

**Statement for the Record**  
**For the May 16 Hearing on**  
**Tax Exempt Organizations**  
*on behalf of the*  
**American Bankers Association**  
*before the*  
**Oversight Subcommittee**  
*of the*  
**Committee on Ways and Means**  
**United States House of Representatives**

Chairman Boustany, Ranking Member Lewis and members of the Subcommittee, the American Bankers Association (ABA) appreciates the opportunity to submit a statement for the record for the hearing on tax-exempt organizations. The American Bankers Association represents banks of all sizes and charters and is the voice for the nation’s \$14 trillion banking industry and its two million employees.

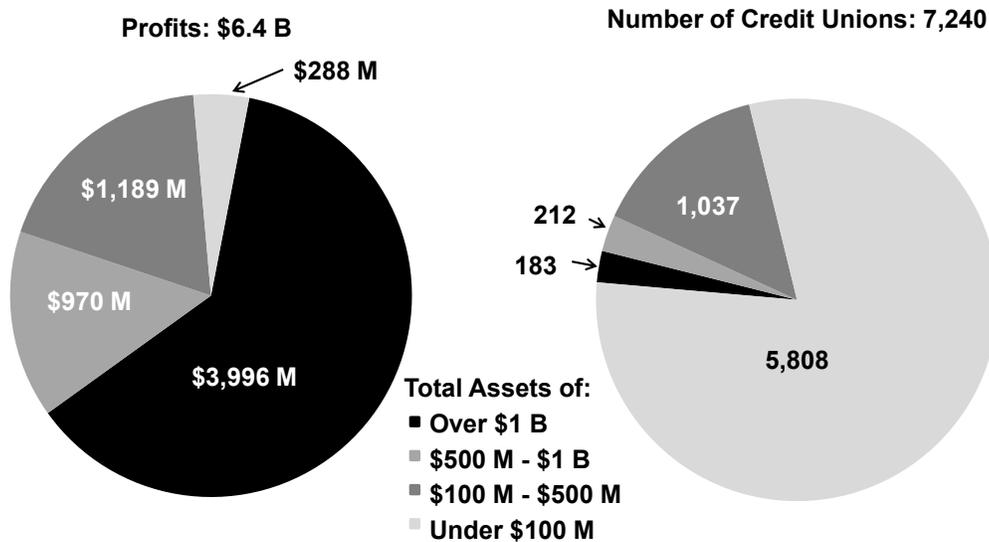
While the hearing focused on compliance and reporting requirements for universities and hospitals, our comments focus on the compliance and reporting issues for another, tax-favored sector: credit unions. Originally credit unions were created and granted their tax exemption to serve people of modest means. However, many of these tax-exempt organizations have now morphed from serving “people of small means” to become full service, financially sophisticated institutions that compete head-to-head with local taxpaying banks.

ABA commends the Subcommittee for its plans to hold a series of hearings on tax-exempt organizations. We encourage the Committee to hold a hearing specifically on credit unions as tax-exempt entities. Credit unions represent a significant tax expenditure: since 2001 they have enjoyed the privilege of ***not paying an estimated \$20.5 billion in federal corporate income taxes***. They have almost twice the assets as tax-exempt institutions in higher education and fifteen percent more assets than tax-exempt hospitals. The size and taxpayer benefits conferred certainly make them worthy of careful Congressional investigation to assure this large tax expenditure is directed where Congress intended.

Many of today’s credit unions are a far cry from the small, traditional credit unions that served distinct groups of “people of small means,” which Congress sought to assist when it provided tax subsidies to credit unions in the 1930s. There are now 183 credit unions that have more than \$1 billion in assets each; these credit unions hold 48.6 percent of all credit union assets but represent only 2.5 percent of the total number of credit unions. *These 183 large credit unions are larger than 91 percent of all banks, and nearly indistinguishable from taxpaying community banks.* Indeed, these credit unions compete for the same loans as their community bank counterparts, but credit unions pay no taxes. Credit unions were not intended to be simply tax exempt banks.

## Credit Union Tax Subsidy Benefits Largest Institutions

**77% of Industry Profits Held by Less Than 6% of Credit Unions**



Source: NCUA. Data as of 4Q2011.

As Congress examines the affordability of tax expenditures in the face of rising debt levels, it should target the credit union tax expenditure. The need for the credit union tax exemption has all but disappeared.

In this statement, ABA’s comments will focus on three key points:

- Transparency requires credit unions to successfully demonstrate service to people of modest means to assure taxpayers their tax subsidy is being properly employed.

- Federal credit union corporate governance disclosures should mirror those of most tax exempt institutions.
- The credit union tax exemption should be eliminated, particularly for credit unions that have strayed from their mission of service to people of modest means.

## **I. Credit Unions Should Be Required to Demonstrate Service to People of Modest Means**

Tax exempt institutions should be required to demonstrate to taxpayers that the tax subsidy is being used as Congress intended. Credit unions have no requirement now to do so.

The exemption in the tax code for credit unions was created in the early 20th Century to incent more consumer lending, especially to people of modest means, because at that time there were fewer options to obtain credit. This was reaffirmed when Congress passed the Credit Union Membership Access Act of 1998:

[C]redit unions, unlike many other participants in the financial services market, are exempt from Federal and most State taxes because they are member-owned, democratically operated, not-for-profit organizations generally managed by volunteer boards of directors *and because they have the specified mission of meeting the credit and savings needs of consumers, especially persons of modest means.* [emphasis added]

Credit unions steadfastly refuse to define “modest means,” thus evading the simple determination of whether they are fulfilling their mission. Available evidence shows that they are not. According to data from a 2006 study by the U.S. Government Accountability Office (GAO), credit unions serve proportionately more upper income customers than banks and fewer low-income customers than banks. The GAO found that “14 percent of credit union customers were of low-income and 17 percent were of moderate-income, compared with 24 percent and 16 percent for banks.”<sup>1</sup> Moreover, GAO found that 49 percent of credit union customers were upper income compared to 41 percent for banks.

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<sup>1</sup>United States Government Accountability Office, Credit Unions: Greater Transparency Needed on Who Credit Unions Serve and on Senior Executive Compensation Arrangements, November 2006, GAO-07-29, p20.

Moreover, credit unions' own surveys suggest that their image of serving moderate and lower income people is no longer valid. The typical credit union member has higher than average income, more years of education and is more likely to own a home than non-credit union members.<sup>2</sup> Thus, the credit union tax expenditure is subsidizing financial services to individuals who do not need it and who otherwise have access to basic banking services. Basic transparency would surely shine light on this discrepancy.

More concrete demonstration of serving people of modest means is needed. This was what the GAO recommended in two studies, one in 2003 and the other in 2006, suggesting that NCUA develop more tangible indicators to determine whether credit unions have provided greater access to services in underserved areas or fulfilled their tax-exempt mission. *The recommendations have not yet been fully implemented.*

At a hearing in 2005, former NCUA Chairman D'Amours expressed his frustration over past efforts to have credit unions add to their business plans how they intend to reach out to low-income people. He said he had been told by the credit unions during his tenure that "credit unions were never really intended to serve anything but the middle class." He also said that his agency's effort of more than three years was "fiercely resisted." He said at that time:

It is amazing that we can't get a definition of what "modest means" amounts to. But the truth is that that is not happen stance; they want it that way... I hope that this [hearing]...will result in something positive coming from the U.S. Congress. As I said earlier, if it doesn't come from Congress, it is not going to happen.

With the privilege of federal income tax exemption and a mandated mission of serving persons of modest means or those with moderate and lower incomes, credit unions must be more transparent with those definitions and their application. The current amorphous definition leaves credit union members, taxpayers and tax policy decision-makers without clear and fundamental information to understand how credit unions meet their congressionally-defined mission.

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<sup>2</sup> CUNA National Member Survey, 2002.

## II. Credit Union Corporate Governance Disclosures Should Mirror That of Other Tax Exempt Organizations

Credit unions must be more transparent in the information about expenditures, such as executive compensation and charitable donations. Most tax-exempt organizations, including universities and hospitals, must disclose the compensation of senior officials to the Internal Revenue Service in the Form 990—a form that has become an important tool for determining the transparency and accountability of tax-exempt organizations.<sup>3</sup> By publicly disclosing this information, the Form 990 fosters good corporate governance as it attempts to ensure that the tax expenditure is being appropriately employed.<sup>4</sup>

State-chartered credit unions are required to file a Form 990, but federal credit unions are not. Since federal credit unions are cooperatives, the member-owners have a right to know the total compensation paid to senior officials. For example, if Public Service Credit Union of Denver had been a federal credit union (rather than state-chartered), information regarding the \$9.8 million base compensation of its CEO and President would not have been disclosed. His 2010 pay package was almost 20 times the average for comparable sized credit unions according to press reports.<sup>5</sup>

Federal credit unions should be required to file Form 990 information just like state-chartered credit unions and most other tax-exempt institutions. Expanding the public's opportunities to review executive salaries would promote improved corporate governance and greater credit union accountability. ***It would inform Congress, taxpayers, and credit union members about whether this valuable tax subsidy is going towards the credit union mission or is subsidizing credit union management.***

NCUA, as the primary supervisor over these federal tax exempt organizations, has the authority to require all federal credit unions to file this Form 990 information. The GAO suggested this in 2006: “NCUA could require all federally insured credit unions to include

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<sup>3</sup>According to data compiled from the Urban Institute's National Center For Charitable Statistics, around eighty percent of registered higher education organizations and hospitals file the form.

<sup>4</sup>Form 990 filers are also required to describe the organization's program service accomplishments for each of its three largest program services.

<sup>5</sup> According to a Denver Post article, the credit union salary data is from Executive Compensation Solutions.

compensation and benefit data for senior executive officers in the call reports that are submitted on a quarterly basis—an option that NCUA officials indicated was under current consideration.” NCUA has failed to act.

In fact, NCUA is moving even further away from ensuring transparency by eliminating its charitable contribution rule. Now, any federal credit union can make donations without the prior approval of its board of directors and without regulatory restrictions as to recipients. This makes credit union management less accountable to its members. Congress should insist that NCUA take action for greater transparency and accountability.

### **III. The Credit Union Tax Exemption Should Be Eliminated**

Over the last 75 years, credit unions have changed and for many credit unions their tax exemption is no longer appropriate. Credit unions’ expansion into new business activities and the liberalization of their fields of membership—which has allowed credit unions to serve ever-larger geographic areas—has made them indistinguishable from banks. In fact, credit unions are seeking additional authority to make commercial loans, further moving them away from their mission of serving consumers of modest means.

The evidence suggests that the credit union tax exemption is fueling the rapid growth of this industry. Some credit unions are using their tax-exempt status to sponsor college bowl games, build multi-million dollar headquarters or to buy the naming rights to stadiums and arenas. While many credit unions remain true to their original mission, a growing number of credit unions have abandoned their roots and inappropriately taken advantage of their tax-exempt status to gain ever-increasing market share.

Moreover, basic economics tells us that this tax expenditure puts credit unions at a competitive advantage relative to other financial institutions providing identical services, because it distorts economic behavior and the allocation of resources within the financial services sector. The Congressional Research Service said that credit union growth in assets in the 1980s, 1990s and through 2009 was more rapid than other depository industries.<sup>6</sup> In 2005, there were about 260 credit unions with assets over \$500 million and a little over 100 with assets

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<sup>6</sup>United States Congressional Research Service, *Should Credit Unions Be Taxed?*, May 2010, 97-548, p.17.

greater than \$1 billion. Today, almost 400 credit unions have assets over \$500 million and those with more than \$1 billion in assets have increased to 183. Total credit union assets now exceed \$1 trillion.

History has demonstrated that becoming a taxpaying entity does not drive an industry out of business. Savings associations once enjoyed a tax benefit; however, as the industry grew and gained sophistication and powers, the justification supporting the tax benefit evaporated. Congress repealed the tax benefit in 1951 and phased it out over time. Loss of the tax exemption did not drive savings associations out of business; they adjusted and continue to serve their communities and customers.

The Congressional Research Service said, "...many believe that an economically neutral tax system requires that financial institutions engaged in similar activities should have the same tax treatment..."<sup>7</sup> ABA agrees.

#### **IV. Conclusion**

Today, credit unions compete head-to-head with local taxpaying banks. Yet the tax treatment of credit unions does not reflect the metamorphosis of credit unions to modern financial institutions. In 2011, banks paid \$50 billion in federal income taxes, supporting everything from social services to the defense of our country. Credit unions paid nothing in federal taxes. As the Subcommittee continues to focus on tax-exempt organizations, ABA strongly encourages review of the tax status of the credit unions, particularly with respect to those that have diversified to the point that they bear no resemblance to the traditional credit unions Congress envisioned to be worthy of preferred tax status. The credit union tax expenditure no longer supports the public policy of providing financial services to low- and moderate-income consumers. Abolishing the credit union tax expenditure would help reduce the U.S. debt and eliminate distortions in the financial services industry. Having a hearing specifically on the credit union tax-expenditure would be a good first step in this process.

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<sup>7</sup> Ibid., p. 17