capabilities of their respective lending staffs and the principles of sound risk management. In consideration of these precepts, NCUA already has efforts underway to strengthen the regulatory qualifications that credit union officials must have to serve as business lenders.

Let me assure you: **If legislative changes increase or eliminate the current aggregate MBL cap, NCUA would promptly revise our regulation to ensure that additional capacity in the credit union system would not result in unintended safety and soundness concerns.**

As one of the most important changes, NCUA would only permit credit unions to increase their MBL capacities on a gradual basis by adopting a tiered approval process. In addition to other regulatory changes, the agency would develop procedures to fully monitor MBL growth.

Earlier this month, NCUA joined the other Federal Financial Institution Examination Council members in advocating prudent lending to creditworthy small businesses. We recognize the importance of small businesses in leading our nation's recovery efforts. As such, we support efforts to allow credit unions to provide businesses additional avenues of credit when appropriate under a comprehensive regulatory framework.

Sincerely,

Debbie Matz
Chairman

CC: Michael Barr
Assistant Secretary for Financial Institutions

An Open Letter to President Obama and Members of the House and Senate from Those Who Create Jobs

Dear Mr. President, Senators and Members of Congress:

As you focus on overcoming the challenges of our nation's economy, it is important to assemble and use all the tools at your disposal. To date, the primary focus has been both a taxpayer financed rescue and economic stimulus package.

Despite these measures, credit continues to be a problem for businesses of all sizes - businesses which create jobs. We would like to suggest another step that could inject up to $10 billion into the economy according to those associated with credit unions.

We urge you to allow credit unions to expand lending to their business members.

- **Credit unions continue to lend even when banks have cut back;**
- **Credit unions play a vital role in providing capital to underserved communities and small businesses; and,**
- **Credit Unions understand the special needs of their business members and can make loans that banks will not.**

Easing business lending limits on credit unions will cost taxpayers nothing, and will provide much needed credit into our economy. We urge you to support lifting the lending cap.

Americans for Tax Reform
Competitive Enterprise Institute
Ford Motor Minority Dealer Association
League of United Latin American Citizens (LULAC)
Manufactured Housing Institute
National Association of Mortgage Brokers
National Cooperative Business Association
National Cooperative Grocers Association
National Association of Realtors*

National Farmers Union
National Small Business Association
NCB Capital Impact
National Association of Professional Insurance Agents
National Association for the Self-Employed
National Association of Manufacturers
National Council of Textile Organizations
Council of Insurance Agents and Brokers*

Center on Risk, Regulation, & Markets at the Heartland Institute *

* New Signatories

America's Credit Unions.
Serving their 90 million members everyday.

AMERICA'S CREDIT UNIONS

For more information, visit www.CUNA.org

CUNA
Credit Union National Association