BORDER FEDERAL CREDIT UNION

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Testimony of

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Subcommittee on Financial Institutions and Consumer Credit

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"Challenges Facing Community Financial Institutions in Texas"

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Introduction

Chairman Capito and Members of the Subcommittee, thank you very much for the opportunity to testify at today's hearing. My name is Maria J. Martinez and I am President and Chief Executive Officer of Border Federal Credit Union in Del Rio, Texas, a $107 million credit union serving approximately 22,000 members. Border FCU is a community credit union serving thirteen counties, mostly designated as distressed/underserved areas. Border FCU has a low income designation and it's also certified by the US Treasury as a Community Development Financial Institution. I am also a charter member and the Chairman of the Board of the Network of Latino Credit Unions and Professionals incorporated in 2006 to promote the credit union philosophy within the Latino community and with a vision to empower the Latino Community to build family wealth, develop economic opportunity, and secure financial stability. I have over 20 years of executive level experience serving credit unions.

I have been asked today to testify on the challenges facing community financial institutions in Texas. Of the many challenges, my testimony today will focus on the following:

- The Member Business Lending Cap
- Regulatory Burden
- Examination Issues, and
- The Lack of Consumers' Financial Education & Awareness

Attached to my testimony you will also find an overview of Texas economy and credit union operations prepared by the Credit Union National Association.

The Member Business Lending Cap

The current cap of 12.25 percent of a credit union's total assets is obstructing a crucial source of capital to small businesses at a time that it's desperately needed. This cap should be increased to 27.5 percent as proposed by HR 1418, introduced by Representatives Royce and McCarthy.

My credit union does not offer business loans currently. Why? Because the cap presents a significant disincentive to a credit union my size to begin making small business loans. At roughly $100 million dollars, my credit unions MBL cap would be about $12 million. In order to do business lending, I would have to hire business loan officers and establish a plan that could result in ending the program and laying off the loan officers after making only a few dozen loans. An expanded cap may provide more incentive for a credit union my size to engage in this type of lending. But beyond the impact this legislation may have on smaller credit unions, the positive impact that this legislation could have on communities throughout Texas and across the country is hard to deny.

Credit unions have been doing business lending for over 100 years – the first 90 years they did so without a cap. During the financial crisis, credit unions expanded their business loan portfolios. They stood with their members during the tough times. That is what credit unions do. Now, the credit unions that contributed the most to the growth of recent years are approaching the cap. Nearly 500 credit unions are making decisions daily to manage the cap. Some have stopped lending to new business members. Others have had to restrict what they lend. This is not happening because examiners are discouraging lending. It's happening because the law tells credit unions they have to stop. If the law isn't changed, the credit unions that helped keep small businesses going during the crisis will not be there to help them during the recovery.

The jobs this legislation could create are real. And you can have confidence that credit unions would lend the estimated $13 billion in the first year because credit unions loaned to their members in the darkest hours of the financial crisis; they have the capacity and experience to stay with them in the recovery, if Congress gives them permission.

Regulatory Burden

For credit unions, our greatest challenges are the ever growing regulatory burdens in the wake of the financial crisis and statutory restrictions on member services.

Credit unions did not cause the financial crisis, but we have been affected by it. One of the drivers for credit union performance and stability during the financial crisis has to do with the structure of credit unions. As financial cooperatives, credit unions tend to be less risky and more member-friendly because the members – the users – of the credit unions are also the owners. Nevertheless, credit unions are being subjected to ever expanding consumer protection and safety and soundness regulation in the wake of the financial crisis. These seemingly unending changes in regulatory requirements make it more complicated for us to serve our members. It is not necessarily any one single regulation that is overly burdensome but rather the totality of regulations, the frequency with which the regulations change, and the sometimes varying application of the regulation by field examiners which sometimes conflicts with or expands upon the original intent of the regulation. For credit unions, the unending increase in the complexity of regulatory burden is all more perplexing given the health of the Federal Deposit Insurance Fund and the National Credit Union Share Insurance Fund, during the recent financial crisis.

To give you a sense of what we are up against in terms of regulatory burden, according to our national trade association, the Credit Union National Association, there are at least 27 rulemaking proposals pending at various agencies including the National Credit Union Administration, the Consumer Financial Protection Bureau, the Department of

Housing and Urban Development, the Federal Housing Finance Agency, the Financial Accounting Foundation, and the Internal Revenue Service. As these rules are finalized, my credit union may have to change the way that we offer products to our members; we will have to train our staff on the new rules; we will have to modify our forms. We will dedicate a significant amount of our members' resources complying with new rules. The flood of regulations creates an unnecessary burden without any measure of the effectiveness of these changes, and there is no end in sight.

We would prefer to spend our resources on promoting our mission of financial literacy and the development of new products to serve the needs of our members within our local communities.

While the new Consumer Financial Protection Bureau seems to be approaching its job with a watchful eye toward minimizing regulations and has sought ongoing input from credit unions on its work, concerns remain. One of the first regulations finalized by the CFPB has to do with remittances. It is over 400 pages long. My credit union does 10-15 international remittances per month. As this regulation is implemented, I question whether it will make sense for us to continue to offer this service to our members if this proposal goes through, even though this is something that a small number of my members depend on. While we only do a small number of remittances, I imagine that many of my colleagues across Texas and throughout the country will face a similar dilemma. When credit unions are forced to pull back services because of regulatory burden, the impact is felt disproportionately on those who have the most fragile access to mainstream financial services.

Of course, the CFPB is not the only agency writing rules with which credit unions must comply. The National Credit Union Administration continues to be active in the rule writing business, notwithstanding the relative health and strong performance of the credit union system, issuing proposed rules recently on troubled debt restructuring, emergency liquidity and loan participations.

The impact of ever increasing, rarely decreasing regulatory burden crisis can be seen vividly in the movement toward consolidation in the credit union industry. The cost of complying with all of the regulations is the same for a small credit union as it is for a larger one; however, smaller credit unions obviously have fewer resources and keeping up with the ever increasing burden is often the straw that breaks the camel's back.

I encourage you to continue your vigorous oversight of the various regulatory agencies to ensure that the rules that they promulgate are necessary and appropriate, that there is some measurement of their effectiveness, and that if there are rules which are outdated or obsolete, they are removed from the books.

One example of a change that should be made has to do with the requirement under Regulation E that ATMs carry a physical disclosure of potential fees associated with transactions in addition to an electronic disclosure. Sadly, some have taken advantage of the private right of action under this rule to deface ATMs and then sue the financial institution for noncompliance. I have heard some of my colleagues have taken extraordinary steps to document their compliance – even sending staff to photograph their ATMs on a frequent basis. This is an outrageously unfortunate cost of complying with a rule that serves little value to consumers in an age where an electronic disclosure of actual costs is universally available. The resources credit unions spend documenting compliance with this obsolete requirement should be put to better use serving their members. If the CFPB will not eliminate this requirement by rule, Congress should do so by law.

During the development of the Dodd-Frank Act, credit unions strongly supported a provision that requires the CFPB to review outdated, unnecessary and unduly burdensome regulations with an eye toward reducing regulatory burden. I hope that the Committee will ask the CFPB to regularly report on their efforts in this regard.

Examination Issues

The examination is a vital part of operating a financial institution. However, the process creates interpretation inconsistencies. At times, it seems there is a separation between the "policy" as stated by the regulatory leadership and what occurs locally during the exam. It is important that examiners not over-regulate or exceed their authority. Border FCU is very fortunate to have a positive professional relationship with our examiners that has allowed transparency in the exam to focus on safety and soundness. Yet, as field examiners try to interpret the will of the regulatory agency, and the agency is interpreting Congress directives, our credit unions get caught in the middle as we try to comply and interpret what's mandated in order to run a successful institution. It is important that examiners be consistent when treating regulations and guidance and that they have a respectful and professional relationship with credit unions.

I urge you to consider improvements to the examination process. Passing HR 3461, the Financial Institutions Examination Fairness and Reform Act, which addresses the exam process, would be a positive step in balancing the relationship between the regulator and the regulated. It will also encourage a more transparent and consistent examination process. Also, as you consider these improvements, please ensure that costs to implement these are not transferred to the credit unions.

The Lack of Consumers' Financial Education & Awareness

Finally, I would be remiss if I did not encourage the Committee to continue supporting financial literacy and awareness programs. It is important that consumers be equipped with the knowledge, confidence and skills necessary to make intelligent decisions when investing and/or borrowing funds. As communities grow and jobs are created, free or low cost programs must be accessible to consumers within the financial industry to assist them with financial education.

As a society we must not only be ready to create jobs, but also diligently promote financial awareness so that when a person starts earning a paycheck they can make the best use of those funds. Consumers need objective information in order to avoid financial failure.

As a Texas community credit union, serving diversified areas consisting of underserved societies, areas where oil and gas exploration is booming and a military base, Border FCU has taken a proactive approach to provide financial education through free programs such as HUD counseling services, budgeting workshops and volunteer income tax preparation. Border FCU also targets financial education among the youth through volunteer staff that takes the junior achievement and National Endowment for Financial Education (NEFE) programs to the local schools and offers a youth financial summer camp.

I ask the Committee to support financial literacy programs. We all know that an educated consumer is the best client of any institution.

Conclusion

Madame Chairman and Members of the Subcommittee, thank you very much for coming to Texas and holding this hearing. I appreciate the attention that you're giving to these issues and credit unions look forward to working with you.

Overview of the Texas economy and Credit Union Operations

The Texas Economy

While far from unscathed, the state of Texas largely was spared from the most severe consequences of the global financial crisis and subsequent economic downturn. The combination of relatively fast population growth, a relatively large oil and gas sector, and housing markets that did not inflate as dramatically as those nationally all helped to temper dislocations in the state's economy.

Selected Economic/Demographic Comparisons
Sources: Bureau of Census, Bureau of Labor Statistics, Federal Housing Finance Agency, CUNA E&S.

	Texas	United States
Population growth:		
2000-2010	20.6%	9.7%
2010-2011 (Census Estimate)	2.1%	0.92%
Home price changes (FHFA All-transactions index):		
Decade prior to peak	+54%	+93%
Change since start of downturn	-5%	-16%
Change in past year	-1%	-3%
Unemployment Trends:		
Rate at start of downturn	4.4%	5.0%
Peak	8.2%	10.1%
Current rate	7.4%	8.3%
Change over past year	-0.8%	-0.8%
Employment Trends:		
Change vs. start of downturn	+123,000	-5.6 million
Change vs. year-ago	+205,000	+2.0 million

Note: Employment/unemployment is as of 1/12 for US; 12/11 for TX.

It is especially important to note that the labor market in Texas did not decline as severely and is improving faster than is the US labor market. Total non-farm employment in Texas is now above pre-recession levels. All but four of the state's twenty-five MSAs report unemployment rates that are below the national norm and all but one reports a year-over-year decline in unemployment rates.

Texas Credit Unions:

Texas is home to 535 credit unions, which now serve 7.7 million members and manage $73 billion in total assets. The state's credit unions are relatively small institutions. The median asset size is $20 million and the average size is roughly $115 million. In contrast the average Texas bank is over five times larger, with nearly $600 million in assets.

Despite both the competitive challenges arising from their relatively small size and the obvious economic challenges, Texas credit unions remained "in the game" throughout the crisis and continue to perform at a high level. Since the start of the downturn, loans at Texas credit unions have increased

25% and savings balances increased by 44%. Collectively, credit unions in the state have added over 725,000 members since December 2007.

Of course the Texas economy's relatively favorable performance over the past several years has translated into fewer dislocations in the operations of financial institutions in the state.

In all, only eight Texas credit unions failed since the start of the economic downturn. The failure rate in Texas credit unions is nearly identical to the national failure rate among all U.S. credit unions and the rate of failure is less than one-third of the 4.7% rate experienced by the nation's banking institutions.

Financial Institution Failure Rates* Since the Start of the Crisis (2008-2011) Sources: FDIC, NCUA, CUNA.	
Texas Credit Unions	1.3%
Texas Banks	1.4%
U.S. Credit Unions	1.2%
U.S. Banks	4.7%
* Number of total 2008-2011 failures as a percent of total institutions on 12/31/07.	

It's important to note that unlike the nation's banking institutions, credit unions – both nationally and in Texas – required no massive taxpayer bailout to remain solvent.

The capital ratio at Texas credit unions began the downturn at 11.2% - a historical high-point. Since then, consistently strong savings growth, relatively weak loan growth arising from household deleveraging and recession-related earnings pressures have combined to cause the aggregate capital ratio to decline to 9.7% by year-end 2011. Still, this average is nearly four percentage points higher than the level at which credit unions are considered "adequately capitalized" and nearly three percentage points above the regulatory level needed to be considered "well capitalized". Overall, 95% of the state's 535 credit unions are well capitalized with net worth-to-asset ratios of at least 7%.

While challenges still are evident, asset quality at Texas credit unions has remained relatively strong throughout the downturn. The 60+ day dollar delinquency rate remains elevated but declined from a cyclical high of 1.46% at the end of 2009 to 1.23% at the end of 2011. In contrast, the credit union delinquency rate nationally was 1.60% at year-end 2011.

Loan loss rates peaked at 0.95% in 2009 but declined to 0.89% in 2010 and 0.75% in 2011 at Texas credit unions. The 2011 loan loss rate is roughly 20% lower than the rates reported by all US credit unions (0.91%) and by the state's banking institutions (0.89%) in the year and is less than one-half the rate reported by banking institutions nationally (1.60%).

Prepared by the Credit Union National Association, Economics and Statistics
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