
From Church Basement to Conglomerate:

The Need For A Fresh Look at the Largest Credit Unions

Credit Unions' Tax Exemption Was An Effort To Provide Financial Services To Underbanked Communities

Inception

- Credit unions were originally exempted from federal corporate income taxes to encourage a specific mission:
 - To serve consumers of modest means, united by a common bond, with basic services, such as deposit accounts and small loans

Maturity

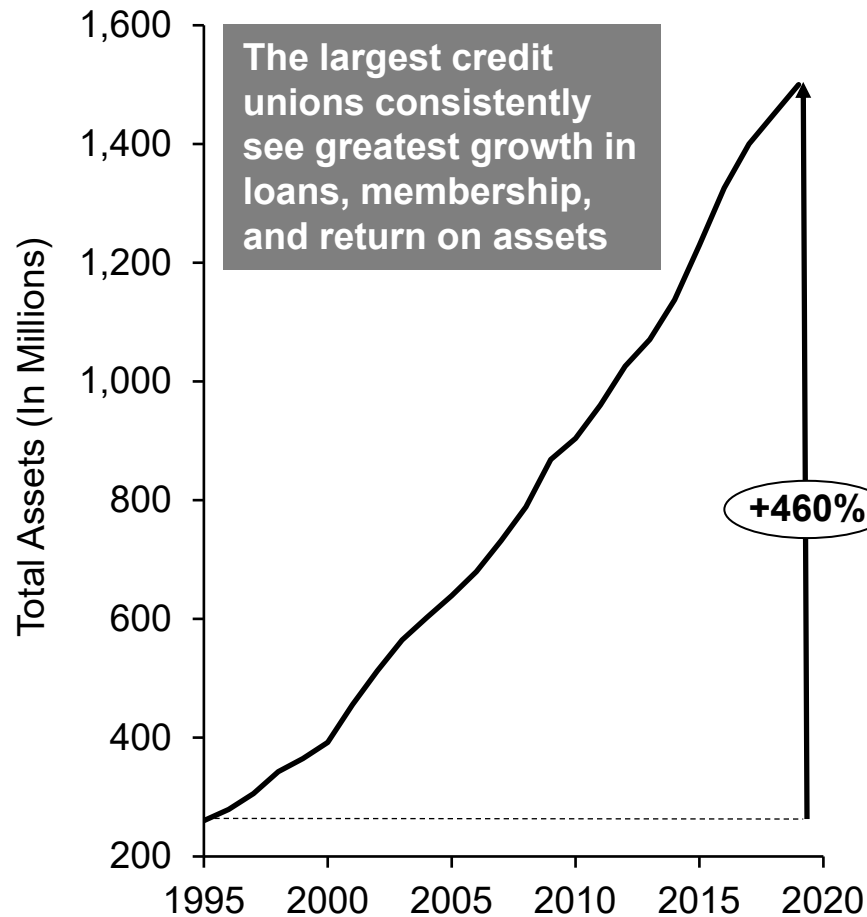
- In the last few decades, membership restrictions have relaxed so that the largest credit unions can accept virtually any customer who walks in the door
- Lending regulations have also been relaxed, leading to a shifted focus on commercial lending
- As a result, the number of credit unions with more than \$1 billion in assets has exponentially grown from the few that existed in the 1990s

Present

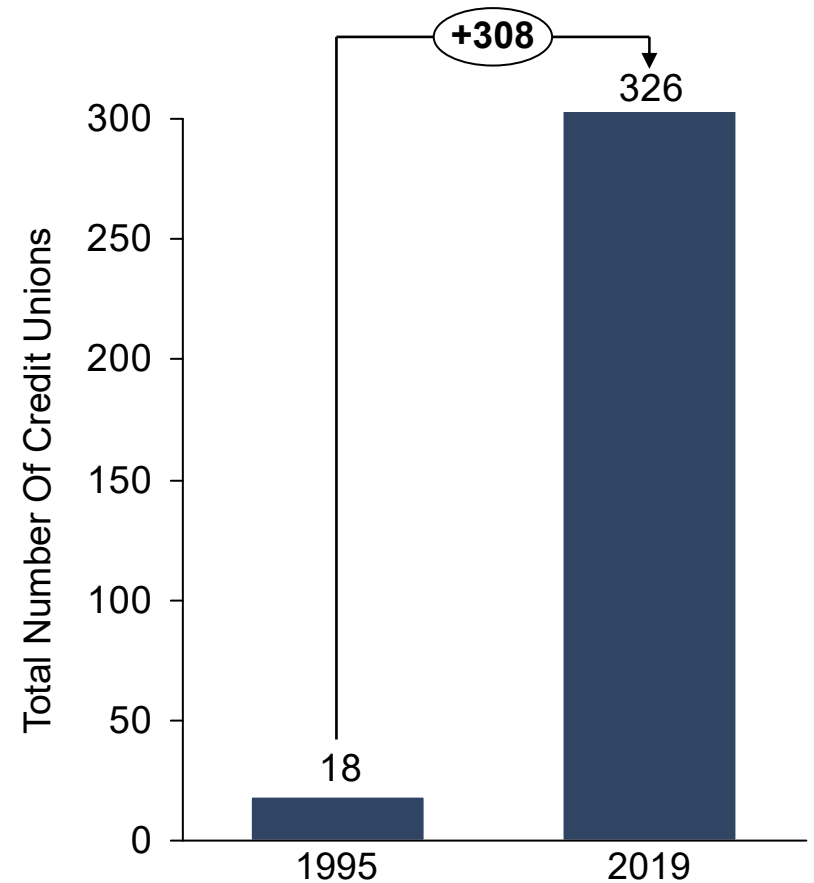
- Today, credit unions have expanded into a \$1.5 trillion-dollar industry that pays no federal corporate income taxes
- Credit unions are increasingly buying banks – leveraging a tax benefit to permanently take taxpaying entities off the tax rolls
- The tax exemption will cost taxpayers more than \$24 billion over the next decade
- Congress needs to take a fresh look at how the credit union tax exemption is being used

The Credit Union Industry Has Evolved And Grown Increasingly Large In The Last Few Decades

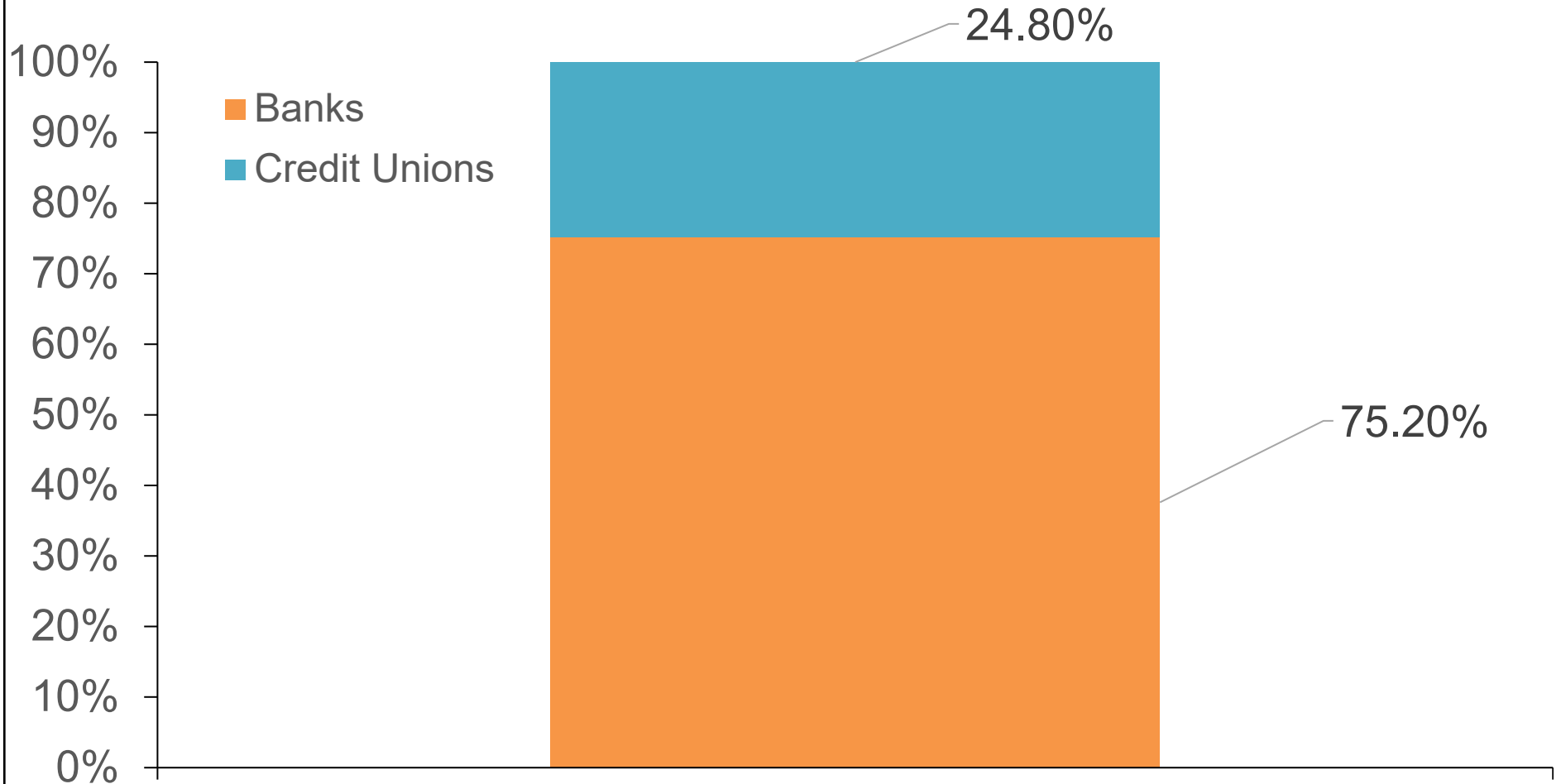
Total Credit Union Industry Assets, Over Time



Number Of Credit Unions With More Than A Billion Dollars In Assets



Deposit Market Share in Virginia



Source: SNL Financial

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Deposit Market Share

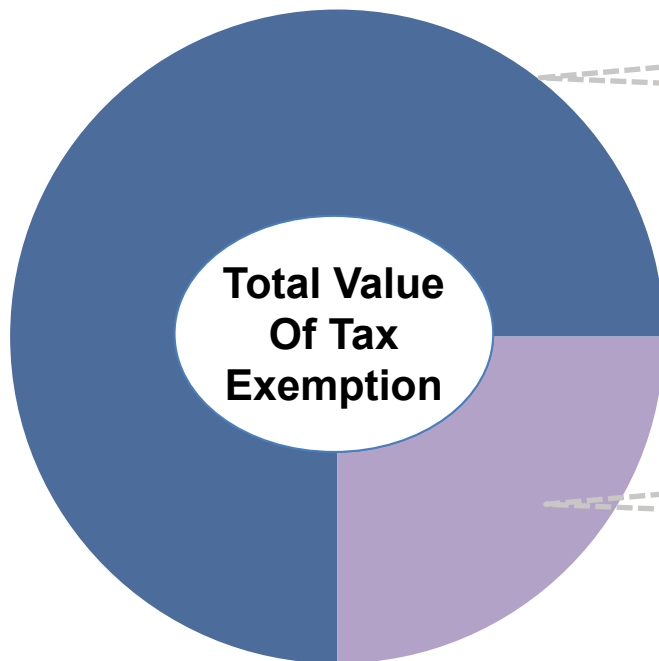


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The Tax Exemption Benefits Skew Disproportionately To 5% of Credit Unions - Those Over \$1 Billion In Assets

Total Share Of Tax Exemption Benefit, By Credit Union Size

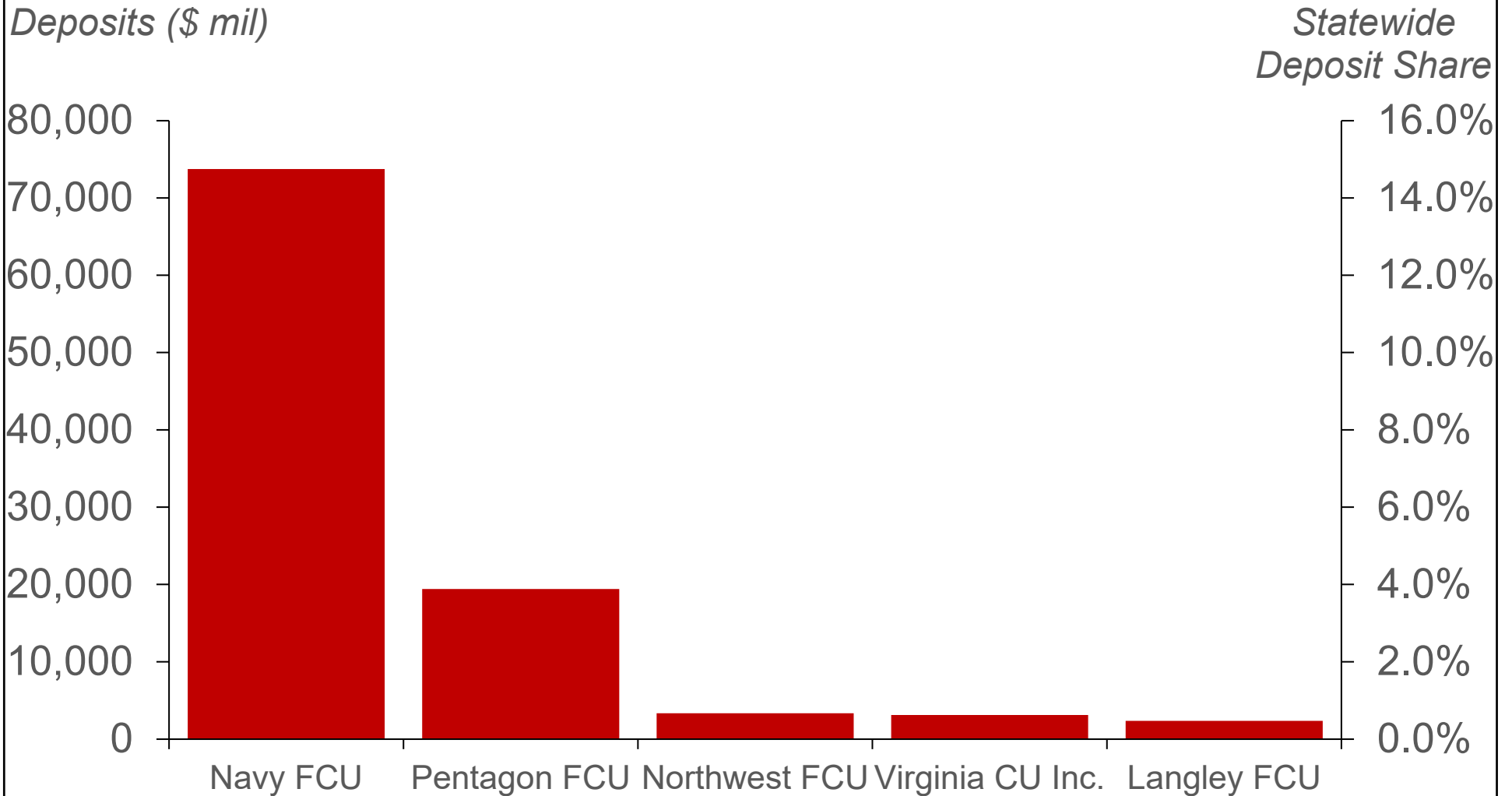
■ >\$1 Billion In Assets ■ <\$1 Billion In Assets



Nearly 75 percent of the tax benefit goes to 326 credit unions with over \$1 billion in assets, or roughly 5 percent of the entire industry

Barely 25 percent of the tax benefit goes to the remaining 95 percent of the industry, the ~5,200 credit unions with assets of less than \$1 billion

Virginia Top Credit Unions



Source: SNL Financial

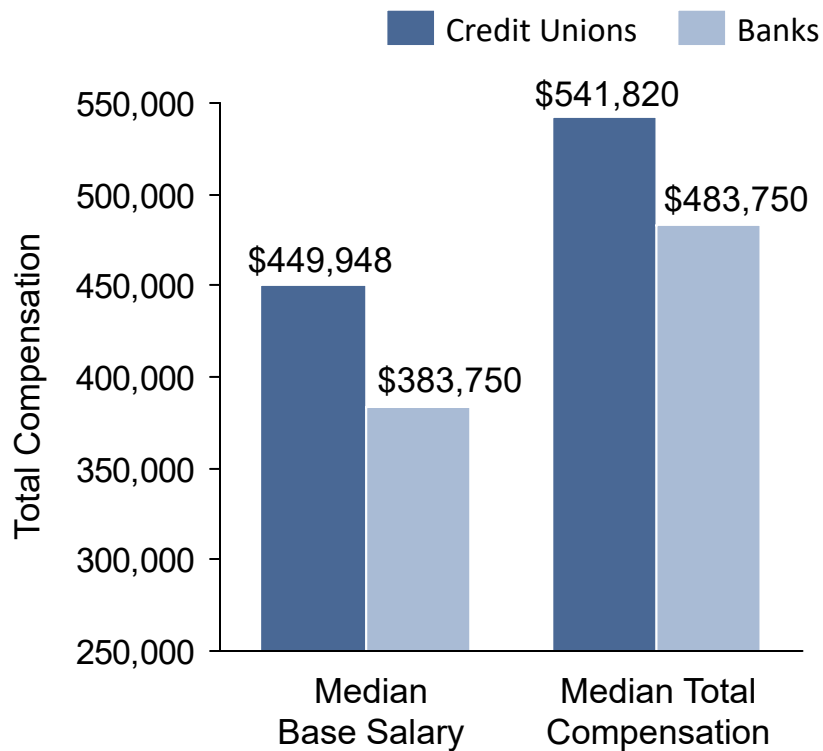
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The Largest Credit Unions Often Use Tax Savings For Commercial Sponsorships And High Executive Salaries

Large credit union CEOs receive, on average, higher cash compensation compared to their CEO counterparts at banks of similar sizes



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Source: [Credit Union Executive Compensation Survey](#)

Credit Unions Use Tax Exemption For Commercial Sponsorships

Credit Union Times

Golden 1 Inks \$120 Million Naming Rights Deal

THE DENVER POST

Denver credit-union CEO David Maus' \$11 million pay package stuns industry

The San Diego Union-Tribune

Holiday Bowl gets San Diego County Credit Union as new title sponsor



PenFed Plans HQ Shift After \$164 Million Buy in Tysons Corner



American Bankers Association

Field of Membership is the Key to Credit Union Policy

12 U.S.C. 1759

(b) MEMBERSHIP FIELD. Subject to the other provisions of this section, the membership of any Federal credit union shall be limited to the membership described in one of the following categories:

(1) SINGLE COMMON-BOND CREDIT UNION. One group that has a common bond of occupation or association.

(2) MULTIPLE COMMON-BOND CREDIT UNION. More than one group—

(A) each of which has (within the group) a common bond of occupation or association; and


(B) the number of members, each of which (at the time the group is first included within the field of membership of a credit union described in this paragraph) does not exceed any numerical limitation applicable under subsection (d).

(3) COMMUNITY CREDIT UNION. Persons or organizations within a well-defined local community, neighborhood, or rural district.

Literally, Anyone Can Join: Membership Restrictions Basically Irrelevant at Large Credit Unions


- Credit unions were based on a simple concept—a common bond—where members all came from the same employer, church, school, or community.
- That concept is no longer relevant at the largest credit unions where often, literally, anyone can join.
- Credit unions are also increasingly targeting the affluent – despite a statutory admonition to serve consumers of modest means.
- By approving these membership expansions, *credit union regulators* are determining the size and scope of the tax exemption, not tax policymakers.






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The 4 top myths with #creditunions 1) can't join 2) it's for those in need 3) lack of access to money and 4) are too small #CUNAACUC

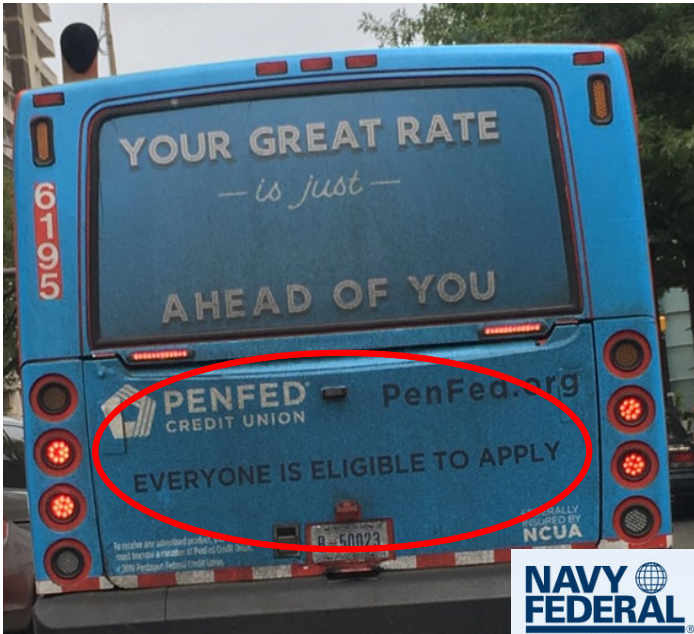
11:01 AM - 27 Jun 2017

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  3  4



Virginia is Front and Center on Field of Membership Fights



Some of the largest and most aggressive credit unions in the country are from Virginia.

- PenFed – no field of membership restrictions at all
- Navy Federal – includes DOD contractors (i.e., partners at major consulting firms like Booz Allen and Deloitte)
- Virginia Credit Union / Medical Society of VA (more later)
- Northern Virginia was textbook example of NCUA overreach in field of membership litigation



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Membership Eligibility

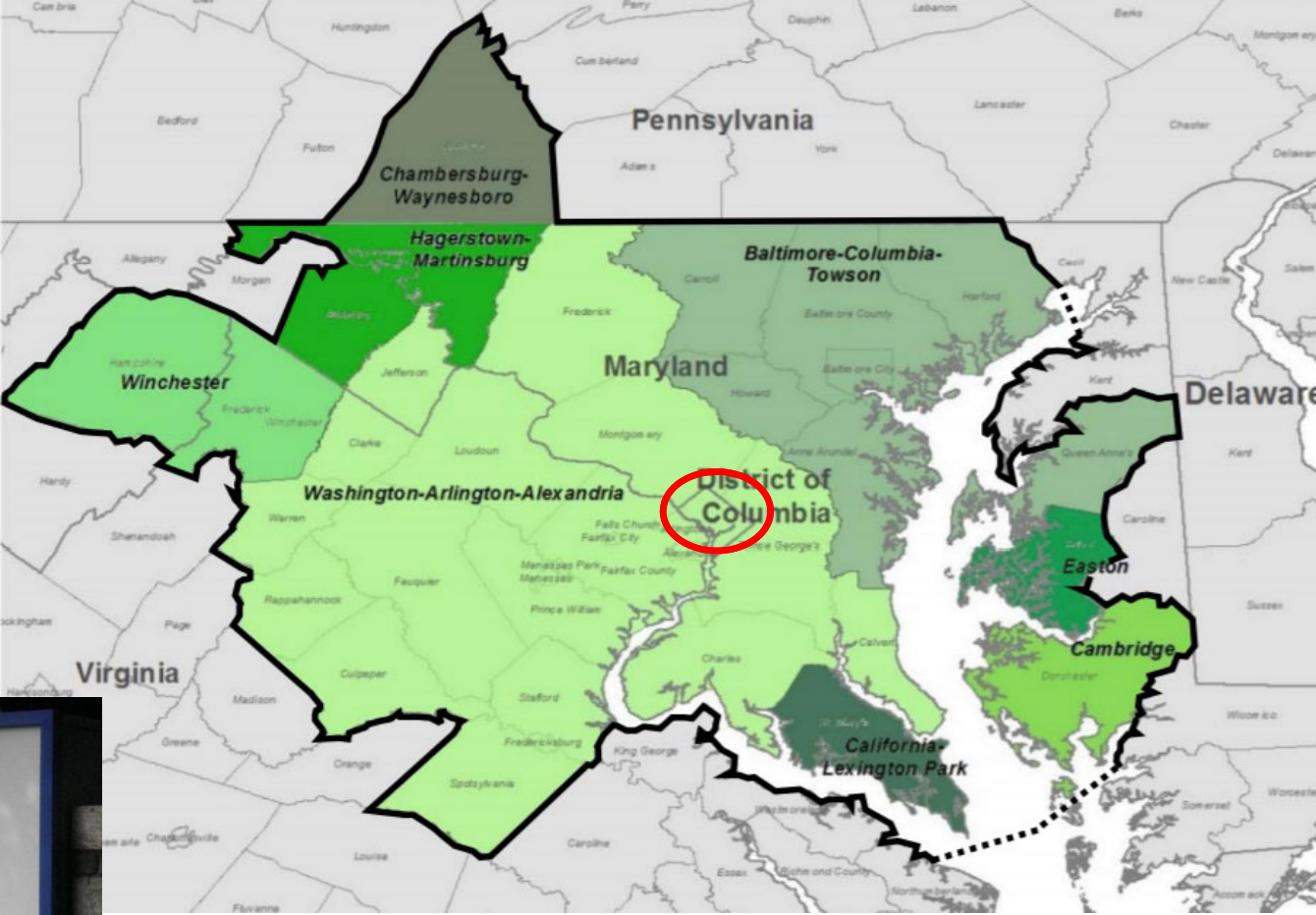
Am I Eligible for Membership?



Our field of membership goes beyond current and retired members of the armed forces to include their families and household members, Department of Defense personnel and more.

ABA litigation at the federal level

... and the meaning of a “well-defined local community”



American Bankers Association.

Regulatory Arbitrage Exists, and Compounds the Tax Disparity

- Credit unions are **exempt from CRA** (although a few states have applied similar requirements to state chartered credit unions with positive results).
- The credit union **risk based capital** scheme, which applies only to CUs over \$500 million, has yet to be implemented—even though every single bank in America has lived with Basel III for nearly a decade.
- The exemption level for **commercial real estate appraisals** was recently increased to \$1 million – twice the level enjoyed by banks. Although this is a developer’s dream, higher thresholds could increase long-term risk across the financial system.
- Credit unions have a statutory **business lending cap** of 12.25% of assets, but can evade it through buying and selling loan participations to banks or credit unions. Purchased and sold participations do not count—at all—against the cap.

Sherrrod Brown
SENATOR for OHIO

BROOKINGS

SERIES: Series on Financial Markets and Regulation

Bank-like credit unions should follow bank rules
Aaron Klein Thursday, June 28, 2018

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United States Senate
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
WASHINGTON, DC 20510-6075
July 16, 2019

The Honorable Rodney Hood
Chairman
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

Dear Chairman Hood:

Last year, prior to your confirmation as a Member of the Board, the National Credit Union Administration (NCUA) proposed to raise the current appraisal exemption for commercial real estate loans from \$250,000 to \$1 million. NCUA characterized this as a “significant increase” in the threshold and noted that the percentage of commercial loans exempted from appraisals would increase from 27 percent to 66 percent.¹

Following your testimony before the Senate Committee on Banking, Housing, and Urban Affairs on May 15, 2019, I submitted a series of written questions regarding the October 2018 proposed rule. As of the writing of this letter, my office has not received a response. However, on July 15, 2019, NCUA published the agenda for its board meeting this Thursday, July 18, 2019. This agenda includes consideration of “NCUA Rules and Regulations, Real Estate Appraisals.”²

As I indicated in the questions I submitted in May, I remain deeply concerned that the proposed significant increase in the appraisal threshold would pose undue risks to credit unions and their members. Before adopting a final rule amending the commercial appraisal exemption threshold, request that you provide written responses to the following questions.

**The Credit-Union Equality Commitment:
An Analytical Assessment***

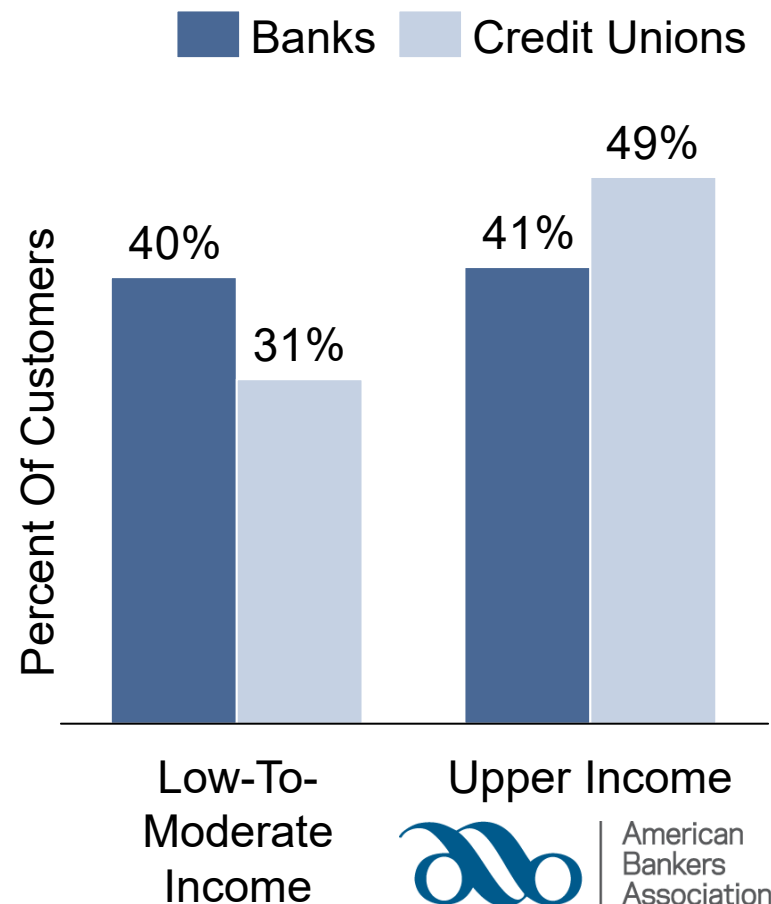
Federal Financial Analytics, Inc.
www.fedfin.com
June 25, 2019

Credit Unions Serve Fewer Low-Income Communities Than Banks Despite Their Growing Assets

With no CRA Obligations, Credit Unions Primarily Serve Upper-Income Customers.

- Credit unions were granted the tax exemption to serve customers of modest means—their customer base no longer reflects this intent.
- Now, credit unions serve mostly upper income patrons and have fewer low income members.

Credit Union Customers Compared To Bank Customers

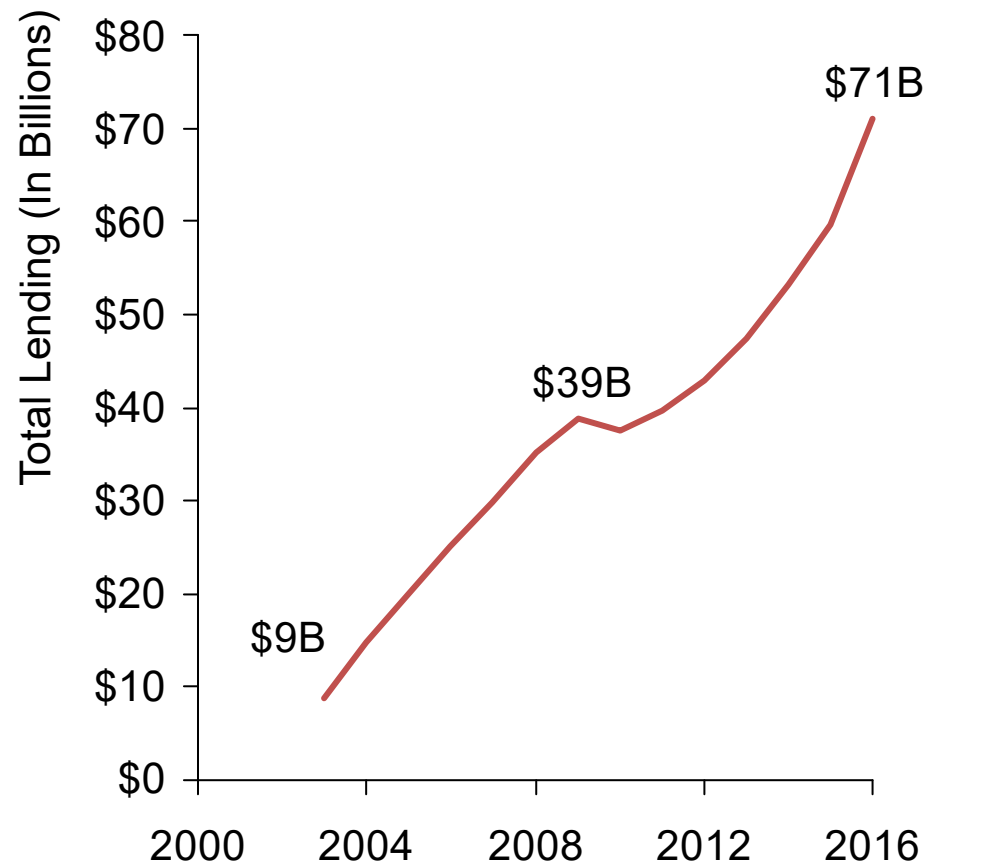


Credit Unions Engage In Commercial Lending Similar To Banks But Do Not Pay The Same Taxes

Lending Beyond Original Scope

- Credit unions now engage in business activity similar to banks, especially in complex commercial lending.
- Credit unions' business lending has increased rapidly since 2003, doubling in the last decade alone.
- More than 20 percent of all credit union loans are indirect auto loans originated to non-credit union members through car dealers; although the consumer must join the credit union, this generally only occurs after underwriting. Common bond?

Total Credit Union Business Lending Over Time



Credit Unions are Increasingly Buying Banks

- At least 39 banks have agreed to be sold to credit unions since 2012, with 14 deals announced so far this year – more than in all of 2018.
- Consultants and investment bankers are increasingly pitching banks to sell, or at least consider, credit union bidders, noting the shortcut for CRA review and that credit unions must pay in cash because they have no stock.
- ABA hears that credit unions are sometimes paying a higher multiple than bank buyers, which makes sense given the tax advantage.
- ABA has worked to increase public attention on these deals. Policymakers are also often very concerned about this trend, given it leverages the tax advantage to take a taxpayer off the taxrolls.

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The image shows two screenshots of news articles. The top screenshot is from The Wall Street Journal, dated September 3, 2019, by Lalita Clozel. The article is titled "Credit Unions Go On Bank Buying Spree" and discusses how not-for-profit financial firms have acquired a record number of banks since last year. It includes an illustration of a man and a woman walking past a building labeled "BANK" and a video player titled "A Brief History of Retail Banking". The bottom screenshot is from the Federal Reserve Bank of St. Louis, dated Thursday, April 11, 2019, by Andrew P. Meyer. The article is titled "Why Are More Credit Unions Buying Community Banks?" and discusses the trend of credit unions acquiring banks and thrifts, noting that this is driven by regulatory compliance and business-model challenges. It includes a "KEY TAKEAWAYS" section with three bullet points and a photo of a woman at a desk.

THE WALL STREET JOURNAL.
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MARKETS | FINANCE
Credit Unions Go On Bank Buying Spree
Not-for-profit financial firms have acquired a record number of banks since last year

FEDERAL RESERVE BANK of ST. LOUIS
CENTRAL TO AMERICA'S ECONOMY®

Home > Publications > Regional Economist > First Quarter 2019 >

Why Are More Credit Unions Buying Community Banks?

KEY TAKEAWAYS

- Acquiring banks and thrifts has become another way for some credit unions to grow in size.
- This trend is growing but remains small—only seven deals in 2018—because of regulatory and business-model challenges.
- Small banks with strong community ties and banks with different specialties, such as business lending, can be appealing to credit unions.

By **Andrew P. Meyer**
Thursday, April 11, 2019

In the current banking environment, there is a strong perception that bigger is better. Although banks and thrifts (hereafter referred to as "banks") have been consolidating for decades, the trend has accelerated in recent years. One factor driving this trend is regulatory compliance data from the Conference of State Bank Supervisors (CSBS) 2018 Community Banks has shown that the bigger the bank, the less it spends on compliance as a percentage of total asset base.

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February 22, 2019 04:17 PM

Community bankers' nightmare comes true

Golden Eagle in Woodstock recently became the first area bank to sell to a credit union. It won't be the last. Bankers who aren't selling are unhappy.

STEVE DANIELS

American Bankers Association®

Credit Union Bank M&A: Growing Across the Country

<u>Acquiring Credit Union</u>	<u>CU State</u>	<u>Target Bank</u>	<u>Bank State</u>	<u>Deal Announced</u>
Family Security Credit Union	AL	Bank of Pine Hill	AL	2017
IBM Southeast Employees Credit Union	FL	Mackinac Savings Bank	FL	2017
Advia Credit Union	MI	Peoples Bank	WI	2017
Honor Credit Union	MI	Citizens State Bank of Ontonagon	MI	2017
Trona Valley Community Federal Credit Union	WY	State Bank	WY	2017
Lake Michigan Credit Union	MI	Encore Bank	FL	2017
Georgia's Own Credit Union	GA	State Bank of Georgia	GA	2017
SRP Federal Credit Union	SC	Southern Bank	GA	2017
Achieva Credit Union	FL	Preferred Community Bank	FL	2018
Superior Choice Credit Union	WI	Dairyland State Bank	WI	2018
Evansville Teachers Federal Credit Union	IN	American Founders Bank	KY	2018
LGE Community Credit Union	GA	Georgia Heritage Bank	GA	2018
Sound Credit Union	WA	The Bank of Washington	WA	2018
IBM Southeast Employees Credit Union	FL	The Oculina Bank	FL	2018
Advia Credit Union	MI	Golden Eagle Community Bank	IL	2018
VyStar Credit Union	FL	Citizens State Bank	FL	2019
Central Florida Educators Credit Union	FL	Fidelity Bank of Florida	FL	2019
Fairwinds Credit Union	FL	Friends Bank	FL	2019
Power Financial Credit Union	FL	TransCapital Bank	FL	2019
MidFlorida CU	FL	Community Bank & Trust of Florida	FL	2019
Arizona Federal Credit Union	AZ	Pinnacle Bank	AZ	2019
Verve Credit Union	WI	South Central Bank	IL	2019
Corporate America Credit Union	IL	Ben Franklin Financial	IL	2019
First South Financial	TN	WinFirst Financial	KY	2019
3 Rivers Federal Credit Union	IN	West End Indiana Bank	IN	2019
Indiana Members Credit Union	IN	Commerce Bank	IN	2019
Elevations Credit Union	CO	Cache Bank & Trust	CO	2019



Credit Unions Are Clearly Aware of the Regulatory and Tax Arbitrage of Which They Are Taking Advantage

Lawmakers should be upset that the tax advantage and regulatory structure is being abused by credit unions. Behind closed doors—as prominent CU industry lawyers made clear pitching banks on selling to credit unions at the “Acquire/Be Acquired” conference in 2017—credit unions are in on the joke.

Pricing

Higher Multiple? – **Yes**

- 1. Expense Reductions Inherent for CUs
(This is completely unfair for Banks).**
- 2. CUs prefer owning Real Estate**
- 3. CUs have limited ways to raise
and deploy capital**

The trend of credit unions buying banks is similar to the corporate inversions that attracted so much attention a few years back – without the need to move to the Caymans.

Deal Positives

- 100% Cash
- Higher Multiple
- Branches and Employees Protected
- Regulatory Shortcuts
 - i. No CRA
 - ii. Exempt from HSR
 - iii. Streamlined FDIC Application



What ABA and State Bankers Associations Are Doing to Help

- An aggressive, coordinated strategy of third-party voices
- Targeted lobbying by ABA, state associations, and influential bankers
- Funded research projects
- Communications amplification to force policy discussion among federal and state policymakers
- Litigation that challenges NCUA excess

What You Can Do to Help

- Talk to your lawmakers. A conversation at home in the grocery store is always more effective than anything that happens in Washington. Make sure they understand:
 - At *\$1.5 trillion*, credit unions today are not the mom-and-pop operations of old.
 - Just 5% of the industry achieves 75% of the tax benefit. Focusing on the largest segment limits political blowback.
 - When credit unions buy banks, they can't say they are different from banks at the same time. The tax and regulatory treatment of the industry should match the facts on the ground.
 - Congress should conduct oversight on this issue to focus regulators on improvements to this industry.

What You Can Do to Help

- Outreach to VBA for coordinated activities, e.g., member meetings, media opportunities.
- Consider outreach to local community groups and state officials that highlight the local tax implications of credit union expansion – including when credit unions buy banks.
 - State officials can put limits on acquisitions of state chartered banks. For example, they could require credit unions that buy banks to change charters and become a bank in order to complete the deal.
 - State officials could also mandate CRA-reviews for acquisitions of state chartered banks, or CRA-like requirements for state chartered credit unions.
- Reach out to us for targeted guidance for federal engagement.

Thank you!

- We are happy to discuss specifics in detail at any time.