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Testimony of

Peter Skillern, Executive Director of the

Community Reinvestment Association of North Carolina before the

United States Senate Banking Committee, Financial Institution Subcommittee,

Wednesday, July 8, 2009.

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Thank you, Senator Johnson, for the opportunity to testify today on lenders, consumers and the economy in rural areas. I am Peter Skillern, Executive Director of the Community Reinvestment Association of North Carolina, a nonprofit community advocacy and development agency.[1]

North Carolina has strong rural and banking sectors. Eighty-five of our one hundred counties are rural and 50% of the population lives there.[2] North Carolina has 106 credit unions and 106 banks ranging from the largest bank in the country, Bank of America at $2.4 trillion in assets, to Mount Gilead Savings and Loan at $9.8 million, [3]

The current economic stresses for our rural communities and small financial institutions are significant. They are best understood in the context of two long-term trends: 1) a decline in the rural economy, and 2) the consolidation of the financial sector. Our policy

[1] For a fuller description, please visit www.cra-nc.org

[2] North Carolina Rural Center Data Center, http://www.ncruralcenter.org/databank/

[3] FDIC Institutional Data http://www2.fdic.gov/idasp/main.asp

recommendations are 1) to reform the broader regulatory financial system for stability, and 2) to invest in rural communities for recovery and growth.

1) Rural Economies Are in Long-Term Decline

The economic crisis facing the nation impacts North Carolina hard, with the fifth highest unemployment rate in the country at 11.4%.[4] It hurts our rural counties harder with 19 counties—such as Scotland, McDowell, and Edgecombe--experiencing unemployment from 14%-17%.[5] These unemployment rates are years in the making.

Rural North Carolina did not recover from the 2001 recession. Between 2002 and 2005 the manufacturing sectors of textile, apparel and furniture lost more than 88,000 jobs. In the past year more than 22,000 factory jobs were lost, particularly in the factories producing parts for the auto industry.[6] North Carolina still produces more tobacco than any other state, but changes for tobacco and the agricultural sector are dramatically reducing the number of small family farmers.[7] While rural counties in the scenic mountains and coast and the exurbs of our cities have enjoyed net in-migration, 40 rural counties lost population in the past decade. The North Carolina rural population is more likely to be older, poorer and have lower educational attainment. Median rural household incomes are 25% lower than in urban areas and poverty rates are 36% higher.[8] Due to

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[4] United States Department of Labor, http://www.bls.gov/web/laumstrk.htm

[5] Bureau of Labor Statistics, http://data.bls.gov/PDQ/outside.jsp?survey=la

[6] North Carolina Rural Center, http://www.ncruralcenter.org/databank/trendpage_Employment.asp

[7] North Carolina Rural Center, http://www.ncruralcenter.org/databank/trendpage_Agriculture.asp

[8] North Carolina Rural Center, http://www.ncruralcenter.org/databank/trendpage_Income.asp

low wages, rural residents face a housing affordability gap even though home prices on average are lower. As a result, 24% of the housing stock in rural areas is manufactured homes compared to 8% in urban areas.[9] New home construction often consists of second homes for retirees in the Blue Ridge Mountains and Outer Banks. The foreclosure rate for rural areas has jumped correspondingly with the credit crisis and the increase in unemployment. This recession intensifies a long-term restructuring of the economy in rural communities.

2) Small Financial Institutions are Declining as the Financial Sector Consolidates

During the economic crisis a number of small banks across the nation have failed—two in North Carolina in 2009—but far more have been lost through consolidation over time. Nationally, the number of banks with under $100 million in assets dropped by 5,410 from 1992 to 2008.[10] In North Carolina, rural counties hold 50% of the population and 50% of bank branches. Yet rural bank branches hold only 15.7% of deposit assets (down from 27% in 1996.)[11] Nationally, approximately 4,000 small banks made 100 or fewer mortgages in 2007.[12] In all, these smaller lenders account for 1.8% of all national mortgage activity. North Carolina CDFI credit unions are facing declining deposits, higher delinquencies and adverse regulatory pressure to curtail lending. The result could be closures. Small banks are at a competitive disadvantage in terms of pricing, products

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[9] US Census 2000, Units in Structure, Summary File 3, Table H30)

[10] It Takes More Than a Village: The Decline of the Community Bank, Celent, http://reports.celent.com/PressReleases/200901293/VillageBank.asp

[11] FDIC Institutional Data http://www2.fdic.gov/idasp/main.asp

[12] FFIEC, HMDA Analysis by CRA-NC

and geographical service area. Small banks in rural communities are facing a long-term restructuring in the economy and a correspondingly declining share of deposit assets and lending activities.

By contrast, the consolidation of assets and market share of mega-banks has increased. In 1995, the top 5 banks had 11% deposit share; today, they have nearly 40%.[13] In the first quarter, 56% of mortgage activity was conducted by four lenders.[14] The consolidation of Country Wide and Merrill Lynch into Bank of America, Washington Mutual into JP Morgan Chase, and Wachovia Bank into Wells Fargo has further consolidated the financial services sector, making institutions that are "too big to fail" even bigger. Ironically, these institutions contributed in part to the credit crisis through unethical, irresponsible business and lending practices.

The collapse of North Carolina's homegrown Wachovia Bank through exotic mortgage lending and the troubles of Bank of America in Wall Street deals contrast sharply with the stability small banks have provided. As a rule, small banks and credit unions avoided subprime credit and managed their resources well. These local institutions provide stability and diversification in the financial sector. They offer leadership to local civic engagements and credit to small businesses for job creation, mortgages for homeownership, small farm loans for agriculture, affordable deposit and checking services to consumers. The attached map compares bank branch coverage by the seven

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[13] It Takes More Than a Village: The Decline of the Community Bank, Celent, http://reports.celent.com/PressReleases/200901293/VillageBank.asp

[14] Mortgage Daily, http://www.mortgagedaily.com/PressRelease051109.asp

largest banks compared to all bank branches.[15] Without smaller institutions, many areas would go unserved. By definition these financial institutions are small, but are fundamental economic building blocks to our rural economy. Banking policy and regulatory oversight should support small banks and credit unions as essential to the local ecology of credit and commerce.

3) Financial Reform Will Help Consumers, Lenders and Rural Communities

Consumers in rural and urban areas face similar lending abuses. Rural areas had a higher percentage of subprime high-cost loans than urban areas (17.4% compared to 15.5% in 2004), although the actual volume is significantly lower.[16] Rural areas have a high rate of Refund Anticipation Loans, which correspond to higher levels of poverty and uptake of the federal Earned Income Tax Credit. Payday lenders are prevalent in the rural areas of the 35 states that allow this usurious lending. Consumers need better protections from unsound and unscrupulous lending practices.

Harmed by the lack of financial regulatory oversight of *other* lending institutions, small banks and rural communities will benefit from the needed financial regulatory reform of our system as a whole. Attached to my written testimony are full descriptions of five principles for reform: responsibility, accountability, transparency, equal access and avoidance of conflict of interest. Also included is a discussion of how these six principles apply both to lenders and to the

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[15] Finpro, USA Branches, Bank Branch Ownership 03/16/2009 www.finpronj.com

[16] Carsey Institute, Policy Brief Number 4, Fall 2006. http://www.carseyinstitute.unh.edu/publications/PB_predatorylending.pdf

regulatory system.[17] Based on the principles, the Community Reinvestment Association of North Carolina in particular is supportive of the CRA Modernization Act HB 1492 and President Obama's recommendation for the Financial Product Safety Commission as part of broader reform initiatives. Faced with a rising tide of foreclosures and insufficient loan modification programs, we ask the United States Senate to pass judicial loan modification to manage foreclosure losses for lenders, borrowers and taxpayers.

Although the problems created by the financial crisis and recession are felt by every community and the solutions needed are national in scope, it would be a mistake to assume that urban and rural communities will shake off the recession with equal speed. The data in my testimony indicates that long-term challenges for small banks and rural communities are systemic as well as cyclical. North Carolina's economic recovery of the 2001 recession through technology, commerce and finance masked the lack of recovery in the rural areas. Unless we invest in rebuilding these communities, no banks of any size will thrive.

4) Invest in Rural Communities

My concluding recommendation to Congress is to expand the Neighborhood Stabilization Program (NSP) both in scale of funding and in scope to include rural areas. NSP funds are to help deal with the consequences of the foreclosure crisis in revitalizing abandoned and foreclosed properties and rebuilding distressed communities. $6 billion dollars was

[17] Developed by the, Woodstock Institute, California Reinvestment Coalition, Neighborhood Economic Development Advocacy Project, Community Reinvestment Association of North Carolina.

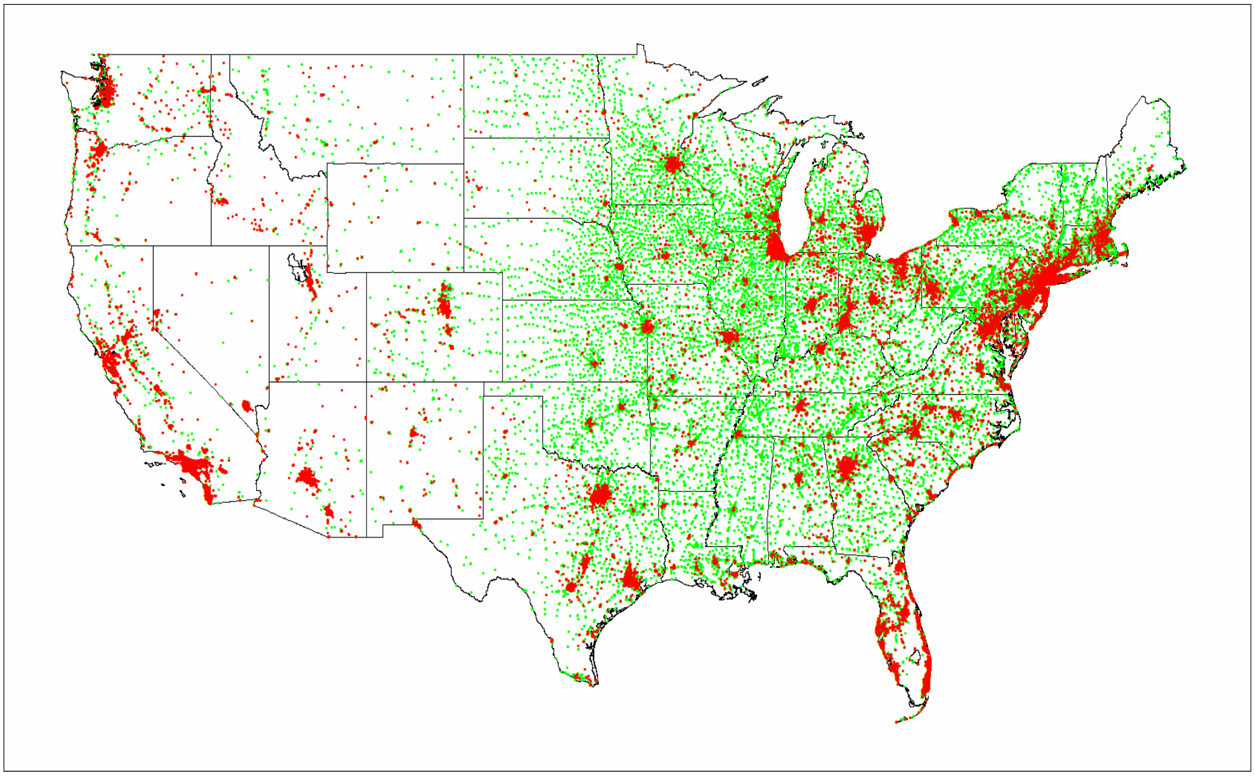
committed to NSP for communities. By comparison, $700 billion was authorized for TARP funding for banks. Please increase the amount of funding for NSP.

NSP rules favor urban areas and exclude rural needs. Nationally 70% of foreclosures are in urban areas and 30% in rural. In North Carolina no rural area met the NSP needs test due to a lack of concentration. Yet in the aggregate, there are more foreclosures in rural counties than urban counties. This pattern is found in 23 other states such as Georgia, Indiana, New Hampshire, New Mexico.[18] Increased funding and rural inclusion will allow banks to move REOs off their balance sheets in partnership with nonprofits and local governments to rehabilitate the housing stock and rebuild their communities. The future for rural communities and banks is brighter if we recognize and act on the need for financial regulatory reform and investment in our communities through initiatives such as the Neighborhood Stabilization Program.

Thank you very much for your attention.

[18] CRA-NC analysis of Table 1: Foreclosure Needs Scores within States by CDBG Jurisdiction -- October 28, 2008, *Source: Analysis by the Local Initiative Support Corporation provided by the Foreclosure Response project*

Branch locations of Top 7 banks (red) overlaid on all banks others (green) as of March 16, 2009



Source: Finpro www.finpro.com

Principles for Financial and Regulatory Reform

1. **Responsibility:** Financial Institutions must offer financial products and services that are appropriate and suitable to the needs and abilities of the consumers. Regulators must regulate financial institutions so as to ensure that they are providing access to responsible and fair credit and loans.

2. **Accountability**: Financial institutions must refrain from, and be held accountable for, offering harmful financial products and services and engaging in practices that harm individuals and communities. Regulators must be held to high standards for their regulation and oversight of financial institutions and accurately report to the public on a regular basis. Laws and regulations must provide strong enforcement mechanisms to ensure accountability and provide meaningful redress to those harmed by irresponsible actions of financial instructions. Regulators must vigorously enforce these laws and rules. Federal regulations must establish a minimum floor for consumer protections that may be exceeded by states and localities.

3. **Transparency**: Financial institutions must fully, fairly, and clearly disclose all costs, terms and risks of financial products and services and avoid or disclose any conflicts of interests with other financial institutions, actors, or regulators. Regulators must demand transparency from regulated institutions and be transparent about their role in regulating financial institutions.

4. **Avoid conflicts of interest**: Financial institutions must avoid all conflicts of interest with other financial players and regulators. Where potential conflicts are allowed, financial institutions must fully, fairly and clearly disclose the conflict to consumers and regulators. Regulators must be objective in their regulation and oversight of financial institutions, act in the public interest (not the interest of the financial institutions they regulate), and prohibit financial institutions from engaging in conflicts of interest. Regulatory policies and financial practices that create an inherent conflict of interest that could harm consumers or the economy must be prohibited or, at a minimum, closely regulated.

5. **Avoid systemic risk**: Financial institutions must not engage in practices that create unreasonable risk to the financial system. Regulators must provide comprehensive and effective regulation and oversight of financial institutions and activities that create systemic risk to individuals, communities and the economy. Policymakers and regulators must implement changes in their oversight policies based on the reality that financial institutions that are "too big to fail" are too big to exist.

6. **Equal access**: Financial institutions must offer appropriate and suitable financial products and services to all persons and communities without regard to race, color, national origin, religion, gender, familial status, disability, or sexual orientation. Regulators must monitor whether all persons and communities have equal access to mainstream financial products and services and hold financial institutions accountable by vigorously enforcing nondiscrimination laws and rules.