STATEMENT

OF

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"A REVIEW OF THE CREDIT UNION TAX EXEMPTION"

BEFORE THE

COMMITTEE
ON
WAYS AND MEANS
UNITED STATES HOUSE OF REPRESENTATIVES

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Written Statement For The Record
Of the National Credit Union Administration
House Ways and Means Committee Hearing
On A Review Of The Credit Union Tax Exemption
Thursday, November 3, 2005

Chairman Thomas, Ranking Member Rangel and Members of the Ways and Means Committee: on behalf of the National Credit Union Administration ("NCUA"), thank you for the opportunity to be here today to present the Agency's views on "A Review of the Credit Union Tax Exemption." NCUA recognizes and supports this and previous Administrations' and Congressional policy favoring the continued tax exemption for credit unions as important public policy.

NCUA's primary mission is to ensure the safety and soundness of federally insured credit unions. It performs this important public policy function by first examining and insuring all Federal credit unions, and second, in coordination with the state regulators, participating in the supervision of federally insured state chartered credit unions. In its capacity as the administrator for the National Credit Union Share Insurance Fund ("NCUSIF"), NCUA provides oversight and supervision to approximately 8,800 federally insured credit unions, representing over 96 percent of all credit unions and 84.5 million credit union members. As credit union cooperatives, federally insured credit unions vary in size; however, their cooperative structure and purpose is identical. They are strongly capitalized and present minimal risk to the NCUSIF, the Treasury and ultimately to the American taxpayers. The NCUSIF has never required taxpayer support.

Especially important to this discussion on credit union tax exemption is the Federal law that specifies strict system capital ("net worth") standards known as Prompt Corrective Action. By law, written and overseen by the Financial Services Committee, federally insured credit unions are alone among insured financial institutions in how they can build and maintain net worth. Specifically, they are limited to using only their retained earnings to meet their statutory capital requirements. Taxation threatens to diminish that sole source of capital by reducing the ability to generate net income and cause other adverse changes. Eventually, as credit union net worth ratios decline to levels that require additions to retained earnings in order to meet statutory and regulatory capital requirements, taxation may result in behavior modifications that could undermine the continuation of the cooperative credit union system.

Any consideration of repealing the credit union tax exemption should include a very careful analysis of the effects on the public policy benefits of the credit union system. From our standpoint as the insurer of member share accounts and the safety and soundness regulator for federal credit unions, NCUA believes that a thorough analysis leads to the firm conclusion that the tax exemption is sound Congressional policy and should remain in place if Congress desires to preserve the cooperative structure most capable of providing financial services to people of modest means.

In 2001, the Treasury Department reviewed, along with several other issues, the credit union tax exemption. The report offered no administrative or legislative changes regarding the exemption.[1]

The billions of dollars in annual consumer benefits provided by credit unions are derived by the credit union structure being member owned, democratically controlled, tax-exempt cooperatives. This cooperative structure supports the organizational incentive of credit unions to provide affordable services to their consumer owners, rather than to maximize profits to outside investors or stockholders. Though credit unions comprise only a small segment of the financial services marketplace, approximately six percent of federally insured institutions' assets, the effect of this minimal competition assures better rates and services for users of all financial institutions.

The cooperative structure has remained unchanged since the inception of credit unions in the United States as financial cooperatives for working Americans, and, most importantly, it remains intact today as credit unions fulfill their purpose of serving a broader base of American consumers, especially those of low and moderate income. It is a structure that has remained unchanged as other financial intermediaries have entered the consumer financial services market, and as both credit unions and others have adapted to consumer demand for change in the methods of delivery of financial services.

Review of this issue leads NCUA to conclude that repeal of the tax exemption may have consequences not intended by Congress, including altering the delivery of financial services to a broad range of Americans.

A likely response to taxation, for many credit unions, would be to convert to bank charters. It may be difficult to justify retaining a cooperative credit union charter, with the associated limitations on membership and powers in conjunction with higher capital requirements, when subjected to the additional expense of taxation. The history of the mutual thrift industry and recent developments in the credit union system demonstrate there are financial incentives for management to convert their cooperative charters to bank charters. The probable effect of taxation would be to accelerate these conversions. The remaining credit unions subject to taxation will also likely seek expanded authorities and the removal of currently imposed limitations to offset the expense of taxation. The

[1] U.S. Department of the Treasury *"Comparing Credit Unions and other Depository Institutions"* (January 2001).

combined effect of these trends would clearly threaten the existence of the cooperative not-for-profit credit union system.

The tax-exempt status of credit unions has enabled these institutions to provide Americans from all walks of life to have greater access to affordable financial services. The present structure is successfully serving 84.5 million credit union members and empowers many Americans, especially those outside the financial mainstream, to be introduced to the financial services marketplace. It is this same success that argues most strongly for the retention of this important statutory mandate if a viable financial alternative is the desired result.

It is because of their unique cooperative structure, and in the interests of maintaining it, that credit unions have had tax-exempt status since 1917. This status was affirmed and formally codified for federal credit unions in 1937, and reaffirmed by Congress in both 1951 and 1998. The original justification for tax-exempt status remains valid, and should not be changed if Congress wishes to maintain a financially sound, cooperative credit union system.

CREDIT UNIONS ARE UNIQUE

Credit unions are distinguishable from other financial institutions in their structural and operational characteristics. As the U.S. Treasury Department noted in their 2001 study of credit unions:[2]

> Many banks and thrifts exhibit one or more of the following five characteristics; ***but only credit unions exhibit all five together***.
>
> First, credit unions are member-owned, and each member is entitled to one vote in selecting board members and in certain other decisions. Although other mutual institutions are also member-owned, voting rights are generally allocated according to the size of the mutual member's deposits, rather then being "one member, one vote."
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> Second, credit unions do not issue capital stock. Credit unions create capital, or net worth, by retaining earnings. Most credit unions begin with no net worth and gradually build it over time.
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> Third, credit unions rely on volunteer, unpaid boards of directors whom the members elect from the ranks of membership.
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> Fourth, credit unions operate as not-for-profit institutions, in contrast to shareholder-owned depository institutions. All earnings are retained as capital or returned to the members in the form of interest on share accounts, lower interest rates on loans, or otherwise used to provide products or services.

[2] *Id.* at 6-7 (January 2001)(citations omitted)(emphasis added).

> Fifth, credit unions may only accept as members those individuals identified in a credit union's articulated field of membership. Generally, a field of membership may consist of a single group of individuals that share a common bond; more than one group, each of which consists of individuals sharing a common bond; or geographical community. A common bond may take one of three forms: an occupational bond applies to the employees of a firm; and associational bond applies to members of an association; and a geographical bond applies to individuals living, working, attending school, or worshipping within a particular defined community.

While credit unions provide many of the basic services that one would expect from a depository institution, including share (deposit) accounts, share draft (checking) accounts, personal loans, auto loans, mortgages, and small business loans, Congress limited the permissible activities of federal credit unions in many areas.

These limitations serve to illustrate the very real differences compared to other depository institutions. These include, among other things, limitations on lending and investment authorities, rates of interest they may charge, constraints on capital, and field of membership restrictions.

In addition to their distinctive structure and services, the basic role of credit unions is also very different from that of banks and thrifts. Most importantly, credit unions, unlike banks, are not motivated by profit or the desire to maximize the investment of their stockholders. Rather, credit unions focus on the mission of serving their members and enabling them to receive loan and share (deposit) rates on favorable terms. Pursuant to the Federal Credit Union Act, a federal credit union is specifically defined as "a cooperative association organized … for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes …."[3]

Throughout the history of credit unions in the United States, credit unions have been one of the first sources of financial services to working people. Many credit unions established their first offices within faith-based organizations, association halls, steel mills, factories, military bases, and other work places, providing basic, and later expanded, financial services to those not within the mainstream of the financial marketplace. In many instances, credit unions had been the only alternative to payday lenders, pawn shops, or loan sharks.

As industry and the economy changed, communities expanded through improved transportation, and social and associational organizations waned in the United States, credit unions necessarily adapted in order to continue to fulfill their mission of providing cooperative financial services.

With various industries shuttering their plants, credit unions relocated their offices outside of the work locations in order to continue serving their members. Many of these

[3] 12 U.S.C. § 1752(1).

members, victims of plant closings and job losses in a shifting economy, became small business owners, with credit unions willingly providing the first source of capital to their venture. Many of these small business owners could not provide the same benefits received from large industrial companies, but still pursued the opportunity of providing the benefit of credit union ownership and financial service to their employees.

Credit unions, like all financial institutions, have evolved to meet the basic financial needs of their members. Credit unions provide the financial services now available due to changing and improving technology while remaining true to the cooperative structure. They have successfully provided these services without abandoning their unique structure as member-owned, democratically controlled cooperatives. An underlying tenet to these advances was, and continues to be, the belief that those of modest means should not be restricted to modest services.

HISTORY OF THE CREDIT UNION TAX EXEMPTION

The cooperative nature of credit unions was the original basis for the credit union tax exemption. Importantly, credit unions have not abandoned this statutory mandate.

When credit unions first appeared in this country they were purely creations of state law, and thus, until the passage of the Federal Credit Union Act in 1934, there were only state chartered credit unions. When a federal income tax was first passed, credit unions were not specifically exempted from tax, although other classes of organizations conducted for the mutual benefit of individuals were exempted. Credit unions received tax-exempt status in 1917, pursuant to an administrative ruling issued by the U.S. Attorney General. In his ruling, the Attorney General found that the tax exemption for these other organizations extended to credit unions as they "are organized and operated for mutual purposes and without profit."[4]

With the passage of the Federal Credit Union Act in 1934, the federal credit union charter was created. Though the Act did not specifically create a tax exemption for this new federal charter, the Attorney General's ruling was extended to effectively provide an exemption. This exemption, however, did not apply to the taxation of federal credit unions by states in which the credit union is located. States could tax federal credit unions as long as the tax was in the same manner and did not exceed the rate imposed on other domestic banking corporations.[5]

In 1937, the Federal Credit Union Act was amended to create a specific tax exemption for federal credit unions.[6] In his testimony in support of the tax exemption, the Governor of the Farm Credit Administration (who supervised federal credit unions at the time) stated:

[4] 31 Op. Atty. Gen. 176 (1917).
[5] Pub. L. No. 467, c. 750, 48 Stat. 1216 (June 26, 1934).
[6] Pub. L. No. 416, c.3, § 4, 51 Stat. 4 (December 6, 1937).

> Many States tax domestic banking corporations in relation to their share capital. In view of the fact that federal credit unions may not accept deposits, their share capital represents a much greater proportion of their total resources than is the case in other financial institutions. Experience with Federal credit unions since the passage of the original act indicates that such taxation, therefore, places a disproportionate and excessive burden on them. Furthermore, these credit unions are mutual or cooperative organizations operated entirely by and for their members and in view of this fact it is appropriate, we feel that local taxation should be levied on the members rather than the organization itself.[7]

A Report from the U.S. House of Representatives delineated two reasons for ultimately granting federal credit unions a tax exemption. First, they found that taxing credit unions on their shares (deposits) in the manner that banks are taxed on their capital shares places a disproportionate and excessive burden on credit unions, because credit union shares function as deposits. Second, they found that credit unions are mutual or cooperative organizations operated entirely by and for their members.[8]

Pursuant to the changes made in 1937 the Federal Credit Union Act currently exempts all federal credit unions from:

> … all taxation now or hereafter imposed by the United States or by any State, Territorial, or local taxing authority; except that any real property and any tangible personal property of such Federal credit union shall be subject to Federal, State, Territorial, and local taxation to the same extent as other similar property is taxed.[9]

Thus, federal credit unions were exempted from most, but not all taxes. This is the current state of the tax exemption for Federal credit unions.[10]

For many years credit unions were not the only depository institutions exempted from taxation. Among others, mutual savings banks and savings and loan associations were also exempted. In 1951, Congress found that mutual thrifts had essentially lost the essence of their mutuality. Accordingly, mutual savings banks and savings and loan associations lost their tax exemption. However, the exemption for federal credit unions was left intact, and expresses statutory tax-exempt status was afforded to state-chartered credit unions, essentially affirming that credit unions remained true to their cooperative nature.

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[7] Testimony of Governor Meyer, Farm Credit Administration before a Subcommittee of the Committee on Banking and Currency, U.S. Senate, 75th Cong., 1st Sess. (May 11, 1937).

[8] H.R. REP. NO. 1579, 75th Cong., 1st Sess. P.2.

[9] 12 U.S.C. § 1768.

[10] This section of the Federal Credit Union Act was amended in 1959, however, the changes did not affect this particular part of the section.

In 1998, the tax treatment of credit unions was again affirmed. The Credit Union Membership Access Act of 1998 stated the findings and intent of Congress with respect to the tax exemption:

> Credit 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.[11]

CREDIT UNIONS' MARKET SHARE HAS REMAINED CONSTANT

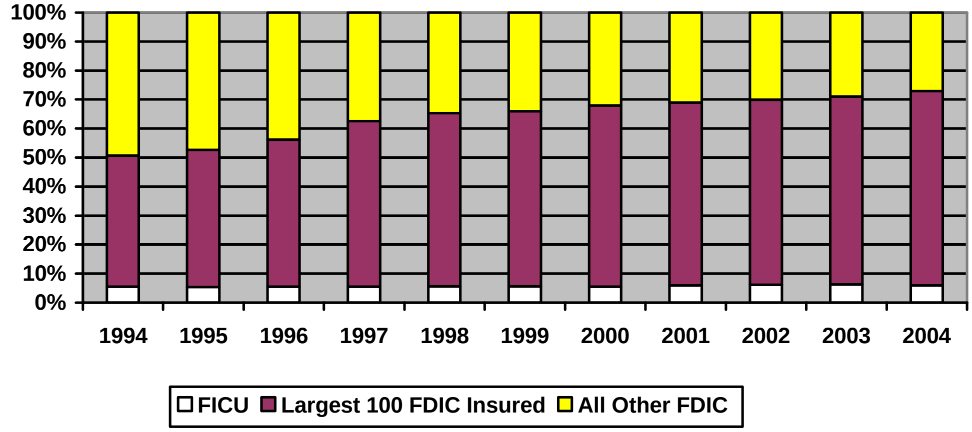
More diversified fields of membership in both multiple group and community charters means that individual credit unions are more diversified in their loan assets and therefore present less risk to the NCUSIF. This is contrasted with the historical predominance of single-employer common bonds, which increased safety and soundness problems in the credit union system in the 1970s when numerous industrial companies failed and their "single sponsor" credit unions followed suit as unemployed members defaulted on their loans.

Moreover, recent trends in field of membership expansions, including both conversions to community charters and expansions by adding underserved areas, allow credit unions to do a better job of fulfilling their historic and important mission of serving persons of modest means. Thus, recent field of membership trends have both reduced risk in the credit union system and enabled credit unions to better fulfill their statutory purpose.

With this success, however, credit unions are not gaining market share at the expense of banks and thrifts. In 2004, federally insured credit unions held merely six percent of total financial industry assets; essentially the same level since 1992. While the percentage of industry assets held by smaller banks and thrifts is declining, this decrease did not result in an increase in market share for credit unions. The combined assets of all federally insured credit unions as of December 31, 2004 -- $647 billion in total -- are less than the total assets of any of the three largest banks as of December 31, 2004.[12]

[11] Pub. L. No. 105-219, 112 Stat. 913 (August 7, 1998).
[12] Source: http://www.fdic.gov. As of December 31, 2004, JP Morgan Chase Bank, N.A. had $967.3 billion in assets, Bank of America, N.A. had $771.6 billion in assets and Citibank, N.A. had $694.5 billion in assets.

Federally Insured Deposit Institutions
Market Share



Source: FDIC financial call report data, NCUA financial call report data

Along with a limited market share, the size of the credit unions within the system remains small. Average and median asset size of federally insured credit unions – as of June 30, 2005 – reflects an average asset size of $75.5 million and a median asset size of less than $12 million in assets.

	All Federally Insured Credit Unions (FICUs) As of June 30, 2005			
	# of FICU	% of Total	Assets	% of total
<$10 Million	4,097	46.2%	15,396,929,628	2.3%
$10-$50 Million	2,810	31.7%	66,684,864,271	10.0%
$50-$100 Million	774	8.7%	54,445,882,179	8.1%
$100-$500 Million	922	10.4%	198,115,394,051	29.6%
$500 Million - $1 Billion	155	1.7%	105,889,848,338	15.8%
$1-5 Billion	97	1.1%	166,321,482,089	24.8%
>$5 Billion	6	0.1%	62,861,279,695	9.4%
Total	8,861	100.0%	669,715,680,251	100.0%

CREDIT UNIONS ARE SERVING PEOPLE OF MODEST MEANS

Federal credit unions were formed during the height of the great depression to provide working people with access to affordable financial services through a cooperatively owned financial institution. This type of financial institution provided workers an opportunity to save a portion of their wages and have access to reasonably priced loans for "provident and productive purposes."

Credit unions have not deviated from their original structure and purpose, providing their members with an opportunity to improve their financial well-being through share and loan products designed to meet their financial needs in an ever changing financial and economic environment. The ability to meet the statutory purpose is dependent on a number of factors, including diversification of fields of membership.

Recognizing the difficulty credit unions encounter in serving a greater proportion of low and moderate income members Congress, in 1970, established authority for low-income designated credit unions to accept non-member share deposits. This authority, which by NCUA regulation is available to credit unions who serve a majority of members with a median household income at or less than 80% of the national median household income, provides qualifying credit unions with an ability to raise share deposits from outside of the credit union's membership to support further lending, products and services to their members.

Currently, approximately 12% of credit unions have received this designation from the NCUA. These more than 1,000 credit unions are providing their members the financial services identified as best meeting their needs at an affordable cost.

Since 1994, NCUA regulations have authorized all Federal credit unions to add underserved areas to their fields of membership, using the terminology "low income communities." In 1998, the Credit Union Membership Access Act was passed which authorized multiple group chartering previously overturned by the Supreme Court. In this Act, Congress recognized the authority of multiple group credit unions to serve "underserved areas" and established a specific definition for that term. For consistency, NCUA regulations were revised to apply this terminology to all credit unions when adding low income areas in need of service. Since 1999, more than 650 federal credit unions have added 1,406 underserved areas to their fields of membership. This authorization has allowed credit unions to serve low and moderate income areas and facilitate affordable financial services to individuals who often have been left behind to predatory lenders. Many of these credit unions are of a sufficient asset size to provide these underserved areas with improved and an expanded array of financial products and services at reasonable costs.

NCUA has also done much to encourage credit unions to serve the unbanked and those of low and moderate income. NCUA's Access Across America Initiative promotes the benefits of the low-income designation for eligible credit unions and encourages credit unions to make use of the "underserved area authority." Also, NCUA established in the mid-1990s the Economic Development Specialist ("EDS") position to further credit union service in low-income and underserved areas. In 2001, the NCUA Board established a national small credit union program initiative and centralized the EDS position to the newly created Office of Small Credit Union Initiatives. Presently there are 15 EDS positions dedicated to working with groups interested in chartering credit unions and those credit unions serving or interested in serving members in underserved areas. This office also conducts workshops throughout the nation that provide smaller credit unions with best practices, potential service opportunities, and technical assistance on operations and staff training.

Based on recent financial information collected by the NCUA in our quarterly call reports, average and median share deposit and loan balances in the credit union system demonstrate credit unions are serving members who hold low share deposit and loan balances. Of greater significance is the comparison of average and median share deposit and loan balances between low-income designated credit unions and the total population of federally insured credit unions. In general, average and median balances in federally insured credit unions mirror those in low-income designated credit unions.

Average and Median Credit Union (CU) Share Deposit Balances As of June 30, 2005							
All Federally Insured CUs	**Share Deposits**	**Share Drafts**	**Money Market**	**Share Certificates**	**IRA / Keogh**	**All Other Shares**	**All Shares**
Average Balance	3,293	2,491	23,127	17,320	11,110	40,440	3,279
Median	2,916	2,028	21,034	13,186	9,866	824	2,905
Low-Income CUs							
Average Balance	2,417	1,818	23,645	15,476	10,797	1,738	2,354
Median	2,126	1,558	20,249	12,135	10,003	695	2,086
All Community CUs							
Average Balance	3,037	1,969	22,198	14,881	10,371	3,034	2,999
Median	2,891	1,764	21,191	13,461	9,527	807	2,863

Average and Median Credit Union (CU) Loan Balances As of June 30, 2005								
All Federally Insured CUs	**Loans / Leases**	**Credit Card**	**Other Unsecured Loans**	**New Vehicle**	**Used Vehicle**	**1st Mortgage**	**Other Real Estate**	**All Other Loans**
Average Balance	8,046	1,466	2,659	13,930	8,217	79,620	27,561	8,221
Median	7,089	1,344	2,287	14,074	8,142	66,809	24,836	6,162
All Low Income CUs								
Average Balance	6,327	1,256	2,293	13,679	7,396	49,818	26,387	7,637
Median	5,800	1,150	1,999	13,919	7,371	42,085	22,950	5,253
All Community CUs								
Average Balance	8,732	1,420	2,415	14,592	8,216	72,277	26,443	8,341
Median	8,124	1,302	2,169	14,592	8,152	61,779	24,588	6,630

The discrepancy between federally insured credit unions and low-income designated credit unions on average and median first mortgage balances seems to indicate federally insured credit unions make larger loans. However, based on data gathered from the Census Bureau’s American Housing Survey for the United States completed in 2003, the median mortgage loan balance is $82,010 for all occupied residential units compared to the $66,809 reported for median mortgage loan balances for federally insured credit unions. This information shows federally insured credit unions holding smaller balanced first mortgage loans. Collectively, the data supports the conclusion federally insured credit unions grant many smaller-balanced loans and are, therefore, serving members requesting lower balanced loans.

Home Mortgage Disclosure Act ("HMDA") data also reflects the continued focus of credit unions on making credit available to borrowers of low and moderate means. As shown in the following table containing 2003 HMDA data, credit unions deny fewer loans to both minority and white borrowers than other financial institutions. Although serving a smaller market base, credit unions focused on reaching out to all segments of their membership.

2003 HMDA Data
Mortgage Denial Rates

		White	Tot Min	Am Ind	Asian	Black	Hisp	Joint	Other	N/A	Total
OCC	Applications	6,373,248	1,931,002	33,509	377,521	532,776	632,830	221,805	132,561	1,086,700	9,390,950
1,091	Denial Rate	12.1%	21.8%	25.0%	12.0%	28.5%	25.6%	12.5%	18.2%	18.0%	14.9%
FRB	Applications	1,916,573	511,367	6,794	89,451	155,796	183,974	50,648	24,704	353,173	2,781,113
565	Denial Rate	9.1%	18.1%	19.7%	10.1%	22.2%	21.0%	9.3%	15.2%	14.8%	11.6%
FDIC	Applications	1,859,365	403,427	7,108	78,147	111,072	143,839	41,755	21,506	248,342	2,511,134
2,587	Denial Rate	10.1%	19.7%	20.6%	12.8%	27.6%	19.5%	11.8%	17.5%	19.8%	12.7%
OTS	Applications	2,993,023	968,616	10,435	236,263	227,144	345,828	96,002	52,944	637,048	4,598,687
674	Denial Rate	10.3%	17.7%	18.5%	13.3%	22.0%	19.1%	12.0%	17.7%	17.0%	12.8%
NCUA	Applications	685,145	161,138	3,656	24,851	51,469	43,925	30,013	7,224	138,853	985,136
1,920	Denial Rate	5.5%	13.2%	11.6%	7.5%	18.0%	15.2%	6.5%	12.6%	11.5%	7.7%
HUD	Applications	5,825,625	2,883,838	46,476	330,703	893,277	1,005,229	255,504	352,649	3,045,896	11,755,359
1,181	Denial Rate	19.6%	26.4%	30.5%	15.0%	31.2%	21.8%	17.6%	42.7%	29.5%	23.9%
National	Applications	19,652,979	6,859,388	107,978	1,136,936	1,971,534	2,355,625	695,727	591,588	5,510,012	32,022,379
8,018	Denial Rate	13.5%	22.5%	25.6%	13.0%	28.1%	22.1%	13.8%	32.6%	24.0%	17.2%

In fact, as reported in the 2005 National Community Reinvestment Coalition paper, "Credit Unions: True to Their Mission?", HMDA data for calendar year 2003 shows that credit unions made a higher percentage of single family mortgage loans to low and moderate income borrowers (24.2% compared to 23.2%) than banks. In addition, credit unions significantly increased home purchase loans to low and moderate income borrowers to 28.3% of their loan portfolios at 2003 from 23.6% at 2001, while bank lending in this area stayed relatively constant (28.6% in 2001 and 28.9% in 2003).

In recent years, legislative, regulatory, and policy changes have resulted in more credit unions serving communities with low and moderate income borrowers. In fact, NCUA data demonstrates that credit unions are reaching out to serve low-income residents and are adopting underserved areas into their fields of membership. Those credit unions that have adopted underserved areas have more than doubled their membership growth as compared to the credit union system as a whole.

As members from these areas become familiar with the products and services offered, credit unions will likely receive more loan applications and further improve their penetration of the low and moderate income lending market.

NEED FOR THE CONTINUATION OF THE TAX EXEMPTION

Credit unions are tax-exempt because of their cooperative structure and not-for-profit mission. While this cooperative structure, and not the other limitations on powers, is what entitles credit unions to a tax exemption, it is important to note that these limitations restrict credit union activities compared to other types of depository institutions. Despite these limitations, the tax exemption offers an incentive for credit unions to remain true to their mission of serving members of all income levels. If credit unions' tax status was changed, credit unions would have less incentive to remain credit unions. If these not-for-profits were to be taxed, many credit unions would probably choose to convert to other types of institutions in order to have expanded powers. Without credit unions, predatory lenders may become the financial service provider by default for many Americans who now rely on credit unions for essential credit union services.

An exodus of the larger, well-capitalized credit unions would have a detrimental effect on the entire credit union system. These institutions provide a support structure for the entire credit union system, as demonstrated in the aftermath of Hurricanes Katrina, Rita, and Wilma.

Credit unions provide support to one another through credit union service organizations, shared branching networks, other partnership arrangements, and credit union league supported programs. If significant numbers of larger credit unions depart the system, the pressures related to earnings and capital accumulation would increase significantly for those credit unions remaining within the system. This may result in an increase in the number of credit union failures.

Loss of critical mass of larger credit unions may also result in the credit union system no longer being economically viable. The largest 13% of federally insured credit unions (over $100 million in assets) hold almost 80% of the system's assets. Conceivably, 87% of all federally insured credit unions would remain, but these would only hold 20% of the current financial resources of the system.

The potential costs to the credit union system outweigh any anticipated revenue gains that may be realized by taxing credit unions. Estimates put annual tax revenue gains at between $1.2 billion to $1.5 billion annually.[13] Using cost benefit analysis, leaving aside

[13] U.S. Department of the Treasury "*Comparing Credit Unions and other Depository Institutions*" at 32 (January 2001); Congressional Budget Office, "*Budget Options*" at 301 (February 2005).

the mission of serving those of modest means, the dollar return to consumers and the economy far exceed these tax revenue estimates. One recent study of North Carolina financial institutions estimated that each credit union member saves $130 a year through lower loan rates, lower fees, and higher returns on savings.[14] If applied to all members nationally this would equate to $11 billion in savings passed on to credit union members.

Finally, if credit unions are taxed, all consumers, not just credit union members, will be detrimentally affected. It is estimated that by losing the positive influence of credit unions, bank customers will pay an additional $4 billion in higher rates, higher fees, and lower returns on deposits.[15] This is in addition to a decline in service quality and convenience, reduced access to basic financial services, and no check on the proliferation of predatory financial service providers.

CONCLUSION

Credit unions exist for the purpose of promoting thrift and providing a source of credit for their members. Since their inception, credit unions have been organized as democratically controlled, not-for-profit cooperatives, managed by a volunteer board of directors elected by and from the membership. These characteristics define the uniqueness of credit unions that serves as the basis for their tax exemption. All of these characteristics are as true today as they were almost a century ago when the tax exemption was first extended to credit unions.

As recently as 1998, Congress noted that the credit union system began as a cooperative effort to serve the credit needs of individuals of modest means, and that credit unions continue to fulfill that public purpose. Field of membership policy changes since 1998, and associated trends in charter expansions, have served to fulfill this special mission. Credit unions of all sizes continue their tradition of supporting one another through service organizations, shared branching networks, participation lending, inter-credit union deposits, technical assistance, and other methods of ensuring continuation of service to all segments of their membership, including low and moderate income members.

Federally insured credit unions provide billions of dollars of benefits annually to consumers by assuring that competitive rates and services are offered in the financial marketplace. Repeal of the tax exemption would result in pressure on credit unions to move away from their not-for-profit cooperative structure causing a systemic risk throughout the system. Congress should carefully consider these implications in determining whether to repeal the credit union tax exemption.

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[14] The University of North Carolina at Chapel Hill, William E. Jackson III,*"The Benefits of Credit Unions to North Carolina Consumers of Financial Services,"* at 3 (April 2005).

[15] The American University, *"An Analysis of the Benefits of Credit Unions to Bank Loan Customers,"* (September 2004); Idaho State University, *"An Estimate of the Influence of Credit Unions on Bank CD and Money Market Deposits in the US,"* (January 2005).