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In tax reform, banks see opening against credit unions

By **COLIN WILHELM** | 02/09/17 05:06 AM EST

The war between banks and credit unions over a tax exemption for the latter has a new battleground: the House Republican tax reform plan.

Banks see a way to break through the current stalemate by pushing to include an end to the exemption in the House GOP's yet-to-be released comprehensive tax reform plan.

For decades, bankers have lobbied Congress to take away the federal provision granted to credit unions because they are member-owned, nonprofit cooperatives. Banks argue that credit unions have evolved into something closer to banks and should be treated as such.

“Absolutely. 110 percent, as part of tax reform we’ll be looking for equitable treatment with

credit unions that essentially have become tax-free banks,” said Paul Merski, executive vice president for congressional relations and strategy at the Independent Community Bankers of America. “They’re no longer sticking to their original charter and mission.”

The American Bankers Association agreed.

“Whether it’s in a standalone bill or a part of this package we have a longstanding passion on this issue,” said Bob Davis, executive vice president of mortgage markets, financial management, and public policy for the association.

But credit unions are counting on the increased bank pressure to run into the same brick wall of constituent concerns among lawmakers that has kept the exemption safe in the past.

“With a Republican Congress, with a Republican president, credit unions can make the case that, ‘You didn’t come here to raise taxes, you came here to lower them,’” said John McKechnie, a senior partner with the lobbying firm Total Spectrum who has worked on behalf of credit unions.

“We’ve talked with the leadership of Senate Finance and House Ways and Means and the credit union tax exemption continues to get a lot of support,” said Brad Thaler, vice president of legislative affairs for the National Association of Federally-Insured Credit Unions. “It would be taking money out of pockets the same way a tax increase would.”

In a tit-for-tat, Thaler said credit unions would be more than happy to encourage Congress to take a longer look at tax treatment of banks incorporated under subchapter S of the corporate tax code. Those banks, which are owned by no more than 100 shareholders, enjoy federal tax treatment similar to credit unions. In 2015 the Federal Deposit Insurance Corp. counted over 2,000 U.S. banks organized under subchapter S.

“If they went after our tax exemption we’d point out that they could go after tax benefits for banks, which might be more palatable to members of Congress,” Thaler said.

The fact that credit unions disproportionately serve members of the armed forces could also be brought up to make changes less politically savory for Congress.

The ICBA’s Merski called that as a bluff.

The comparison between subchapter S banks and credit unions, “is kind of apples and oranges,” he said. “I think if anything [subchapter S bank shareholders] might benefit from the marginal [tax] rates going down,” since the income from those banks is counted

towards personal income of the shareholders due to their pass-through status.

The current House Republican blueprint for tax reform would also lower the tax rate for pass-throughs to 25 percent, and Merski pointed to closing the credit union exemption as a potential pay-for in that plan. In a projected estimate for fiscal years 2015-2019, the Joint Committee on Taxation said that doing so would raise \$12.7 billion in revenue. That might not be enough to move the needle much on the overall price of comprehensive tax reform, which is in the trillions, but the threat could be enough to make credit unions play defense during the drafting.

Still, credit union supporters said they would rather work with banks on the financial regulatory reform effort likely to pass the House this Congress rather than spend energy on a new front in their longstanding fight with banks.

“There are a lot of areas where banks and credit unions have common interest,” said Thaler.