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February 25, 2014

The Honorable Dave Camp
Chairman
Committee on Ways & Means
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Sander Levin
Ranking Member
Committee on Ways & Means
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman Camp and Ranking Member Levin:

On behalf of the nearly 7,000 community banks represented by ICBA, which are organized in a variety of forms, including mutuals and C and S corporations, I would like to express our strong support for comprehensive tax reform and to thank you for your dedicated and persistent efforts in this regard. Done correctly, comprehensive tax reform could help strengthen the economy and provide relief to the millions of individuals and small businesses served by community banks. We appreciate how very challenging it is to reform the tax code, and we are committed to continuing to work with you as the process unfolds. I would also like to use this opportunity to reiterate the principles we believe are necessary for any tax system.

Business Interest Deduction. The vast majority of small businesses do not have access to equity markets and rely on debt financing. Any change in the deductibility of interest on business debt would be extremely disruptive to these businesses which play a disproportionate role in job creation. Tax reform should preserve the ability of businesses to deduct interest.

Preservation of the Subchapter S Business Model. More than 2,000 community banks, approximately one third of all banks, are organized under Subchapter S of the tax code. Any reforms to the tax code should not only preserve this model but help strengthen it as well. Corporate and individual tax reform should be undertaken together, and the top individual margin rate should be held in approximate parity with the top corporate rate so that the Subchapter S model is not disadvantaged relative to the C corporation model. Further, tax reform should be used to enhance the viability of the Subchapter S model by: raising the shareholder limit to 200, allowing Subchapter S banks to issue preferred shares, and allowing Subchapter S shares to be held in an IRA. These reforms would allow Subchapter S banks to meet regulators' persistent demands for higher capital levels.

Opposition to New Commercial Bank Taxes. ICBA has consistently opposed new taxes or fees specifically targeting the commercial banking sector or their customers. In our view, tax policy should be neutral and not target a specific industry sector. Sector-specific taxes distort the market and generate counterproductive outcomes. Even when such taxes exempt community banks, they set a troubling precedent: Once the tax code is opened up to target a specific sector it is difficult to contain the size, scope, and broader application of the tax.

Promote Savings and Investment. Tax reform should work to increase private savings and investment. The current tax code discourages or even punishes savings and investment with double or even triple taxation. A superior tax system would promote savings not punish it.

Credit Union and Farm Credit System Tax Exemptions. Tax reform is a prime opportunity for review of the controversial tax exemption enjoyed by the credit unions and the Farm Credit System (FCS). Credit unions are becoming harder and harder to distinguish from the taxpaying banks with which they directly compete. Their efforts to raise the statutory cap on credit union commercial lending, if successful, would further blur that distinction. Most importantly, the credit union tax exemption comes at a significant cost to taxpayers. The most comprehensive estimate to date, done by the independent Tax Foundation, valued the tax subsidy at \$31.3 billion over 10 years¹. The Debt Reduction Task Force of the Bipartisan Policy Center, chaired by former Senator Pete Domenici and former OMB Director Alice Rivlin, considered eliminating the tax exemption for credit unions. The Joint Committee on Taxation, the Office of Management and Budget, and the Congressional Budget Office (CBO) have all identified the credit union subsidy as a growing tax expenditure.

The FCS has continued to grow rapidly in recent years and now has approximately \$250 billion in total assets. With over \$4.3 billion in net profits in 2012, the FCS tax burden would equate to well over \$1 billion annually in tax revenue and \$10 to \$15 billion in potential new revenue over a 10 year budget cycle, a tax expenditure that will only grow larger in the future. In addition, many of the associations of the FCS are large, multi-billion dollar entities that compete against much smaller community banks. Their GSE status allows them to access funds from Wall Street at a subsidized rate only slightly above the Treasury's cost of borrowing. There is no policy rationale for continuing tax exemptions for multi-billion dollar entities that compete with community banks for the same customers while offering the same or similar products and services.

Thank you again for your commitment to sensible, growth-oriented tax reform. We look forward to reviewing your forthcoming discussion draft.

Sincerely,

/s/

Camden R. Fine
President & CEO

CC: Members of the House Ways & Means Committee

¹ "Competitive Advantage: A Study of the Federal Tax Exemption for Credit Unions." Tax Foundation. February 28, 2005.
URL: <http://taxfoundation.org/article/competitive-advantage-study-federal-tax-exemption-credit-unions>