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CREDIT UNIONS

The California Bankers Association Credit Union Task Force

Background

A number of California credit unions have evolved from small "community" institutions that served a specific membership into goliath financial institutions whose field of membership have evolved in some cases, to include nearly half of the counties in the state. These institutions who once offered limited products for the benefit of a small group of similar employees now offer virtually every product banks and other financial institutions offer, but they do so largely without having to pay taxes. The affect of the aggressive growth of credit unions in California has been the near takeover of markets in areas such as auto lending and this growth comes at the direct expense of California's community banks – institutions that pay taxes and have been part of economic fabric of local communities for decades.

Since 1994, California has seen its non-taxable credit unions grow their assets and increase their profitability. For instance, asset growth among California credit unions has quadrupled since 1994 and their net income has increased more than seven-fold (from \$165.6 million in 1994 to \$1.3 billion in 2002 according to statistics from the California Department of Financial Institutions). This growth has come without California receiving any taxable revenue, without local counties and cities receiving the type of community reinvestments required of banks and without depositors receiving the same safety and soundness statutory and regulatory requirements of those who use financial institutions such as banks. In addition, credit unions have fought against and repeatedly refused to accept any community reinvestment requirements.

Credit Union Initiatives Task Force

The California Bankers Association (CBA) is taking strong measures to level the playing field between credit unions and community banks and to publicize the difference between the two types of institutions. To that end, CBA has formed the Credit Union Initiatives Task Force which is developing a federal and state strategic plan to address the anti-competitive effects of credit unions.

The task force first identified those issues that have an anti-competitive effect between credit unions and community banks. To date, the task force has identified five core issues that need to be studied and addressed. These issues include: (1) taxation, (2) field of membership, (3) scope of products and services, (4) regulatory control of risks and (5) community reinvestment act obligations.

The task force next looks to work with legislators, the American Bar Association and the bankers associations of other states to study these differences, to determine the extent to which there are anti-competitive effects and to determine if California and its credit union depositors are receiving the benefit they believe is actually being conferred. Through it all however, CBA remains committed to a maintaining a vibrant financial climate in California and to maintaining a healthy competition between and amongst financial institutions.

RULE	FEDERAL CREDIT UNION	STATE CREDIT UNION	STATE CHARTERED BANK
<u>Common Bond</u>	Three types: occupation, association, and community. A community is a well-defined local community, neighborhood, or rural district. A federal CU may serve multiple groups each having a common bond of occupation or association. Unlike California, there is no allowance for a multiple community CU.	Three types: occupation, association, and groups within a "well-defined neighborhood, community, or rural district." A CU may serve multiple groups from one or more of these three types of groups.	N/A
<u>Capital Adequacy</u>	A federal credit union must maintain a net worth of at least 6% (adequately capitalized), as measured by the ratio of net worth to total assets.	A state CU whose share accounts are insured by the NCUSI Fund must maintain the same equity capital level as is required for a federal CU that is "adequately capitalized." As to CUs whose share accounts are insured other than by the National Credit Union Share Insurance (NCUSI) Fund: <i>CU in operation more than 4 years.</i> A CU that has been in operation for more than 4 years must maintain a regular reserve of 4-6% of total risk assets. <i>CU in operation less than 4 years.</i> Regular reserves must be maintained at a level specified by the DFI Commissioner.	State banks must meet two minimum capital requirements: (1) 4% Tier 1 capital to total assets; and (2) a total risk-based capital ratio of 8% capital to risk-weighted assets.
<u>Community Reinvestment Act</u>	Federal CUs are not subject to CRA.	State CUs are not subject to CRA.	Subject to CRA

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<u>Trust Powers</u>	Federal credit unions may offer trust services only through Credit Union Service Organizations (CUSOs).	A CU may not exercise trust powers unless it qualifies as a trust company under California law.	A state bank may engage in trust activities if permitted by its bylaws and upon application to the Commissioner of Financial Institutions. Deposits with the State Treasurer are required.
<u>Business Loans</u>	The aggregate limit on outstanding business loans is the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets. The member business loan limit to one member or group of associated members is the greater of 15% of the CU's net worth or \$100,000.	Same as federal credit unions	Authorized.
<u>Loan Limits to Single Borrower</u>	A federal credit union's lending to any one member is limited to 10% of unimpaired capital and surplus, that is, 10% of the amount equal to a federal credit union's net worth plus its deposits. Commercial lending-- the aggregate amount of business loans outstanding to any one member may not exceed 15% of reserves or \$100,000, whichever is higher.	As to an individual CU member or a family, total obligations (exclusive of amounts secured by shares or certificates for funds) cannot exceed 10% of the CU's savings capital. The savings capital of a CU is the aggregate of payments made by members on shares.	Unsecured--to any one person is limited to 15 percent of the sum of the shareholders' equity, allowance for loan losses, capital notes, and debentures of the bank. Obligations, secured and unsecured, in all is limited to 25 percent of the same.

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<u>Credit Union Service Organizations (CUSOs)</u>	Federal credit unions may own as a subsidiary or jointly with others a CUSO. Federal credit unions may only invest up to 1% of their capital in such entities and may lend an amount up to 1% of their capital to such entities. CUSOs may engage in a wide range of activities, only some of which a federal credit union may engage in directly. However, all CUSO activities must be approved by the NCUA Board.	CUSOs are governed by the general corporations' law, which permits an entity to engage in any business that is not prohibited by law. The Department of Financial Institutions, which supervises CUs, does not require a CU to notify the department when the CU it establishes a wholly-owned CUSO that performs services only to the parent CU.	State banks are authorized to invest in various kinds of companies, including those formed to perform check and data processing, hold real estate, engage in a safe deposit business, engage in the trust business, and invest in small businesses. Generally, the level of investments is subject to limits expressed as a percentage of shareholder equity.
<u>Management Interlocks</u>	Similar to banks, except that the prohibition does not apply to service at credit unions; that is, the interlock restrictions apply only as to credit unions and other financial institutions, but not to other credit unions.	Same as federal credit unions	Management official may not serve at the same time on more than one unaffiliated bank if the banks have offices in the same community. Other rules apply to banks in the same RMSA and to banks with large assets.
<u>Prompt Corrective Action</u>	Banks and credit unions are subject to a similar regulatory system of prompt corrective action.		