



Testimony of

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On behalf of

The National Association of Federal Credit Unions

“H.R. 1418: The Small Business Lending Enhancement Act of 2011”

Before the

House Financial Services Committee

Subcommittee on Financial Institutions and Consumer Credit

October 12, 2011

Introduction

Good afternoon, Chairman Capito, Ranking Member Maloney and Members of the Subcommittee. My name is Gary Grinnell and I am testifying today on behalf of the National Association of Federal Credit Unions (NAFCU). I appreciate the opportunity to share my views with the committee on H.R. 1418 and credit union member business lending. I have been with Corning Federal Credit Union since 1997, and have served as President/CEO since 2007.

Corning Credit Union was founded in 1936 in Corning, NY in an effort to keep Corning Glass Works employees from being victimized by street-corner lenders. Today, we have over 79,000 members and \$896 million in assets. We have 250 employees and 17 branches in New York, Pennsylvania and in the Wilmington, North Carolina area.

As you may know, NAFCU is the only national organization that exclusively represents the interests of the nation's federally chartered credit unions. NAFCU is comprised of nearly 800 member-owned and operated federal credit unions. NAFCU member credit unions collectively account for approximately 62 percent of the assets of federally chartered credit unions. NAFCU and the entire credit union community appreciate the opportunity to participate in this discussion regarding member business lending. We hope you will agree that raising the artificial and outdated job-killing cap on member business lending is overdue and a necessary pro-growth step that will help small businesses and communities recover from the current economic crisis. NAFCU believes H.R. 1418 is about jobs - saving jobs, creating jobs and helping America recover and grow stronger. Who could be opposed to job creation and making our economy stronger? It's time to put aside the tired old arguments of greedy bankers and put jobs, our

economy and America first. Today's hearing and the ultimate enactment of H.R. 1418 is an important step in doing just that.

Background on Credit Unions

Historically, credit unions have served a unique function in the delivery of necessary financial services to Americans, including making business loans. Established by an act of Congress in 1934, the federal credit union system was created, and has been recognized, as a way to promote thrift and to make financial services available to all Americans, many of whom would otherwise have limited access to financial services. Congress established credit unions as an alternative to banks and to fill a precise public need—a niche that credit unions fill today for nearly 93 million Americans.

Every credit union is a cooperative institution organized “for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes.” (12 USC 1752(1)). While more than 75 years have passed since the *Federal Credit Union Act* (FCUA) was signed into law, two fundamental principles regarding the operation of credit unions remain every bit as important today as in 1934:

- Credit unions remain totally committed to providing their members with efficient, low cost, personal service; and,
- Credit unions continue to emphasize traditional cooperative values such as democracy and volunteerism.

The nation's approximately 7,200 federally insured credit unions serve a different purpose and have a fundamentally different structure than banks. Credit unions exist solely for the purpose of providing financial services to their members—while banks aim to make a profit for a limited number of shareholders. As owners of cooperative financial institutions united by a common bond, all credit union members have an equal say in the operation of their credit union—“one member, one vote”—regardless of the dollar amount they have on account. These singular rights extend all the way from making basic operating decisions to electing the board of directors—something unheard of among for-profit, stock-owned banks. Unlike their counterparts at banks and thrifts, federal credit union directors generally serve without remuneration—a fact epitomizing the true “volunteer spirit” permeating the credit union community.

Credit unions continue to play a very important role in the lives of millions of Americans from all walks of life. As consolidation of the commercial banking sector has progressed with the resulting de-personalization in the delivery of financial services by banks, the emphasis in consumers' minds has begun to shift not only to services provided but also—and in many cases more importantly—to quality and cost. While many banks have increased their fees and cut their customer service as of late, credit unions are second to none in providing their members with quality personal service at the lowest possible cost.

Although it is not the subject of this hearing today, I would be remiss if I did not personally thank you Chairman Capito, and all of those who supported the recent efforts to try to bring needed changes to the Durbin debit interchange price-control provision that was added to the *Dodd-Frank Wall Street Reform and Consumer Protection Act*. Like member business lending,

this issue is of great importance to credit unions and the consumers they serve, as it will have a direct impact on the ability of credit unions to meet the needs of their membership.

Background on Credit Union Member Business Lending and the Arbitrary Cap

When Congress passed the *Credit Union Membership Access Act* (CUMAA) (P.L.105-219) in 1998, it put in place restrictions on the ability of credit unions to offer member business loans. Credit unions had existed for nearly 90 years without these restrictions. In 1998, Congress codified the definition of a member business loan and limited a credit union's member business lending to the lesser of either 1.75 times the net worth of a well-capitalized credit union or 12.25 percent of total assets.

CUMAA also established, by definition, that a business loan of \$50,000 and above is a member business loan that counts toward the cap. This number was not indexed and has not been adjusted for inflation in the more than 13 years since enactment, eroding the *de minimis* level. Where many vehicle loans or small lines of credit may have been initially exempt from the cap in 1998, many of those that meet the needs of small business today, are now included into the cap due to this erosion. To put this in perspective relative to inflation since 1998, what cost \$50,000 in 1998 costs \$69,500, using the August consumer price index data. That is a 39% rate of inflation change that is completely ignored by current law and which greatly hampers a credit union's ability to meet its members' needs.

Also, pursuant to section 203 of CUMAA, Congress mandated that the Treasury Department study the issue of credit unions and member business lending. In January 2001, the Treasury Department released the study, “Credit Union Member Business Lending” and found the following: “...credit union’s business lending currently has no effect on the viability and profitability of other insured depository institutions.” (p. 41). Additionally, when examining the issue of whether modifying the arbitrary cap would help increase loans to businesses, the study found that “...relaxation of membership restrictions in the Act should serve to further increase member business lending...” (p. 41).

As stated above, the 2001 Treasury study found that credit unions do not pose a threat to the viability and profitability of banks, but that in certain cases, they could be an important source of competition for banks. It is important to note that credit unions have a nominal market share of the total commercial lending universe (approximately 5% of all small business loans from insured depository institutions), and are not a threat to banks (who control nearly 95% of all small business loans from insured depository institutions) in this environment.

A 2011 study commissioned by the SBA's Office of Advocacy affirms these findings. (James A. Wilcox, *The Increasing Importance of Credit Unions in Small Business Lending*, Small Business Research Summary, SBA Office of Advocacy, No. 387 (Sept. 2011)). The SBA study also shows, importantly, that credit union business lending has increased in terms of the percentage of their assets both before and during the 2007-2010 financial crisis while banks' has decreased. This demonstrates not only the need for lifting the MBL cap in order to meet credit union members' demand, but also that credit unions continued to meet the capital needs of their

business members even during the most difficult of times. One of the findings of the study was that bank business lending was largely unaffected by changes in credit unions' business lending. Additional analysis in the study also found that credit unions' business lending can actually help offset declines in bank business lending during a recession.

Member Business Lending at Corning Credit Union

Corning Federal Credit Union (CCU) currently exceeds 80% of its current cap, and we forecast that we will reach the cap by mid-2012 if Congress does not act. On the business lending side, we have a well diversified portfolio with minimal delinquencies (a delinquency ratio of 0.36%). Our commercial losses have also been minimal as we have an experienced lending staff and a sincere and devoted membership. For the last two years, we have been recognized as the top small community lender by the Small Business Administration in the 34 counties that make up the SBA district in which we are located.

CCU has been an important source of funding for existing, new and growing businesses in the Southern Tier and Finger Lakes region of New York, and the greater Wilmington area of North Carolina since 2006. During the recent economic downturn, as banks in our markets, and particularly in the Wilmington area stopped lending to their clients, CCU has been able to fill an important need to provide these businesses with the funding they need to continue to grow and create jobs.

We started our Business Services program in 2006 in response to demand from our existing membership, and recognition of a gap of such services within our local community. We took a planned and deliberative approach toward starting our program, hiring an outside consultant to help us explore the opportunity and put a detailed, strategic plan together. We have deliberately hired experienced commercial lenders and business services professionals from outside the organization. We have added jobs over the past several years to support our growth and member demand, and now have commercial loan officers, credit analysts, business development officers, supervisors, administrative staff and business account specialists on staff.

There are a number of stories of people we have helped with our business lending program.

A developer in upstate NY turned to us after a local bank that was financing this developer's apartment project tightened up in 2009. The bank pulled back on their original commitment and offered him a much higher rate. They initially financed the entire construction project and at the time of their change in heart, the building was fully occupied. In this situation, the bank took the risk during the construction phase and apparently was not interested in the final project. This developer decided against fighting the change in commitment from the bank, and instead pursued financing elsewhere rather than spending time and money in a lawsuit. CCU was able to refinance the deal and help the developer complete his project and move on to other successful development projects in the upstate NY area, saving critical construction and trades jobs in the process.

A long-time restaurant owner maintained a relationship with an upstate NY bank for decades. He kept all of his business deposits at the bank, and had a commercial mortgage with them. His loan officer at the bank never visited him at any point for years after the loan closed. After years of loyalty to this bank and consistently meeting his loan obligations, he was assessed an arbitrary and onerous transaction service fee on his deposit account, which the bank refused to waive. He decided to move his relationship elsewhere and ended up refinancing the mortgage and moving his entire deposit relationship to CCU.

In 2007, one of our members in upstate NY had a dream of starting up her own pet care business. She worked with the local small business development center to create a comprehensive business plan. She approached a large bank for startup capital, but they had no interest in the loan. Based on a recommendation from another business owner, she approached CCU. Thinking creatively and with the help of the US Small Business Administration, we were able to put together a package of financing to help this member get her dream off the ground. CCU has since assisted her as her business has grown at a rate of 18-20% per year. She has expanded the business with additional services and added half a dozen jobs to the local community.

Mayor Bill Saffo of Wilmington, NC, a port city of over 100,000 residents in one of the fastest-growing regions in North Carolina, turned to us after he received numerous calls to his office from small business owners desperate to obtain financing to keep their doors open and projects on track. The banks, both local and national, have aggressively moved to slash access to credit in this market, in a severe backlash to their risky lending and investment practices prior to the crash. In a move to reduce their own commercial loan portfolios, they have called loans and

lines of credit, and forced businesses to pay off their loans early or at renewal regardless of the borrowers' payment history and creditworthiness. The mayor recognized that one of the few financial institutions that bucked this trend is Corning Credit Union. We expanded our presence in the Wilmington market over the past few years, opening two additional branches and hiring experienced people to help develop the business. In numerous instances we have worked with our local business community to provide needed financing which has helped to save and create jobs. Bill Saffo, the mayor of the eighth largest city in North Carolina is a strong proponent of HR 1418. He has directly witnessed how the banks have stripped local businesses of their access to credit while at the same time Corning Credit Union has continued to invest in his community.

We even helped a bank employee in Wilmington, NC, when she couldn't get help from her industry. This member is a commercial lender who works at a community bank in Wilmington. She also owns rental properties in the Wilmington area. After a bank informed her that they would not renew her commercial mortgage after the initial five-year balloon period, she wasn't even able to obtain financing from her employer let alone other banks in the area. She came to CCU, and we were able to refinance her investment property loans for her.

These are just a handful of examples of the people we can help and the jobs we can create with our business lending program. Because we are approaching the cap, we have refrained from advertising or marketing our business services. We have not aggressively pursued additional business to help our communities and support job creation because we have more demand right now than room to lend under our cap. At the current pace of demand that is coming through our doors, we will hit the cap by mid-2012.

In addition, because of our proximity to the cap, and limited ability to grow, we have not hired additional employees recently. If the cap were lifted, we would hire at least two additional employees immediately. We have spent the past six years growing our business lending and business services expertise, infrastructure and support. Given our proximity to our cap, we will need to seriously consider what to do with these highly skilled and well-compensated professionals if we no longer have the ability to actively lend to small businesses. Additionally, we are holding off opening new offices in certain growing markets (where there is demand for commercial loans) because we are running out of capacity under our cap to lend to small businesses. Due to our strong balance sheet we have a significant amount of cash available to lend (almost \$300 million) but our hands are tied because of the arbitrary cap. We should emphasize that this \$300 million is not taxpayer dollars or government stimulus. It is cash from our depositors that can be used as a source of credit for productive purposes such as helping small businesses in our communities.

We are just reaching the point now (because of our growth and demand) that we are going to have to start turning business away because of the cap. We expect the frequency we will be forced to pass on deals will increase rapidly over the next 6 to 12 months, and those jobs that would be created from those loans may not exist. That is why I am here today to ask for your help to raise this outdated cap. We have the capital, the expertise, and the desire to make a positive impact in our community. Let us help create more jobs.

Myth vs. Reality on MBL

Many in the banking community who oppose the aid to small business that changes to the cap would bring often try to cite safety and soundness issues related to credit unions and business lending. Perhaps the better question would be whether a number of banks should be making commercial business loans. An examination of 2nd quarter 2011 call report data shows that credit unions with MBL's actually have lower business loan losses (0.87% annualized net charge-offs) than commercial lending banks (1.17% annualized net charge-offs). The average size of a credit union member business loan is approximately \$222,000, which mitigates credit risk and is evidence that these loans are truly loans to small businesses. Evidence from our members also indicates that many small businesses turn to credit unions after they have been told that the bank does not want their business anymore. It must be noted that despite what some bankers may want you to believe, member business lending is not a new endeavor for credit unions. Credit unions have been making safe and sound member business loans for over 100 years.

The banking industry also argues that the credit union MBL cap should not be raised due to the credit union federal tax exemption. What the banking industry conveniently forgets to mention is that a large number of banks do not pay corporate federal income tax because of their Subchapter S status. There are approximately 2,358 Subchapter S banks that avoid federal income taxes today. What the banking trades don't want you to know, is that one estimated value of the Subchapter S federal tax break for banks is \$2.05 billion for 2010, *which is significantly greater* than the estimated value of the entire credit union tax expenditure (\$1.27

billion) for FY2010 as included in the President's FY2012 budget. Perhaps more investigation is needed on the unfair advantage banks have over credit unions due to their Subchapter S federal tax break.

The banking industry also claims that raising the member business lending cap would somehow distract credit unions from serving underserved populations. Here they also forget to mention how they have sued the National Credit Union Administration in the past as part of an effort to prevent credit unions from reaching out to serve more underserved areas. Credit unions have a long history of demonstrated service to underserved communities and outperforming banks as evidenced by historical Home Mortgage Disclosure Act (HMDA) data. Creating jobs is one of the most important ways to help underserved communities in these tough economic times. Raising this arbitrary, job-killing member business lending cap will help create these much needed jobs.

Some critics claim that only a limited percentage of credit unions are actually at the arbitrary member business lending cap and therefore nothing needs to be done. This view fails to see the big picture of how the arbitrary cap acts as a deterrent for efforts to increase business lending and create American jobs. Successful business lending programs like ours at Corning Credit Union require investment in human and other resources by the institution. Those credit unions that have some member business lending but are not near the cap, have an artificial disincentive in the arbitrary cap. Nearly 2,200 credit unions make member business loans. If they are successful in growing and expanding their business lending program, they will ultimately reach

this arbitrary barrier forcing them to scale down what they invested in to build up. Furthermore, a number of credit unions are discouraged from establishing member business lending programs, as the cap creates artificial limits to their potential for lending, potentially skewing the cost-benefit analysis of investing in a member business lending program and discouraging them from getting involved at all.

One final point must be made in response to the argument that only a few hundred credit unions are near the cap would directly benefit from raising the cap. The concept of helping only a limited number of institutions did not stop Congress from making \$30 billion in taxpayer dollars available to community banks last year under the Small Business Lending Fund. Only a few hundred community banks have taken taxpayer money under that program, a significant number of which did not even use it for business lending. H.R. 1418 has a lot less cost and a lot more benefit than that well-intentioned, but unsuccessful effort.

At Corning Credit Union, we started our business lending program in 2006 and our successful, managed growth has us already approaching the cap today. As we approach the cap, we have actually had to scale back promoting our business lending program to those who may need credit, as the artificial cap is crimping the ability for us to meet the existing demand of our membership. If this artificial cap were raised, we could create more jobs internally and help small businesses create more jobs in our community.

H.R. 1418, the *Small Business Lending Enhancement Act*

In April of 2011, Representatives Ed Royce and Carolyn McCarthy introduced the *Small Business Lending Enhancement Act* (H.R. 1418), which would raise the arbitrary credit union member business lending cap to 27.5 % of total assets, up from 12.25%, and help stimulate the nation's struggling economy by increasing access to credit for small business owners. This important legislation has over 85 bipartisan co-sponsors. Identical bipartisan legislation (S. 509) has been introduced in the Senate.

The *Small Business Lending Enhancement Act* is a well thought out solution that includes important provisions to ensure that safety and soundness concerns are addressed. This bill is not about helping credit unions - it is about helping small businesses create jobs.

In order to see its cap increased, a credit union would need to meet strict eligibility requirements to gradually increase its member business lending portfolio, including: being well capitalized [currently at least a 7% net worth ratio]; having at least 5 years of member business lending experience; must be at or above 80% of the current 12.25% cap for at least 1 year before applying; and, must be able to demonstrate sound underwriting and servicing based on historical performance and strong management. The requirements in this legislation mirror those endorsed last year by Treasury Secretary Timothy Geithner and NCUA Chairman Debbie Matz.

As evidenced by the strict eligibility requirements outlined above, the *Small Business Lending Enhancement Act* was specifically tailored to address concerns that raising the current cap could somehow create safety and soundness issues.

Unlike efforts enacted by Congress to provide \$30 billion to promote business lending at community banks, credit unions don't need to take taxpayer dollars to make worthwhile loans. While similar legislation to H.R. 1418 scored at a cost of \$77 million over 5 years according to a 2010 CBO estimate, it should be noted that this cost does not take into account added tax revenue that would be gained from the businesses and jobs created by enacting this legislation. This pales in comparison to the price tag for what Congress did for the community banks in the last Congress when the *Small Business Jobs Act* created a \$30 billion "Small Business Lending Fund" (SBLF) with the intention of encouraging community banks to lend to small businesses. To date the program has created very few if any jobs, and has done little to spur economic growth for its \$30 billion price tag. Furthermore, it has been reported that only about 332 banks received funding under the \$30 billion program. An October 6th *Wall Street Journal* article entitled "Tale of Two Loan Funds" described how nearly 40% of those who took funds used them to pay off TARP obligations, instead of making needed loans to America's small businesses. In the article, one community banker even admitted "It's a bit of a shell game." Furthermore, this same article noted that banks denied up to 60% of small business loan applications this year. Clearly this is something Congress should investigate further. Credit unions don't think creating jobs for the American economy is a game and we don't need taxpayer funds to do it. It is a serious business, and we stand ready for the task.

Failing to consider legislation to raise the arbitrary member business lending cap last Congress was a missed opportunity to further assist small businesses create jobs and help move the economy in a positive direction. NAFCU and its member credit unions ask that the *Small*

Business Lending Enhancement Act be considered by the Financial Services Committee and on the House floor as soon as possible.

Industry estimates that enacting H.R. 1418 could help spur over \$13 billion in new lending and create over 140,000 new jobs in the first year alone. In an environment, where job creation is so important, it is unfathomable to the nation's 93 million credit union members that Congress would not move forward with such a bipartisan commonsense approach that has no sound policy argument against it, only misguided opposition from the banking industry.

We understand that community banks are seeking their own forms of relief as part of the *Communities First Act*, H.R. 1697. One approach to provide fair relief to all would be to combine both bills and pass as a package. While this may not be the first choice for banks and credit unions, it may be a fair compromise to aiding our nation's community institutions and putting job creation first. Failure to consider raising the member business lending cap for credit unions, while at the same time advancing H.R. 1697 and its provisions, would likely lead to public opposition from NAFCU and the entire credit union community, its members, and small businesses.

Credit unions have been vital in helping our country recover from the financial crisis, and members of Congress on both sides of the aisle recognize that they were not the cause of it. Many credit unions have capital to lend small businesses across the country and are in a position to further assist in recovery efforts and help create jobs. However, due to the outdated and arbitrary member business lending cap, their ability to help stimulate the economy by providing

credit to small businesses is hampered. Removing or modifying the outdated and arbitrary, job-killing credit union member business lending cap would provide needed economic stimulus at no cost to taxpayers and no increase to the federal deficit. Credit Unions have their own capital and liquidity ready to invest in their communities and help their members. Enacting H.R. 1418 will free up those funds to help create American jobs.

Conclusion

The artificial credit union member business lending cap established in 1998 is arbitrary and outdated. In short, it is killing thousands of potential jobs in the economy. The need for such a cap was questioned by the Treasury Department as far back as 2001. Credit union member business lending is not a threat to the banking industry which currently controls nearly 95% of all small business lending at insured depository institutions. While NAFCU believes that no statutory cap should be in place, a number of credit unions like mine, and the millions of members we serve, would benefit from the enactment of H.R. 1418, the *Small Business Lending Enhancement Act*. This legislation would provide a practical and well-thought out approach to raising the arbitrary threshold, while addressing concerns about rapid growth and safety and soundness. This is a real bipartisan jobs package that everybody should be able to support.

We thank you for your time and the opportunity to testify before you here today on this important issue to credit unions and our nation's economy. I would welcome any questions that you may have.