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Why so many credit unions are buying community banks

Article

The news: A Michigan-based credit union, **DFCU Financial**, said it plans to acquire **First Citrus Bank** of Tampa, Florida, in a deal estimated to be worth about $105 million.

More on the deal: The combined entity will have approximately $7.1 billion in assets, nearly $800 million in capital, and 33 branches across its footprint in Michigan and Florida.

- Ryan Goldberg, president & CEO of DFCU, said the deal "represents DFCU's **initial expansion into Florida and a significant increase in commercial lending presence and expertise."**
- It's expected to close during Q4 2022.

Trendspotting: DFCU is t**he seventh credit union this year** to announce its intention to acquire a bank.

- Michael Bell, co-chair of the financial institutions practice at Detroit-based law firm Honigman, told the Financial Brand that he **expects some 25 or more of these deals to be announced in 2022**. Bell has represented credit unions in about 40 whole-bank deals, plus purchases of bank branches, since 2011.
- S&P Global spoke with two deal advisers that work on credit union-bank acquisitions who said they **"anticipate around 20 such announcements in 2022."**
- 2021 saw 13 instances of credit unions buying banks, but **the all-time record of 19 such deals was set in 2019,** according to American Banker.

What's the opportunity? Credit unions are using their acquisitions of community banks to enter new markets in other geographic areas, add expertise and diversify its balance sheet, add members, drive economies of scale, and expand their commercial lending.

The deals may also be a defensive move—the credit union could buy a neighboring community bank to block a competitor from entering or expanding its presence in the credit union's marketplace. Or credit unions could be seeking a bank's more advanced digital capabilities.

In other words, credit unions make these deals pretty much **for the same reason as one community or regional bank would buy another.**

What's the problem? Community bankers say credit unions are abusing their tax-exempt status to outbid banks in acquisitions and derive an unfair competitive advantage. And they claim these acquisitions have a negative impact on communities:

- They result in the loss of tax revenue when a bank is acquired by a tax-exempt credit union.
- Credit unions aren't required to abide by the Community Reinvestment Act (CRA) and have no regulatory incentive to provide financing to lower income communities.

- Analysis by the Government Accountability Office showed that credit unions are now serving more middle- and upper-income customers, rather than customers of “small means”—the congressional mandate behind the credit union tax exemption. That adds to banks’ objection to the very liberal interpretations of membership rules for credit unions.

Legal pushback and lobbying efforts: Colorado and Iowa have barred state-chartered banks from selling to credit unions. And the Independent Community Bankers of America (ICBA) and other community banking groups have lobbied federal and state lawmakers to curb credit union-bank deals.

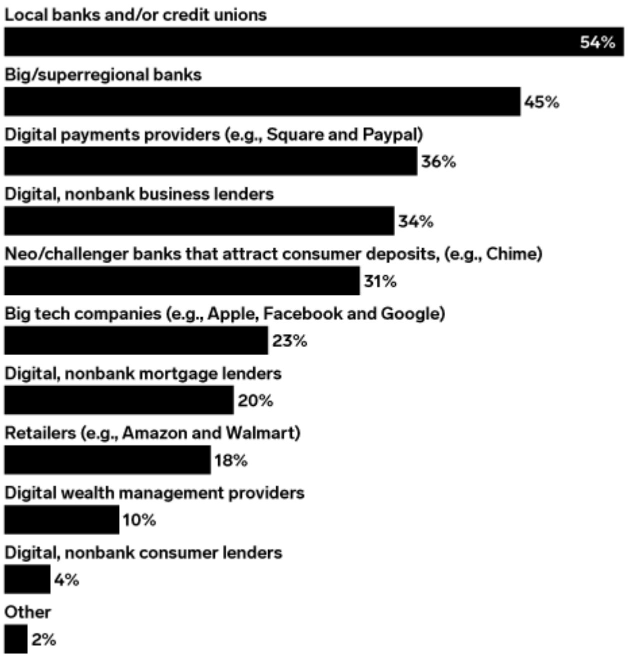
- The ICBA proposed a 10% exit fee on a bank's assets or liabilities when selling to credit unions.
- Under another proposal, a tax-exempt entity like a credit union buying a for-profit entity would lose its not-for-profit status and take on the acquired entity's tax position.

Will the trend escalate? When a credit union purchases a bank, multiple regulators are involved. The legal process is more complex, and the costs associated with the transaction are higher. So, as anomalous and alarming as they may appear, these acquisitions—relatively small in number—aren’t likely to become an existential threat to community banks. Bank-to-bank deals will continue to dominate M&A activity in financial services. Bell told Bankbeat that he expects no more than 15 to 20 such transactions annually: “These will always be in the minority and that will not change,” he said.

In the longer term, Biden's executive order regarding consolidation could be a signal that the executive branch may eventually take a look at credit union acquisitions of banks.

Competitive Threats to Their Bank According to US Financial Executives, July 2021

% of respondents



Note: respondents were asked to select no more than three
Source: Bank Director, "2021 Technology Survey" sponsored by CDW, Aug 31, 2021

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