Testimony of

Kim D. Saunders

On Behalf of

Mechanics and Farmers Bank

Before the

Committee on Financial Services

Subcommittee on Oversight and Investigations

United States House of Representatives

October 30, 2007

M&F

MECHANICS AND FARMERS BANK

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Executive Summary

In August 2006, the Federal Deposit Insurance Corporation's (FDIC) Vice Chairman Martin J. Gruenberg identified some of the challenges to minority banks' operating in a highly profitable manner: (a) the relatively higher cost of doing business in communities with incomes below market average, (b) high immigrant populations, (c) a smaller deposit base, and (d) a preference for in-person service.

To assist minority banks in addressing these unique challenges, as well as facilitating capital investments in these institutions, I recommend the Committee on Financial Services consider legislation (a) to ensure that bank regulators provide the necessary notification regarding the array of technical assistance services that are available and (b) to amend regulatory peer group benchmarking and examination evaluations to recognize the differences between minority banks and UBPR-designated peer groups. Finally, although I recognize that federal tax legislation is outside the purview of this committee, the ability of minority banks to raise capital would be enhanced if the CDFI Fund guidelines were modified to allow tax credits for investments in these institutions.

Mr. Chairman and other distinguished members of the Committee; my name is Kim D. Saunders. I am President and CEO of M&F Bancorp, Inc., and Mechanics and Farmers Bank. M&F is a $223 million community bank that conducts business in four of North Carolina's largest markets. The Bank is celebrating its 100th anniversary throughout 2007 and 2008, and our parent company currently is anticipating approval of a merger agreement that should elevate Mechanics and Farmers Bank into the top five largest African-American owned banks in the United States.

On behalf of the Boards of Directors of M&F Bancorp, Inc. and Mechanics and Farmers Bank, I am honored to provide you with comments on this very important subject of "Preserving and Expanding Minority Banks". Even as we look forward to realizing incremental growth through the consummation of our first merger since 1921, we recognize that the business environment in which we operate is becoming more challenging on every front.

In the face of all the economic issues affecting the banking industry that we see daily in the media, and that this committee has heard about numerous times in the past months, the pressure on the ability of community banks and minority-owned financial institutions to operate profitably may be even more intense than on the rest of the industry.

The Government Accountability Office rightly observes in its October 2006 report on Minority Banks that "minority banks can play an important role in serving the financial needs of historically underserved communities and growing populations of minorities." Because this is true, this hearing today and any resulting actions will resonate far beyond these chambers, and I thank the Committee for giving time to these matters.

M&F's own mission and track record bear out the truth of the GAO's assessment of the role of minority banks. 100 years ago this year, Mechanics and Farmers Bank was founded out of the need for African-Americans in Durham, North Carolina to have a safe and secure place to deposit and earn interest on their savings, to have access to financing for their businesses and homes, and to build wealth for their families and their communities.

Today, we are a full-service commercial bank offering a wide range of consumer and commercial depository and loan products, as well as online banking, bill payment and cash management. We are among a select few banks in North Carolina designated as a Community Development Financial Institution, and have twice been recipients of Bank Enterprise Awards through the CDFI Fund of the United States Treasury, based largely upon our financing activities in economically distressed communities and for our commitment to promoting proficiency in personal financial management in our markets.

As we have been since our inception, we are committed to reinvesting our resources, both human and financial, into the communities where we live and do business. Our Board, management and staff are dedicated to our modeling a "best-practices" based organization that delivers a double bottom-line return, in that we are committed to doing well by doing good. We're proud and privileged that, throughout our footprint, customers readily step forward to share their views on the impact that M&F Bank has had on their businesses, their communities, and on their own or their families' wellbeing. They consistently express pride in our success, in our sustained presence in their neighborhoods and our continued support of their concerns.

The story of M&F Bank is a microcosm, a case study, of the essential role that minority banks play. Our story illustrates the reasons that it is imperative that minority banks be preserved, or better yet, strengthened and expanded.

People of color have financial options today that were not available at the turn of the 20th century, however, that does not mean that the playing field is level. The GAO report highlights the disparities in performance and utilization of regulatory agencies' services among minority banks, and yet, we must delve deeper.

Our experience with banking regulators at M&F Bank has generally been positive and productive, facilitated in great part by the fact that we have a number of former bank examiners in senior staff positions. Our Board emphasizes transparency and cooperation with regulatory agencies, and management consistently takes the position that full and proactive disclosure is the best policy in all matters. However, the GAO report points to an extremely low rate of utilization of technical assistance among minority banks, which indicates the existence of other factors influencing the result that are not spoken to in the report.

In considering the goal of assisting regulators in their efforts to support minority banks, I would like to discuss the following areas:

- How utilization of technical assistance among minority banks may be increased
- The effectiveness of banking regulators' efforts to implement suggestions in the GAO report

- Legislative and regulatory steps that should be taken to help preserve and expand minority banks
- The critical role minority financial institutions play in our nation's economy

Minority bank use of technical assistance would be enhanced by banking regulators being proactive in providing adequate notice regarding the scope and availability of this assistance.

There is anecdotal evidence at least that minority banks insufficiently use the technical assistance that is available due to the lack of adequate notification regarding this assistance. Banking regulators should correspond at least semi-annually with the CEOs of the minority banks they oversee, to apprise them of the forms of technical assistance that may be available, and to provide the appropriate contact information for future reference. Bank regulators should also utilize this opportunity to determine if other forms of technical assistance and services could be provided which are available and pertinent to the institution. Regulators should be proactive in communicating to minority banks, especially those deemed to be low-performing.

As I stated earlier, our relationship with regulators has been productive on the whole, but I only recently learned that the FDIC has regional coordinators whose responsibilities include annual contact with the minority institutions in their respective region. Institutions are not able to utilize services where notice of these services is inadequate.

Bank regulators' compliance with FIRREA's goal of preserving and strengthening minority banks has been ineffective.

I referred earlier to challenges to highly profitable operations faced by minority banks. In August 2006, the Federal Deposit Insurance Corporation's (FDIC) Vice Chairman Martin J. Gruenberg identified some of those challenges: (a) the relatively higher cost of doing business in communities with incomes below market average, (b) high immigrant populations, (c) a smaller deposit base, and (d) a preference for in-person service.

Recognizing these obstacles, a primary goal of FIRREA was to create a framework within which regulators would act to help preserve and strengthen minority institutions. A recent interagency conference took place this past July to discuss how best to address what, as we as members of the National Bankers Association have described, as non-compliance by regulators with several provisions of FIRREA. Just a few weeks ago in our home base city of Durham, NC, representatives from several regulatory agencies advised the NBA's 80th Annual Convention on steps their respective agencies were taking to support minority institutions; speakers included Sheila Bair, Director of the FDIC; Randy Kroszner, Member of the Federal Reserve Board of Governors; and John Reich, Director of the Office of Thrift Supervision(OTS).

Given the challenging operating circumstances outlined earlier, regulators' efforts and requirements to preserve and promote the expansion of minority banks have been at best ineffective. My next point focuses on recommendations that, if implemented, offer the potential, I believe, of meaningful and substantive assistance for minority banks.

Take specific legislative steps to assist minority banks to raise capital and to operate efficiently.

Let me state clearly that in no way do the recommendations made in this testimony suggest that the standards of banking safety and soundness be compromised in any way, or that this committee consider any measure that would create increased risk for the banking system. My bank, and those of my colleagues, share the regulators' goals of ensuring the safety and soundness of the banking system.

A major concern is that the market places such a significant discount on the value of minority banks that we are placed at a significant disadvantage, regardless of our stature or profitability, in our abilities to raise capital. . Yet, we all acknowledge the importance of minority banks to the economic fabric of our nation's communities. As a result, I respectfully submit that the Financial Services Committee has the means to address this, expeditiously and efficiently, by ensuring that bank regulators provide the necessary notification regarding the array of technical assistance services that are available. This would allow minority banks to operate more efficiently and attract capital.

Moreover, while the Financial Services Committee does not have jurisdiction over taxes, which is the under the purview of the Ways and Means Committee, there is a palpable role for incentives. Specifically, the CDFI Fund guidelines should be modified to include awarding tax credits for investments in minority banks.

The GAO report clearly highlights the difference in performance between minority and majority banks. These differences are shown to be both traditionally and universally experienced among minority banks. However, the regulatory benchmarks by which minority banks' performance is graded always compare these institutions with the UBPR-designated peer groups, such that a truly equitable comparison of performance factors is not considered or possible. The Financial Services Committee should also consider legislation so that regulatory peer group benchmarking and examination evaluations are tailored to recognize these differences, just as there exists now certain examination differences for money center banks versus smaller community banks.

The GAO report points out, and the NBA has repeatedly articulated, that minority banks express concern and frustration that regulators often fail to demonstrate sensitivity to and understanding of the unique challenges they face. It may be especially true in this case, when the overwhelming evidence demonstrates that minority banks' performance is affected by numerous factors <u>not experienced</u> by the banks to which their performance is being compared, and graded by the regulators.

Regulators should modify the grading process utilized in bank examinations such that minority banks are compared to a peer group of other minority banks, and within the context of this peer group structure, apply the factors of safety and soundness. In that way, more than just asset size and general market descriptions would be taken into consideration, and a more meaningful comparison of a minority bank's performance could be made.

Minority financial institutions play a critical role in our nation's economy.

Minority-owned businesses are an essential component of the small business sector that creates jobs, fosters stable communities and promotes economic vitality. In addition to being integral to America's small business landscape, minority-owned financial institutions provide an economic foundation for communities that historically have been underserved.

With respect to the current "crisis" surrounding the subprime mortgage market, I respectfully submit to the Committee that minority banks are expert at providing financing to underserved, financially illiterate, and unsophisticated borrowers in a safe, and sound manner. It is very likely, that had the market and nation better recognized the resource that minority banking institutions represent, the damage that has occurred – both in terms of financial losses and negative impact on the industry's reputation - could have been mitigated to a significant degree.

From a historical perspective, M&F Bank and many other minority banks have been catalysts for change in the markets they serve. Were you to research the genesis of these banks, you would find many instances where entire communities were underserved or even completely ignored by the mainstream banks.. Banks like M&F answered the call of those underserved communities to open a branch so that they would have convenient, equitable access to banking services. Then those mainstream banks – who until then had been quite content to allow people to travel across town to their existing locations – suddenly found those unserved or underserved markets to be a worthwhile place for a bank branch.

More often than not, the branch locations of minority banks reside in the very communities referred to in CRA guidelines. Stated another way, laws and regulations had to be created to compel banks to provide access to credit to the very same communities where we have placed our branches and operate daily. While CRA rewards majority banks for honoring the letter of the law, minority banks have long embodied the spirit of the law.

In the 99 years since we opened our doors, M&F Bank has successfully balanced our mission to provide access to high-quality, competitively positioned depository and loan products with our responsibility to operate a sound, secure and profitable institution. We have been blessed to enjoy 99 years of consecutive profitability, weathering the Great Depression and numerous economic cycles. Underlying these goals is our founding and ongoing commitment to reach out to the communities we serve in meaningful ways. We look forward to continuing to do so for centuries to come.

It is the sincere wish of the Boards of Directors of M&F Bancorp, Inc. and Mechanics and Farmers Bank that this committee will consider the recommendations made today, and take the necessary actions to truly "Preserve and Expand Minority Banks'.

Again, I am honored and appreciate the opportunity to testify, and I am available for questions and comments from this distinguished panel.