Credit Union National Association

Credit Unions' Strongest Advocate™

Regulatory Burden Financial Impact Study

EXECUTIVE SUMMARY

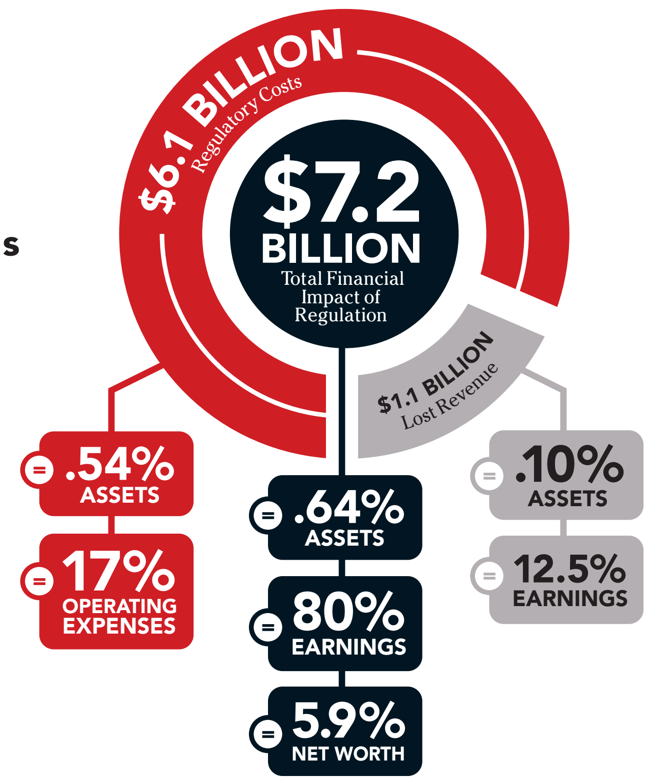
Credit unions recognize that they operate in a regulated industry and must bear reasonable costs of regulation. However, the total financial impact of regulation on credit unions and their members is high and has increased dramatically since the recent financial crisis.

With the support of state credit union Leagues, CUNA commissioned Cornerstone Advisors to perform a rigorous analysis of the current financial impact of regulation on credit unions, and how much it has changed since 2010.

Cornerstone Advisors conducted a two-phased study to gain an in-depth examination and quantify the impact of regulation at small, medium and large credit unions. The study gathered data in terms of increased costs, including staffing, third party expenses and capitalized expenses, and reduced revenue opportunities.

These financial impacts are considerable in terms of the scale of credit union operations.

Cost of Regulatory Burden to Credit Unions in 2014



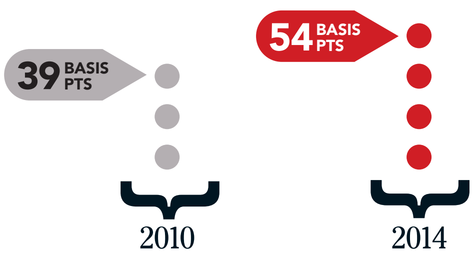
This summary was prepared by CUNA. Readers are encouraged to refer to the full study.

cuna.org/regburden

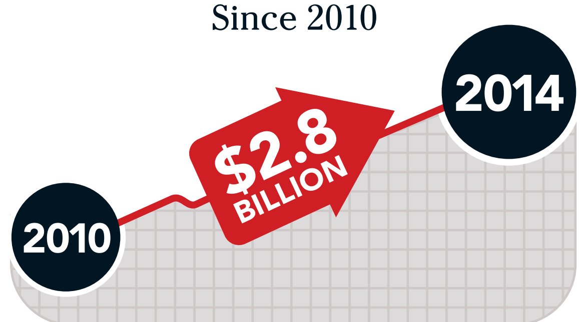
INCREASE IN REGULATORY IMPACT SINCE 2010

The regulatory cost of 54 basis points of assets in 2014 represents a 15 basis point increase from the 39 basis point cost the study found in 2010. This means that regulatory costs for credit unions in 2014 were $1.7 billion higher than they would have been without the changes that occurred from 2010 to 2014. Adding the 10 basis point reduction in revenues ($1.1 billion) yields an increase in total financial impact of 25 basis points ($2.8 billion), from 39 basis points to 64 basis points.

Regulatory Cost Increase
$1.7 Billion



Increase in Total Financial Impact
Since 2010

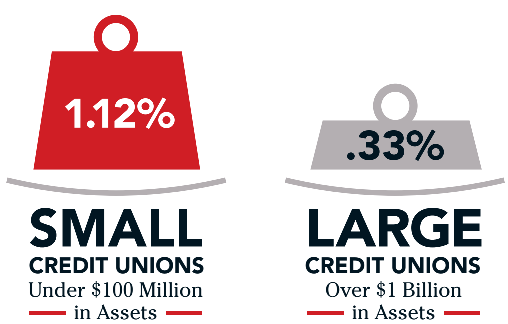


LOST REVENUE

The study considered how revenue has been influenced by regulation, especially by changes in regulation. Participants identified a number of business lines that had been affected by regulatory changes, primarily related to lending and interchange income.

Although, lending revenue has no doubt been affected by regulation, the amount is difficult to accurately quantify. Therefore, the only revenue reduction included in the study is that due to reduced interchange income as a result of the Durbin Amendment to the Dodd Frank Act. This means the study's $1.1 billion estimate for revenue reduction underestimates the actual amount.

Small Credit Unions Bear the Brunt of Regulatory Burden



Compares regulatory costs relative to assets

REGULATORY IMPACTS AND CREDIT UNION SIZE

The study found dramatic evidence of differential impacts by credit union size. Cost impacts were much stronger at smaller versus larger credit unions. There are basic fixed costs associated with complying with regulations, and at larger credit unions these costs can be spread over a larger asset base. In contrast, adverse revenue impacts were stronger at larger than smaller credit unions. This is because members of larger credit unions are more likely to generate interchange income by using a debit card from their credit union.

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TYPES OF REGULATORY COST

The study collected data on three types of costs related to regulation: staff costs, third party expenses and depreciation of capitalized costs. For each cost category, care was taken to include only that portion of the costs that are driven by regulatory requirements. For example, for compliance staff, time spent on compliance with internal policies not required by regulation was not included as a regulatory expense.

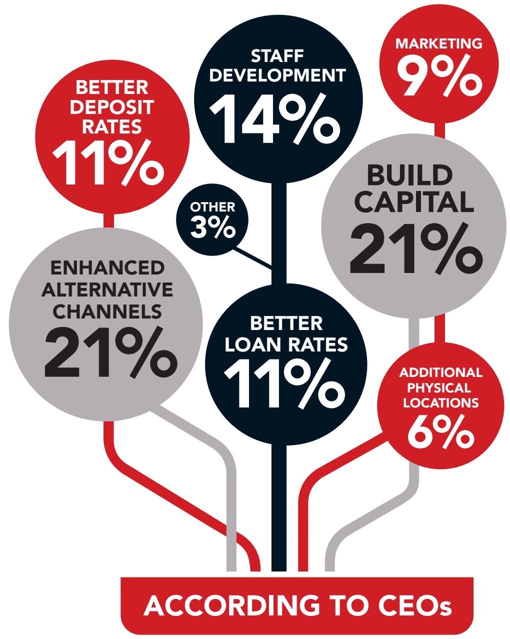
The largest component of regulatory expense was for staff, at 74% of the total. This is not surprising as compensation typically accounts for about half of total credit union operation expenses.

Of the staff costs driven by regulation, the largest component came in member-facing staff. This suggests that credit unions have to employ more such staff than otherwise, and/or that member facing staff have to divert much of their attention from serving members to complying with regulations.

STRATEGIC IMPACTS

The study solicited credit union CEOs' views on how the funds devoted to regulation would have been reallocated within the credit union had they not been drained by regulation. Better member pricing, better service delivery, and institutional strengthening topped the CEO's lists.

In addition to extensive data collection, the study solicited participating CEOs' viewpoints of where they had seen the greatest increase in regulatory impact in the areas of greater costs, reduced productivity, and reduced revenues. The greatest cost and productivity impacts occurred in compliance, mortgage and consumer lending and internal audit. The greatest revenue impacts were in mortgage lending, debit interchange and payments.



KEY THEMES

As a result of engaging with credit union executives over several months while conducting the study, Cornerstone Advisors analysts catalogued four key features of how credit unions view the impact of regulation:

UNCERTAINTY & AMBIGUITY around written rules complicates compliance.

INCONSISTENT INTERPRETATION of rules by examiners frustrates operations.

A STEADY STREAM of NEW REGULATIONS creates costly change management.

"ONE SIZE FITS ALL" rules are unfair and ineffective.

CONCLUSION

The study found that the costs that credit unions bear as a result of regulation, even when conservatively measured, are very high, and have increased substantially since the financial crisis and Great Recession. The burden is particularly egregious for smaller institutions.

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