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# Growth of large-scale credit unions in Iowa: implications for public policy

Robert W. Jolly

*Iowa State University*, [rjolly@iastate.edu](mailto:rjolly@iastate.edu)

Gary D. Koppenhaver

*Iowa State University*

Joshua D. Roe

*Iowa State University*

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# Growth of large-scale credit unions in Iowa: implications for public policy

## **Abstract**

Over the past two decades, the financial services industry has experienced a significant increase in competition and internal rivalry. Driven by deregulation and advances in information technologies, many historical institutional distinctions among financial intermediaries have disappeared or blurred considerably. The fundamental assumption that has guided many of the policy changes is that consumers are best served when businesses offering the same services are allowed to compete within a similar regulatory or institutional environment. Despite this general leveling of the playing field, credit unions continue to operate under tax and regulatory rules that differ, in important ways, from most of the firms in the financial services industry. Many of the tax and regulatory distinctions arose in the early 20th century during a time when credit unions were being established to meet the needs of individuals or communities that could not or were not being adequately served by commercial banks. However, as the financial services industry has evolved, the justification for continuing or maintaining credit unions

## **Keywords**

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# **Growth of Large–Scale Credit Unions in Iowa: Implications for Public Policy**

**Robert W. Jolly**  
**Professor of Economics**

**Gary D. Koppenhaver**  
**Associate Professor of Finance**

**Joshua D. Roe**  
**Research Assistant in Economics**

**Iowa State University**  
**Ames, Iowa**

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## **Background**

Over the past two decades, the financial services industry has experienced a significant increase in competition and internal rivalry. Driven by deregulation and advances in information technologies, many historical institutional distinctions among financial intermediaries have disappeared or blurred considerably. The fundamental assumption that has guided many of the policy changes is that consumers are best served when businesses offering the same services are allowed to compete within a similar regulatory or institutional environment. Despite this general leveling of the playing field, credit unions continue to operate under tax and regulatory rules that differ, in important ways, from most of the firms in the financial services industry.

Many of the tax and regulatory distinctions arose in the early 20th century during a time when credit unions were being established to meet the needs of individuals or communities that could not or were not being adequately served by commercial banks. However, as the financial services industry has evolved, the justification for continuing or maintaining credit unions' tax and regulatory status has been questioned and disputed by bankers and staunchly defended by credit union officials.

This report examines recent changes occurring in the structure and performance of credit unions and banks in Iowa. Specific objectives are as follows:

- Describe changes in the size distribution of credit unions and banks in Iowa.
- Identify the key regulatory or tax differences between the two types of financial intermediaries.
- Review the economic rationale for the existing tax and regulatory differences.
- Where possible, assess the impacts of these institutional factors on performance and competition.

- Briefly list unresolved policy issues that merit further scrutiny by the public and the financial services industry in Iowa.

### **Overview of Key Differences between Credit Unions and Banks**

Credit unions differ from banks in several important ways. Below is a list of some of the key differences:

1. As cooperatives, credit unions are owned and democratically governed (one member, one vote) by their members. Banks are investor-owned firms (and may be closely held or publicly traded) governed by stockholders, usually in proportion to their equity position.
2. In a credit union, net income or surplus may be retained to build capital or distributed to members in the form of dividends, lower loan rates, higher deposit rates, or increased or enhanced services. Banks can retain and reinvest income to build capital, to enhance customer services, or to pay dividends to stockholders.
3. A credit union's net income is not subject to federal income tax and may be exempt from many state and local taxes as well. Banks are subject to the same federal taxes imposed on any corporation. In Iowa, banks also pay a state-level franchise tax on their net income.
4. Credit unions may be partially subsidized by their sponsoring organization, especially with respect to fixed assets.
5. Credit unions cannot raise equity through capital markets or outside investors. As is the case with all cooperatives, equity is acquired from retained earnings. Publicly traded banks can acquire equity through capital markets. Closely held

- banks—the most common situation for community banks—could increase equity from outside private investors. However for smaller, closely held banks, retained earnings are the major source of equity growth.
6. Credit union customers are members who meet well-defined membership (common bond) criteria. The common bond may be based on occupation, membership in an organization, or residence within a specific community. Bank customers are not subject to membership criteria.
  7. Directors of credit unions, in general, are elected by members and serve as volunteers. Bank directors are appointed to represent stockholders and are compensated for their time.
  8. In general, deposits at credit unions and banks are insured up to \$100,000 per individual. Banks pay a risk-adjusted premium to the Federal Deposit Insurance Corporation (FDIC) that is treated as a business expense. Credit unions maintain a pooled revolving fund managed by the National Credit Union Administration (NCUA) equal to approximately 1% of insured shares and deposits. Credit unions can receive dividends on their shares in the insurance fund. Credit unions treat shares in the NCUA fund as assets on the books of the fund and individual credit unions.
  9. Credit unions are not subject to the provisions of the Community Reinvestment Act as are banks. However, there is an implicit expectation that credit unions will serve individuals of “modest means” in exchange for favorable tax and regulatory treatment.

## **Brief History of Credit Union Development<sup>1</sup>**

Financial cooperatives, including credit unions emerged in the latter part of the 17th and early 18th century. Benjamin Franklin's Philadelphia Contributorship, organized in 1752, was one of the first financial cooperatives in North America. This fire insurance mutual was patterned after an earlier London-based association established 50 years earlier.

In the middle of the 19th century, a number of working class consumer cooperatives were established in Europe. The most famous of these was the Rochdale Society in England, which was established in 1846. The Rochdale Society articulated many of the principles that guide cooperatives today. Some of the key principles include the following:

- open membership,
- equity provided by members,
- democratic control,
- net income distribution by patronage or use of services,
- limited member equity and dividends,
- goods and services exchanged at market prices, and
- political neutrality.

Working class consumer cooperatives were brought to North America in the mid-19th century by immigrant groups. These cooperative "stores" were often organized around shared occupational, community, or ethnic bonds.

About the same time, agricultural cooperatives, again with European roots and based on Rochdale Society principles, developed in North America. The agricultural cooperatives

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<sup>1</sup> This section draws on Fairbairn (2004), Chmura Economics and Analytics (2004), National Credit Union Administration (undated), and World Council of Credit Unions (2003).



provided inputs, supplies, marketing, and processing services to farmers battling distance, isolation, and the market power of railroads and processing plants.

Credit unions also were a product of 19th century Europe. In the 1850s, Friedrich Raiffeisen and Herman Schulze-Delitzsch, both Germans, established simple credit societies or unions to address the credit needs of poor farmers and small shopkeepers. The credit unions were based on the concept of extending credit to the poor who lacked access to commercial banks by using pooled savings to finance loans and collective decision-making and oversight of the loan-making process.

The first credit union in North America was organized in Quebec by Alphonse and Dorimene Desjardins in 1900. The Desjardins also were concerned about usury and the lack of credit available to poor Canadians. They modeled their *caisse populaire* after the existing European credit unions.

In 1909, Desjardins helped organize a credit union in New Hampshire—the first in the United States. Desjardins' work came to the attention of Pierre Jay, the Commissioner of Banking in Massachusetts and Edward Filene, a wealthy merchant who had founded a retail store that served working class families. Both men believed access to credit would enable poor working class families to improve their well being. The two men worked to establish the Massachusetts Credit Union Association in 1914. In 1920, Filene recruited Ray Bergengren, a poverty lawyer, to manage the Massachusetts Credit Union Association. A short time later, they established the Credit Union National Extension Bureau, financed by Filene, to extend the credit union concept throughout the United States. By the mid-1930s, 32 states had passed enabling legislation for credit unions. Iowa's law was passed in 1925. In 1934, President Roosevelt signed

the Federal Credit Union Act. This act, as amended, remains the key federal law for credit unions.

Because credit unions arose in response to social problems, and were, for the most part, championed by social reformers, it is not surprising that they have been viewed by public officials as instruments of public policy rather than simply as businesses. The tax status of credit unions was one of several policy decisions made to foster the early development of this industry. When the federal income tax was enacted in 1913, credit unions were not exempt from taxation. The U.S. Attorney General ruled in 1917 that because other newly established cooperative banks, such as the Federal Land Bank, were exempt from taxation, credit unions should be as well. This ruling continued until the passage of the Federal Credit Union Act in 1934 that stated that credit unions were taxable entities and that the tax burden should be commensurate with that imposed on commercial banks (United States Department of the Treasury, 2001b).

This tax obligation was removed by statute in 1937 with an amendment to the Federal Credit Union Act. The amendment stated that the income and reserves of credit unions shall be exempt from federal (and state) taxes. The justification for this exemption seems to be based on the belief that

- credit union member's shares were more like bank deposits than equity, even though they were placed at risk by the members;
- credit unions are owned and operated by members with a common bond; and
- Credit unions resemble thrifts and mutual savings banks, which were at the time, also tax exempt.

In 1951, the tax exemptions for thrifts and mutual savings banks were repealed because lawmakers believed that the exemptions created a competitive advantage over banks and that

thrifts and mutual banks had lost their “mutuality” through expansion of membership eligibility. Credit unions retained their tax-exempt status. This situation has continued to the present.

Along with their tax status, credit unions also have been regulated in terms of membership. Two dimensions or criteria for credit union membership have existed, in one form or another, since their inception in the 19th century.

#### Modest or Small Means

The first credit unions were explicitly established to assist disenfranchised or low-income groups unable to obtain financial services from the established banking industry.

#### Common Bond

Membership in a credit union historically was based around some unifying or common characteristic (Leggett and Strand, 2002). A common bond might reflect occupation, community, ethnicity, or religious belief. Because of the common bond, a credit union is able to use information and social capital available within the group to reduce the transaction costs of financial intermediation. Early credit unions resemble microcredit (or group lending institutions) currently used in developing and transition economies (Robinson, 2003; Hung, 2003). In both cases, small, relatively homogenous groups can provide the underwriting and monitoring services needed for financial intermediation more efficiently than can commercial or public lenders. In this way, small credit unions or other microfinance institutions can gather savings, secure other funds, and extend credit to individuals for whom credit would not be made available or would only be available at high rates of interest.

The intent of the 1934 Credit Union Act clearly identifies the needs of individuals of modest means as a justification for the legislation. This act also established the requirement that credit unions possess a common bond.

In 1982, the NCUA ruled that credit unions could use a broader definition for membership—the “multiple common bond.” A multiple common bond is one consisting of several unrelated businesses, organizations, or communities. The justification for this change was the need to diversify membership to protect credit unions from recession affecting the industry or community defined by the narrow common bond. This ruling by the NCUA was legally challenged by the banking industry, and in 1998 the U.S. Supreme Court decided that multiple common bonds did, in fact, violate the 1934 Act. Subsequently, the Credit Union Membership Access Act of 1998 (CUMAA) overturned the U.S. Supreme Court ruling and reestablished multiple and community common bonds.

The economic role of the common bond has been weakened by three other events.

- In 1970, an amendment to the Federal Credit Union Act, created the National Credit Union Share Insurance Fund. By insuring members’ shares or deposits, the incentives for self-underwriting and monitoring were essentially eliminated.
- With the growth of some credit unions, the ability of members to provide oversight for the intermediation process was significantly reduced. In addition, there is a natural pooling of uncorrelated or nonsystematic risk that occurs when the number of members grows. Because there is safety in numbers, the need for a common bond is much less (and much less feasible) as a credit union grows.
- Technological advances in information collection and sharing has reduced the need for the common bond to control credit or default risk.

Credit unions also have faced regulatory changes in response to safety and soundness concerns. A thorough comparison of the regulatory requirements of banks, thrifts, and credit

unions is provided in United States Department of the Treasury (2001b). We highlight four of the major events.

- In 1934, the Credit Union National Association (CUNA) is created to serve as an advocate for and a service business to credit unions.
- In 1970, the National Credit Union Administration was created to serve as an independent regulatory body for credit unions.
- In 1980, the Depository Institution Deregulation and Monetary Control Act established reserve requirements for credit unions' transaction accounts.
- A series of regulatory changes beginning in 1992 have gradually expanded credit unions' lending authority and eligible financial services. In their 2001 report, the U.S. Treasury concludes that credit unions face nearly the same safety and soundness regulations as other depository institutions. The primary exception is that credit unions have a more liberal limit on loans to an individual borrower.

### **Public Policy and Credit Union Development**

This quick historical review does not fully reflect the details nor the scope of credit union development throughout the world. However, it does highlight a number of key points.

1. Credit unions developed largely in response to the inability of poor households, farmers, or small merchants to obtain credit, at competitive rates, from the established banking sector. Although some credit rationing of this type could be attributed to discrimination and exploitation of borrowers, it also reflects that banks were unable to cost-effectively

- assess the impact that additional credit would have on the repayment capacity of farms and small businesses,
- assess the credit worthiness of borrowers seeking consumer loans,
- adequately collateralize loans,
- monitor and supervise borrowers, and
- enforce loan contracts in default.

Credit unions, by relying on member savings and member involvement in loan granting and monitoring, were able to manage the information and incentive problems at lower cost than were banks.

2. Legislation authorizing or chartering credit unions usually included language that stated support for their continued efforts to serve groups or individuals without adequate access to credit. Preferential regulatory and tax treatment was, in general, granted in exchange for credit unions' commitment to this societal goal.

The policy question that remains is whether or not favorable tax and regulatory treatment that was provided to credit unions in 1930s can be justified today. Two economic concepts are relevant to this discussion:

1. In a market economy, public policy, or governmental intervention, is usually justified as a means to resolve market failures. A market failure is the result of the market's inability to allocate resources in a manner that best meets the interests of society. Credit rationing to certain groups or regions and can be the result of market failure. A lack of information, or very costly information, can make the cost of extending and monitoring credit so high that lenders will

refuse to make loans. One way to resolve this market failure is create a lending institution, a credit union, that can be self-monitoring. Early legislation for most types of cooperatives created specific advantages not available to competing firms to increase the likelihood that the new cooperatives could succeed and fulfill their societal mission. (The Capper-Volstead Act of 1922 that exempted farmer cooperatives from antitrust enforcement is one of the most striking examples of this policy approach.) The policy dilemma is to decide how long and in what form the regulatory or tax advantages should be continued.

2. Rent seeking is economic activity by firms or individuals that focuses on retaining or expanding regulatory or tax treatment that captures benefits that would occur only because of these public policies. Rent seeking uses resources for lobbying or influence peddling and results in a transfer of benefits from one group to another. Rent seeking by competing interests will, in most cases, be pursued even if all parties would be better if they ceased. Once created, an opportunity for extracting rents will be maintained and defended by the benefiting groups.

To conclude this section, we briefly summarize the unresolved issues that underlie the taxation and regulation of credit unions.

### **Tax Treatment**

Credit unions are not taxed on income or gains in net worth. This exemption was established shortly after the federal income tax was introduced. Several justifications for exemption have been proposed:

- Cooperatives are businesses that are organized on the basis of social principles, not business principles. Because the owners of the cooperative are also its customers, the incentives to optimize stockholder's wealth are weak. In other words, cooperatives are inherently less efficient than investor-owned firms. A tax break helps overcome this inefficiency. A counter argument suggests that cooperatives with homogenous membership can be more efficient than an equivalent investor-owned firm. (Hart and Moore, 1998).
- Because credit unions are intended to meet the needs of persons with "small means," a tax benefit serves as a means to transfer income to these individuals.
- The tax benefit can be used to pay higher deposit rates, to coax savings out of lower income households or to reduce the interest rate on loans to encourage poor households to take on profitable, but riskier projects.
- The tax benefit could be used to reduce the cost of providing enhanced financial services to poor households. For example, providing an ATM in a lower income or rural neighborhood.
- Finally, the tax benefit can be used for what economists refer to as "expense preferences"—higher salaries, greater staff support, and plush offices. Some recent research has shown that expense preferences in credit unions do exist, in particular for those with residential common bonds (Frame et al., 2003)

A summary of tax provisions for financial intermediaries is given in Table 1. Because credit unions are cooperatives, a comparison with the cooperative Farm Credit System and nonfinancial cooperatives also is given. Note that unlike credit unions, other cooperatives also are taxed on some of their income.



## **Regulatory Treatment**

Because the self-policing ability of credit unions declines with greater asset size and weaker common bonds, the need for regulatory oversight has increased. As stated above, a review by the U.S. Treasury suggests supervision of credit unions is equivalent to other depository institutions—with a few exceptions.

## **Common Bond**

The common bond requirement of credit unions has a clear economic role: it enables financial resources to reach individuals or communities where credit rationing is occurring because of high lending costs or risks. However, broadening the common bond, in terms of membership size, affiliation, or diversity, means that the common bond no longer plays this role. Furthermore, with share insurance, the incentives for self-monitoring are greatly reduced.

Broadening the membership base of credit unions has been justified because it can

- reduce credit union lending risk through membership and industry diversification, and
- reduce credit union costs by capturing economies of size or scope.

In effect, the broadened definition of credit union membership means that there is no meaningful restriction on membership. In other words, the trade area of a credit union, defined in terms of multiple counties, is essentially the same as for other depository institutions operating within the same trade area. A recent article shows that distance still matters in lending (Brevoort and Hannan, 2004). Despite technological innovations the median distance between small business borrowers and their lenders only increased from 9 to 10 miles between 1993 and 1998. Table 2 shows the geographic regions of the largest credit unions in Iowa.

## **Serving Individuals of “Small” Means**

One of the key justifications for the existing tax and regulatory treatment of credit unions is that they serve a social purpose by extending financial services to individuals of small means. Several studies have examined this issue with somewhat mixed results (Jacob et al., 2002; GAO, 2003; Haller et al., 2003). In general, however, it seems that members of credit unions are not significantly different from the customers of other depository institutions. This result is not too surprising if, in fact, membership in a credit union is effectively unconstrained. Credit unions and other depository institutions seem to compete in the same market and are in effect “perfect strategic substitutes.” Recent research shows “causation” between interest rates charged by banks and credit unions (Feinberg and Rahman, 2001; Emmons and Schmid, 2004), an indication of competitive interaction between credit union and banks within a defined trade area. If the two types of lenders served distinct markets, their interest rates would not be statistically linked.

## **Analysis of Credit Unions in Iowa**

In this section, we examine several structural changes occurring in the credit union and banking industry in Iowa between 1998 and 2003. In addition, we present information comparing the financial performance of Iowa credit unions and banks. The data were obtained from publicly available call reports. In this report, with one exception, only banks and credit unions headquartered in Iowa are included in the analysis. We exclude banks and thrifts headquartered elsewhere that branch into Iowa.

In Figure 1, we look at the impact of mergers and acquisitions on numbers and size of banks and credit unions over the past 5 years. Both types of institutions show declining numbers and increases in mean size. On average, credit unions are significantly smaller institutions than are banks.

Figures 2 and 3 compare shifts in the distribution of banks and asset volume by size of bank from 1998 to 2003. In general, we see a decline in the number of banks smaller than \$65 million. Banks with \$100–300 million in assets increased by more than 60% during this period. Market share changes, in general, follow the changes in bank size distribution. Growth in market share occurred in banks with \$65–500 million in assets. The concentration in asset volume in Iowa-headquartered banks greater than \$500 million in assets decreased from 1998 to 2003. However, the largest banks maintained the greatest market share over this period.

The size distribution of Iowa-based credit unions is given in Figure 4. The size distribution of credit unions differs significantly from banks. Most credit unions in Iowa are very small institutions with less than \$10 million in assets. As with banks, however, we see a declining number of small credit unions and growth in those with \$35–65 million in assets and credit unions with more than \$100 million in assets. Changes in the distribution of credit union assets shown in Figure 5 generally follow the change in size distribution. Asset concentration has increased in mid-sized credit unions—those with \$35–65 million in and for those with assets greater than \$300 million. In 2003, credit unions with assets greater than \$100 million represented 6% of all credit unions in Iowa, but controlled approximately 57% of all credit union assets. In comparison, 31% of all Iowa-headquartered banks were greater than \$100 million in assets and controlled 71% of all assets.

In Figure 6, we show the relative real growth in total bank and credit union assets from 1998. In this case, asset growth is the result of industry expansion, not consolidation of banks and credit unions. The rate of expansion in credit union assets is nearly double that of banks headquartered in Iowa. Bank assets have shown little real growth since 1998.

In Figure 7, we show the real deposit growth for all depository institutions in Iowa. Bank deposits are for all FDIC-insured institutions, including thrifts as well as branches of outside banks. As with assets, credit unions are exhibiting a significantly higher growth rate in deposits. This growth in deposits must come from sources outside the credit union industry and may be due to increasing deposits by existing members or new members.

The changes in asset composition for all banks and credit unions between 2000 and 2003 are shown in Figure 8. Iowa credit unions have a larger proportion of consumer, credit card, and automobile loans than do banks. Real estate lending for consumer, commercial, and agricultural purposes is approximately the same. Banks show a much greater proportion of business loans. Note, however, that member business loans in credit unions that are less than \$50,000 would be classified as individual loans. Since 2000, the composition of bank assets has been fairly stable.

In Tables 2, a and b, 3, a and b, and 4, a and b, we present average and common size 1999 and 2003 balance sheets and income statements for three size groupings of Iowa-headquartered banks and credit unions. Note that very small banks and credit unions, those with assets less than \$10 million, have been dropped from the sample. We also have dropped banks with assets more than more than \$1.5 billion. Because our data set excludes large banks branching into this state, by eliminating very large banks headquartered in Iowa, our size categories are more comparable with credit unions. Table 5 gives a general description of the measures used to construct and compare bank and credit union financial statements.

In Table 6, we present selected financial performance measures for the three size groups of credit unions and banks for 1999 and 2003. The definitions for the reported measures are given in Table 7. Note that there are very few credit unions in the medium size category, which can influence the reliability of the estimated values. Note, too, that average asset sizes for large

credit unions and banks are not significantly different. However, average assets for small credit unions are significantly different from those of small banks.

Below are a few observations on relative financial performance.

1. The average interest rate paid on deposits in 2003 is significantly higher for banks. In 1999, the deposit rates are generally not higher for banks, but the difference is not statistically significant at the 10% level.
2. The average loan rate is significantly higher for small credit unions compared with small banks. The loan rate for medium- and large-sized credit union and banks is not statistically different. Because we are only able to compute an average loan rate for each institution, we are unable to account for differences in loan portfolio composition. For example, if interest rates on individual loans tend to be higher than business loans, we would expect the average loan rate for credit unions to be higher than banks, given their apparent concentration in individual loans.
3. The yield on earning assets, which would include income from securities and other interest-bearing sources, is significantly higher for credit unions in both 1991 and 2003.
4. Credit unions tend to have higher loan-to-deposit ratios than banks for all size categories. These differences are statistically significant only in selected years and size categories.
5. The loan loss allowance, as a proportion to total loans, is significantly higher for banks than credit unions for all three size groups.

6. Noninterest income, in general, is a measure of fees collected. Fee income for all banks, as a percentage of total assets, is significantly lower than that for credit unions.
7. Noninterest expense and wages as a percentage of assets are significantly greater for credit unions than banks.
8. The profitability measures, returns on assets and equity, are calculated on a pretax basis for banks. In 2003, the banks outperformed their credit union counterparts by using these profitable measures. The same relationships were observed in 1999, but they were not statistically significant for small- and medium-sized institutions.
9. The equity multiplier, total assets divided by total equity, is not significantly different between banks and credit unions.

This relatively simple comparison of financial performance between credit unions and banks cannot settle any of the long-standing arguments between the two types of financial institutions. But it does raise a number of important points. Taken at face value, there seems to be little evidence that the potential organizational advantages or the tax and regulatory treatment for credit unions translate into lower loan rates, higher deposit rates, or reduced fees for members. Furthermore, we see that credit unions have higher wage bills and other noninterest expense compared with banks. This difference may reflect expense preferences. It also may be the result of credit unions' sizeable individual loan portfolio and greater loan servicing requirements.

We mentioned earlier that credit unions' tax advantages might be used to offer an expanded level of services compared with banks of similar size. Table 8, adapted from the

Jefferson Institute report, summarizes the frequency of various services and products offered by credit unions by size. We do not have equivalent data for banks. However, information in Table 8 suggests relatively few differences in the types of services and products offered by banks and larger credit unions.

### **Remaining Policy Questions**

At the outset, we said that the tax and regulatory policy has been tilted toward credit unions, relative to banks since the 1930s. This tilt was justified at the time, because there were significant numbers of households and communities that, for a variety of reasons, were not or could not be served by the existing banking system.

The question remaining is whether the advantages offered to credit unions can still be justified. There is a cost to tax preferences. Tax preferences shift the tax burden from one group to another. And they can influence the performance and competitiveness of those institutions not eligible for the tax preference. Policymakers and the tax-paying public need to ask whether they are getting what they are paying for.

Public discussions of the appropriate tax and regulatory treatment of credit unions frequently confuse two important, but somewhat separate issues. We briefly restate the two issues and their importance.

1. Should financial intermediaries be organized as investor-owned firms or as cooperatives?
2. Should financial cooperatives (or credit unions in this case) receive preferential tax and regulatory treatment to allow them to carry out a specific societal mission?

The answer to the first question is really not one of public policy. If credit unions and banks are allowed to compete under the same conditions, the market will sort things out. If members of a credit union want to see earnings distributed as patronage, as interest rate differentials or as higher staffing levels and more offices, it is their choice to do so. After all, they own the business and they can accept a return from that business in ways that seem most appropriate. If these advantages, along with opportunities for self-governance result in growth, then there is a benefit to consumers. If banks can operate more efficiently because of the strong incentives created by ownership, pay a return to equity, and meet customer needs and increase their market share—well and good. Competition among firms with different organization, business models, or strategy is generally beneficial to society. The answer to the second question is the crucial one for public policy.

In our view, as credit unions have grown in size, complexity, in their range of services, and in the extent of the markets that they serve, they have no more inherent (or structural) capacity to reach individuals of “small means” than do banks. To fulfill this mission, credit unions would be characterized by small size, a narrow common bond, and financial products targeted to the needs of households or businesses unable to obtain credit from commercial sources.

If banks and larger credit unions are equally able to meet the needs of persons of small means, then it makes little sense, from a public policy perspective, to provide tax or regulatory advantages to one and not the other.



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**Table 1: Taxation of Financial Intermediaries and Cooperatives in Iowa**

	<b>Banks</b>		<b>Credit Unions</b>	<b>Farm Credit System</b>	<b>Cooperatives</b>
	<b>C Corporation</b>	<b>S Corporation</b>			
<b>Federal</b>	<ul style="list-style-type: none"> <li>Income and capital gains taxed as ordinary income at corporate level.</li> <li>Dividends to stockholders not deductible as a business expense.</li> <li>Dividends are taxable to stockholders.</li> </ul>	<ul style="list-style-type: none"> <li>Ordinarily corporation does not pay taxes.</li> <li>Income and capital gains are passed through to stockholders who pay tax.</li> </ul>	<ul style="list-style-type: none"> <li>Ordinary income and capital gains are not taxed.</li> </ul>	<ul style="list-style-type: none"> <li>All income from Federal Land Banks, Federal Land Bank Associations not taxed.</li> <li>Earnings from PCA and Bank for Cooperatives allocated to patronage are not taxable at the corporate level but taxed to members.</li> <li>Unallocated PCA and Bank for Cooperatives earnings, taxed at corporate level.</li> </ul>	<ul style="list-style-type: none"> <li>Income allocated to patronage is not taxable at the corporate level but is taxed to members.</li> <li>Unallocated earnings are taxed at the corporate level.</li> </ul>
<b>Iowa</b>	<ul style="list-style-type: none"> <li>Follows federal rules.</li> <li>Pay a 5% franchise tax on income as financial institutions.</li> </ul>	<ul style="list-style-type: none"> <li>Follows federal rules.</li> <li>Pay a 5% franchise tax on income as financial institutions.</li> </ul>	<ul style="list-style-type: none"> <li>Income is not taxed. Exempt from franchise tax.</li> </ul>	<ul style="list-style-type: none"> <li>Follows federal rules.</li> </ul>	<ul style="list-style-type: none"> <li>Follows federal rules.</li> </ul>

Source: Neil E. Harl, personal communication.

**Table 2: Iowa Credit Unions with more than \$100 Million in Assets, 2003**

Name	Headquarters	Assets (Mill \$)	Members	Counties Served			
				Iowa	Illinois	Wisconsin	Missouri
John Deere Community	Waterloo	858.66	104,603	32			
Collins Community	Cedar Rapids	342.16	49,210	8			
Dupaco Community	Dubuque	326.08	37,077	13	4	4	
University of Iowa Community	Iowa City	322.46	35,503	14			
Du Trac Community	Dubuque	245.97	34,106	6	4	1	
Greater Iowa Community Choice	Ames Johnston	201.56 154.62	29,384 24,027	28 20			
Deere Community Federated	Ottumwa	137.10	36,272	57			8
Linn Area	Cedar Rapids	120.37	20,561	8			
Alcoa Employees & Community	Bettendorf	118.32	20,830	4	4		

Source: Iowa Department of Commerce Credit Union Division at  
<http://www.iacudiv.state.ia.us/Public/fieldofmembership/membersearch.htm>.

**Table 3a: Iowa Financial Institutions Average Balance Sheet by Asset Groups, 1999 and 2003**

	Small (10–65M)					
	Banks			Credit Unions		
	1999	2003	% Change	1999	2003	% Change
No. of Institutions	269	185	-31.2	53	55	3.8
<b>Assets</b>						
Cash	1.50	1.97	31.2	N/A	3.05	N/A
Cash Equivalents	1.10	0.00	-100.0	N/A	0.08	N/A
<b>Total Cash &amp; Equivalents</b>	2.60	1.97	-24.1	N/A	3.13	N/A
<b>Loans</b>						
Lease Receivable	0.06	0.03	-51.8	0.04	0.00	-95.4
Individual Loans	2.15	1.83	-15.2	10.41	10.72	3.0
Real Estate Loans	11.29	13.40	18.7	5.01	6.37	27.2
Business Loans	8.23	9.21	11.9	1.31	1.39	6.1
Total Loans	21.73	24.46	12.5	17.12	18.49	8.0
Allowance for Loan Loss	0.31	0.35	11.3	0.16	0.13	-18.0
<b>Net Loans</b>	21.42	24.11	12.6	16.96	18.36	8.3
<b>Investments</b>						
Available for Sale	7.92	8.69	9.8	0.38	0.42	10.2
Held to Maturity	2.61	2.54	-2.8	0.05	0.21	292.0%
Other Investments	N/A	N/A	N/A	N/A	4.73	N/A
Total Investments	9.43	11.23	19.1	N/A	5.16	N/A
Fixed Assets	0.48	0.52	7.7	0.63	0.74	17.1
Intangible Assets	0.14	0.21	50.2	N/A	N/A	N/A
NCUA Insurance Deposit	N/A	N/A	N/A	0.19	0.23	20.0
Other Assets	N/A	N/A	N/A	0.15	0.16	12.5
<b>Total Assets</b>	36.11	39.54	9.5	23.02	27.79	20.7
<b>Liabilities</b>						
Deposits	30.56	32.84	7.5	N/A	N/A	N/A
Other Liabilities	1.80	2.32	28.4	0.39	0.50	27.0
<b>Shares</b>						
Share Drafts	N/A	N/A	N/A	2.79	3.14	12.4
Regular Shares	N/A	N/A	N/A	8.34	11.04	32.5
Other Shares	N/A	N/A	N/A	8.97	9.94	10.8
<b>Total Liabilities</b>	32.37	35.16	8.6	20.49	24.63	20.2
<b>Equity</b>						
Common Stock	0.28	0.27	-3.5	N/A	N/A	N/A
Preferred Stock	0.00	0.00	-100.0	N/A	N/A	N/A
Undivided Earnings	2.09	2.46	17.7	0.85	1.23	43.9
Other Equity	1.37	1.65	20.5	0.00	1.94	100.0
<b>Total Equity</b>	3.74	4.38	17.0	0.85	3.16	271.7
<b>Total Liabilities &amp; Equity</b>	36.11	39.54	9.5	21.35	27.79	30.2

Table 3a: Continued

	Medium (65–100 M)					
	Banks			Credit Unions		
	1999	2003	% Change	1999	2003	% Change
No. of Institutions	79	91	15.2	4	2	-50.0
<b>Assets</b>						
Cash	3.17	3.50	10.5	N/A	18.63	N/A
Cash Equivalents	1.59	0.00	-100.0	N/A	0.00	N/A
<b>Total Cash &amp; Equivalents</b>	4.76	3.50	-26.5	N/A	18.63	N/A
<b>Loans</b>						
Lease Receivable	0.21	0.28	31.2	0.11	0.00	-100.0
Individual Loans	4.58	3.69	-19.4	29.40	36.50	24.1
Real Estate Loans	26.47	28.92	9.3	26.75	20.58	-23.1
Business Loans	18.60	17.62	-5.3	2.43	1.64	-32.4
Total Loans	49.86	50.51	1.3	58.70	58.72	0.0
Allowance for Loan Loss	0.68	0.65	-4.5	0.54	0.61	13.2
<b>Net Loans</b>	49.18	49.86	1.4	58.16	58.11	-0.1
<b>Investments</b>						
Available for Sale	19.18	19.92	3.8	2.74	1.03	-62.6
Held to Maturity	3.37	2.15	-36.2	0.00	0.00	0.0
Other Investments	N/A	N/A	N/A	N/A	15.14	N/A
Total Investments	20.96	22.07	5.3	N/A	16.17	N/A
Fixed Assets	1.08	1.18	9.9	2.09	2.59	24.1
Intangible Assets	0.29	0.32	10.0	N/A	N/A	N/A
NCUA Insurance Deposit	N/A	N/A	N/A	0.64	0.82	28.9
Other Assets	N/A	N/A	N/A	0.85	0.46	-45.6
<b>Total Assets</b>	80.20	80.63	0.5	79.77	96.78	21.3
<b>Liabilities</b>						
Deposits	67.72	65.98	-2.6	N/A	N/A	N/A
Other Liabilities	5.08	6.32	24.4	1.27	0.40	-68.3
<b>Shares</b>						
Share Drafts	N/A	N/A	N/A	13.49	14.15	4.8
Regular Shares	N/A	N/A	N/A	32.98	31.83	-3.5
Other Shares	N/A	N/A	N/A	23.50	40.85	73.9
<b>Total Liabilities</b>	72.80	72.30	-0.7	71.24	87.23	22.4
<b>Equity</b>						
Common Stock	0.48	0.51	6.6	N/A	N/A	N/A
Preferred Stock	0.02	0.00	-100.0	N/A	N/A	N/A
Undivided Earnings	4.67	4.86	4.1	4.29	3.74	-12.9
Other Equity	2.23	2.97	33.2	0.00	5.81	100.0
<b>Total Equity</b>	7.40	8.33	12.7	4.29	9.55	122.4
<b>Total Liabilities &amp; Equity</b>	80.20	80.63	0.5	75.54	96.78	28.1

Table 3a: Continued

## Large (100 M–1.5 B)

	Banks			Credit Unions		
	1999	2003	%	1999	2003	%
			Change			Change
No. of Institutions	79	112	41.8	6	10	66.7
<b>Assets</b>						
Cash	18.47	29.88	61.8	N/A	11.78	N/A
Cash Equivalents	0.00	0.00	0.0	N/A	0.04	N/A
<b>Total Cash &amp; Equivalents</b>	30.11	29.88	-0.7	N/A	11.83	N/A
<b>Loans</b>						
Lease Receivable	1.11	0.60	-45.7	0.42	0.00	-99.5
Individual Loans	24.01	8.69	-63.8	76.53	97.06	26.8
Real Estate Loans	98.81	85.56	-13.4	94.33	101.06	7.1
Business Loans	59.12	48.67	-17.7	8.60	12.33	43.4
Total Loans	182.44	143.52	-21.3	179.89	210.46	17.0
Allowance for Loan Loss	2.60	1.97	-24.2	1.12	1.33	18.5
<b>Net Loans</b>	179.84	141.56	-21.3	178.77	209.13	17.0
<b>Investments</b>						
Available for Sale	74.89	54.09	-27.8	10.73	4.84	-54.9
Held to Maturity	6.38	2.39	-62.6	27.36	31.25	14.2
Other Investments	N/A	N/A	N/A	N/A	10.85	N/A
Total Investments	72.36	56.48	-22.0	N/A	46.94	N/A
Fixed Assets	4.14	3.42	-17.5	5.36	7.17	33.9
Intangible Assets	0.86	2.60	200.7	N/A	N/A	N/A
NCUA Insurance Deposit	N/A	N/A	N/A	1.87	2.16	15.6
Other Assets	N/A	N/A	N/A	4.01	3.65	-9.0
<b>Total Assets</b>	306.78	248.47	-19.0	253.22	282.73	11.7
<b>Liabilities</b>						
Deposits	241.03	200.71	-16.7	N/A	N/A	N/A
Other Liabilities	41.08	23.67	-42.4	19.25	15.75	-18.2
<b>Shares</b>						
Share Drafts	N/A	N/A	N/A	29.84	31.97	7.2
Regular Shares	N/A	N/A	N/A	74.52	82.95	11.3
Other Shares	N/A	N/A	N/A	105.35	123.04	16.8
<b>Total Liabilities</b>	282.10	224.38	-20.5	228.96	253.71	10.8
<b>Equity</b>						
Common Stock	1.64	1.40	-15.0	N/A	N/A	N/A
Preferred Stock	0.00	0.00	0.0	N/A	N/A	N/A
Undivided Earnings	12.49	11.12	-11.0	11.67	15.23	30.5
Other Equity	10.53	11.57	9.9	0.00	13.79	100.0
<b>Total Equity</b>	24.67	24.09	-2.4	11.67	29.02	148.6
<b>Total Liabilities &amp; Equity</b>	306.78	248.47	-19.0	240.63	282.73	17.5



**Table 3b: Iowa Financial Institutions Common Size Balance Sheet, 1999 and 2003  
Small (10–65 M)**

	<b>Banks</b>		<b>Credit Unions</b>	
	1999	2003	1999	2003
No. of Institutions	269	185	53	55
<b>Assets</b>				
Cash	4.2%	5.0%	N/A	11.0%
Cash Equivalents	3.0%	0.0%	N/A	0.3%
<b>Total Cash &amp; Equivalents</b>	7.2%	5.0%	N/A	11.3%
<b>Loans</b>				
Lease Receivable	0.2%	0.1%	0.2%	0.0%
Individual Loans	6.0%	4.6%	45.2%	38.6%
Real Estate Loans	31.3%	33.9%	21.8%	22.9%
Business Loans	22.8%	23.3%	5.7%	5.0%
Total Loans	60.2%	61.9%	74.4%	66.5%
Allowance for Loan Loss	0.9%	0.9%	0.7%	0.5%
<b>Net Loans</b>	59.3%	61.0%	73.7%	66.1%
<b>Investments</b>				
Available for Sale	21.9%	22.0%	1.7%	1.5%
Held to Maturity	7.2%	6.4%	0.2%	0.7%
Other Investments	N/A	N/A	N/A	17.0%
Total Investments	26.1%		N/A	18.6%
Fixed Assets	1.3%	1.3%	2.7%	2.7%
Intangible Assets	0.4%	0.5%	N/A	N/A
NCUA Insurance Deposit	N/A	N/A	0.8%	0.8%
Other Assets	N/A	N/A	0.6%	0.6%
<b>Total Assets</b>	100.0%	100.0%	100.0%	100.0%
<b>Liabilities</b>				
Deposits	84.6%	83.1%	N/A	N/A
Other Liabilities	5.0%	5.9%	1.7%	1.8%
<b>Shares</b>				
Share Drafts	N/A	N/A	12.1%	11.3%
Regular Shares	N/A	N/A	36.2%	39.7%
Other Shares	N/A	N/A	39.0%	35.8%
<b>Total Liabilities</b>	89.6%	88.9%	89.0%	88.6%
<b>Equity</b>				
Common Stock	0.8%	0.7%	N/A	N/A
Preferred Stock	0.0%	0.0%	N/A	N/A
Undivided Earnings	5.8%	6.2%	3.7%	4.4%
Other Equity	3.8%	4.2%	0.0%	7.0%
<b>Total Equity</b>	10.4%	11.1%	3.7%	11.4%
<b>Total Liabilities &amp; Equity</b>	100.0%	100.0%	100.0%	100.0%

Table 3b: Continued

	Medium (65–100 M)			
	Banks		Credit Unions	
	1999	2003	1999	2003
No. of Institutions	79	91	4	2
<b>Assets</b>				
Cash	4.0%	4.3%	N/A	19.2%
Cash Equivalents	2.0%	0.0%	N/A	0.0%
<b>Total Cash &amp; Equivalents</b>	5.9%	4.3%	N/A	19.2%
<b>Loans</b>				
Lease Receivable	0.3%	0.3%	0.1%	0.0%
Individual Loans	5.7%	4.6%	36.9%	37.7%
Real Estate Loans	33.0%	35.9%	33.5%	21.3%
Business Loans	23.2%	21.9%	3.1%	1.7%
Total Loans	62.2%	62.6%	73.6%	60.7%
Allowance for Loan Loss	0.8%	0.8%	0.7%	0.6%
<b>Net Loans</b>	61.3%	61.8%	72.9%	60.0%
<b>Investments</b>				
Available for Sale	23.9%	24.7%	3.4%	1.1%
Held to Maturity	4.2%	2.7%	0.0%	0.0%
Other Investments	N/A	N/A	N/A	15.6%
Total Investments	26.1%	27.4%	N/A	16.7%
Fixed Assets	1.3%	1.5%	2.6%	2.7%
Intangible Assets	0.4%	0.4%	N/A	N/A
NCUA Insurance Deposit	N/A	N/A	0.8%	0.8%
Other Assets	N/A	N/A	1.1%	0.5%
<b>Total Assets</b>	100.0%	100.0%	100.0%	100.0%
<b>Liabilities</b>				
Deposits	84.4%	81.8%	N/A	N/A
Other Liabilities	6.3%	7.8%	1.6%	0.4%
<b>Shares</b>				
Share Drafts	N/A	N/A	16.9%	14.6%
Regular Shares	N/A	N/A	41.3%	32.9%
Other Shares	N/A	N/A	29.5%	42.2%
<b>Total Liabilities</b>	90.8%	89.7%	89.3%	90.1%
<b>Equity</b>				
Common Stock	0.6%	0.6%	N/A	N/A
Preferred Stock	0.0%	0.0%	N/A	N/A
Undivided Earnings	5.8%	6.0%	5.4%	3.9%
Other Equity	2.8%	3.7%	0.0%	6.0%
<b>Total Equity</b>	9.2%	10.3%	5.4%	9.9%
<b>Total Liabilities &amp; Equity</b>	100.0%	100.0%	100.0%	100.0%

Table 3b: Continued

	Large (100 M–1.5 B)			
	Banks		Credit Unions	
	1999	2003	1999	2003
No. of Institutions	79	112	6	10
<b>Assets</b>				
Cash	6.0%	12.0%	N/A	4.2%
Cash Equivalents	0.0%	0.0%	N/A	0.0%
<b>Total Cash &amp; Equivalents</b>	9.8%	12.0%	N/A	4.2%
<b>Loans</b>				
Lease Receivable	0.4%	0.2%	0.2%	0.0%
Individual Loans	7.8%	3.5%	30.2%	34.3%
Real Estate Loans	32.2%	34.4%	37.3%	35.7%
Business Loans	19.3%	19.6%	3.4%	4.4%
Total Loans	59.5%	57.8%	71.0%	74.4%
Allowance for Loan Loss	0.8%	0.8%	0.4%	0.5%
<b>Net Loans</b>	58.6%	57.0%	70.6%	74.0%
<b>Investments</b>				
Available for Sale	24.4%	21.8%	4.2%	1.7%
Held to Maturity	2.1%	1.0%	10.8%	11.1%
Other Investments	N/A	N/A	N/A	3.8%
Total Investments	23.6%	22.7%	N/A	16.6%
Fixed Assets	1.4%	1.4%	2.1%	2.5%
Intangible Assets	0.3%	1.0%	N/A	N/A
NCUA Insurance Deposit	N/A	N/A	0.7%	0.8%
Other Assets	N/A	N/A	1.6%	1.3%
<b>Total Assets</b>	100.0%	100.0%	100.0%	100.0%
<b>Liabilities</b>				
Deposits	78.6%	80.8%	N/A	N/A
Other Liabilities	13.4%	9.5%	7.6%	5.6%
<b>Shares</b>				
Share Drafts	N/A	N/A	11.8%	11.3%
Regular Shares	N/A	N/A	29.4%	29.3%
Other Shares	N/A	N/A	41.6%	43.5%
<b>Total Liabilities</b>	92.0%	90.3%	90.4%	89.7%
<b>Equity</b>				
Common Stock	0.5%	0.6%	N/A	N/A
Preferred Stock	0.0%	0.0%	N/A	N/A
Undivided Earnings	4.1%	4.5%	4.6%	5.4%
Other Equity	3.4%	4.7%	0.0%	4.9%
<b>Total Equity</b>	8.0%	9.7%	4.6%	10.3%
<b>Total Liabilities &amp; Equity</b>	100.0%	100.0%	100.0%	100.0%

**Table 4a: Iowa Financial Institutions Average Income Statement by Asset Groups, 1999 and 2003**  
**Small (10–65 M)**

	<b>Banks</b>			<b>Credit Unions</b>		
	1999	2003	% Change	1999	2003	% Change
No. of Institutions	269	185	-31.2	53	55	3.8
<b>Income</b>						
<b>Interest Income</b>						
Interest on Loans	1.79	1.63	-8.9	1.46	1.32	-9.2
Other Interest Income	0.68	0.47	-31.8	0.26	0.18	-28.7
<b>Total</b>	<b>2.47</b>	<b>2.09</b>	<b>-15.2</b>	<b>1.72</b>	<b>1.51</b>	<b>-12.1</b>
<b>Noninterest Income</b>	<b>0.18</b>	<b>0.23</b>	<b>26.9</b>	<b>0.24</b>	<b>0.31</b>	<b>27.2</b>
<b>Total Income</b>	<b>2.65</b>	<b>2.32</b>	<b>-12.4</b>	<b>1.96</b>	<b>1.81</b>	<b>-7.3</b>
<b>Expense</b>						
<b>Interest Expense</b>						
Interest on Deposits (Shares)	1.14	0.63	-44.8	0.71	0.41	-42.3
Other Interest Expense	0.07	0.08	22.3	0.01	0.01	-9.9
<b>Total</b>	<b>1.21</b>	<b>0.71</b>	<b>-41.0</b>	<b>0.72</b>	<b>0.42</b>	<b>-42.3</b>
<b>Noninterest Expense</b>						
Salaries & Benefits	0.53	0.60	14.3	0.44	0.53	19.0
Other Noninterest Expense	0.39	0.42	9.0	0.53	0.59	11.6
<b>Total</b>	<b>0.92</b>	<b>1.03</b>	<b>12.0</b>	<b>0.97</b>	<b>1.11</b>	<b>15.0</b>
<b>Total Expense</b>	<b>2.12</b>	<b>1.74</b>	<b>-18.1</b>	<b>1.69</b>	<b>1.53</b>	<b>-9.4</b>
<b>Net Income Bbefore Taxes</b>	<b>0.53</b>	<b>0.58</b>	<b>10.7</b>	<b>0.27</b>	<b>0.28</b>	<b>6.3</b>
<b>Provision For Loan Losses</b>	<b>0.31</b>	<b>0.35</b>	<b>11.3</b>	<b>0.16</b>	<b>0.13</b>	<b>-18.0</b>
<b>Securities Gains &amp; Losses</b>	<b>-0.14</b>	<b>0.08</b>	<b>-158.6</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>
<b>Applicable Income Taxes</b>	<b>0.11</b>	<b>0.09</b>	<b>-12.4</b>	<b>0.00</b>	<b>0.00</b>	<b>0</b>
<b>Net Income</b>	<b>0.42</b>	<b>0.49</b>	<b>16.5</b>	<b>0.27</b>	<b>0.28</b>	<b>6.3</b>
<b>Net Charge-offs</b>	<b>0.05</b>	<b>0.04</b>	<b>-26.0</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>
<b>Preferred Stock Dividends</b>	<b>0.00</b>	<b>0.00</b>	<b>0.0</b>	<b>0.00</b>	<b>0.00</b>	<b>0</b>
<b>Common Stock Dividends</b>	<b>0.22</b>	<b>0.30</b>	<b>39.4</b>	<b>0.00</b>	<b>0.00</b>	<b>0</b>
<b>Net Operating Income</b>	<b>0.42</b>	<b>0.49</b>	<b>16.5</b>	<b>0.94</b>	<b>0.96</b>	<b>1.9</b>

Table 4a: Continued

	Medium (65–100 M)					
	Banks			Credit Unions		
	1999	2003	% Change	1999	2003	% Change
No. of Institutions	79	91	15.2	4	2	–50.0
<b>Income</b>						
<b>Interest Income</b>						
Interest on Loans	4.04	3.29	–18.7	4.69	4.02	–14.4
Other Interest Income	1.42	0.88	–38.4	0.83	0.57	–31.5
<b>Total</b>	5.46	4.16	–23.8	5.52	4.59	–16.9
<b>Noninterest Income</b>	0.44	0.48	10.0	0.88	0.96	9.0
<b>Total Income</b>	5.90	4.64	–21.3	6.40	5.54	–13.4
<b>Expense</b>						
<b>Interest Expense</b>						
Interest on Deposits (Shares)	2.53	1.25	–50.5	2.20	1.22	–44.5
Other Interest Expense	0.20	0.25	20.6	0.01	0.00	–85.3
<b>Total</b>	2.74	1.50	–45.2	2.22	1.23	–44.7
<b>Noninterest Expense</b>						
Salaries & Benefits	1.06	1.14	7.4	1.40	1.62	15.6
Other Noninterest Expense	0.87	0.85	–2.0	1.84	1.74	–5.4
<b>Total</b>	1.92	1.99	3.2	3.24	3.36	3.7
<b>Total Expense</b>	4.66	3.49	–25.2	5.46	4.58	–16.0
<b>Net Income before Taxes</b>	1.23	1.15	–6.5	0.94	0.96	1.9
<b>Provision for Loan Losses</b>	0.68	0.65	–4.5	0.54	0.61	13.2
<b>Securities Gains &amp; Losses</b>	–0.31	0.21	–168.5	N/A	N/A	N/A
<b>Applicable Income Taxes</b>	0.25	0.17	–31.5	0.00	0.00	0
<b>Net Income</b>	0.98	0.98	–0.1	0.94	0.96	1.9
<b>Net Charge-offs</b>	0.07	0.08	0.5	N/A	N/A	N/A
<b>Preferred Stock Dividends</b>	0.00	0.00	0.0	0.00	0.00	0
<b>Common Stock Dividends</b>	0.58	0.52	–11.1	0.00	0.00	0
<b>Net Operating Income</b>	0.98	0.98	–0.1	0.94	0.96	1.9

Table 4a: Continued

	Large (100 M–1.5 B)					
	Banks			Credit Unions		
	1999	2003	% Change	1999	2003	% Change
No. of Institutions	79	112	41.8	6	10	66.7
<b>Income</b>						
<b>Interest Income</b>						
Interest on Loans	15.25	9.06	–40.6	13.60	12.76	–6.2
Other Interest Income	5.31	2.79	–47.5	3.77	1.75	–53.7
<b>Total</b>	20.56	11.85	–42.4	17.37	14.50	–16.5
<b>Noninterest Income</b>	5.17	6.28	21.6	2.36	4.04	71.3
<b>Total Income</b>	25.73	18.14	–29.5	19.72	18.54	–6.0
<b>Expense</b>						
<b>Interest Expense</b>						
Interest on Deposits (Shares)	8.41	3.20	–61.9	7.82	3.99	–49.0
Other Interest Expense	1.40	0.72	–48.2	0.51	0.51	0.8
<b>Total</b>	9.81	3.93	–60.0	8.33	4.50	–46.0
<b>Noninterest Expense</b>						
Salaries & Benefits	4.40	4.13	–6.3	4.24	5.31	25.3
Other Noninterest Expense	5.49	5.94	8.2	4.22	4.95	17.4
<b>Total</b>	9.89	10.06	1.7	8.46	10.26	21.4
<b>Total Expense</b>	19.70	13.99	–29.0	16.79	14.76	–12.0
<b>Net Income before Taxes</b>	6.03	4.15	–31.2	2.94	3.78	28.5
<b>Provision for Loan Losses</b>	2.60	1.97	–24.2	1.12	1.33	18.5
<b>Securities Gains &amp; Losses</b>	–1.02	0.82	–180.4	N/A	N/A	N/A
<b>Applicable Income Taxes</b>	1.37	0.85	–38.0	0.00	0.00	0
<b>Net Income</b>	4.66	3.30	–29.2	2.94	3.78	28.5
<b>Net Charge-offs</b>	0.35	0.29	–16.7	N/A	N/A	N/A
<b>Preferred Stock Dividends</b>	0.00	0.00	0.0	0.00	0.00	0
<b>Common Stock Dividends</b>	2.25	2.17	–3.7	0.00	0.00	0
<b>Net Operating Income</b>	4.66	3.30	–29.2	2.94	3.78	28.5

**Table 4b: Iowa Financial Institutions Common Size Income Statement, 1999 and 2003**

	<b>Small (10–65 M)</b>			
	<b>Banks</b>		<b>Credit Unions</b>	
	1999	2003	1999	2003
No. of Institutions	269	185	53	55
<b>Income</b>				
<b>Interest Income</b>				
Interest on Loans	67.4%	70.1%	74.5%	73.0%
Other Interest Income	25.8%	20.1%	13.2%	10.1%
<b>Total</b>	93.2%	90.2%	87.7%	83.1%
<b>Noninterest Income</b>	6.8%	9.8%	12.3%	16.9%
<b>Total Income</b>	100.0%	100.0%	100.0%	100.0%
<b>Expense</b>				
<b>Interest Expense</b>				
Interest on Deposits (Shares)	43.0%	27.1%	36.3%	22.6%
Other Interest Expense	2.6%	3.6%	0.4%	0.4%
<b>Total</b>	45.5%	30.6%	36.8%	22.9%
<b>Noninterest Expense</b>				
Salaries & Benefits	19.9%	26.0%	22.6%	29.0%
Other Noninterest Expense	14.7%	18.3%	26.9%	32.4%
<b>Total</b>	34.6%	44.3%	49.5%	61.4%
<b>Total Expense</b>	80.2%	74.9%	86.3%	84.3%
<b>Net Income before Taxes</b>	19.8%	25.1%	13.7%	15.7%
<b>Provision for Loan Losses</b>	11.8%	15.0%	8.2%	7.3%
<b>Securities Gains &amp; Losses</b>	-5.3%	3.6%	N/A	N/A
<b>Applicable Income Taxes</b>	4.0%	4.0%	0.0%	0.0%
<b>Net Income</b>	15.8%	21.0%	13.7%	15.7%
<b>Net Charge-offs</b>	1.8%	1.6%	N/A	N/A
<b>Preferred Stock Dividends</b>	0.0%	0.0%	0.0%	0.0%
<b>Common Stock Dividends</b>	8.1%	13.0%	0.0%	0.0%
<b>Net Operating Income</b>	15.8%	21.0%	48.1%	52.9%

Table 4b: Continued

	Medium (65–100 M)			
	Banks		Credit Unions	
	1999	2003	1999	2003
No. of Institutions	79	91	4	2
<b>Income</b>				
<b>Interest Income</b>				
Interest on Loans	68.5%	70.8%	73.3%	72.5%
Other Interest Income	24.1%	18.9%	13.0%	10.3%
<b>Total</b>	92.6%	89.7%	86.3%	82.7%
<b>Noninterest Income</b>	7.4%	10.3%	13.7%	17.3%
<b>Total Income</b>	100.0%	100.0%	100.0%	100.0%
<b>Expense</b>				
<b>Interest Expense</b>				
Interest on Deposits (Shares)	43.0%	27.0%	34.4%	22.0%
Other Interest Expense	3.5%	5.3%	0.2%	0.0%
<b>Total</b>	46.4%	32.3%	34.7%	22.1%
<b>Noninterest Expense</b>				
Salaries & Benefits	18.0%	24.5%	21.9%	29.2%
Other Noninterest Expense	14.7%	18.3%	28.7%	31.4%
<b>Total</b>	32.6%	42.8%	50.6%	60.6%
<b>Total Expense</b>	79.1%	75.1%	85.3%	82.7%
<b>Net Income before Taxes</b>	20.9%	24.9%	14.7%	17.3%
<b>Provision for Loan Losses</b>	11.5%	13.9%	8.5%	11.1%
<b>Securities Gains &amp; Losses</b>	-5.3%	4.6%	N/A	N/A
<b>Applicable Income Taxes</b>	4.3%	3.7%	0.0%	0.0%
<b>Net Income</b>	16.6%	21.1%	14.7%	17.3%
<b>Net Charge-offs</b>	1.3%	1.6%	N/A	N/A
<b>Preferred Stock Dividends</b>	0.0%	0.0%	0.0%	0.0%
<b>Common Stock Dividends</b>	9.8%	11.1%	0.0%	0.0%
<b>Net Operating Income</b>	16.6%	21.1%	14.7%	17.3%



Table 4b: Continued

	Large (100 M–1.5 B)			
	Banks		Credit Unions	
	1999	2003	1999	2003
No. of Institutions	79	112	6	10
<b>Income</b>				
<b>Interest Income</b>				
Interest on Loans	59.3%	50.0%	68.9%	68.8%
Other Interest Income	20.6%	15.4%	19.1%	9.4%
<b>Total</b>	<b>79.9%</b>	<b>65.4%</b>	<b>88.1%</b>	<b>78.2%</b>
<b>Noninterest Income</b>	20.1%	34.6%	11.9%	21.8%
<b>Total Income</b>	100.0%	100.0%	100.0%	100.0%
<b>Expense</b>				
<b>Interest Expense</b>				
Interest on Deposits (Shares)	32.7%	17.6%	39.6%	21.5%
Other Interest Expense	5.4%	4.0%	2.6%	2.8%
<b>Total</b>	<b>38.1%</b>	<b>21.6%</b>	<b>42.2%</b>	<b>24.3%</b>
<b>Noninterest Expense</b>				
Salaries & Benefits	17.1%	22.8%	21.5%	28.7%
Other Noninterest Expense	21.3%	32.7%	21.4%	26.7%
<b>Total</b>	<b>38.4%</b>	<b>55.5%</b>	<b>42.9%</b>	<b>55.4%</b>
<b>Total Expense</b>	76.6%	77.1%	85.1%	79.6%
<b>Net Income before Taxes</b>	23.4%	22.9%	14.9%	20.4%
<b>Provision for Loan Losses</b>	10.1%	10.8%	5.7%	7.2%
<b>Securities Gains &amp; Losses</b>	-3.9%	4.5%	N/A	N/A
<b>Applicable Income Taxes</b>	5.3%	4.7%	0.0%	0.0%
<b>Net Income</b>	18.1%	18.2%	14.9%	20.4%
<b>Net Charge-offs</b>	1.4%	1.6%	N/A	N/A
<b>Preferred Stock Dividends</b>	0.0%	0.0%	0.0%	0.0%
<b>Common Stock Dividends</b>	8.7%	12.0%	0.0%	0.0%
<b>Net Operating Income</b>	18.1%	18.2%	14.9%	20.4%

<b>Table 5: Call Report Comparison of Banks and Credit Unions</b>	
<b>Banks</b>	<b>Credit Unions</b>
<b>Assets:</b>	
Cash	Cash
Cash Equivalents Federal Funds Sold	Cash Equivalents
Lease Receivable	Lease Receivable
Individual Loans	Credit Card Loans Other Unsecured Loans New Vehicle Loans Used Vehicle Loans
Real Estate Loans	First Mortgage Real Estate Loans Other Real Estate Loans
Commercial & Industrial Loans	Not Available
Agricultural Loans	Agricultural Loans (Separate Line Item, Cannot Be Individually Subtracted from "Total Loans")
Allowance for Loan & Lease Loss	Allowance for Loan & Lease Loss
Fixed Assets	Real Estate Owned Land & Building Other Fixed Assets
Available for Sale Investments	Available for Sale Investments
Held to Maturity Investments	Held to Maturity Investments
Not Available	Other Investments
Total Investments	Total Investments
Not Applicable	NCUA Insurance Deposit
Not Available	Other Assets
<b>Liabilities</b>	
Deposits	Share Drafts Regular Shares Other Shares
Other Liabilities	Other Liabilities
<b>Equity</b>	
Common Stock	Not Applicable
Preferred Stock	Not Applicable
Undivided Earnings	Undivided Earnings
Other Equity	Other Equity
<b>Interest Income</b>	
Income from Loans	Income from Loans
Other Interest Income	Other Interest Income
<b>Noninterest Income</b>	<b>Noninterest Income</b>
<b>Interest Expense</b>	
Interest on Deposits	Interest on Deposits
Not Applicable	Interest on Shares (In the Interest Expense Category)
Other Interest Expense	Other Interest Expense
<b>Noninterest Expense:</b>	
Salaries & Benefits	Salaries & Benefits
Other Noninterest Expense	Other Noninterest Expense
<b>Net Income before Taxes</b>	<b>Net Income</b>
Provision for Loan & Lease Losses Securities Gains & Losses Applicable Income Taxes Net Income after Taxes	Not Applicable

**Table 6: Iowa Financial Institutions' 1999 and 2003 Average Summary Ratios**

	Small (10–65 M)						Medium (65–100 M)			
	1999		2003			1999		2003		
	Banks	Credit Unions	Banks	Credit Unions	Banks	Credit Unions	Banks	Credit Unions		
No. of Institutions	269	53	185	55	79	4	91	2		
Ave. Asset Value	36.11	23.02 ***	39.54	27.79 ***	80.20	79.77	80.63	96.78 ***		
<b>Cost of Funds</b>										
Ave. Deposit Rate	3.69%	3.59%	1.90%	1.70% ***	3.75%	3.15% ***	1.91%	1.40% ***		
<b>Lending</b>										
Average Loan Rate	8.20%	8.64% ***	6.99%	7.36% **	8.04%	8.00%	6.64%	6.84%		
Net Loans/Deposits	70.77%	83.32% ***	70.27%	73.06%	73.68%	82.86%	74.67%	66.92% ***		
Loan Loss/Total Loans	1.49%	0.96% ***	1.53%	0.80% ***	1.36%	0.97%	1.31%	1.04% *		
Yield on Earning Assets	7.38%	10.96% ***	6.10%	10.31% ***	7.34%	9.55% ***	5.79%	7.82% ***		
<b>Operating</b>										
Noninterest Income/Assets	0.49%	0.97% ***	0.58%	1.01% ***	0.54%	1.12% ***	0.59%	1.00% *		
Noninterest Expense/Assets	2.60%	4.13% ***	2.66%	3.83% ***	2.40%	4.13% ***	2.46%	3.50% *		
Wages/Assets	1.50%	1.89% ***	1.58%	1.81% ***	1.32%	1.79% ***	1.41%	1.68%		
Efficiency	63.59%	78.33% ***	63.8	79.6 ***	60.92%	77.47% ***	63.25%	77.77% ***		
<b>Profitability</b>										
ROA	0.91%	0.89%	1.10%	0.78% ***	1.09%	0.95%	1.12%	0.60% ***		
ROE	9.10%	8.16%	10.15%	6.68% ***	12.24%	9.10% **	11.42%	6.18% ***		
<b>Solvency</b>										
Equity Multiplier	10.74%	11.18%	11.36%	11.50%	9.30%	10.44%	10.39%	9.85%		

\*Statistically different at the 10% level

\*\*Statistically different at the 5% level

\*\*\*Statistically different at the 1% level

**Table 6: Continued**

**Large (100 M–1.5 B)**

	1999		2003		
	Banks	Credit Unions	Banks	Credit Unions	
No. of Institutions	82	6	120	10	
Ave. Asset Value	306.78	253.22	248.47	282.73	
<b>Cost of Funds</b>					
Average Deposit Rate	3.71%	3.72%	1.94%	1.62%	***
<b>Lending</b>					
Ave. Loan Rate	7.94%	7.64%	6.52%	6.35%	
Net Loans/Deposits	81.38%	87.48%	78.56%	88.80%	***
Loan Loss/Total Loans	1.27%	0.64%	1.30%	0.61%	***
Yield on Earning Assets	7.41%	9.76%	5.75%	7.07%	***
<b>Operating</b>					
Noninterest Income/Assets	0.72%	1.01%	0.76%	1.61%	***
Noninterest Expense/Assets	2.37%	3.43%	2.42%	3.99%	***
Wages/Assets	1.32%	1.68%	1.38%	2.01%	***
Efficiency	62.12%	74.21%	70.81%	73.09%	**
<b>Profitability</b>					
ROA	1.23%	0.93%	1.25%	1.04%	**
ROE	13.57%	10.15%	12.90%	10.74%	*
<b>Solvency</b>					
Equity Multiplier	9.31%	9.59%	1.75%	10.08%	

\*Statistically different at the 10% level

\*\*Statistically different at the 5% level

\*\*\*Statistically different at the 1% level

## Table 7: Description of Summary Ratios

### Cost of Funds

$$\text{Average Deposit Rate} = \frac{\text{Interest on Deposits}}{\text{Total Deposits}}$$

### Lending

$$\text{Average Loan Rate} = \frac{\text{Interest Income From Loans}}{\text{Total Loans}}$$

$$\text{Net Loans/Deposits} = \frac{\text{Net Loans}}{\text{Total Deposits}}$$

$$\text{Loan Loss/Total Loans} = \frac{\text{Allowance for Loan and Lease Loss}}{\text{Total Loans}}$$

$$\text{Percent Individual Loans} = \frac{\text{Loans to Individuals}}{\text{Total Loans}}$$

### Operating

$$\text{Non Interest Income/Assets} = \frac{\text{Non Interest Income}}{\text{Total Assets}}$$

$$\text{Non Interest Expense/Assets} = \frac{\text{Non Interest Expense}}{\text{Total Assets}}$$

$$\text{Wages/Assets} = \frac{\text{Salaries and Benefits}}{\text{Total Assets}}$$

$$\text{Return on Earning Assets} = \frac{\text{Interest Income}}{\text{Total Assets less Cash, Fixed, and Intangible Assets}}$$

$$\text{Efficiency} = \frac{\text{Non Interest Expense}}{\text{Net Interest Income} + \text{Non Interest Income}}$$

**Table 7: Continued**

**Profitability**

$$\text{ROA} = \frac{\text{Net Income Before Taxes}}{\text{Total Assets}}$$

$$\text{ROE} = \frac{\text{Net Income Before Taxes}}{\text{Total Equity}}$$

**Solvency**

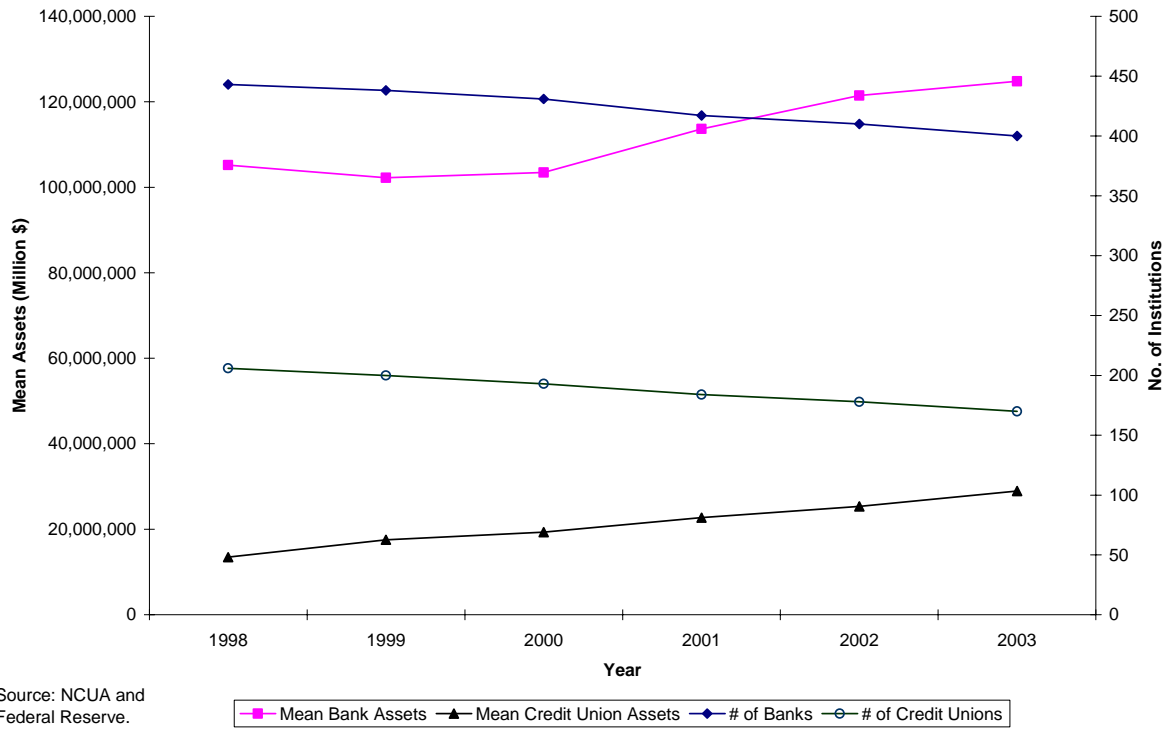
$$\text{Equity Multiplier} = \frac{\text{Total Equity}}{\text{Total Assets}}$$

$$\text{Current Ratio} = \frac{\text{Total Assets}}{\text{Total Liabilities}}$$

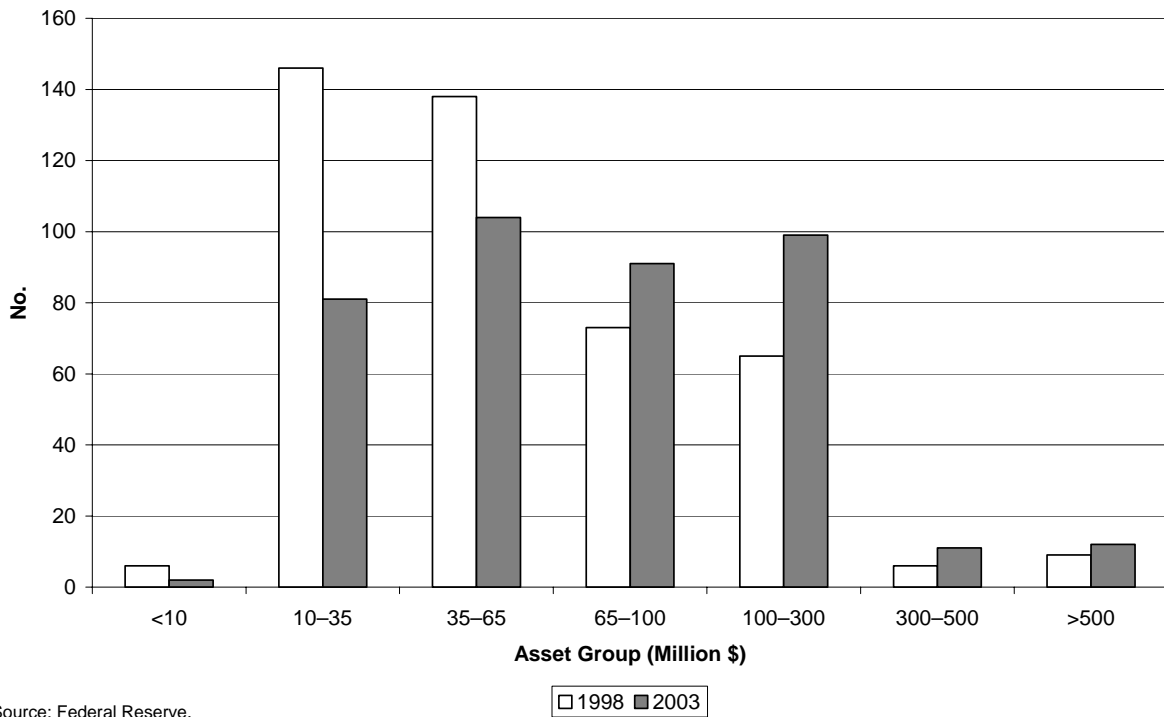
**Table 8. Credit Union Services by Asset Size, in Millions**

	%					
	<b>\$10– 20</b>	<b>\$20– 50</b>	<b>\$50– 100</b>	<b>\$100– 200</b>	<b>\$200– 500</b>	<b>\$500+</b>
Common bond includes community	34.1	47.5	55.0	59.9	63.6	51.7
Stock/bond brokerage	9.3	21.1	37.8	58.2	75.5	84.7
Mutual funds	7.0	18.5	33.9	60.6	77.1	86.6
Savings bonds	19.2	30.1	43.5	57.0	63.8	55.7
Life savings insurance	49.3	44.8	42.7	35.5	39.5	36.5
Direct deposit						
Federal recurring payments	86.8	92.8	91.4	96.1	95.9	94.0
Net pay	86.2	92.2	91.8	95.2	95.1	96.6
Home banking						
Audio response	59.5	82.0	93.6	97.3	98.0	97.3
Personal computers	35.1	62.3	85.3	93.3	98.0	98.7
Have Web site	62.9	85.2	94.2	97.7	98.7	100.0
Cashier's checks	60.0	75.3	83.7	88.1	89.6	96.7
Travelers checks	77.9	90.5	95.2	94.9	98.4	97.3
Safe deposit boxes	9.5	27.6	47.6	62.0	67.7	66.7
Credit counseling	41.7	46.7	49.0	55.6	65.4	68.5
Formal financial planning	6.7	15.7	28.0	53.3	65.7	64.4
ATM cards	74.4	89.1	95.2	97.3	98.8	100.0
Credit cards	66.8	86.4	92.0	94.3	95.6	96.0
Share drafts	88.1	95.7	96.4	98.3	98.7	100.0
Visa/Mastercard debit cards	66.8	32.1	89.8	94.5	97.2	98.0
Certificates	84.1	92.3	96.6	97.3	98.7	96.4
Individual retirement accounts (IRAs)	77.2	90.7	96.6	95.7	100.0	99.3
ROTH IRAs	66.8	84.5	91.5	94.3	97.6	99.3
Business checking	32.2	39.0	44.9	47.8	52.4	33.2
First mortgages	45.3	72.1	84.3	93.1	94.0	98.0
Plane/boat/recreational vehicle loans	87.5	90.7	93.4	97.0	97.2	95.2
Guaranteed student loans	21.1	30.8	42.7	43.8	47.2	52.0
Other student loans	18.5	27.7	31.6	36.9	41.2	52.4

**Figure 1: Number of Financial Institutions and Mean Asset Size, 1998–2003**

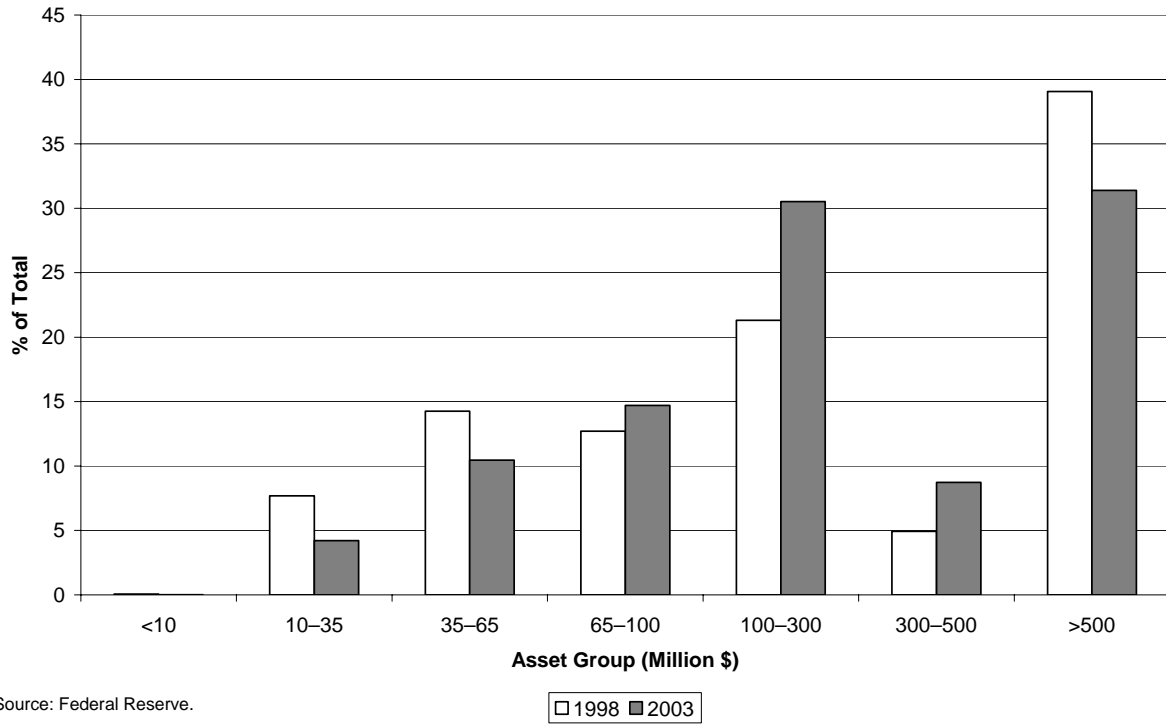


**Figure 2: Number of Iowa Banks, by Asset Group, 1998 and 2003**

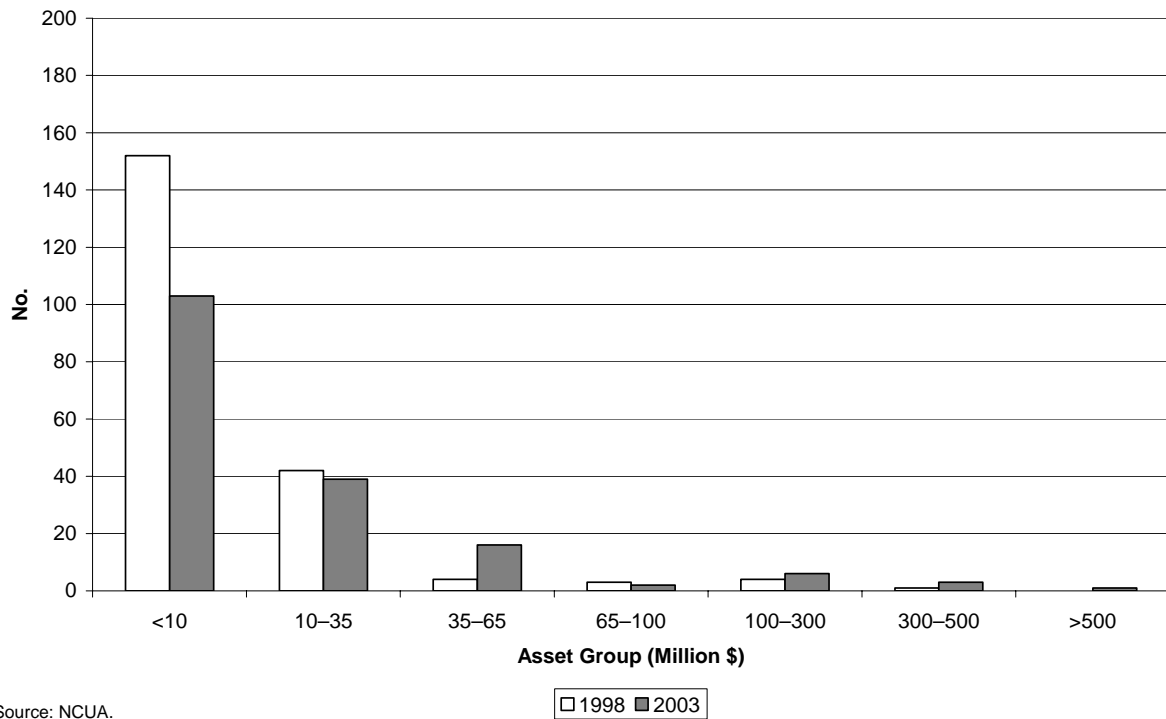




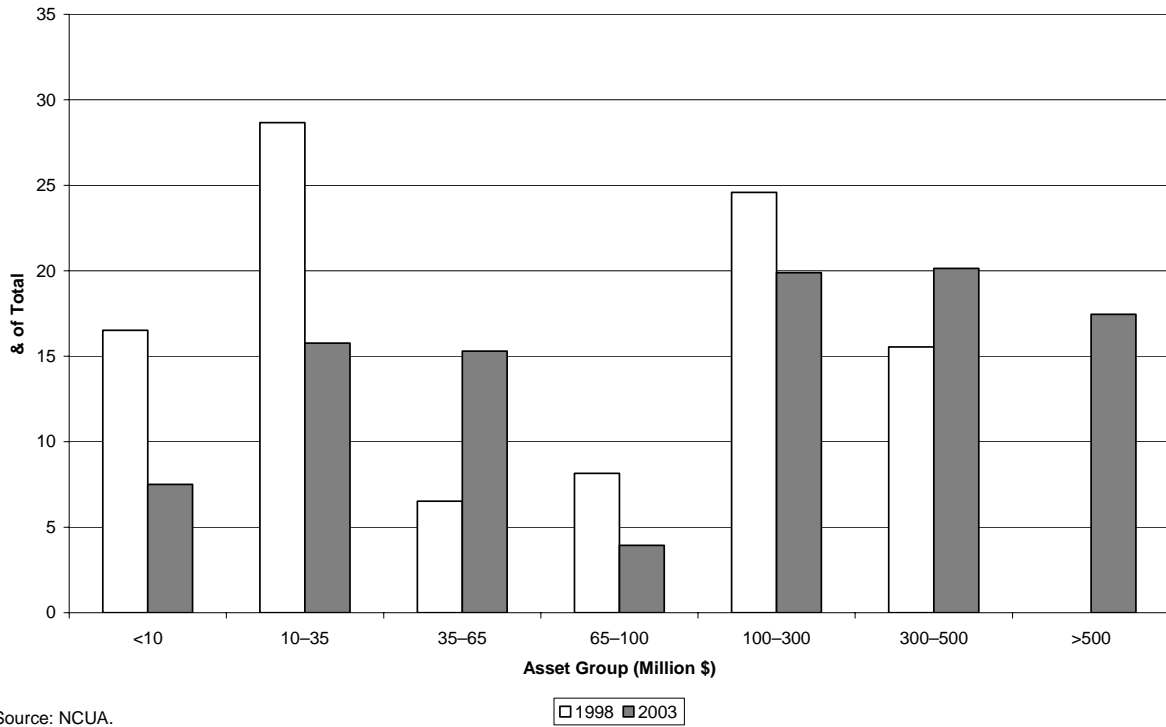
**Figure 3: Iowa Bank Asset Market Share, by Asset Group, 1998 and 2003**



**Figure 4: Number of Iowa Credit Unions, by Asset Group, 1998 and 2003**

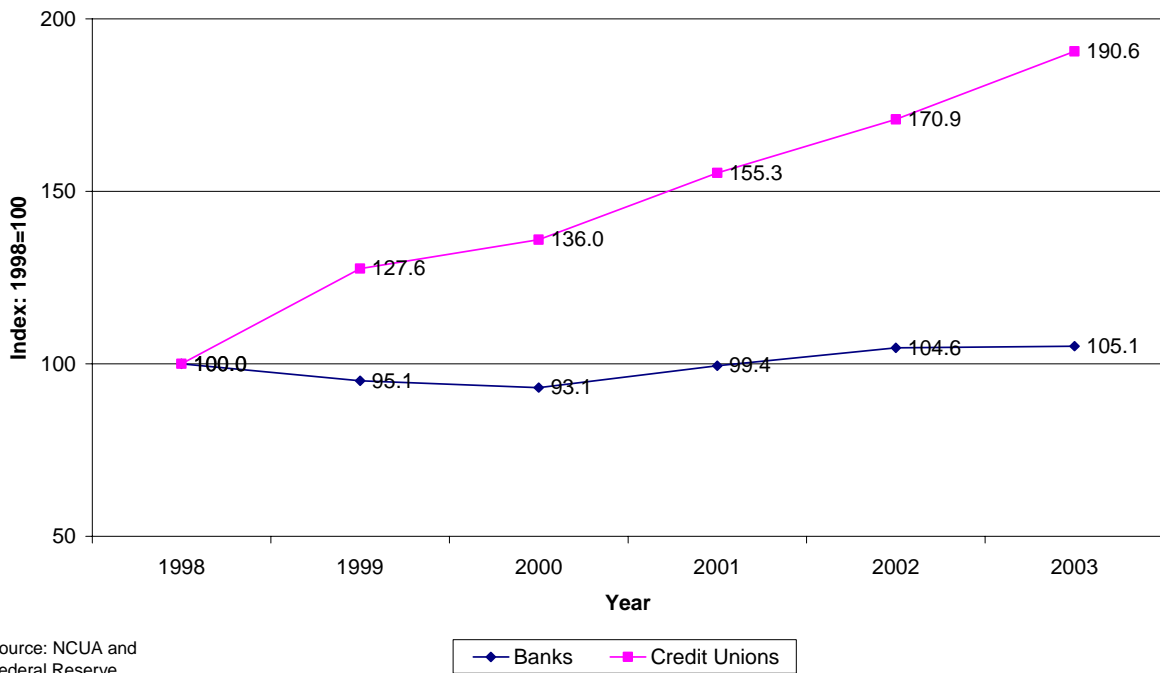


**Figure 5: Iowa Credit Union Asset Market Share, by Asset Groups, 1998 and 2003**



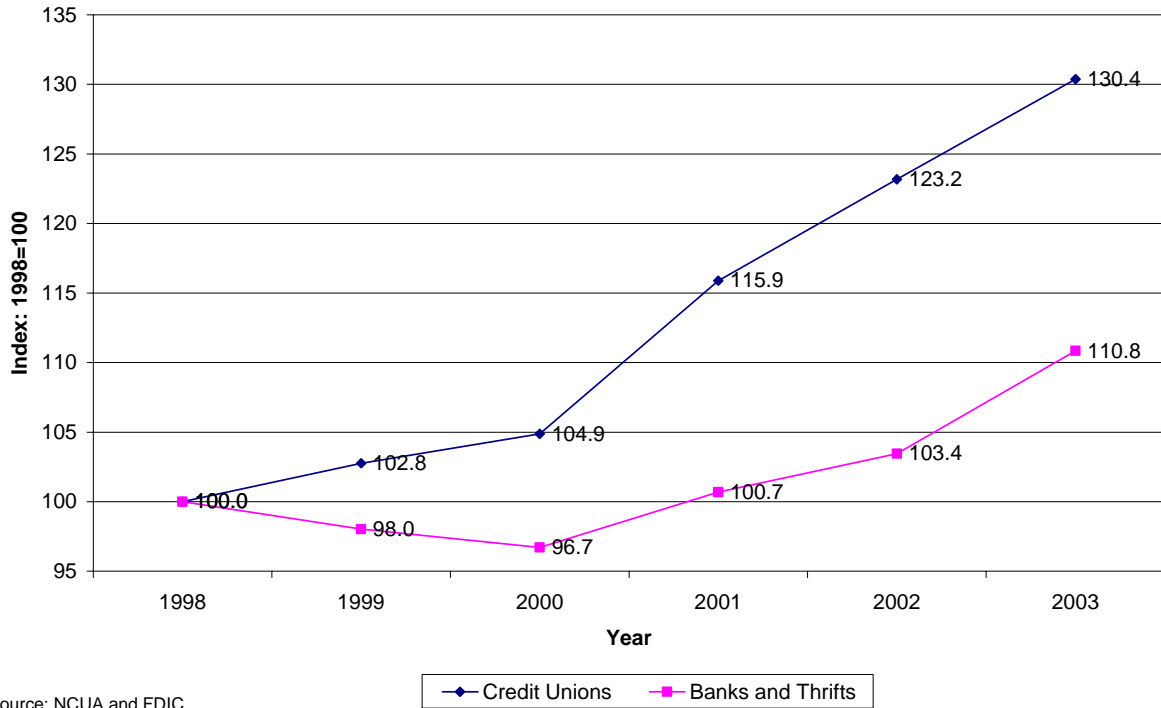
Source: NCUA.

**Figure 6: Real Average Asset Growth in Depository Institutions, 1998-2003**



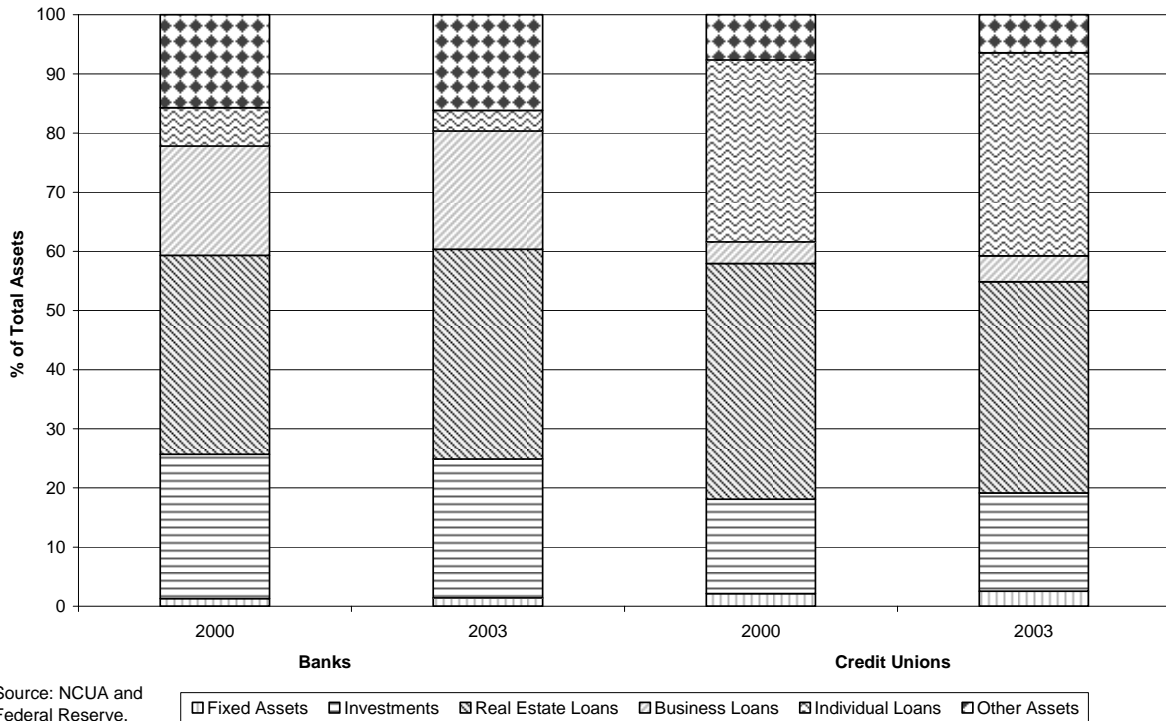
Source: NCUA and Federal Reserve.

**Figure 7: Real Deposit Growth in Depository Institutions, 1998–2003**



Source: NCUA and FDIC.

**Figure 8: Iowa Depository Institutions more than 100 M in Assets, Asset Compositions, 2000 and 2003**



Source: NCUA and Federal Reserve.