INDEPENDENT COMMUNITY BANKERS of AMERICA®

September 26, 2022

ICBA Talking Points on Credit Unions

HEADLINES

- Credit unions are violating the limits established by Congress to justify their tax exemption.

- Credit union acquisitions of community banks diminish tax revenues, solidify the publicly subsidized sector of the financial services industry, and increase the portion of the industry exempt from Community Reinvestment Act oversight.

- Congress should hold hearings to investigate the credit union tax exemption and impose an "exit fee" on their bank acquisitions to capture the tax revenue lost due to these transactions.

FACTS WITH NUMBERS

- Community banks led the financial response to the coronavirus pandemic, accounting for roughly 60 percent of Paycheck Protection Program loans and saving an estimated 49 million jobs.

- But the credit union tax exemption is contributing to the growing phenomenon of tax-subsidized credit unions buying taxpaying community banks.

- Further, the tax exemption allows credit unions to make inflated purchase offers well above the book value of acquired community banks.

- The credit union tax exemption dates to 1934, when Congress chartered credit unions as not-for-profit institutions to serve people of modest means with a "common bond" of occupation or association. But this nearly 100-year-old law hasn't been updated since it was passed.

- While it took credit unions 106 years to hit the $1 trillion asset threshold in 2015, they needed just six years to double in size and pass $2 trillion in assets in 2021.

a. Taxpayer impact

  - Credit union purchases of community banks—which peaked in 2019 and are again on the rise—is an alarming trend because credit unions don't pay taxes, unlike their tax-paying community bank targets.

  - While community banks contributed over $12 billion in tax revenue in 2020, the credit union industry enjoys a tax exemption worth at least $2 billion per year and rising.

- The federal tax exemption for more than $1.8 trillion in credit union assets continues to grow with each credit union-community bank acquisition because bank assets become tax exempt when bought by a credit union.

- While credit unions paid nothing in federal taxes last year, nurses, teachers, and cashiers had a total tax liability of more than $56.6 billion, $19.8 billion, and $11.8 billion, respectively.

b. Consumer impact

- These deals not only hamper tax revenue, but also restrict access to financial services.

- For instance, they increase the portion of the financial services industry exempt from the Community Reinvestment Act (CRA), which assesses whether financial institutions are meeting the needs of low- and moderate-income communities.

- While the CRA applies to community banks and virtually every other depository institution, credit unions are fully exempt.

- Further, the credit union industry's regulator—the National Credit Union Administration—continues expanding the powers of the industry it is charged with regulating without adequately examining compliance with consumer protection directives.

c. Underserved community impact

- Credit unions were established a century ago to serve people of modest means with a common bond, but the data show they are falling short of that mission.

- Today, less than 10 percent of credit unions are physically located in an economically distressed community and only 13 percent are in low- and moderate-income areas, according to ICBA research.

- Community banks outnumber credit unions by a 2-1 margin in low-income or distressed communities and are more likely to lend in census tracts with above-average poverty and unemployment, according to Home Mortgage Disclosure Act data.

d. Small-business impact

- Further, these deals risk displacing a critical provider of capital to small businesses.

- The nation's community banks account for roughly 60% of U.S. small-business loans and made 60% of federal Paycheck Protection Program loans to save an estimated 49 million jobs during the pandemic — outpacing credit union PPP lending by a factor of 16 to 1.

e. Consolidation impact

- Credit union-community bank combinations further financial services consolidation, reducing the availability of local financial institutions in communities most in need of them.

- And community banks aren't the only local institutions affected by this trend. Traditional credit unions themselves are declining as larger credit unions expand and account for more of the tax burden.
  - Credit unions in every asset category under $500 million lost both members and loans in 2020.
  - Meanwhile, credit unions over $1 billion comprise 8 percent of the industry but 74 percent of its tax exemption.
  - Representatives of smaller, community-based credit unions are beginning to question the tax exemption for the largest and most growth-oriented of these financial firms.

f. Transparency concerns

- Finally, these acquisitions lack transparency, with credit union executives using their members' savings to buy out bank owners in largely private deals.

- In fact, credit unions can leverage the savings from their tax exemption to make inflated offers for healthy institutions.

g. States leading momentum for policy review

- Policymakers in several states have begun responding to the negative impact of these deals:
  - Mississippi enacted a law requiring acquired bank assets to remain under the control of an FDIC-insured institution.
  - The Nebraska banking department separately ruled that only chartered financial institutions organized to do business in the state may participate in a cross-industry acquisition or merger — rejecting an attempted bank acquisition by an out-of-state credit union.
  - And Colorado state lawmakers voted down legislation to allow credit unions to hold municipal deposits and other public funds.

STORIES

- While many credit unions are virtually indistinguishable from taxpaying banks, the credit union industry's federal regulator—the National Credit Union Administration—continues finding new ways to increase the powers of the industry it is charged with regulating, calling into further question the justification for the tax exemption.

- The NCUA has allowed outside investors to profit from the credit union tax subsidy, repeatedly delayed capital requirements more than a decade after the financial crisis, and allowed credit unions to include wealthy suburbs of metropolitan areas in their fields of membership while leaving out their urban cores.

- Most recently, the NCUA has proposed deregulating for-profit companies owned by credit unions even though these companies are not supervised by the agency and are exempt from Federal Credit Union Act consumer protections.

- The NCUA has also repeatedly delayed implementing risk-based capital rules for large credit unions. In his dissent before taking over as NCUA chairman, board member Todd Harper noted that risk-based capital rules went into effect for banks years ago. "We are forgetting the past repeatedly, just like characters in Groundhog Day," he said.

- Former NCUA Chairman and board member Mark McWatters has also admitted that the industry's fund insuring credit union deposits would be at risk without taxpayer subsidies. This admission underscores the need for Congress to review this sizable tax exemption.

RECOMMENDATIONS

- While states have started to respond, this is a matter of national importance, and taxpayers are entitled to know more about how the subsidy they fund is being used to underwrite financial services consolidation.

- With the number of credit union-bank acquisitions likely to continue increasing as the economy reopens, ICBA is advocating an "exit fee" on these acquisitions to capture the value of the tax revenue that is lost once the business activity of the acquired bank becomes tax-exempt.

- Further, Congress should also hold hearings to investigate the impact of this trend and the role of the credit union tax exemption and lax NCUA oversight.

- Lawmakers can get a firmer grasp on what has contributed to the growing acquisition trend by requesting a Government Accountability Office study on the evolution of the credit union industry and NCUA supervision.

- There is precedent should Congress reconsider the credit union tax exemption. In 1951, Congress revoked the tax exemption for building and loan associations, cooperative banks, and mutual savings banks, finding that these institutions operated much like commercial banks and should be taxed accordingly.

- As policymakers work to support consumers, small businesses, and the taxpaying community banks that sustain local communities, their first stop should be reexamining the credit union tax exemption and NCUA's lax oversight.

ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

ADDITIONAL INFORMATION

How ICBA Is Combatting Credit Union Overreach: Wake Up Campaign

- ICBA continues calling on policymakers and the public to "Wake Up" to the risky practices, costly tax subsidies, and irresponsibly lax oversight of the nation's credit unions.
- ICBA polling conducted by Morning Consult found 61% of U.S. adults said it is important that their financial institution does not receive taxpayer subsidies—raising questions about public support for credit unions' tax and regulatory exemptions.
- Credit union acquisitions of community banks was a core plank of ICBA grassroots meetings with congressional offices during the 2022 ICBA Capital Summit in Washington.
- ICBA is strongly opposing House legislation to expand credit unions' fields of membership and commercial lending powers without requiring proper documentation or oversight.
- ICBA is supporting Sen. Jon Ossoff's (D-Ga.) efforts to develop legislation to authorize the NCUA to examine credit union third-party service providers for cyber risk and to require credit unions to report cyber incidents to the NCUA, as advocated by ICBA.
- ICBA has called on the Justice Department to revise its policies on bank mergers to better address nonbank competitors, including credit unions.
- ICBA Chairman Brad Bolton wrote in an American Banker op-ed that while credit union advocates support credit unions leveraging their tax exemption to acquire community banks, these subsidized transactions harm local communities.
- Meanwhile, ICBA has been running a digital campaign featuring a recently released ICBA video urging Americans to advocate congressional hearings on how credit unions are taxed and regulated.
- Community bankers can continue urging Congress to hold hearings on the credit union tax exemption using a customizable message to lawmakers on ICBA's Wake Up page and its Wake Up Messaging Playbook.