House State and Local Government Committee
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House Bill 221 – Opponent Testimony

Paul Thompson – President, First Federal Savings and Loan of Newark

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Good afternoon, Chairman Blair, Ranking Member Clyde and members of the State and Local Government Committee. Thank you for the opportunity to speak before you today.

My name is Paul Thompson. I am the President of First Federal Savings and Loan Association of Newark, Ohio. First Federal is a mutually-owned federally chartered thrift, founded in 1934, has $167 million in assets with 5 full-service offices. We operate in both Licking and Franklin counties, serving over 11,000 families. I am here before you today to express my strong opposition to House Bill 221.

By offering the same products and services as banks and thrifts, and serving broad geographic areas, credit unions have become indistinguishable from banks and thrifts. Credit unions even refer to themselves as "banks" in their advertisements. One credit union, serving a six-county area in Northwest Ohio touts itself as "Your Lifetime Banking Partner." Another credit union in our market area routinely advertises "Live Here, Work Here, Worship Here…BANK HERE."

I believe some background on financial institutions such as First Federal would be beneficial. We operate under a mutual charter. This means our institution is owned by our customers. We do not have stockholders. Accordingly, we do not issue stock nor do we pay dividends. We were created for the benefit of the community, as a safe place to deposit money to be loaned back into the community. This structure is very similar to a credit union. Operating a small mutual thrift gives me great perspective to explain the similarities that exist between mutual thrifts and credit unions:

- Like traditional credit unions, mutual institutions are owned by its depositors.
- Mutual institutions were created to serve the communities in which they operate; credit unions were created to serve a specific class of membership.
- Like traditional credit unions, mutual institutions offer basic consumer banking services.

- Like traditional credit unions, mutual institutions operate without the pressures of producing returns to stockholders.

Yet, there are some very stark differences:

- Unlike credit unions, mutual institutions pay the federal income tax and the state financial institutions tax.
- Unlike credit unions our service to low-to-moderate income customers, which is required by the Community Reinvestment Act (CRA), is monitored and reported to the public and examined by our regulator. There is an implicit expectation that credit unions will serve individuals of "modest means" in exchange for favorable tax and regulatory treatment. However, effectiveness is neither subject to examination or reporting to the public by their regulator.
- Mutual thrifts are required by the FDIC to pay a risk-adjusted insurance premium, based in part, on the risk profile of the institution. Credit unions maintain a pooled revolving fund managed by the National Credit Union Administration (NCUA) equal to approximately 1% of insured shares and deposits. There is no provision for credit unions that engage in higher risk activities to provide additional funding to protect their insurance fund.
- Some credit unions are still privately insured. This option became prohibited for thrifts following the savings & loan crisis in the 1980s.

There are 44 mutual thrifts operating in Ohio today. Mutual institutions have existed in this country for more than 100 years, well before credit unions came into existence. Mutual associations lost their tax exemption in 1952, when Congress determined that they were becoming very "bank-like," unfairly permitting them to compete with other taxpaying financial institutions (commercial banks). At that time, mutuals could not even offer checking accounts, much less business loans. Yet many of today's credit unions look more like commercial banks than the mutuals that lost their tax-exempt status more than 60 years ago. For all intents and purposes, mutual institutions are simply tax-paying credit unions.

Based on these fundamental differences, I believe it would not be sound public policy to allow credit unions to become public depositories. Credit unions should not be permitted to hold tax-payer dollars without paying their fair share in taxes.

Though the sponsors and advocates of this bill have attempted to shift this committee's attention away from the tax issue, it is unclear how the legislature can engage in a discussion that involves ANY credit union expansion of power without addressing the tax subsidy, while at the same time not being held to the same regulatory framework that tax-paying financial institutions face.

According to the Ohio Department of Taxation, if an activity is exempt from tax, the foregone tax revenue is a measured tax expenditure incurred by the State, which is tax subsidization. The Ohio Bankers League has calculated the subsidization cost to the State of Ohio to be more than $20 million per year. Add in the federal tax subsidy and the government has created a pricing advantage in excess of 35%. This is a pricing advantage that no longer is justified, given the evolution of the credit union industry from self-help cooperatives serving people of "modest

means” into tax-preferred banks serving Ohio’s general public. No similar cooperative business enjoys a similar tax subsidy. Other types of cooperatives are prohibited from serving non-members. If they are discovered serving non-members, taxation is triggered. Yet, credit unions are not held to that same standard.

There are also considerable safety and soundness concerns associated with permitting credit unions to become public depositories. Recently, the NCUA Board approved several revisions to its loan participation rule. Credit unions are no longer required to underwrite loan participations to the same standards they use when originating their own loans. Additionally, they are now permitted to purchase single-originator concentrations in loan participations of up to $5 million or 100% of net worth, <u>whichever is greater</u>. By contrast, regulatory restrictions on loans to one borrower for tax-paying financial institutions are limited to 15% of capital. By rule, a credit union could invest 100% of its capital in one loan and if that loan goes bad, the credit union could fail. Clearly, if this were to happen, public deposits would be at risk.

I’d like to provide you with an example that illustrates some of the inequities I have raised. Just last week, we were competing for a very sound commercial real estate loan in the amount of $2.8 million. We priced the loan very attractively, offering a below-market interest rate. On Thursday, we learned that a credit union was offering a rate that was .50% below the rate we were quoting. You can imagine my reaction. I cannot find the words to articulate the level of my frustration. Please don’t misunderstand. I am a competitor. I grew up with 3 siblings, played 3 sports, and if you got your mouth bloodied you got back on the field and worked like crazy to win the next round. The problem here is not that we lost the loan, but rather that the playing field is not level. I’m quite certain that these borrowers of “modest means” will be well pleased with their new loan.

In conclusion, I simply ask that you do the right thing. The credit union tax exemption is no longer defensible. Therefore, please deny ANY request for expansion of powers to credit unions, including but not limited to their request to become public depositories in the State of Ohio. Doing anything else will only exacerbate an already serious problem.

Mr. Chairman, members of the committee, I thank you for your attention. This concludes my prepared remarks. I would be happy to answer any questions you may have.