ICBA
INDEPENDENT COMMUNITY BANKERS of AMERICA

Testimony of

William C. Rosacker
President, United Bankers' Bank

On behalf of the
Independent Community Bankers of America

Before the

Congress of the United States
House of Representatives
Committee on Small Business

Hearing on

"The Role of Credit Cards in Small Business Financing"

April 3, 2008
Washington, D.C.

Chairwoman Velazquez, Ranking Member Chabot, Members of the Committee, my name is Bill Rosacker and I am President of United Bankers' Bank in Bloomington, Minnesota. I am pleased to be here today on behalf of the Independent Community Bankers of America (ICBA).

"Bankers' banks" are unique in the community banking sector, as our customers and shareholders are actually the community banks themselves. The 702 community banks served by United Bankers' Bank need correspondent banking services[1] because they lack the scale to provide these services themselves, yet need to compete with large multinational banks as well as other non-bank financial institutions. Through bankers' banks[2], community banks can obtain these critical services, allowing them to focus their resources on controlling costs, improving management services, and achieving a reasonable margin.

On behalf of ICBA's nearly 5,000 member banks, I want to express our appreciation for the opportunity to testify on the important role credit cards play in supporting America's small businesses and entrepreneurs. Access to credit is critical in today's economy. Small business is one of the key drivers for this country's economy and many entrepreneurs rely on credit cards to get their businesses up and running. In my testimony today, I would like to focus on three main points: first, how community banks are able to help local small businesses run and finance their operations successfully through the use of credit cards; second, how community banks – as small businesses themselves – benefit from the ability to

[1] Bankers' bank correspondent services include: merchant acquirer settlement, commercial payroll services, commercial underwriting, check clearing, international payments, domestic wires, compliance consulting, loan participations and syndications, and a variety of investment, trust and operational services.

[2] Bankers' banks were formed beginning in the early 1980's in reaction to the fact that traditional large commercial banks offering bank to bank correspondent services often competed with their community bank respondents. For example, community banks readily share loan participations with bankers' banks, knowing that the bankers' bank will not, indeed cannot, steal the non-bank customer from the community bank. This relationship of trust may not exist in traditional correspondent relationships.

offer credit card products to consumers and entrepreneurs; and finally, I would like to discuss the legislative and regulatory landscape facing community bankers and their small business customers.

Credit Cards Benefit Small Businesses

As consumers, we all recognize the convenience that credit cards afford us in our daily transactions, since they are accepted at over 24 million locations worldwide[3]. Credit cards are open-ended credit plans, as opposed to installment plans like a mortgage or car payment. As a result, credit cards are the only loan or credit product that, generally, allows the consumer to control how much he will owe, and whether he will pay any finance charge or just be a convenience user.

While many consumers may take this financial flexibility for granted, for small business owners, credit cards can prove to be the difference between getting an organization off the ground or becoming mired in paperwork and regulation. Community banks are incubators for small businesses, and play a vital role in providing the all-important access to capital that entrepreneurs need to succeed. While community banks only account for a small percentage of total domestic banking assets, we provide nearly a third (32.7%) of the total dollar amount of bank business loans under $100,000[4], many in the form of small business credit card products. When a small business has no track record, access to funding through a credit card can be the key resource that helps get the business going.

---

[3] See http://www.electronicpaymentscoalition.org/value/business-economy.html

[4] U.S. Small Business Administration, Office of Advocacy. *Small Business and Micro Business Lending in the United States, for Data Years 2005-2006.* February, 2008.

The 2007 ICBA Community Bank Payments Survey[5] revealed that more than 60% of respondent banks offer small business credit cards, and data from a recent National Small Business Association survey showed that credit cards are a leading source of financing for fledgling businesses[6]. A community banker's ability to offer small business credit cards at competitive rates and terms to entrepreneurs in our local towns is critical to supporting the engine of small business that drives our economy.

The small business owner who chooses to bank with an ICBA member community bank immediately gains the advantage of local decision making. This might not seem important on its face, but when the person actually making the lending decision for a small business is hundreds of miles away and doesn't really know the circumstances of the person sitting in a bank branch asking for a line of credit or the characteristics of the local market, that small businessperson is at a disadvantage. Community bankers know their customers and live and work in their neighborhoods. The community banker often knows the capabilities and needs of the principals of a small business and the local community, and can help them where help is needed. And should the small business find itself in a tough financial situation, both the banker and the owner have much more of a vested interest in making sure the business succeeds.

When a community banker issues a small business credit card, the end user immediately adds the flexibility of a new source of capital that can help them meet their dynamic financial needs while establishing business credit. From an operational perspective, credit cards greatly simplify accounting records and cash flow management. For example, in

---

[5] To view an executive summary, please visit http://www.icba.org/publications/2007paymentssurvey.cfm?ItemNumber=38445

[6] National Small Business Association. *2007 NSBA Survey of Small and Mid-Sized Businesses*. Accessed at http://www.nsba.biz/docs/surveynewfinal.pdf

businesses which require a high volume of daily purchases – whether fuel for a small fleet of trucks, daily orders to vendors for automotive repair parts, or supporting employees on travel – small businesses need a ready source of cash. By using a small business credit card to finance theses expenditures, the businessman can free up what liquid assets he has available to be reinvested into the business to help it grow, rather than tying it up in making trade credit payments. Small business credit cards allow the businessperson to more easily track itemized and categorized expenditures, greatly simplifying the bookkeeping process, and saving time and money. In addition, it has been my experience – and data from a Federal Reserve study on small business finances[7] supports this – the large majority of small business credit cardholders pay their statement balance in full each month, using it as a transaction account. This provides almost the same convenience as does a regular checking account.

If a small business is involved in retail sales, the benefits from card acceptance to its profitability and operation are very significant. For example, they and their customers are assured a consistent payment experience, are protected against many types of fraud, and do not have to keep as much cash on hand or accept checks. In addition, the business receives guaranteed funds in its account immediately while mitigating through the payments chain the credit risk and other compliance burdens, and does not have to extend credit directly. The evidence is clear[8] that consumers are likely to spend more when they shop with credit cards. These factors can greatly help small merchants with sales volume as well as earning repeat customers. After all, increasing customer transactions is arguably the best source of capital available.

[7] Mach, Trace L. & John D. Wolken. "Financial Services Used by Small Businesses: Evidence from the 2003 Survey of Small Business Finances." Federal Reserve Board. October, 2006.
[8] See, for example: http://www.electronicpaymentscoalition.org/value/business-economy.html

Many community banks serve the vital role of linking small retailers into the electronic payment networks by serving as merchant acquiring banks -- i.e. a member of Visa or MasterCard that maintains the merchant relationship and receives the card transactions from the merchant. Just as consumers should always shop around for a financial institution that best meets their banking needs, a merchant who is setting up a credit card acceptance process has the ability to shop around for a level of service, customer support, and range of fees that best fits their business plan. If a merchant opts to sign with a community bank, at the end of the day, it is getting tremendous value because of the benefits of electronic payments and the sophisticated payments infrastructure that a community banker can utilize to complete a transaction quickly and securely. This acceptance is important to the viability of local merchants and the economic base of many communities.

Community Banks as Small Businesses

While community banks are often lumped into the broad category of “bankers,” it is important to keep in mind that community banks are small businesses themselves. As small businesses, we face our own unique set of challenges in a very competitive marketplace. Contrary to popular belief, for many community banks, the consumer and business credit cards we offer are not always sources of tremendous profits. The real value often lies in our basic ability to offer these popular products to consumers and merchants. For many community bankers, the high level of personal service we can provide is what makes card products valuable, not gigantic revenues. Offering community bank-branded cards creates a stronger relationship with the customer, and encourages loyalty for the long run. In other words, many community bankers offer these products as a customer service, not a source of revenue. We offer these credit cards to help our customers.

Across the industry, credit cards are very small-margin products. This is especially true for community banks, which do not issue consumer and corporate credit cards at volumes near those of the larger issuers. Frankly, that is better for our business model and gives us a competitive advantage. For the consumer or small business owner, that means they have more choices: they can choose to do business with the megabank with call centers all over the globe, or they can get that same product with local customer service at competitive and often better rates. Community banks want to provide their small business customers with a range of services, not just reap profit off credit cards, hoping to build a positive relationship that will last. Community banks are conservative lenders who have no desire to trap their local customers in never-ending cycles of debt.

Community Banks and Regulatory Burden

One unique challenge facing both start-up and established community banks on a daily basis is the burden of government regulation. Regulatory and paperwork requirements impose a disproportionate burden on community banks, diminishing their profitability and their ability to attract capital, support the credit needs of their consumer and small business customers, serve their communities and contribute to their local economies. For example, compliance with Sarbanes Oxley Section 404 requirements alone cost my bank thousands of dollars last year.

There are a number of troubling legislative proposals currently before Congress that would increase or create new statutory requirements for credit card issuers by restricting certain practices, limiting our ability to control for risk, or regulating interchange rates. If enacted, these measures would greatly increase the cumulative regulatory burden for community banks that is often disproportionate to the risk they pose. The increased regulatory risks, costs and burdens which may result from the enactment of these proposals could be the tipping point that causes some community banks to discontinue offering credit cards products. The consolidation in the credit card industry has been increasing rapidly and the unintended consequences that might result from any new requirement – be it legislative or regulatory – could involve higher rates and fees to absorb additional regulatory costs, and a diminution in options for consumers and small businesses.

That said, there is also opportunity for Congress to enact measures that would make it easier for small businesses and community banks to grow and succeed. ICBA would like to thank you, Chairwoman Velazquez, for introducing the "Communities First Act," H.R. 1869, which provides much needed regulatory burden and tax relief for community banks, their customers, and their communities.

Conclusion

Even in the best of economic times, small businesses can struggle in their search for capital. Community bankers are well-positioned to meet these needs, be it through traditional loans or highly competitive business credit card offerings. Local businesses are not always better served by a financial institution just because of its tremendous size. The support structure built on local decision-making and long-term relationships unique to the community bank business model is a proven formula to help entrepreneurs succeed.

Credit cards have assumed a prominent role in supporting the financial needs of small businesses across the country, for many of the positive reasons I've described. While traditional lending will remain a strong source of capital, the use of credit cards can allow, for example, a start-up firm to manage its operating capital needs as it works to establish its own credit. More generally, a small business that can diversify the types of credit it utilizes can find it easier to meet the dynamic needs of the business, while at the same time simplifying its bookkeeping.

For community bankers, our ability to issue cards and act as merchant acquirers creates more competition, giving more options to small businesses and merchants. Our business model is based on the ability to attract and keep customers for the long-term, and the only way we can do that is through the highest levels of personal service and competitive product offerings. Small businesses are the backbone of the U.S. economy, and community banks – as small businesses ourselves – are proud of the role we play in their financial success.

As legislative measures impacting the dynamic and vibrant credit card marketplace continue to be addressed, ICBA urges Congress to act with caution – if at all – on any proposal that would increase the regulatory burden on community banks. As I described, community banks often run a credit card business at very narrow margins, often less than 1%, and place great value on the relationship that offering can build. In today's economic environment, every source of capital needs to be an option for a small business, and adding further regulatory costs will make it increasingly difficult for community bankers to remain a viable choice to meet the needs of small businesses in search of credit card products.

Again, on behalf of ICBA and our 5,000 community bank members, thank you for the invitation to testify on this important issue. I look forward to your questions.