

Alabama Credit Unions & Banker Myths

Bumper profits and a massive concentration of market share aren't enough for Alabama's bankers. They want more. And they seem willing to do anything to get it. Indeed, banking industry publications recently distributed to state policy-makers use anecdotes, half-truths, and innuendo in an all-out assault on the state's credit unions. While it's true that Alabama credit unions are growing, they aren't, as bankers suggest, taking over the world. They remain true to their original purpose. And they certainly aren't harming the state's banks.

Growth: Banking institution deposits in Alabama grew by \$10.2 billion in the five years ending June 2003. *Since 1998 Alabama banking deposits have grown 22% more than the total growth recorded by the state's credit unions since credit unions began operating in the state in 1927!*

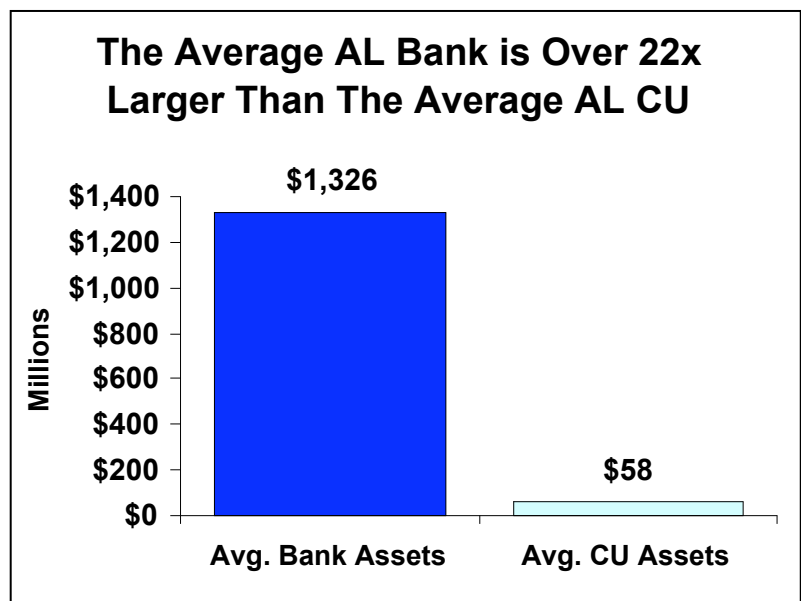
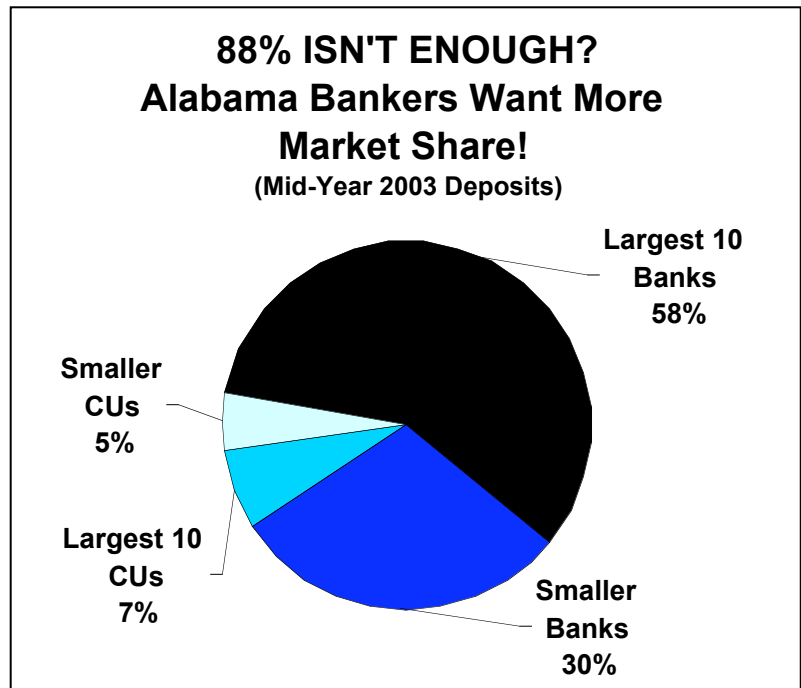
Market Share: Banking institutions control 88% of all financial institution deposits in the state of Alabama – a market share that is virtually unchanged over the past decade.

Small banks in Alabama have a lot more significant competitive threats to worry about than the threat of credit union competition. Indeed, at the mid-year 2003, the largest 10 banking institutions control 58% of total deposits in the state (or 66% of total banking deposits). In contrast, credit unions control just 12% of the market and the largest 10 credit unions control just 7% of the deposit market in Alabama.

Bank trade associations helped create these mega-banks and multi-state conglomerates. Then, when their smaller constituents complain about competitive pressures they use credit unions as scapegoats.

If bank trade groups spent less time attacking Alabama credit unions they could spend more time using their considerable resources advising and counseling small banks on strategies to deal with the stiff competition from the multi-state mega-bank conglomerates they helped create and from non-depository rivals such as mutual fund companies and insurance companies.

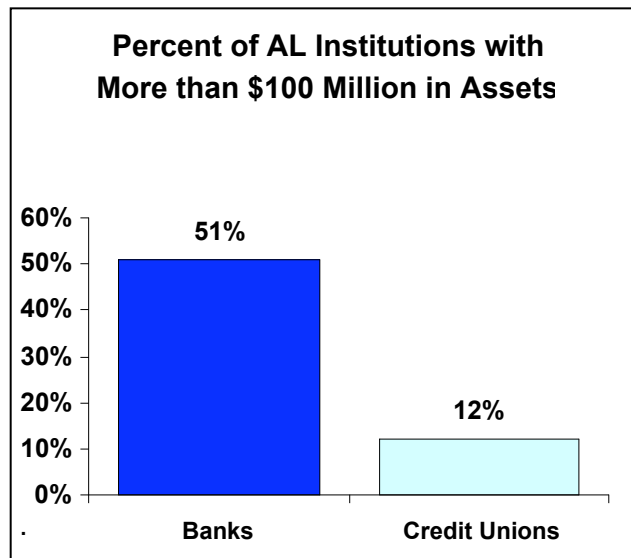
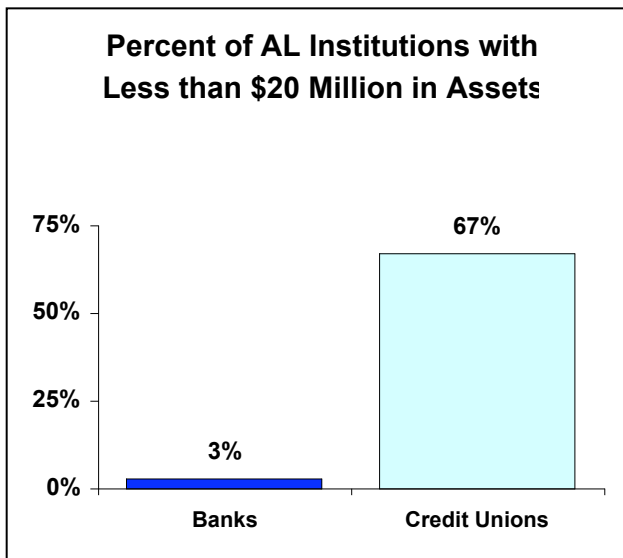
Size: The average Alabama-headquartered banking institution is over twenty-two times larger than the average



Alabama credit union: The average Alabama bank has \$1.3 BILLION in assets, whereas the average Alabama credit union has just \$58 MILLION in assets.

Overall 96% of the depository institutions in Alabama that have less than \$20 million in assets are credit unions. In fact, 112 of the state’s 168 credit unions (i.e., 67% of all Alabama credit unions) have less than \$20 million in assets. Only five of Alabama’s 162 banking institutions (i.e., 3% of all Alabama banking institutions) have \$20 million or less in total assets.

At the other end of the spectrum, over half of the state’s banking institutions have \$100 million or more in assets. Only 12% of Alabama credit unions are this large. **Overall, Alabama banking institutions control 97% of the assets in the state’s largest financial institutions (defined as institutions with \$100 million or more in total assets). Alabama credit unions control just 3% of the total assets in these large institutions.**

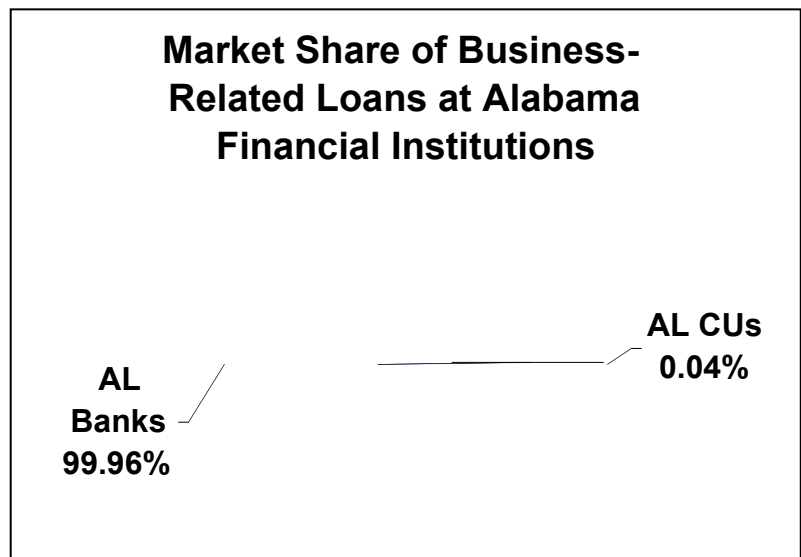


Business Lending: Alabama credit unions have granted business purpose loans to their members since they began operating in the state in the 1920s.

Yet Alabama credit unions control less than one-tenth of one percent of business purpose loans held by the state’s depository institutions at year-end 2003.

Moreover, laws restrict credit union business lending to 12.25% of total assets. No other depository has such restrictions.

These numbers reveal that Alabama credit unions have not infringed on the state’s commercial banking empire.



On the other hand, “commercial banks” – so-called because they historically concentrated on commercial lending -- have now morphed into the state’s credit union core business areas. Indeed, morphed commercial banks now control BILLIONS in consumer deposits and BILLIONS in consumer loans in the

investment advisory services, and mutual fund activities. And they have their sights set on the real estate brokerage market as well.

Banker success: Alabama banks are extremely profitable. Alabama banking institution dollar profits have set records in each of the past ten years. Moreover, bank profitability as a percent of assets was equal to 1.30% of average assets in 2003 and averaged 1.22% on average assets in the ten years since 1994. This long-term 10-year earnings average is equal to the U.S. bank average and is 18% higher than the Alabama credit union average during the same period.

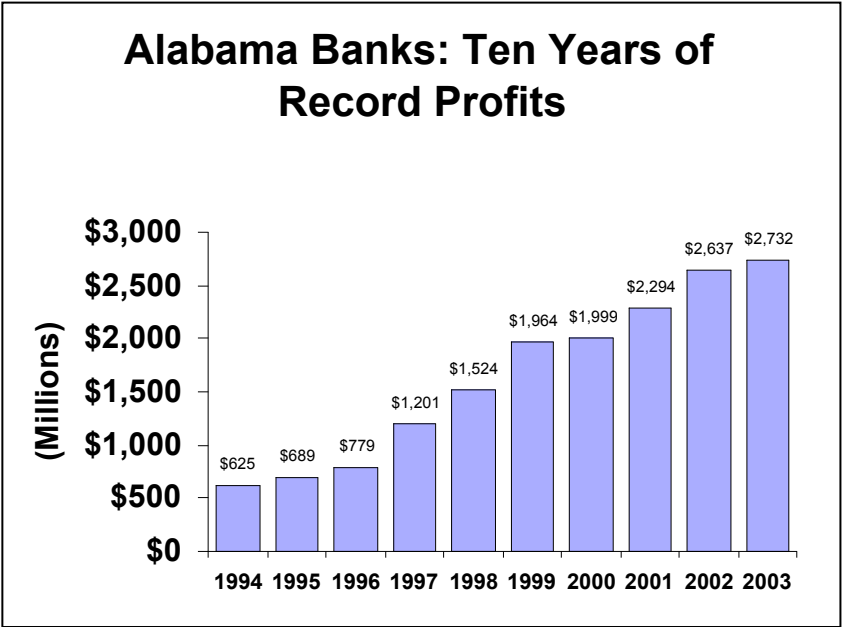
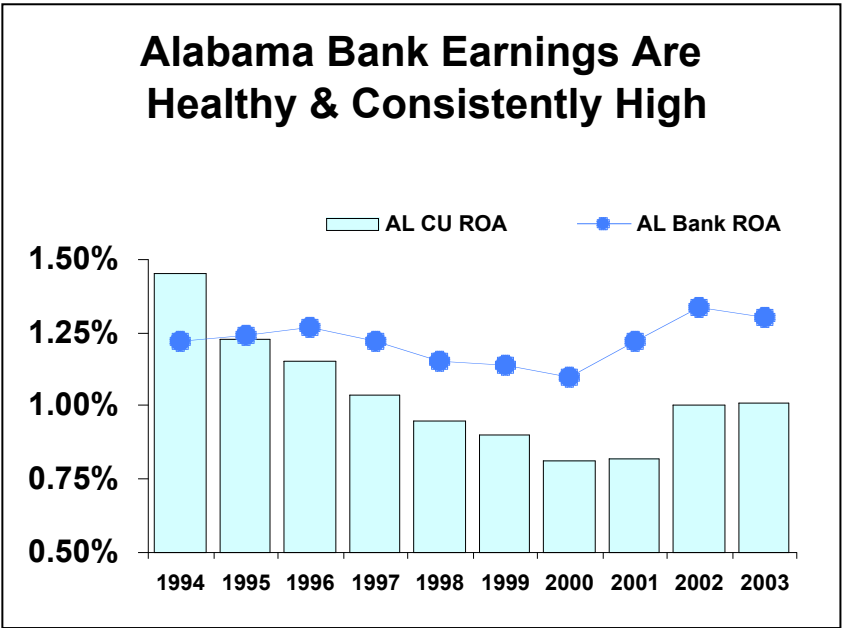
“Community banks in Alabama reported record income”
 - Summer 2003 Federal Deposit Insurance Corporation (FDIC) Alabama State Profile

“Alabama community banks continue to perform well”
 - Summer 2004 Federal Deposit Insurance Corporation (FDIC) Alabama State Profile

Some other interesting facts that belie the notion that Alabama banks are suffering include the following:

- Overall, 23 new banks have been chartered in Alabama since 1994. If bankers truly believed their myth of extreme credit union competition they wouldn't be creating these new institutions.
- Of course, Alabama bankers also like to point out that because they must pay income taxes they are at a competitive disadvantage relative to credit unions. However, Alabama banks have paid more in dividends to stockholders than they paid in income taxes in each of the last ten years.
- Over the last decade, total Alabama bank cash dividends have exceeded bank tax payments by \$4.4 billion (i.e., 57%). If Alabama banks were like credit unions and didn't have stockholders who demand a market rate of return on their investment they would be much more competitive.

Taxation: The credit union tax exemption has nothing to do with institution size, growth, market share, field-of-membership, or portfolio composition. On the contrary, the



credit union tax exemption arises from the fact that credit unions are member-owned, member-directed cooperatives, with each member having one vote. In addition, they promote thrift among members and create a source of credit for provident or productive purposes, including for those of modest means.

Alabama credit unions have not strayed from that historical mission. Bankers may not like the fact that credit unions are tax exempt, but Congress, the President, and the Treasury department does. In fact, each have recently stated their support for continuation of the credit union tax exemption. The “Credit Union Membership Access Act” specifically states that not-for-profit credit unions continue to serve the purpose for which they were created (and for which they earn their tax exemption).

Oddly, at the same time they complain about the credit union tax exemption, bank trade associations have been vigorously lobbying for expansion of bank Subchapter S status. At the end of 2003 there were 23 Subchapter S banks in Alabama. These institutions reported a total of nearly \$4.2 billion in assets and recorded income equal to 1.33% on assets in 2003.

Alabama bank Subchapter S status, which eliminates the double-taxation of bank income, resulted in an estimated total of \$7.1 million in foregone U.S. Treasury revenue in 2003 (this amount is adjusted for the increased taxes bank shareholders pay under this form of organization). Bank lobbying efforts to expand Subchapter S status underline Alabama banker hypocrisy when they claim credit unions should be taxed to help shore-up government finances.

Banks aggressively seek to avoid taxes in many other ways. For example, a recent PBS “Frontline” broadcast – “Tax Me If You Can” outlined how one large bank with \$4 billion in profits in 2002 paid no federal income taxes. In fact, with \$4 billion in profits it actually received a refund in the year. However, the bank’s regulatory reports show \$1 billion in tax expense. This disparity between tax expense as shown on regulatory reports and actual payments to the IRS and state revenue agencies is, according to tax experts, quite large in many cases. Thus while the banker trade groups loudly broadcast bank tax expenses reported on regulatory reports, the actual payments are likely much lower. Perhaps Alabama banks should be required to report their *actual* tax payments to the public. Policy makers may be surprised to learn that closing tax loopholes would result in revenue increases many times larger than the increase that could be obtained by taxing credit unions.

Credit Union Mission: Alabama credit unions remain true to their historical mission. For example, HMDA data consistently shows that, compared to other lenders, the state’s credit unions approve a higher percentage of home loan applications from minority applicants and from low-income applicants. In 2002, for example, Alabama HMDA reports revealed that the state’s credit unions approved 55% of home loan applications from low-income applicants, whereas other lenders in the state approved just 39% of applications from low-income applicants. Thus low-income applicants are about 41% more likely to be approved for a home loan at a credit union than at other financial institutions in the state.

Comparative Interest Rates at Alabama Financial Institutions - 9/13/04			
Product	Credit Union Average	Bank Average	CU Difference
60-month new car	4.97%	6.09%	-1.12 pp
48-month used car	5.21%	6.92%	-1.71pp
Unsecured loan	10.36%	11.83%	-1.47pp
Home equity line	4.24%	4.09%	+0.15pp
Regular savings	1.03%	0.37%	+0.66pp
Interest checking	0.66%	0.34%	+0.32pp
Money market	1.13%	0.45%	+0.68pp

Credit unions pass along their tax advantage to all members. Industry surveys show that the state's credit unions average rates paid on deposits typically exceed banking industry averages and credit union average rates charged on loans typically are lower than banking industry averages.

These differences result in huge savings for Alabama credit union members. For example, on a 60-month \$20,000 new car loan at the current Alabama credit union average rate of 4.97%, a member will pay \$377 per month (or \$22,629 over the life of the loan). In contrast, for that same loan, the average banking customer will pay \$387 per month (or \$23,250 over the life of the loan). An Alabama credit union member would thus save \$621 over the life of this loan.

Economists at the Credit Union National Association have estimated that the overall savings to credit union members in Alabama was \$96 million in 2002 because credit unions typically offer higher interest rates on savings, lower interest rates on loans and have fewer and lower fees.

Moreover, studies have shown that the existence of credit unions helps to keep bank loan interest rates lower, and savings rates higher than it otherwise would be. The banking lobby's feebly veiled attempts to eliminate credit union competition under the guise of a "level playing field" would thus come at a high cost to both credit union members and bank customers.

Conclusions: By almost any measure, the recent success of Alabama banks, both large and small, is astounding.

If Alabama bankers truly believed that life as a credit union offered substantial competitive and operational advantages, they would simply convert their banks to credit unions. None, however, do that. In part this is likely because they know that running a credit union does not bring the competitive windfall their rhetoric suggests. They cringe at the idea of opening their board of directors to democratic elections in which each depositor gets one vote. They wonder what would happen if they stopped paying directors (the vast majority of credit unions are run by volunteer boards). They wince when they contemplate the pay cut that they would likely have to take. And they certainly do what they can to avoid living under credit union rules and regulations (many of which are more stringent those currently faced by banks). For instance, credit union minimum regulatory capital standards are higher than those faced by banks.

Alabama credit unions are "home-grown", member-controlled and (by definition) locally operated financial institutions that remain true to their original purpose. Bankers want policy makers to treat credit unions like banks. But treating credit unions like banks will undoubtedly cause them to behave like banks. That's a bad idea. It might help Alabama's empire-building, morphed, mega-banks by boosting their profits -- but it would certainly harm the state's consumers.