



Submitted via FDIC.gov

May 15, 2021

Mr. John Henrie
Regional Director
Federal Deposit Insurance Corporation
Atlanta Regional Office
10 10th Street, NE, Suite 800
Atlanta, GA 30309-3849

RE: CRA MERGER APPLICATION -- HERITAGE SOUTHEAST BANK (#20210414)

Dear Mr. Henrie,

The Independent Community Bankers of America (ICBA)¹ and the Community Bankers Association of Georgia (CBA)² appreciate this opportunity to comment on Heritage Southeast Bank's Community Reinvestment Act (CRA) merger application, submitted pursuant to its proposed acquisition by Florida's VyStar Credit Union. ICBA and CBA strongly oppose this merger because it will result in a larger, less accountable financial institution that will be exempt from the Community Reinvestment Act (CRA).

We believe this acquisition will lead to a substantial decrease in the CRA-qualifying loans and investments that benefit low- and moderate-income (LMI) customers in Heritage Southeast's assessment areas. Additionally, we believe that this merger will result in branch consolidation and limited access to financial services for LMI customers. Therefore, we urge your office, in the strongest possible terms, to reject this application as contrary to the convenience and needs of the bank's community.

¹ The Independent Community Bankers of America creates and promotes an environment where community banks flourish. ICBA is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education, and high-quality products and services. With nearly 50,000 locations nationwide, community banks constitute 99 percent of all banks, employ more than 700,000 Americans and are the only physical banking presence in one in three U.S. counties.

Holding more than \$5 trillion in assets, over \$4.4 trillion in deposits, and more than \$3.4 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at www.icba.org.

² The Community Bankers Association of Georgia is committed to enhancing community banking in Georgia. With approximately 150 member banks and 200 vendor partners, CBA is the only organization in Georgia that represents the interests of community banks exclusively.

Historical Background

The CRA was enacted in 1977 to ensure that each FDIC-insured depository institution serves the convenience and needs of its entire community, including LMI neighborhoods, consistent with [the bank’s] safe and sound operation.³ For community banks, reinvesting in their communities is more than a mere regulatory obligation, it is the core of their business model. Nevertheless, CRA provides a regulatory safeguard to ensure banks are implementing their community commitment by providing for regular evaluations of their lending, investment, and provision of services to LMI customers and census tracts.

By contrast, credit unions are not subject to the CRA.⁴ According to Congress, the original purpose of credit unions was to meet the “credit needs of individuals of modest means.”⁵ Because of this limited, charitable purpose, credit unions were granted several legal regulatory advantages, including an exemption from Federal income taxes and an exemption from the requirements of CRA.

Over time, however, with the enablement of their regulatory agency, the National Credit Union Administration (NCUA), credit unions have drifted away from their mission of serving those of modest means. This is especially true of large credit unions like VyStar, that have stretched the limits of the common bond requirement of credit unions. These acquisitive institutions have become functionally indistinguishable from regional banks, but subject to less oversight. This mission drift is evident in their trade press – which attacks any attempt to even define how the term “people of modest means” should be defined.⁶

VyStar’s Record of Community Bank Branch Closures

Heritage Southeast is VyStar’s second community bank acquisition in as many years. In August of 2019, VyStar acquired Citizen’s State Bank in Perry, Florida. It is clear VyStar has an extensive expansion plan. In July of 2019 Vysar requested, and was approved by Florida and Georgia state banking regulators, to expand its field of membership into four counties in southeast Georgia. Less than a month later in August of 2019 VyStar acquired Citizen’s State Bank in Perry, Florida. Shortly thereafter, in 2018, VyStar increased its field of membership to include all 49 counties in the northern and central parts of Florida.

In our view, these actions paint a portrait of VyStar as a credit union that prioritizes aggressive growth rather than serving its existing customers of modest means. This is further evidenced by the fact that VyStar moved, sold, or closed Citizens State Bank branches after its acquisition –

³ 12 U.S.C. 2903(a)(1).

⁴ As VyStar’s CEO, Brian Wolfberg said in an interview, that while VyStar intends to focus on providing favorable interest rates, lower fees and good service while also focusing on charitable, civic and nonprofit organizations, that “[t]his is distinct from banks’ mandate to offer community support under the Community Reinvestment Act.” David Bauman, *Credit Union Times Magazine*, “VyStar CU President Accuses ICBA of 'Mischaracterizing' Bank Purchase” (Apr. 8, 2021).

⁵ Pub. L. 105–219, §2, Aug. 7, 1998, 112 Stat. 913.

⁶ Staff Writer, *Credit Union Times Magazine*, “Define Modest Means? CUNA, Don't Do It!” (Aug. 22, 2006), available at: [Define Modest Means? CUNA, Don't Do It! | Credit Union Times \(cutimes.com\)](https://www.cutimes.com/define-modest-means-cuna-dont-do-it/).

despite its claim that it expected to “to keep the \$280 million-asset Citizens State’s four branches and retain all of its employees.”⁷ At the time of its acquisition, Citizens State Bank had branches at the following four locations:

- 2000 South Byron Butler Parkway, Perry 32348 – Head Office
- 4620 Northwest 39th Avenue, Gainesville 32606
- 6450 S.W. Archer Road, Gainesville 32608
- 913 First Avenue, Southeast, Steinhatchee 32359⁸

According to VyStar’s website, at the time of this writing, VyStar maintains a branch at only two of the former Citizen’s State Bank locations: 913 First Avenue, Southeast, Steinhatchee 32359 and 2000 South Byron Butler Parkway, Perry 32348.⁹ **That means that, despite its promises to the contrary, VyStar has either closed, moved, sold or consolidated half of the branches acquired from the Citizen’s State Bank transaction. Distressingly, the now closed 6450 S.W. Archer Road, Gainesville 32608 branch was located in a moderate-income census tract.**

Heritage Southeast Bank is the largest bank ever acquired by a credit union in a purchase and assumption transaction anywhere in the United States. At \$1.6 billion in assets and with 22 branches, its physical footprint in the community is 5.5 times larger than Citizen’s State Bank’s. Given VyStar’s history of acquiring community banks and subsequently closing, relocating, or consolidating branches, we believe that allowing this deal to close will have a significant adverse impact on Heritage Southeast’s LMI customers who depend on access to a physical branch. In particular, we note that Heritage Southeast’s branches in Jacksonville, Florida and St. Mary’s, Georgia could be particularly prone to being closed or consolidated with an existing branch given VyStar’s significant branch presence in the Jacksonville market.

Heritage Southeast’s Community Reinvestment Performance

According to FDIC records, Heritage Southeast Bank and its predecessor institution Heritage Bank have received a Satisfactory CRA rating since at least 2000. The bank has not received any CRA-related complaints since its conversion from a thrift institution to a state, non-member, chartered bank, effective September 1, 1998. Nor have any complaints or exams revealed any violations of the substantive provisions of anti-discriminatory laws and regulations. Allowing the transaction with VyStar to conclude will limit this transparency into the institution’s performance because VyStar is not subject to regular, public exams of its Community Reinvestment Act performance.

Beyond this record of compliance with antidiscrimination laws, Heritage Southeast is a significant lender to small businesses in southern and central Georgia. **According to its most**

⁷ Palash Ghosh, *American Banker*, “VyStar is latest credit union to line up bank acquisition” (Jan. 15, 2019), available at: <https://www.americanbanker.com/creditunions/news/vystar-is-latest-credit-union-to-buy-a-bank>.

⁸ Bank Branch Locator, “Citizens State Bank Locations in Florida,” available at: <https://www.bankbranchlocator.com/citizens-state-bank-fl-locations-in-florida.html>.

⁹ VyStar Credit Union, “Locations,” available at: <https://vystarcu.org/home/locator/atmbranches>.

recent CRA Performance Evaluation, Heritage Southeast made 228 small business loans totaling \$55,035,000 between January 1, 2018 and December 31, 2018.¹⁰ Over \$19,000,000 of these loans were made to businesses inside of Heritage Southeast’s CRA assessment areas.

Much of this important support for local small businesses could be lost following an acquisition by VyStar. Community banks are the leaders in small business lending. According to the Federal Reserve’s Small Business Credit Survey, small business applicants sought a loan at a small bank 44 percent of the time vs. nine percent of the time at a credit union.¹¹ As importantly, 79 percent of independent businesses that used community banks reported they were satisfied with their overall experience, compared with 67 percent for large banks and just 49 percent for online lenders.¹² Community banks were the highest of any category of institution measured by the study.

This commitment to small business lending by community banks was showcased by the Paycheck Protection Program (PPP)¹³, where credit unions had a demonstrably worse record of providing pandemic relief loans. Community banks (defined as banks and savings and loan associations of less than \$10 billion in assets) made 1,565,493 PPP loans totaling over \$95.23 billion. By contrast, credit unions of less than \$10 billion in assets made only 130,743 PPP loans, worth \$4.67 billion. Large credit unions of over \$10 billion in assets, a category to which VyStar would belong if this transaction is consummated, made just 13,580 PPP loans, totaling \$412 million.¹⁴ These striking statistics show that, when the chips were down in the pandemic, small businesses could depend on community banks – not credit unions.

In addition to small business lending and lending to LMI borrowers, according to Heritage Southeast’s most recent CRA exam, the bank “originated 42 community development loans totaling \$25.5 million since the prior evaluation, which represents 6.0 percent of average total loans and 4.6 percent of average total assets, as of September 30, 2019.”^{15 16}

On the investment portion of its most recent CRA exam, Heritage Southeast “made 15 donations totaling \$131,666, which was an increase from the \$39,178 of the prior evaluation.”¹⁷ These donations had the primary purpose of supporting affordable housing and community services for

¹⁰ Federal Deposit Insurance Corporation Division of Depositor and Consumer Protection Atlanta Regional Office, “Community Reinvestment Act Performance Evaluation: Heritage Southeast Bank, Certificate Number: 30846” (Dec. 16, 2019), available at: [ISB Single Rated Area \(fdic.gov\)](https://www.fdic.gov/).

¹¹ Federal Reserve Banks, Report on Employer Firms, “Small Business Credit Survey” at p. 22 (2019), available at: <https://www.fedsmallbusiness.org/medialibrary/fedsmallbusiness/files/2019/sbcs-employer-firms-report.pdf>.

¹² *Id.* at 31.

¹³ PPP loans are fully exempt from the credit union member business lending cap because they are exempt from the definition of a commercial loan. *See* 12 C.F.R. 723.2, *Commercial loan*.

¹⁴ U.S. Small Business Administration, “Paycheck Protection Program (PPP) Report Approvals through 04/18/2021” (Apr. 18, 2021), available at: https://www.sba.gov/sites/default/files/2021-04/PPP_Report_Public_210418-508.pdf.

¹⁵ *Supra* note 10 at 13.

¹⁶ To illustrate how these loans helped Georgia businesses, the bank’s performance evaluation notes that these loans included renewing “a loan totaling \$464,500 to purchase a larger building for a hair salon, located in a low-income geography, that has grown from 2 to 12 stylists” and originating “a loan totaling \$646,900 to a start-up business that created 14 low- and moderate-income jobs.”

¹⁷ *Supra* note 10 at 13.

LMI people in the bank's assessment areas. Through its Heritage Foundation the bank made a \$35,000 donation to Southern Crescent Habitat for Humanity to provide grants to qualified individuals in Clayton County, Georgia. **Because VyStar would not be subject to the Community Development Test of the CRA, there would be no way to evaluate whether the combined institution continues Heritage Southeast's commitment to making community development loans and grants in its communities.**

As a final note, according to the bank's September 30, 2020 call report, Heritage Southeast had \$1.531 billion in assets.¹⁸ This number would place the bank above the FDIC's large bank threshold of \$1.322 billion for the first time in the bank's history. Becoming a large bank would subject Heritage Southeast to the Services Test of the current CRA exam. By being acquired by VyStar, and therefore exempt from CRA, Heritage Southeast would avoid being evaluated under the large bank test. This would decrease transparency into how the institution meets the credit needs of its assessment areas including through analysis of the availability and effectiveness of its systems for delivering retail banking services and the extent and innovativeness of its community development services, as evaluated by the Services Test.¹⁹

Consistency with Safe and Sound Banking Practices

Because of the structural characteristics of the institution types, credit union acquisitions of banks ~~are~~ raise unique safety and soundness concerns. Because credit unions cannot issue stock to finance a transaction, they must fund bank acquisitions with retained earnings or debt. Using debt to finance an acquisition reduces the acquiring credit union's capital ratio and results in an institution that is less able to weather economic downturns or exogenous shocks.

Furthermore, the fact that credit unions are tax exempt means that the premiums they are willing to pay for an acquisition target are substantially higher than the premiums that make financial sense for a competing bank acquirer. When a credit union acquires a bank, the bank's earnings are transformed from being taxable to being tax exempt. Therefore, a credit union receives an automatic increase to the profitability of the acquisition target. Considering this advantage, credit unions are always able to pay a higher multiple for acquired banks than bank competitors – all while simultaneously eroding the federal tax base.

This phenomenon is evident in the pending VyStar-Heritage Southeast deal. **VyStar paid \$195.7 million in cash for Heritage Southeast, 184% of the bank's tangible book value.** News of the deal caused Heritage Southeast's stock (ticker symbol: HSBI) price to jump from \$15.00 on March 31st to \$25.35 on April 1st, a single day increase of 69%. The enormous premium over the bank's tangible book value and the huge increase in its stock price both reflect the fact that credit union-bank deals benefit from regulatory and tax arbitrage more than traditional merger economics of synergies and economies of scale.

¹⁸ Federal Financial Institutions Examination Council, FFIEC 051: Heritage Southeast Bank (Sep. 30, 2020), available at:

<https://cdr.ffiec.gov/public/ViewPDFFacsimile.aspx?subID=1589110&FIName=HERITAGE%20SOUTHEAST%20BANK&CertNum=30846&PDF508=false>.

¹⁹ See 12 C.F.R. 345.24.

According to a recent article in *American Banker*, “Leonard Moreland, Heritage Southeast’s CEO, said the bank was not necessarily looking for a merger partner, but Vystar’s offer was too good to pass up. ‘The pricing side of it was hard to argue with.’”²⁰ This is a very revealing comment because it shows that Heritage Southeast was not actively looking to merge but was instead persuaded to sell out only because it received an offer far in excess of the bank’s market value to any other taxpaying acquirer. While this is undoubtedly a boon for Heritage Southeast’s shareholders, it is not necessarily in the best interests of the communities that the bank serves.

Nor is such a deal necessarily in the best interest of the future stability of VyStar. According to the National Credit Union Administration’s (NCUA) 2015 Risk Based Capital Rule,²¹ goodwill is deducted from the numerator of the Agency’s risk-based capital ratio – marking a change from the Agency’s treatment of goodwill for deals consummated prior to 2016.²² A deal with a premium as outsized as 184% of tangible book value will result in the generation of significant goodwill, thereby lowering the risk-based capital ratio of VyStar during a time of continued economic uncertainty.

Conclusion

Once again, ICBA and CBA appreciate this opportunity to provide feedback to the FDIC on Heritage Southeast Bank’s Community Reinvestment Act (CRA) merger application, submitted pursuant to its proposed acquisition by Florida’s VyStar Credit Union.

The unprecedented size and ambitiousness of this merger will open the floodgates of credit unions acquiring community banks – leading to more tax exempt, less regulated financial institutions. This trend is not in the interest of small businesses or LMI customers, including those served by Heritage Southeast Bank. For this reason, we urge the FDIC to reject Heritage Southeast’s CRA merger application in the strongest terms.

Please feel free to contact us at Michael.Marshall@icba.org or John@cbaofga.com if you have any questions about the positions stated in this letter.

Sincerely,

Mickey Marshall
Director, Regulatory Legal Affairs
Independent Community Bankers of America

²⁰ Ken McCarthy, *Credit Union Journal, American Banker*, “VyStar shrugs off community bank concerns, stays focused on growth” (Apr. 12, 2021), available at: <https://www.americanbanker.com/creditunions/news/vystar-shrugs-off-community-bank-concerns-stays-focused-on-growth>.

²¹ 85 Fed. Reg. 66626.

²² See NCUA, “Report to the House Financial Services Committee on the Final Risk-Based Capital Rule” (Nov. 2015), available at: <https://www.ncua.gov/files/publications/regulation-supervision/final-risk-based-capital-rule-report.pdf>.

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