AMB America's Mutual Banks

Mutual Alert

NCUA Plans to Finalize Sub Debt Rule

Today, the American Banker, published an OpEd piece by the ABA's Rob Nichols regarding the National Credit Union Administration's (NCUA) plan to finalize a rule, as early as this week, that would allow credit unions to issue subordinated debt to "for-profit institutional investors."

Mr. Nichol's states that subordinated debt is an expensive form of capital and this proposal would drive credit unions to focus on products that create the highest yields. This would ultimately turn the credit union's focus from the average member, who they are supposed to serve, to the big investors with greater means. He believes that this will give "big investors" more influence over the credit union than the average member. He argues that credit unions are meant to serve their members who control the institution and the profits are supposed to go back to the members through better rates and dividends. He asserts that the mutual structure supports credit unions receiving tax exemptions and creating sub debt creditors will undermine the legitimacy of that exemption. He bemoans the desire of credit unions to have the benefits of being banks but seek to avoid paying taxes and regulatory requirements.

Many of Mr. Nichols comments are valid. AMB believes that credit unions particularly multibillion dollar credit unions have an unfair advantage over tax paying banks. This competitive advantage is accentuated even more when deployed against community banks. The basis for the tax exemption appears even more dubious when compared with the income tax on mutual community banks. Why are these two different? Well one pays income tax the other doesn't. The point we want to emphasize, as we have in the past, is that mutual banks, who by their structure cannot issue stock, need other forms of capital to grow. ABA attacks on credit union inclusion of sub debt in capital should not be based on the utility of long term sub debt per se. The point which Mr. Nichols fails to emphasize is that tax payer funded growth gives credit unions an unfair competitive advantage against tax paying stock and mutual banks. If structured correctly, sub debt, as proven in the past in the mutual savings bank and insurance industries, is a perfectly good form of long term capital. The ABA should be more sensitive to the capital needs of its mutual members before branding all sub debt as risky. Don't throw the baby out with the bath water.

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