

SMALL BANKS, RADICAL VISION¹

Zach Carter[©]

Local banks can change the world, one neighborly investment at a time. William Spademan is a radical banker. In an era when Wall Street executives frequent talk shows to defend lavish bonuses “earned” through reckless speculation, Spademan has been working to create a new kind of bank that would empower communities instead of enriching a powerful few. “If you give any community the ability to create and control money, [it] can decide for itself what to invest in ... [and] what needs to be done,” Spademan says.

After spending decades in the nonprofit world, Spademan found himself reluctantly turning to the realm of banking in an effort to mitigate economic inequality and assuage poverty. “I was kind of repulsed by the whole idea of economics and money,” Spademan says. His new banking model is informed by years of community activism. Spademan founded the Center for Peace and Justice in Brunswick, Maine, in the late 1980s and continues to operate a group that provides financial support to nonprofit organizations.

For six years, he has been working to develop a new type of financial institution he calls a Common Good Bank. Spademan’s bank combines two common financial structures—a credit union and a public bank corporation—directing the community focus of the former and the profit potential of the latter toward the good of society. It’s an ambitious idea that would give communities democratic control over the creation of money and its distribution—restoring public accountability in the financial system, and funding important public projects that have been ignored by Wall Street financiers.

Large banks today tend to be public companies with stockholders spread all over the globe, especially on Wall Street. The short-term interests of these shareholders are rarely attuned to the well-being of the communities where banks operate. West Coast financial behemoth Wells Fargo, for instance, has long been considered one of the strongest banks in the world for investors. But its stock price benefited significantly from the billions of dollars the bank raked in from the subprime mortgage boom. Wells Fargo’s executives sold these toxic loans off to investors immediately after they had been extended to borrowers, so the bank’s books have stayed clean, even though many of the communities it serves have been devastated. In April 2007, the banking giant paid \$6.8 million to settle a class-action lawsuit filed against the company for predatory subprime mortgage lending in California.

It became common for corporate banks to pursue high-risk ventures to turn high profits, despite the fact that it is astonishingly easy to make money in the banking business. Before risky lending was the norm, banking “used to be called the three-six-three business model,” according to Lawrence J. White, a senior bank regulatory official during the late 1980s. “You borrow money at 3 percent, you lend it out at 6 percent, and you’re on the golf course by 3 p.m.,” says White. Shareholders on Wall Street do not need a bank to make long-term profits; they only need it to garner high returns in the short term. When the stock starts to fall, these speculators can simply sell and move on to other stocks. The pressure on bankers to engage in risky behavior is high, and many banks link executive compensation to the company’s stock price, rewarding short-

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term gains and sacrificing long-term stability. We saw what was going on in the industry in the last few years,” says Curtis Hage, CEO of Home Federal Bank, a community bank based in Sioux Falls, South Dakota, that specializes in mortgage lending. “It was just intolerable to us.”

Hage is no radical. In my half-hour conversation with him, he used the word “conservative” approvingly a total of 22 times. He wasn’t referring to theories of international relations; he was talking about straightforward aversion to risk. He never raises his voice. He wears plaid ties. He has never approved a subprime mortgage or a blockbuster merger, and all of his bank’s loans are made either in the Sioux Falls area or to people with whom the bank has previously worked. Hage believes the best way to make money is to be responsive to community needs. “If we make a loan to a borrower who can’t afford it, we’ve done no service to them, and we’ve created no value,” Hage says. Yet Hage still faces pressure from shareholders to make risky loans, expand his operations, or accept a buyout from a bigger bank with no particular commitment or accountability to the Sioux Falls community. Wells Fargo, in fact, owns a stake in Home Federal, and Wells Fargo is far less threatening than some Wall Street hedge funds.

Speculators Keep Out

Spademan thinks he has found the solution to Hage’s dilemma. He hopes to lock speculators out of the Common Good Bank business by writing founding documents that require new shareholders to be depositors, and by adopting by-laws that allow each shareholder one vote on how to organize the company’s operations. Most corporations grant one vote to each share of stock, a strategy that gives wealthy shareholders more power and allows speculators to rewrite the company’s business practices if they purchase a large-enough stake. Here Spademan borrows from a business model that has thrived in the United States since the Great Depression: the credit union, a democratically governed financial co-op that is owned by its customers.

Michael Sills is the CEO of Evansville Federal Credit Union in Evansville, Indiana, a small collective with about 7,500 members, all with an interest in improving life in Evansville. “One of our employees here was at church, and she talked to Ruth, who is a social worker here in town, about establishing a house for women who have been through alcohol or drug rehab, a kind of transitional house,” Sills said. “So we enlisted our customers and our members to help donate money and do bake sales and car washes—those kinds of things—to generate the money. I think there was a bowl-a-thon, too.” Evansville’s substance-abuse-recovery home is the kind of project that might not get funding from ordinary financial institutions.

Some credit unions also offer unique, socially responsible loans, like Santa Barbara County Federal Credit Union in California, which specializes in lending for solar energy panels. Interest rates on credit union loans are typically lower than those on bank loans, while credit unions usually pay their depositors more than banks. Credit unions almost entirely missed the subprime explosion. But there are significant costs to the credit union charter. Credit unions are barred from turning a profit (aside from a small amount to cushion against losses), so Evansville FCU funds its charity work with bake sales rather than earnings. Credit unions cannot sell stock. If they want to grow, they have to rely on the modest earnings cushion they’ve retained over time to fund any expansion, which makes for a very slow process.

Spademan’s Common Good Banks could get around this problem. They would be stock-based corporations, but with strict rules that require them to be governed like a credit union. What’s more, Common Good Banks could turn a profit, but they would have to spend it on charitable contributions. Owners of the bank would vote on how to distribute profits to various charities, nominated by the owners themselves.

“Each of the depositors is given 100 virtual pennies, and they have to distribute them among the various organizations,” Spademan says. “If you like one organization a lot you could give 60 virtual pennies to that one, and only five to another. When all the voting is done, you add up all the pennies that all the organizations have been given, and those are the proportions in which the profits will be given out.”

This strategy could dramatically expand a community bank’s local role and influence. It would also give communities control of how money is created and invested, even allowing the bank to fund projects that have no hope of generating a financial return. “Our money system is so broken that we don’t even see that it’s silly that there are people who are desperate for work while there are jobs that need to be done,” Spademan says. “Things aren’t happening just because we don’t have an accounting system that can deal with it. That’s crazy.”

Spademan faces some significant challenges getting his program off the ground. The recent wave of bank failures has put the federal deposit insurance fund under pressure, and the FDIC has been approving fewer new bank applications. Since Common Good Bank investors will have no hope of earning a significant financial return, Spademan will have a smaller pool of potential start-up capital than ordinary banks and will need committed organizers to assemble depositors. Fortunately, Spademan appears to be well on his way. Between early March and mid-April, Spademan hired 23 division organizers, each in a different community, to gather the bank’s financing. If he can marshal the capital, Spademan could very well do something radical with the financial system.

Despite all the pressure on Home Federal’s Hage, the survival of his bank proves that a stock-based company can maintain fair lending practices and turn a profit, while the existence of more than 7,800 credit unions in the U.S. proves that democratic finance can work.