

## **THE POLISH CREDIT UNIONS**

**Eugeniusz Gostomski \***

### **Abstract**

Co-operative Credit Unions in Poland have existed since 1992 and are constantly extending their economic potential and their share in the financial services market. The CCUs have a status of a legal person. These banks are non-profit institutions which are created to implement the idea of mutual financial assistance. In order to use their services a potential client has to be a member of one of the CCUs. The members of the CCU can only be people living in the same area or having the same occupation or belonging to the same organization. CCUs offer their own members basic financial services: running a standard bank account, reception of deposits, provision of loans, clearing and settlement of accounts, sale of participation units in investment funds, handling of individual pension accounts, and sale of insurance policies and emission of payment cards. They can also run the accounts of civic associations and people involved in business activity. At the end of 2006 there were 70 credit unions in Poland which together possessed 1584 agencies providing services to their members. The CCUs enlarge their share in the national market of deposits and loans for households, but this share is still of a modest size. At the end of 2005 the assets of CCUs in relation to assets of the banking sector amounted to a mere 0.9%, while in relation to assets of cooperative banks which are their direct competitors, it amounted to 16.3%.

**Keywords:** *Co-operative Credit unions, Banking Services, Households*

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### **INTRODUCTION**

There are over 43 thousand credit unions in the world, offering basic deposit, credit as well as account clearing and settlement services to 157 millions of their members, mainly people of the less wealthy urban areas, protecting them against economic and social exclusion. Members of the credit unions can only be people which are somehow tied together: either by professional bonds, or by living in the same area, being employed in one institution or belonging to an association. Credit

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unions are non-profit organizations. It means that their financial activity, which must be carried out in compliance with principles of economic rationality, is not oriented on the achievement of profit that is supposed to be distributed among their members.

At present credit unions operate in 92 countries on 5 continents. The most fully developed system of credit unions functions in the USA, both as far as the number of credit unions (almost 9000) or the number of their members (86 million people) is concerned, but also because of the amount of loans granted and the aggregate value of deposits. In Europe the best developed network of credit unions operates in Ireland and the United Kingdom (Gostomski, 2007).

In Poland credit unions work as Co-operative Credit Unions (CCUs, in Polish - Spółdzielcze Kasy Oszczędnościowo-Kredytowe - SKOK). They have existed since 1992 and are constantly extending their economic potential and their share in the financial services market. The first Co-operative Credit Unions were created in Poland as a result of the initiative of the „Solidarność” Trade Union, supported technically by the World Committee of Credit Unions and financially by the US Agency for International Development (USAID).

In 1990 a Foundation for Polish Credit Unions was established. Its aim was to provide organizational support, training and consulting assistance to the newly born credit union system. The Foundation, together with the World Council of Credit Unions (WOCC) elaborated a project of creating credit unions in Poland, funded the training of the SKOK personnel and provided seed capital for the Country Bank (in Polish Kasa Krajowa). In order to train employees of credit unions a Post-Lyceum Bank School (in Polish - Policealna Szkoła Bankowa) was established. Later it gained the status of a higher education establishment and since 2001 it has been called the Sopot High School of Finance and Administration (Wyższa Szkoła Finansów i Administracji w Sopocie).

### **LEGAL FOUNDATIONS OF CREDIT UNION ACTIVITIES IN POLAND**

Initially the co-operative credit unions operated on the basis of the act of 23<sup>rd</sup> May 1991 about trade unions (Act, 2001). They had an exclusively factory character, i.e. they could be created and could operate only within the framework of particular enterprises, which were obliged to provide logistic support to them. The newly created credit unions established the Country Co-operative Credit Union Bank (in Polish: Krajowa Spółdzielcza Kasa Oszczędnościowo - Kredytowa), which became the central institution of the Polish Cooperative Credit Union movement, supporting the activity of particular credit unions.

The Country CU Bank prepared a draft of an act on cooperative credit unions, which was adopted by the parliament on 14th December

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1995 (Act, 1995) and became the foundation of the development of co-operative credit union banks in Poland.

The CCUs created on the basis of the above act have a status of a legal person, they are co-operatives, to which the stipulations of the Law on co-operatives are applied in cases not regulated in the act on CCUs.

These banks are non-profit institutions which are created to implement the idea of mutual financial assistance. In order to use their services a potential client has to be a member of one of the CCUs. The members of the CCU can only be people living in the same area or having the same occupation or belonging to the same organization; in particular:

- workers employed in one or several companies,
- people belonging to the same social or professional organization.

Limiting the membership in a collective bank to people having some links to one another reduces costs of assessing the credit worthiness of people wishing to take a loan and minimizes the credit risk. But on the other hand this limitation slows down the growth of collective banks (Golec, 2004).

CCUs offer their own members basic financial services: running a standard bank account, reception of deposits, provision of loans, clearing and settlement of accounts, sale of participation units in investment funds, handling of individual pension accounts, sale of insurance policies and emission of payment cards. They can also run the accounts of civic associations and people involved in business activity. Since May 2002 the Country Co-operative CU Bank has had its own account in the National Bank of Poland, and customers have had access to electronic accounts via the intermediary of the National Account Settlement Chamber (in Polish - Krajowa Izba Rozliczeniowa).

The CCUs were excluded from the provisions of the EU instruction 2000/12/WE which regulates the process of starting up and conducting the activity of credit institutions. This instruction consolidates earlier bank instructions of the EU which had standardized the process of licensing and conduct of activities of credit institutions in the EU countries. Therefore CCUs are not obliged to meet the capital requirements required from banks (the original capital of at least EUR 5 M which in special cases may be reduced to EUR 1 M) and are not subject to the bank audit. The only institution allowed to inspect and supervise the co-operative credit union banks is the Country Co-operative Credit Bank (Jurkowska, 2005). Without doubt it gives the CCUs a certain competitive advantage over cooperative banks which are obliged to meet the requirements concerning the minimum amount of equity capital and systematically provide numerous reports on their activity to financial supervision institutions.

CCUs conduct their activities according to standards defined by the Country Co-operative Bank. It worked out norms of admissible risk for each credit union bank, concerning the amount of capital, credit

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vindication principles, fulfillment of legal regulations and correct realization of financial activity by the CCUs, the bookkeeping, adjustment of rates of interest and terms to maturity as well as the terms of redemption of assets and liabilities. Since May 2002 the co-operative banks have been using data of the Credit Information Offices concerning the degree of credit exposure of people applying for loans.

At first the cooperative credit unions could not provide credit and loans for business purposes, however, since March 2000, this limitation has not been valid any more. Loans and credits can still be provided by the CCUs for a period defined in advance and not longer than three years. An exception from this rule is only the loans and credits for housing purposes.

### **THE SYSTEM OF POLISH CREDIT UNIONS**

CCUs together with institutions associated with them compose the system of Polish credit unions. It has a two-tier organizational structure.

The first level is created by centralised institutions, which constitute the superstructure of cooperative banks. These are: The Country Cooperative Bank, insurance companies (the Mutual Insurance Company of the CCUs and the Life Insurance Company of the CCUs PLC), the insurance intermediary "Asekuracja" and the Company of Investment Funds SKOK SA. The second tier is made of local cooperative credit union banks.

The Country Cooperative Bank has the form of a cooperative whose members are particular CCUs. The membership of the CCUs in the Country Cooperative CU Bank is obligatory. The aim of the activity of the Country Cooperative Bank is to assure the financial stability of cooperative banks and to perform the supervision over cooperative banks from the point of view of security of accumulated savings and compliance of the credit unions activities with the law.

The Country Cooperative CU Bank performs the following functions in relation to the CCUs:

- carries out the inspection of associated cooperative credit unions;
- supervises the cooperative credit unions;
- helps the banks to manage their liquidity if necessary, accepting the excess of resources from them or providing loans to them.

In case the cooperative credit unions do not have sufficient amounts of deposits related to credit needs, the value of received credits from the Country Cooperative CU Bank determines the level of their credit exposure.

CCUs involved in a workout activity or merging with other cooperative banks can apply to the Country Cooperative CU Bank for resources from a stabilization fund which are charged with an interest

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rate lower than the going market rate. The stabilization fund is created from contributions of cooperative banks equal to 1.22% of their assets.

Cooperative bank can invest free financial resources which were not used for the provision of loans for members into the following instruments:

1. investments in banks to the amount guaranteed by the Bank-Guarantee fund;
2. bonds and other securities issued or guaranteed by the State Treasury or the National Bank of Poland.

Cooperative CUs place the remaining resources in the Country Cooperative CU Bank in the form of standard deposits (different kinds of obligatory investments) and investment deposits.

Apart from the above functions the Country Cooperative CU Bank performs educational, advisory, representative, legislative and other functions for the CCUs.

It should be stressed, that the Country Cooperative CU Bank not only fulfils ancillary functions for the cooperative banks, but it is also an entity which carries out its own business activity in the financial market. Profits resulting from this activity supply the stabilization fund.

**The Foundation for the Sake of Polish Credit Unions** realizes the following three basic tasks:

- promotes the Polish system of cooperative credit unions;
- assures a suitable educational offer to employees and members of managing boards of the credit unions,
- supports scientific research activities.

**The High School of Finance and Administrations** educates leaders and workers of the CCUs on Bachelor and postgraduate studies.

**The "Pieniądze i Więż" (Money and Bond) Publishing House** publishes a scientific quarterly magazine of cooperative credit unions "Money and Bond" (in Polish "Pieniądze i Więż"), covering economic, legal and social issues.

**The Mutual Insurance Association SKOK** insures compulsorily the credit unions from various risks, among others from financial losses that may result from fraudulent activity of employees, and first of all insures the deposits accumulated in credit unions by depositors (members) in case of bankruptcy of the credit union.

The "Asekuracja" company as the intermediary between the CCUs and the insurance companies (including the TUW SKOK) negotiates commissions resulting from the sale of insurance policies, prepares offers for insurance services for credit unions taking into consideration their individual needs and coordinates the activities of insurance agents.

The second level of the Polish credit union system is created by **cooperative credit unions. CCUs (SKOKs)** are the organizations of people, not capital. They act for the sake of their own members, offering

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them basic financial services, not for profit. Members of the CSLAs save and lend money together. Among them there are also people with low incomes who would be ignored by banks if they applied for certain services, especially for credit.

In order to become a CSLA member one should:

- file the member's declaration;
- pay the subscription fee (1-30 PLN);
- bring in member's contribution (1-25 PLN), returned in case of resignation from the CU association.

CCUs operate at large companies or social or professional associations, that is why one has to join them as well.

Credit unions are treated as near-banks which do not need to meet the minimum-requirements standards, such as the level of equity funds, as it is the case with banks. Therefore, it is much easier to create a CCU than a bank. However, as a consequence of this, there is a low level of equity in most credit unions, which is their greatest weakness. The average level of equity funds of a CCUs in 2000 amounted to only 237.5 thousand PLN.

In principle the equity funds of the unions are composed of the following assets:

- a fund consisting of members' shares accumulated from payments of member's shares;
- a reserve fund accumulated from the payment of subscriptions of the members of the credit union, from the balance surplus and property values received free of charge.

The equity funds are reduced each time by balance sheet losses of the credit union.

A weakness of the CCUs is comparatively high level of fixed costs, which, under conditions of a limited scale of operating activity is passed on in the form of high individual costs of the offered products. Due to the modest offer of financial services credit unions are not able to offer demanding customers a complex portfolio of financial services, what causes that they use the offer of competitive institutions. A positive side of the CCUs service offer are, however, the insurance services, which assure a fuller satisfaction of the needs of the members of the CUs and allows for a more efficient use of their agencies.

The weaknesses of credit unions are substantially compensated by their strengths. As institutions of which are smaller than banks scale of operations, they are characterized with a greater flexibility, i.e. they can more quickly react to changes in their environment, adapting their own service-offer to the needs of their members. Thanks to the fact that their customers are exclusively members, customers of credit unions characterize themselves with strong attachment to their financial institution. At the same time a good knowledge of customers allows the

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credit unions to more easily respond to the emerging needs and is a prerequisite allowing to simplify the process of investigation of creditworthiness of persons applying for a loan.

Among the strengths of CCUs it is possible to identify the use of assistance of different subjects. This help can be offered by the enterprise, in which the credit union carries out its activity (eg. free access to premises) or by the organs of the local self-government. Also the central government decided to assist the credit unions, relieving them from the obligation to pay that part of the income-tax which is assigned to statutory aims.

CCUs are financially secure institutions. Till now no CU has ever failed. To protect savings accumulated in the credit unions a Protection Savings Program was set up. This program consists of the Stabilization Fund of the Country Credit Union and the TUW SKOK Collective Insurance of Deposits. Resources of the Stabilization fund are derived from payments of each credit union and amount to about 1.22% of their assets. The insurance of savings guarantees the payment of deposits in case of the bankruptcy at a level similar to the one offered by banks where deposits are guaranteed by the Bank-Guarantee Fund.

### **THE DEVELOPMENT OF ACTIVITIES OF COOPERATIVE CREDIT UNIONS IN POLAND**

CCUs have already operated in Poland for 15 years. At that time systematically both the number of agencies, as well as the number of members of credit unions have increased (see Tab. 1). On the other hand the number of independent credit unions grew until 1998, when it reached the highest number - 220 CCUs. Since then, in consequence of consolidation processes which consisted in taking over of smaller, one-departmental and ineffective CCUs by stronger ones, the number of independent CCUs has steadily decreased. The merger has most often been carried out as a result of an initiative of authorities of taken over credit unions and their members. Thus at the end of 2006 there were 70 credit unions in Poland which together possessed 1584 agencies providing services to their members. Among all institutions in Poland offering banking services to the general population the CCUs have at their disposal the greatest network of agencies. This network systematically increases, though the dynamics of this process has considerably weakened in recent years.

At the end of 2005 CCUs operated in 537 towns, and their agencies were concentrated in particular in the Silesian (300 agencies), Mazovian (154) and Lower-Silesian (141) voivodships. Most of all CCUs agencies were located in the following cities: Warsaw (47), Cracow (34), Katowice (34), Poznań (30), Lublin (28) and Gdańsk (28). The number of CCU members has systematically grown. In 2006 it reached the level of 1,520 thousand. Most of them do not use the financial services of banks

at the same time.

**Table 1: Cooperative Credit Unions in Poland from 1992 to 2006**

Years	Number of credit unions	Dynamics of growth of the number of credit unions, previous year= 100	Number of agencies	Dynamics of growth in the number of agencies, previous year = 100
1992	9	X	13	X
1993	35	389	32	246
1994	84	240	106	331
1995	126	150	137	129
1996	168	133	168	127
1997	198	118	237	141
1998	220	111	290	122
1999	158	72	420	145
2000	133	84	560	133
2001	137	103	680	121
2002	120	88	923	136
2003	109	91	1285	139
2004	83	76	1461	114
2005	76	92	1563	107
2006	70	92	1578	101

**Source:** Author's own elaboration on the basis of data provided by the Country Co-operative CU Bank.

At first the CCUs were developed only at the place of work. In the first half of 1990s the scope of their activities was extended and included the members of the organization of a social or a professional character. At the end of 1997 the resolution of the Country Credit Union obliged the credit unions to diversify the composition of members. This duty, given the limitations of development of credit unions in the market, became one of the reasons of consolidation tendencies among them (M. M. Golec, 2004, p. 188).

The CCUs enlarge their share in the national market of deposits and loans for households, but this share is still of a modest size. At the end of 2005 the assets of CCUs in relation to assets of the banking sector amounted to a mere 0.9%, while in relation to assets of cooperative banks which are their direct competitors, it amounted to 16.3% ("Rozwój systemu finansowego w Polsce w 2005 r.", 2006).

It may be derived from the above data (Table 2) that the value of deposits accumulated by CCUs is greater than the total of loan providing activities. CCUs provide most credits and loans to households for consumption purposes. At the end of 2005 they constituted 67% of their total credit portfolio. 9.2% of all CCUs receivables were receivables resulting from housing loans provided. Loans and overdue receivables



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constituted about 12% of all receivables.

**Table 2: Amount of Assets, Deposits and Receivables in Virtue of Loans Given by the CCUs from 1992 to 2005**

Years	Assets (million PLN)	Deposits (million PLN)	Receivables (million PLN)
1992	4	4	3
1993	11	9	9
1994	35	29	26
1995	101	91	83
1996	219	190	161
1997	368	313	281
1998	590	528	412
1999	883	740	668
2000	1199	995	866
2001	1752	1558	1236
2002	2455	2254	1660
2003	3344	3112	2213
2004	4229	3937	2856
2005	5329	4990	3508

**Source:** Own elaboration on the basis of data provided by the Country Co-operative Credit Union Bank.

The composition of CCU deposits is dominated by deposits with an original time of redemption of less than 1 year, while current deposits constituted only 4.4%.

Deposits in CCUs bear generally a higher interest rate than deposits located in banks, while the interest on loans is lower. This makes the offer of the CCUs substantially more attractive for their members than the bank offer. Among the CCUs customers are not only people which do not use bank services because of low incomes, but first of all people who choose the CCUs because of more profitable conditions of depositing their savings and drawing loans than in banks.

The CCUs have good perspectives of development. They will continue to focus their activity on the provision of basic deposit and credit services, but their offer will gradually expand with the sale of insurance policies and participation units in investment funds. However, due to the weak capital base of the CCUs the possibilities of enlargement of their product offer are limited.

The most important threat for further existence of the CCUs would be to include them into the banking sector. If they are subject to bank supervision and the obligation of contribution to the required reserve at the same level as banks is introduced, it would raise the operating costs of credit unions. On the other hand if they were subject to the universal principles of income taxation it would exert a negative influence on the growth of their capital power. Because of the small scale of their activity, the scope of their operations and relatively high unit costs of products

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offered resulting from it they would not have the chance to compete with banks.

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