

Testimony of Nicole Elam
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Before the House Financial Services Committee

“An Unprecedented Investment for Historic Results: How Federal
Support for MDIs and CDFIs Have Launched a New Era for
Disadvantaged Communities”

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Chairwoman Waters, Ranking Member McHenry and members of the committee, good morning and thank you for this opportunity to testify on how federal support for MDIs and CDFIs have launched a new era for disadvantaged communities. It gives me great hope that one of this committee's first hearings of the new year is aimed at shining a light on this critical issue.

My name is Nicole Elam, and I am President and CEO of the National Bankers Association (NBA). The NBA is the leading trade association for the country's Minority Depository Institutions ("MDIs"). A critical part of our mission is to serve as an advocate for the nation's MDIs on all legislative and regulatory matters concerning and affecting our member institutions as well as the communities they serve.

Many of our member institutions are also Community Development Financial Institutions ("CDFIs") and have become banks of last resort for consumers and businesses who are underserved by traditional banks and financial service providers. Members of our association are on the front lines, trying to reduce the economic hardship faced by minority communities, which are historically the most vulnerable during good times and bad. We believe our banks are best positioned to help our communities recover and overcome many of the systemic issues that have placed them at an economic disadvantage.

The House Financial Services Committee and Chairwoman Waters have been instrumental in the inclusion of several provisions in multiple relief packages adopted over the past year that ensure that MDIs and the small businesses and individuals we serve are not forgotten. The creation and implementation of the Emergency Capital Investment Program and the \$3 billion increase in funding the CDFI Fund can help banks like those within the NBA scale up and provide more access to credit for individuals and small businesses in low- and moderate-income communities. The Bipartisan Infrastructure Bill also provides billions of targeted dollars that can be instrumental in addressing the needs in our communities created by a changing climate and systemic exclusion.

The legislation included as a part of today's hearing aligns with the Committee's goal of preserving and protecting MDIs and CDFIs. The measures, taken together, will provide transformational opportunities for these institutions to not only survive but thrive. We support each measure and very much look forward to working with the Committee to ensure their passage into law.

The NBA applauds the Congress for the adoption and considerations of these important measures and looks forward to continuing to work with you on additional legislation to ensure that our communities, hardest hit by the pandemic and systemic inequity, experience lasting, material changes that will support broad and deep economic growth that will benefit all Americans. We believe additional legislation that will allow MDIs to continue to augment their capital bases, includes our banks and communities in opportunities that will flow from the infrastructure bill, and addresses a regulatory process that can hamper our banks' ability to bring the underserved into the financial mainstream continues to be needed.

MDIs and CDFIs have traditionally served as a source of strength and engines of economic development due to their relative concentration in minority and low-income communities as well as their established relationships created over decades of mission driven service. Our banks provide basic banking services to communities and racial minorities, especially Black and Hispanic, that are more likely to be unbanked or underbanked according to a Federal Reserve Report on the Economic Well-Being of U.S. Households in 2020.

Several studies have shown that minorities, especially Black and Brown Americans, are more likely to have bank accounts and access to fair and reasonably priced mortgage and small business loans if there is an MDI in their neighborhood.¹ It is important to note that an average of 70 percent of minorities do not have a bank branch in their neighborhood. At the same time, MDI branches are in census tracts with a 77 percent minority population. Properly scaled, MDI banks are best positioned to address the problem of the unbanked and underbanked and to provide access to capital for minority communities.

Unfortunately, MDIs' smaller size, especially among African American MDIs, has not allowed them to respond as quickly or with as much scale as the current economic situation in LMI communities demands. MDIs only make up 3 percent of all American banks, and Black-owned MDIs only 0.4 percent. When looking at total bank assets, the disparity is even more stark. As of the second quarter of 2021, Black banks held about \$6 billion dollars in total combined assets, as compared to over \$22 trillion dollars in total assets in the U.S. banking system as a whole. Put another way,

¹ [Broady et al, "An analysis of financial institutions in Black-majority communities: Black borrowers and depositors face considerable challenges in accessing banking services," Brookings (2021); Florant et al, "The case for accelerating financial inclusion in black communities," McKinsey & Company (2020); Barth et al, "Minority-Owned Depository Institutions: A Market Overview," Milken Institute (2019)].

Black-owned banks only control 27 thousandths of one percent of total bank assets in the United States.

Given the important role these institutions play in the communities they serve, we need to do more to preserve and promote them. Our obligation in this regard is not just morally justified but required by federal statute. Passed into law in 1989, Section 308 of the Financial Institutions Reform, Recovery, and Enforcement Act, or FIRREA, requires the Treasury, Federal Reserve, OCC, and FDIC to preserve and promote MDIs in a variety of ways, including preserving the number of MDIs. This statutory obligation should be considered a part of Treasury and the regulators' overall mission to maintain stability and public confidence in the nation's financial system.

The Treasury and bank supervisory agencies have, unfortunately, failed to preserve and promote MDIs. The overall number of MDIs has declined by 33 percent since 2008, and among Black-owned MDIs, the problem is especially pronounced, as Black-owned banks have suffered from many of the same conditions and structural lack of access to capital as the Black community. Of the 4,951 total insured commercial banks in the U.S., only 143 are MDIs, and only 19 of those are controlled by Black people. Prior to the Great Recession of 2008-2009, there were 47 Black-owned commercial banks in 2001 in the United States, a loss of nearly 60 percent.

Tier 1 Capital, or the equity invested in a bank, is the most critical component of the resilience of any bank, and it is what allows banks to grow and scale. MDIs have historically lacked access to capital markets that would allow them to scale. Without sufficient Tier 1 Capital, not only are banks limited in the number of deposits they can take in, but they are also hampered in their ability to withstand loan losses. Without access to capital markets or large pools of high-net-worth investors, many MDIs were forced to exhaust their capital reserves, failing as a result. Those who have been able to participate in relief efforts have been limited in the amount of loans that can be extended, even with federal guarantees or direct support, as they are unable to weather significant loan losses.

ECIP

Access to capital will allow MDIs to not only respond better during times of crisis but allow us to reverse the situations in our communities that lead to worse outcomes during crisis. The ECIP capital is a historic step in the right direction but while 57 MDIs will receive \$3.1 billion from the program, many of our banks were not able to access ECIP due to prior regulatory challenges. This is largely based on

examination standards that do not consider the unique business models many mission-driven banks need to employ to provide basic banking services in markets that would otherwise be ignored by the financial services mainstream. We need regulators to be intentional and modernize the examination process for mission-driven banks that don't do business in wealthy areas. We also need to find additional ways to direct capital and business opportunities to those banks and the communities they serve.

We believe the remaining \$300 million held in reserve for appeals should be prioritized for distribution to these institutions. In addition, we would ask you to consider utilizing some of the remaining \$1.75 billion in the CDFI Fund to provide these institutions with much needed capital that they were unable to get through ECIP. By prioritizing these institutions, we believe that Treasury and the regulators can balance their obligations to protect Treasury funds and at the same time insist that institutions operate in a safe and sound manner. We remain convinced about the need to act now to preserve and promote MDIs and direct much-needed capital into banks that have a strong track record of serving the communities Congress intended to target for the ECIP investment.

Climate and Infrastructure

President Biden and Congressional Democrats have made good on their promise to steer money toward front-line communities as the United States makes historic investments in climate resilience and mitigation. The growing climate crisis has disproportionately hit low-income Black and brown communities in great measure because they are under resourced. Communities of color are disproportionately victimized by environmental hazards and are far more likely to live in areas with heavy pollution. People of color are more likely to die of environmental causes, and more than half of the people who live close to hazardous waste are people of color. Tackling environmental injustice and climate resilience in communities of color is important not just for those directly targeted by racial discrimination but also for society at large, as research shows that racism harms the whole economy in different ways.

People of color are on the front lines of the climate crisis. For decades, the power imbalances have constrained communities of color to respond to the impact of climate change and contribute local knowledge to climate solutions. Building political and economic power, as well as speaking up about the challenges, are critical components of climate resilience. It's time to expand the conversation around

climate justice to ensure that all people, regardless of race and ethnicity, are guaranteed protections from the worst effects of climate change.

Provisions in the recently enacted infrastructure law and a \$29 billion provision included in the proposed Build Back Better bill go a long way in mitigating the impacts of the crisis, but MDIs must be included in the financing opportunities that will arise, giving our banks opportunity, but more importantly allowing us to connect our customers to opportunities to strengthen their businesses, add more jobs, and thereby make their communities more resilient.

While we commend Congress on its leadership to date in responding to the current crisis, we firmly believe much work remains to be done in supporting the MDI sector as we respond to the needs of the communities and small businesses that our member institutions serve that have disproportionately shouldered the burden.

Conclusion

The NBA again applauds the Committee for holding this important hearing and for its ongoing efforts to launch a new era for disadvantaged communities and ensure equity for all businesses and communities in the country. While we commend Congress on its leadership to date in responding to various crisis' (economic, health and environmental), we firmly believe much work remains to be done in supporting the MDI sector as we respond to the credit needs of the communities and small businesses that our member institutions serve that disproportionately shoulder the burden in most instances. In this regard, the NBA and its members banks look forward to working closely with the Committee on workable solutions that ensures LMI communities and minority small businesses do not just simply survive but ultimately thrive. Thank you again for the opportunity to testify. I will be pleased to answer any questions.

The NBA has recommended several potential solutions to Congress and the Administration including the following:

Passage of the Ensuring Diversity in Community Banking Act

The bill is a historic and important first step by Congress to more fully embrace its role in supporting MDIs and creating a regulatory and operating environment that will help to ensure that MDIs continue to play a vital role in meeting the banking and credit needs of communities of color throughout the country. The bill also

provides a mechanism to ensure MDIs can be better capitalized and in turn provide services in LMI communities.

Consumer Credit Enhancements

As you know, the vast majority of U.S. economic activity is ultimately driven by consumer spending, and this activity is severely threatened by protocols to protect the public health and slow the progression of the virus. As a result, wage earners in the service sector across many industries are losing their livelihoods. Many of our banks' customers live from check-to-check. This phenomenon has been particularly acute among women, whose jobs have been disproportionately impacted by COVID-19. These are hard-working, low- to moderate-income wage earners, who typically have low balance (\$1,000 or less), high-transaction checking accounts. While we fully support policy proposals to immediately transmit cash to consumers and offer our banks as vehicles to efficiently and effectively deliver that cash to our customers, we also recommend additional support in the form of a Treasury-backed consumer loan loss pool or other credit enhancement mechanism for MDIs that would allow us to offer our customers small-dollar loans that would function like overdraft protection, allowing them to continue to afford essentials like food, shelter, and medicine, without having to resort to expensive, predatory lenders.

Small Business, Faith-Based, Non-Profit Institution Credit Enhancements

The NBA supports proposals to stabilize and protect small businesses during this crisis, in particular streamlined U.S. government guaranteed loans or lines of credit that will allow small businesses to continue to make payroll. Our member banks are perfectly positioned to get this funding into the most vulnerable small businesses, but we need to cut through the red tape at the Small Business Administration to ensure we can make households available to our bank customers.

In addition, we call your attention to the financial predicament that confronts many churches and other faith-based institutions and non-profits. Many of our banks, especially African American MDIs, have traditionally been the lenders of choice and necessity for many churches in their communities. We know from decades of experience that these churches face bleak financial times, as attendance at worship services becomes limited by public health realities, and donations rapidly decline due to financial hardship among their members. These church customers are not only centers of spiritual solace, but often provide vital community services such as daycare, feeding programs, and the like, so it is imperative that we assist them. As such, we ask that Treasury partner with us to create a loan loss reserve or guarantee

pool for churches, other faith-based institutions and non-profits. This would allow us to work with these customers to restructure their loans in advance, extend working capital lines, or provide other assistance to ensure that they are able to survive the downturn, maintain their staffs, and continue to be beacons for their communities.

MDI Investment Tax Credit

A handful of the nation's largest banks have made direct equity investments in MDIs, and some private equity funds have been assembled with a mission of providing long-term private capital to MDIs. The Association believes that a tax credit for equity investments in MDIs would further encourage private-sector investors to make equity investments in our institutions. Given our institutions' track record of impact investments in the LMI communities we serve, we believe that our institutions' work confers enough of a benefit on LMI communities that an investment tax credit is warranted. We look forward to working with House and Senate sponsors to introduce MDI investment tax credit legislation this year.

Amend the Bank Holding Company Act to allow MDIs and CDFI banks under \$3B to raise additional capital without triggering the BHCA's change-of-control provisions

The Bank Holding Company Act's (BHCA) change-of-control provisions are triggered when an investment exceeds 25 percent of the institution's equity. For smaller institutions, like our member banks, relatively small equity investments implicate the BHCA therefore limiting both the attractiveness of smaller banks for investors and the size of the investments that investors are willing to make in our member banks. We are confident that modifications to these rules would allow our banks to attract more private capital and therefore multiply our impact. The BHCA should be modified to allow for significant infusions of non-dilutive equity investments in our member banks. The Association supports legislative proposals that would exempt community banks under \$3 billion from the 25 percent change-of-control provisions of the BHCA to both attract more significant equity investments and to help protect the minority ownership status of our member banks.

Fully Supporting the Community Development Financial Institutions Fund

We fully support increased appropriations for the CDFI Fund and encourage the establishment of a permanent set aside of 40 percent of CDFI Fund appropriations reserved for award, guarantee, and grant programs for minority lending institutions, and required reporting on such activities. We also support the establishment of a new

Office of Minority Community Development Financial Institutions to administer these funds led by a new Deputy Director of Minority Community Development Financial Institutions.

Federal Deposits in Minority Depository Institutions

Current rules require that federal agency deposits in MDIs must be fully collateralized, which has proven an insurmountable hurdle to implementation of the Minority Deposits Program, as doing so locks-up capital that could be mobilized for lending. We call on Congress to clarify that any such deposits may also be insured, including through reciprocal deposits. Doing so will ensure that any such deposits do not pose any financial risk to federal government, while also allowing the deposits to be mobilized for lending and therefore having a positive multiplier effect in the communities in which these banks operate.

Custodial Deposit Program for Covered Minority Depository Institutions

Establish a new program whereby the Treasury Department will deposit into MDIs funds up to the FDIC insured amount, from Funds under management by the Treasury Department. The program is to be implemented by the Treasury Department, working via custodial banks, which can more easily and efficiently distribute the funds across covered MDIs. This initiative will help mobilize stable deposits into MDIs, which will have a multiplier effect on the communities they serve without creating any new exposures or loss risks for the Treasury Department.

Troubled Asset Relief Program Resolution

TARP effectively expired on October 3, 2010—two full years after its inception. After this date, funds could no longer be extended. In 2014, the U.S. government reported a \$15.3 billion profit as a result of TARP. There are, however, MDIs who have not been able to exit the program. These institutions face significant hurdles in raising Tier 1 capital and were limited in their ability to participate in programs such as the Emergency Capital Investment Program created last year by Congress. The Treasury Department should work expeditiously to release these institutions from the program, so they are able to raise capital and better serve the communities in which they operate.

Establish MDI Offices

We strongly support the establishment of dedicated, staffed offices within the Small Business Administration, Department of Treasury, Department of Agriculture, and Consumer Financial Protection Bureau focused on unique issues related to MDIs. Minority participation in SBA and USDA guaranteed lending, especially among African American entrepreneurs, significantly lags that of businesses from majority communities. At SBA, for example, the head of this office should be primarily focused on ensuring that MDIs can more easily participate in core SBA programs, such as the 7(a) program. At USDA, the office should focus on making lending programs such as the Business & Industry Program, as well as USDA mortgage offerings, more accessible to MDIs. These offices should be direct reports to the highest level within these agencies and should report on their progress to Congress annually.