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*Advancing the challenge against unfair credit union expansion.*

## **Banking Industry to Seek Expedited Judicial Action Regarding the Constitutionality of Credit Union Tax Exemptions and Commence Efforts to Seek the Enactment of Legislation Defining the Permissible Scope of Credit Union Community Charters**

For more than four years a group of small and medium sized banks and savings associations have worked with the [Pennsylvania Association of Community Bankers](#) and the [Pennsylvania Bankers Association](#) in extensive litigation challenging so-called community charters issued to credit unions which allow credit unions to serve vast regions of the state in a manner indistinguishable from banks and savings associations while enjoying a near total exemption from state and local taxes. While this litigation has generated significant victories for the banking industry, to prevent proceedings from continuing for years to come, the banking industry has decided to seek expedited judicial review of the constitutionality of credit union tax exemptions and to undertake efforts to seek the enactment of legislation creating a level playing field for competition between expansive credit unions and other financial institutions.

### **Background**

Federal and state law limits credit unions to serving either groups of individuals joined together by occupation or association, or persons living in “well-defined local communities, neighborhoods and rural districts.” In 2003 and 2004 credit unions sought approval from the Pennsylvania Banking Department and the National Credit Union Administration to serve an eight-county area in Pennsylvania and New Jersey surrounding the City of Philadelphia; a six-county area in Central Pennsylvania; and a rural district located within a 40 mile radius of the City of Corry in Northwestern Pennsylvania. The banking industry initiated a variety of proceedings and initiatives in state and federal courts and before the Pennsylvania General Assembly to challenge these applications. As a result of these efforts:

- the application for a charter to serve eight counties in two states in the Philadelphia region was disapproved and the charter was limited to providing service only to Philadelphia and four surrounding counties in Pennsylvania;
- a charter issued to three credit unions to serve a six-county area in Central Pennsylvania was rescinded;
- the application to serve the Corry area was limited to municipalities within the Corry Area School District;
- the PA Supreme Court reversed a decision by the Commonwealth Court refusing to hear a challenge of the charters issued for the five-county Greater Philadelphia Region, and the Commonwealth Court has scheduled argument on the charter appeals for June 2009; and

- the Pennsylvania General Assembly enacted legislation making community charter applications available for review by other financial institutions and created an expedited and informal process for the review of credit union charter applications.

Despite these successes, the fundamental issue which has motivated challenges to credit union community charters remains unresolved - *i.e.*, whether it is fair to provide tax exemptions to one group of financial institutions while imposing substantial taxes on other similarly situated institutions. The banking industry has not challenged the right of credit unions to directly compete with banks and savings associations, and would not challenge their efforts to expand the scope of their geographical operations if they pay taxes. The banking industry is adamantly opposed, however, to the geographical expansion of tax exempt credit union operations beyond well-defined local communities, neighborhoods and rural districts.

In order to present issues immediately to the Supreme Court regarding the constitutionality of credit union tax exemptions, the banking industry has decided to forgo a complex factual hearing before the Commonwealth Court regarding credit union operations and the extent to which credit unions improperly utilize their tax exemptions to subsidize private profit making activities. Instead, the banking industry will ask the PA Supreme Court to decide whether provisions of the Pennsylvania Constitution limiting tax exemptions to charities, governmental organizations, distressed communities, disabled veterans, and individuals in need of assistance due to poverty, age or infirmity, and which declare all other exemptions of property from taxation void, render credit union tax exemptions impermissible.

Based on some archaic 19<sup>th</sup> Century precedent arising prior to the 1968 Pennsylvania Constitutional Convention, the Commonwealth Court had previously rejected claims that credit union tax exemptions are constitutionally impermissible in Pennsylvania and the State Supreme Court decided not to review the Commonwealth Court's decision until other factual issues regarding the operations of credit unions are resolved. By discontinuing its request for a factual hearing before the Commonwealth Court, the actions of the banking industry will now allow this important issue to be directly presented to the State Supreme Court for resolution.

While pursuing an expedited review of the constitutionality of credit union tax exemptions to the Pennsylvania Supreme Court, and continuing to challenge charters issued to serve the five-county Greater Philadelphia Region, the banking industry has also agreed to discuss with credit unions the enactment of legislation to create a level playing field for all financial institutions. These discussions will focus in four principal areas of concern, *i.e.*, (1) creating a reasonable definition of what constitutes well-defined local communities, neighborhoods, or rural districts; (2) ensuring parity of the federal and state treatment of tax exemptions provided to credit unions which confine their operations to well-defined local communities, neighborhoods, or rural districts; (3) allowing credit unions to serve additional areas to the extent their operations are subject to the Mutual Thrift Institutions Tax; and (4) ensuring that credit unions comply with community reinvestment requirements comparable with those imposed upon banks and savings associations.

While the banking industry hopes these efforts will lead to an amicable and mutually beneficial resolution of these issues, absent successful negotiations regarding compromise legislation, the banking industry is also prepared to initiate significant legislative efforts to ensure the fair and equal treatment of all financial institutions on issues of taxation and community reinvestment.