May 28, 2019

RE: AN ACT to amend the general municipal law and the banking law, in relation to allowing credit unions, savings banks, savings and loan associations and federal savings associations to accept and secure deposits from municipal corporations.

MEMORANDUM IN OPPOSITION
S.6079 (Sanders) / A.3262 (Zebrowski)

This memorandum is submitted in strong opposition to the subject legislation by the Independent Bankers Association of New York State, Inc. ("IBANYS") which exclusively represents the interests of community banks located throughout New York State. This bill amends the Banking Law and the General Municipal Law to permit credit unions, savings banks, and savings and loan associations to accept municipal deposits.

Thrift institutions are currently permitted to accept municipal deposits through the creation of a taxable commercial bank subsidiary.

Community banks, according to the New York State Department of Financial Services Community Banking Report in February 2013, provided "…nearly 55% of all small business loans and approximately 90% of small farm loans in the State. Smaller community banks – those with assets of $1 billion or less – hold only about 6% of all FDIC insured banking assets in New York yet make almost 28% of all small business loans, including 43% of small farm loans in the State."

Community banks have a very basic business model which is focused on gathering deposits, of which municipal deposits are a critical component. The deposits are returned to the communities through loans particularly directed to small businesses and small business lending. Community banks are an important engine in the State's economy.

Community banks have approximately 45% of all municipal deposits of all banks in New York while holding only 18% of the bank assets and deposits of New York banks. Community banks' municipal deposits range from 15% to 30% of their deposits. Municipal deposits constitute a significant source of funds to make loans and invest in municipal bonds. Loss of municipal deposits negatively impacts the economies of the communities served by these institutions.

Community banks are not concerned with the competition for municipal deposits from credit unions. There is significant competition for municipal deposits not only from banks but also from investment funds operated on a cooperative basis such as NYCLASS an NYLAF. Credit unions are competing with an unfair advantage as a consequence of their tax status. In a recent credit union paper it states: "Credit unions are exempt from income taxes so would pay no state taxes on the income they earned on those deposits." This paper focuses on State deposits, the bulk of which are held by money center institutions. It points to increased earnings that would flow to the State based on the differential between credit union and bank tax rates.

The credit unions have argued that the increased rate of return due to tax differentials are positive for municipalities, and effectively return the credit unions' tax advantage money to local governments. Their argument misses the point, that their admitted income tax advantage becomes a rate advantage in bidding for municipal or state deposits. The playing field is not level. The credit unions were not given an exemption from income taxes to compete with a significant advantage against community banks that pay taxes.

The credit union paper previously cited states that: “Of course, credit unions use deposits from public entities to make loans at lower interest rates to borrowers in local communities. These lower-rate loans provide economic value by increasing the disposable income available to consumers for spending on other goods and services.” The paper cites the difference in rates for a 5-year auto loan between credit unions and commercial loans. This point of view underlines an important difference – credit unions are focused on making personal loans and mortgages, while community banks are focused on job-creating small business and agriculture loans. To further underline this difference the banks are paying taxes on the interest earned on these loans. Credit unions operate with a federally prescribed lending limit of 12.25% of their assets. Credit unions have a distinctly different business model than community banks, which as a cooperative is member driven.

Municipal bonds are a significant portion of a community bank’s investment portfolio. Community banks often purchase unrated paper from fire districts and other municipal entities. These purchases by community banks save these entities the costs associated with rated investment paper. Credit unions, as tax exempt entities, do not benefit from the purchase of municipal bonds. Recent testimony by the New York State Association of Counties at the recent

Assembly hearing on municipal deposits to credit unions indicated that they were carefully considering the issue based on the consequences. Concern was expressed about access to bank funding in emergency situations where a continuing relationship plays a significant part in access to capital.

Municipal deposits constitute a consequential portion of community bank deposits – deposits which are not won back from consumers by toaster giveaways. Competition from credit unions, investment funds, mutual funds, exchange traded funds, and hedge funds have made deposits more difficult to acquire. Deposits are the lifeblood of community banks' ability to make small business loans. The loss of core funding from municipal deposits would result in a decrease in the amount of loans community banks are able to make and the municipal investments they purchase. Alternative funding for community banks beyond their own deposits will only be available with a high borrowing cost. The community bank's profitability would be impacted potentially causing more of these institutions to consider merger and acquisition, which negatively impacts the communities that they serve.

Credit unions have argued that their impact on the municipal deposit market would be negligible. It should be noted, however, that the figures upon which their argument is based includes state deposits which are principally held by money center banks. Most importantly, the credit unions have continued to acquire banking powers, expanding their franchise without accepting the costs associated with taxes and the additional regulatory regime, such as compliance with the Community Reinvestment Act.

The credit unions' argument for expansion of their powers to accept municipal deposits is grounded on the promise of a better return for municipalities based on their income tax exemption. Community banks only want a level playing field. The alternatives are clear – form a commercial subsidiary as the thrifts are required to, or make the banks' net income from their loans related to municipal deposits fully tax exempt.

Based on the foregoing, ***it is respectfully requested that the subject bill not receive favorable consideration***.