



Commentary by Chip Filson, Callahan & Associates

Should Credit Unions Turn to Banks to Replace the Corporate Network?

In September, the Iowa Credit Union League submitted an application to the Federal Reserve Bank of Chicago and the Comptroller of the Currency to form a holding company and acquire CrediCard National Bank of Tucson, a wholesale credit card bank based in Arizona. The purpose of the bank would be to provide correspondent and credit card processing services that would replace the Iowa Corporate Credit Union if it is unable to continue providing such services under the new Corporate Credit Union rules. This initiative triggered the following email chain among a group of credit union executives and Chip Filson.

First Message to Group:

Call me crazy, but this isn't a bad idea.

First Responder:

I agree, in the short term, but in the end if we are going to create a cooperative credit union alternative serving organizations that require capital investments, why not keep them in the system?

What do you think? Will capital that could re-ignite corporates head out to new solutions? Should we be pulling for a corporate system reinvestment, or should alternative like-kind investments be the focus?

Second Responder:

It seems we are not asking the right question. Why are we unable to create successful solutions within our own structures? To fund and capitalize a bank seems odd to say the least, and a League and other lenders should be asking how their own corporate can offer this same service. . . or alternatively, or in addition, we need to create another special purpose credit union entity.

To conclude that funding a bank is the most beneficial path to the future of credit unions is a clear sign that the charter for credit unions is in desperate need of repair. . . when our industry leaders suggest that other structures and charters are more attractive and create a better solution, are we not suggesting that our own structure is seriously flawed or even broken?

A League creating a bank is not new, just a shock to see the justifications when as leaders

they should be creating the solutions we need within our credit union system.

First Responder Replies:

At dinner last night with two Iowa CEO's, after their initial "that's kind of cool moment," they were wondering why paying a bank regulator's fee and FDIC insurance premiums up front makes any sense over re-engineering the corporates.

Bottom line I think that the NCUA has left the industry wondering if re-capitalizing corporates is an option. No one really understands any vision for what corporates will be in the future. No one really knows that corporates will return and if it will be OK for everyone to talk about them as a positive force and not as a risk. No one is really out there saying corporates are good at anything in a loud and clear voice.

I would hope that the NCUA Board can remind people that the service they would buy from a bank, the Fed, etc. can be competitively bought from credit union solutions. It's time to rekindle the brand.

How do corporates come out swinging with income-statement based services that do not require balance sheet offsets that in the end look too much like re-capitalization and starting over? Somehow we need to get over the idea of "here-we-go-again" and get on with a new design for the future of the industry. I'm just not sure how that vision gets sold with what we see in Washington today.

What do you think, Chip?

Should credit unions turn to banks?

My thoughts are as follows:

1. The most powerful, flexible, and creative charter in the United States today is a corporate credit union charter. Corporates are not subject to PCA, they have broad investment authority, and can create any capital structure the regulators approve: primary, secondary, risk based etc. But the charter is merely a tool, and no matter how well designed the tool may be, if it ends up in the hands of a fool, the tool will not be seen as valuable.
2. Credit unions are already relying more on the banking system, especially with investments. Between June 08 and 09, total credit union investments increased \$40 billion. Approximately \$4 billion of that increase went to corporates and \$13 billion to the banking system.
3. Third parties with credit union relationships are now requiring credit unions to use banks for payments in certain areas of the country.
4. NCUA has yet to countenance the scale of the hole they have helped to dig. The corporates are no longer a financial issue. Resources have always been sufficient to resolve the losses. However, credit unions' confidence in the ability or willingness of the Agency to act in the system's interest continues to decline.
5. Therefore, the Iowa league initiative is a bold and important step.
6. A new era of financial regulation is unfolding. It is not clear what the status of federal creditunion chartering/supervisory, insurance or liquidity structures will be. There will be more opportunities for policy makers to go wrong in overseeing the cooperative system.
7. Building options now is critical. Preferably these would be within the cooperative system. But what seems likely is that even if individual corporates survive, there will be no corporate network to leverage, aggregate, or distribute through. The situation will be analogous to that of individual credit unions having no credit union network solutions to use with each having to find their own business solutions.

I do not want to be irrationally pessimistic. To borrow a phrase from Alexis De Tocqueville commenting on a much earlier phase of American life: "the greatness of America lies not in being more enlightened than any other nation, but rather in her ability to repair her faults." I believe that is also strength of the credit union system. ▀

Article Update:

In November, the Iowa Credit Union League withdrew its application with the Federal Reserve Bank of Chicago to acquire CrediCard National Bank of Tucson. The League indicated the primary roadblock to the purchase came from the Comptroller of the Currency, which preferred a retail, not wholesale, operation for the Bank. The League stated it will continue to pursue "other alternatives" to ensure access to cost-effective processing operations for credit unions given the uncertainty around the corporate credit union network.