THE STORY

OF THE

NORTH SIDE COMMUNITY FEDERAL CREDIT UNION

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The Woodstock Institute

The Woodstock Institute is a not-for-profit organization based in Chicago. For the past twelve years, the Institute has carried out applied research and developed and implemented programs which increase private sector investment in modest-income and minority communities for the benefit of those who live there. It designs programs which bridge the gap between the needs of communities and the resources of banks, savings and loan associations, foundations and others.

The Institute provides a variety of services to community-based organizations, financial institutions, foundations and government agencies, including applied research, policy analysis, program design and evaluation.

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INTRODUCTION

The recent deregulation of financial institutions and the accompanying move of banks and savings and loans away from low-balance, low-income depositors has caused a renewed interest in new vehicles to serve the financial needs of low- and moderate-income neighborhoods. As fees for financial services increase in today's marketplace and affordable consumer credit becomes more difficult to secure, low- and moderate-income neighborhood residents are left with few resources that allow them to participate fully in an economy dependent on financial intermediaries.

In January of 1985, Woodstock Institute began the multi-year Project Credit, designed to identify, develop, and report on new and existing models of credit and financial service provision for low- and moderate-income neighborhoods. This is the first of a series of reports published under Project Credit. It examines community development credit unions as a vehicle for the provision of financial services in low- and moderate-income neighborhoods. A case study of one community development credit union, the North Side Community Federal Credit Union, is used to illustrate the structure, strengths and weaknesses of credit unions.

Since credit unions were introduced in the United States in the early 1900's, they have become an increasingly visible force in America's financial world. In May, 1985, there were 18,240 credit unions with over 50 million members and $129 billion in assets. Despite the size of this financial base, credit unions still view themselves as a movement, not an industry. Unlike other financial institutions, credit unions are owned by their savers and borrowers, which allows them to be particularly sensitive to the needs of their members. Structured so that each member is allowed one vote, regardless of amount on deposit, credit unions give each member an equal voice in decision making regardless of wealth. In practice, this means that profits are distributed back to the membership in the form of higher interest on savings accounts, lower interest on loans, lower or nonexistent fees on services and increased services.

Each credit union is required to define its membership in terms of a common bond which specifically identifies the group it serves. Credit unions can define their common bond in one of three ways: 1) shared place of employment, called "employee" credit unions; 2) membership in an organization (i.e. church), termed "associational" credit unions; or 3) residence or work within a geographic area, called "community development" credit unions. The largest number of credit unions in the United States, over 70% of the total, are employee credit unions. Associational credit unions make up 22% of the market. Community development credit unions are the newest of the three and represent only about 8% of the total.

Community development credit unions were created in the early 1960's to facilitate more local control of money within neighborhoods. They are typically located in low-income, minority urban areas. They are tiny by financial institution standards, and generally small even by credit union standards. However, in some communities they provide the only source of low-cost deposit and credit services. Furthermore, community development credit unions can be an effective tool to address the problems caused by disinvestment and to promote much-needed economic development within low-income and minority neighborhoods.

The North Side Community Federal Credit Union is a community development credit union located in Chicago's Uptown neighborhood. It was established in 1972 as the Uptown People's Credit Union and started as a small associational credit union whose goal was to serve the employees and clients of Uptown's major social service agency. In the twelve years since its founding, it has proved to be a stable, important institution that continues to provide affordable access to credit and deposit services to the residents of its community.

HISTORY OF THE NORTH SIDE COMMUNITY FEDERAL CREDIT UNION

Uptown is a racially-mixed, low-income community located near the lakefront on the north side of Chicago. The 1980 census reports Uptown's median income as only $14,455, less than 70% of the median income for the Chicago SMSA.

For a long time, this community has been a port of entry for incoming groups to Chicago. In the 1950's and 1960's, displaced miners came from the Appalachian region of the South. Most of the Native Americans who moved into Chicago in the 1960's also settled in this area. Other groups such as Japanese-Americans, Hispanic-Americans and Indo-Chinese refugees also made Uptown their first American home. This history is reflected in the community's current racial composition: in 1979, 37.7% of the population was white, 23.3% Hispanic, 14.2% black, 9.9% Asian, and 2.7% American Indian.

The extremes of both wealth and poverty are found in Uptown. Poor residents generally inhabit the numerous multifamily buildings clustered in the eastern part of the neighborhood. In the middle and western sections are many single-family houses occupied by working class, middle- and lower-income residents. Very high-income residents are found in the luxurious high rises and mansions which line the streets fronting on Lake Michigan.

Historically, Uptown residents have been active in trying to solve problems in the neighborhood. People have organized around local issues such as inadequate schools, a need for more social services, and better housing for local residents. During this process, many residents became aware that economic problems were at the root of many social problems. In particular, it became clear that the neighborhood banks were not adequately meeting the needs of the neighborhood.

Research done in the early 1970's showed that over 70% of the deposits at the two largest neighborhood banks came from the Uptown and Edgewater communities. Yet neighborhood leaders felt that these banks were not providing the kinds of services residents needed and were reluctant to extend credit in the neighborhood. They knew that low-income residents needed low-cost banking services, small loans and friendly explanations of credit terms. Middle-income residents needed mortgages and home improvements loans. To respond to these needs, a group of eight neighborhood women who had been involved in these issues decided to establish a credit union which would function as a community bank. They saw a credit union as a vehicle to enable residents to buy their own homes, build up their credit ratings, and get small loans at affordable rates. They hoped that a credit union would also provide consumer education for its members and educate school children in consumer economics.

Today, twelve years after its founding, the North Side Community Federal Credit Union is a community development credit union whose members live and/or work in the area bounded by Hollywood Street on the north, Diversey Avenue on the south, the Lake on the east, and Damen Avenue on the west. It has over 1,000 members, $600,000 in deposits, a professional manager and two branch offices. It offers savings accounts (share accounts), certificates of deposit, small consumer loans, car loans, home improvement loans and first mortgage loans. It does not carry out cash transactions such as check cashing, but it does offer payroll deduction to local employers. As of Spring, 1984, the credit union had made over $2 million dollars in loans in the Uptown-Lakeview area. Between 1981 and 1984 it doubled its deposits size, and it is currently preparing to offer checking accounts to its members.

One of the most unique aspects of the North Side Community Federal Credit Union is its approach to lending. The Board of Directors has consistently made small loans the top priority. In addition, the Credit Union strives to ensure that its lending policies are flexible and geared to the needs of community residents. While small consumer loans are the bread and butter of the credit union's lending, throughout the years it has done a significant amount of what is termed "development lending", loans designed to have a larger impact on the neighborhood.

The Credit Union's current loan portfolio consists of 57% consumer loans and 43% development loans. The most common consumer loans are for debt consolidation, used car repair and purchase, furniture and appliance purchase, vacation expenses, and medical expenses. Most of these loans are very small and they are unlikely to interest other lenders. The most common development loans are cash flow loans for not-for-profit organizations and small home improvement loans to low-income members. These loans are extremely difficult to finance through traditional lenders; however, they have a very positive impact on the neighborhood.

STARTING A CREDIT UNION

Organizing and Chartering the Credit Union

The first step in forming a credit union is to build support for the idea. The initial group of eight women who founded the Uptown Peoples Credit Union began to recruit their neighbors and friends in 1973. The women asked people to show their support for a community credit union through a commitment to purchase at least one share for $5.00*; there was no membership fee. In order to show the credit union regulatory agency that there were enough people who wanted to join the credit union, founding members had to gather 200 such pledges. This took almost a year.

Founding leaders of the Credit Union felt that an associational credit union would be the best type to establish. Since the leadership consisted primarily of employees or friends of Uptown Hull House, they sought sponsorship from Hull House Association, a city-wide umbrella organization of social service agencies. They were successful in securing this sponsorship and in reaching an agreement that the Credit Union office could be located at Uptown Hull House. Sponsorship of an associational credit union by Hull House Association meant that eligible members were restricted to employees, volunteers or clients of Uptown Hull House, residents of Uptown, and employees and volunteers of Hull House Association.

The second hurdle confronted by the founding members was the need to raise money for start-up costs and first year expenses. The initial expenses included charter fees, purchase of office supplies and equipment, marketing, office space, insurance and loan loss reserves. One of the most significant expenses, office space and utilities, was provided by Uptown Hull House. Uptown Hull House also donated staff time and shared

* In credit union terms, shares are the equivalent of savings. Because the members also own the credit union, the shares are also the equivalent of stock.

its reception services with the credit union. To help pay for the other start-up costs, the founders held a garage sale which raised about $5,000. Despite the success of the sale and the support of Uptown Hull House, the Credit Union found it still needed money for ongoing operating expenses in the first year. To address this problem, the members held a pumpkin sale, sharing the proceeds with Uptown Hull House. The pumpkin sale was so successful in generating revenue and in pulling members together that it became an annual event.

CREDIT UNION MANAGEMENT

Governance

Credit union regulations require all credit unions to be governed by a board of directors elected from and by the credit union membership. Board members are elected for a set period of time at the annual membership meeting and traditionally serve without pay. The North Side Community Federal Credit Union has a 15-member board whose members are elected for staggered 1- to 3-year terms. Board meetings are held once a month.

A dedicated board of directors is critical to the maintenance and growth of a credit union. The board not only makes the decisions that establish policy but also oversees the overall operations of the credit union. This often entails actually running the day-to-day operations when the credit union is young and is without any or enough paid staff.

Credit union regulations require two standing committees: a supervisory committee and a credit committee. The supervisory committee is responsible for auditing the books and records of the credit union annually, and for performing a 100% verification of all members' accounts at least once every two years. The credit committee is responsible for all decisions on loan applications, requests for loan extensions and refinancing. In addition, this committee arranges for counseling for members in the wise use of credit. It can perform these duties directly or delegate them to a paid or volunteer loan officer.

The board of directors can establish other committees that they find helpful. In addition to the supervisory and credit committees, the North Side Community Federal Credit Union has established an executive committee, a marketing committee, a personnel policies committee, and a delinquency control committee. Due to the special needs of a community development credit committee, the marketing committee has also established a development subcommittee.

Management

Due to an initial lack of resources, credit unions are often managed by their members, especially in the early years. This is part of the educational process of the membership and is an element which helps to establish a sense of ownership among the members. For many years the Uptown People's Credit Union was managed on a day-to-day basis by its Board and other volunteers. However, as the Credit Union grew, it became impossible to continue total dependency on volunteers. The first step in changing to professional management was the hiring of a CETA* worker in 1976 to keep the books.

Finally, in 1981, the Board hired the first full-time manager of the Credit Union. This was a very significant step that produced results far beyond the expectations of the Board. In approximately two and a half years, deposits at the credit union doubled from $300,000 to $600,000, the charter was changed to reflect the fact that the Credit Union was a community development credit union, and services were expanded. In addition, professional full-time management freed the board to concentrate on long-range planning and policy issues. The result has been improved procedures, a clear sense of goals, and organizational growth.

* CETA was a federal employment and training program that allowed employers hiring disadvantaged workers to recover up to 80% of the qualifying employee's salary.

Technical Assistance

The task of managing a credit union involves technical knowledge. Because deposits in credit unions are insured just like those in other financial institutions, they are subject to federal and sometimes state regulations of their activities. In addition, day-to-day management of even a small credit union requires an understanding of bookkeeping, methodical record keeping, and management of cash flow.

Since the Board of Directors has the overall responsibility for the credit union, its members need to be trained in the basics of credit union governance and management. Those staff and volunteers responsible for day-to-day operations as well as the supervisory committee members need to be well informed on credit union regulations, recordkeeping, and membership services. Finally, the loan committee needs to have a good understanding of loan underwriting, credit union loan policy and regulations and personal budgeting.

Credit unions have several resources on which they can call for training and help in the technical aspects of credit union management. The North Side Community Federal Credit Union received assistance from the Illinois Credit Union League which provided training and materials. The League also suggested procedures and forms to be used for transactions. In addition, membership in the League and in the National Federation of Community Development Credit Unions has provided ongoing advice about regulatory changes.

Critical to the successful management of a credit union is access to professional advice such as accounting and legal services. Because new credit unions have such limited resources, most try to arrange for these services at minimal or no charge. This can be done through pro bono arrangements with appropriate professionals or through recruitment of board members that can either provide the service or have access to providers of the services.

THE BUSINESS FOCUS OF CREDIT UNIONS

As financial institutions, credit unions have a responsibility to their depositors to prudently manage their operations so as to ensure the safety of the deposits. However, credit unions are formed to serve the needs of their members. Many times leadership of credit unions view these two sets of goals as in opposition to each other. For a credit union to succeed, a balance must be found and clearly articulated to the membership.

The most common way that the conflict between the two goals manifests itself in young credit unions is in a high rate of loan delinquencies and defaults. Because of the perceived conflict between running a business and running a social service, community development credit unions often are particularly vulnerable to this problem.

In 1979-80, loan delinquency reached crisis proportions at the North Side Community Federal Credit Union. The credit union had been founded with the intention of providing access to credit to borrowers unwelcome at traditional financial institutions. In the attempt to meet this goal, traditional measures of creditworthiness such as past credit history, ability to repay and employment stability were often overlooked. To compound the problem, all transactions were recorded by hand and it was difficult to track delinquency on a timely basis. The Board of Directors was faced with the choice of continuing to be a "grant making" institution that would eventually be shut down by the regulators or of developing a prudent, methodical approach to loan approval and delinquency follow-up.

The Board chose the latter. Delinquency control measures were established and written down. All seriously delinquent loans were sent to a collection agency, a computerized record of loan accounts was established so that delinquencies could be tracked more easily and a delinquency control committee was appointed. Loan delinquency fell to more acceptable levels within a few months.

As the credit union professionalized its management and improved delinquency control measures, the Board began to focus on other aspects important to the Credit Union's growth. One of the most complex problems the North Side Community Federal Credit Union faced was the high concentration of members with account balances of $500 and less. Not only were the majority of accounts small, but most members made an above average number of deposits and withdrawals. The Credit Union was formed to serve this membership, but these low-balance accounts are very expensive to service and maintain. In order to keep the Credit Union profitable, higher balance accounts were needed. North Side is addressing this issue by developing new marketing efforts designed to attract higher balance accounts, recruiting new payroll deduction employers and actively pursuing non-member deposits from socially conscious investors.

Planning plays a very important part in any organization's development and growth, yet the limitations imposed by lack of resources may often postpone the planning process. The North Side Community Federal Credit Union did not hold its first Board/staff planning session until June, 1983. At that session, a 5-year plan with targeted objectives specified for each year was developed. This plan has been updated and has served not only as a guide for decision making but also as a measure of progress.

THE COMMUNITY DEVELOPMENT POTENTIAL OF CREDIT UNIONS

The ownership structure of credit unions provides an opportunity to create a financial institution that works with and within the community. The unique role played by financial institutions in the economy makes this opportunity particularly significant. By helping to recycle the capital of a community through lending, credit unions can multiply the value of that capital. In addition, credit unions can encourage residents to increase their wealth by providing affordable access to deposit services.

One of the key ways community development credit unions have participated in the economic development of their communities has been through innovative lending. The flexibility of credit unions allows them to develop underwriting standards matched to community realities and to look for new ways to structure loan programs targeted to community needs.

The North Side Community Federal Credit Union is an excellent example of the ways in which credit unions can maximize their community development potential. The community development focus of this credit union has enabled other community organizations to do their job better by providing cash flow loans at critical times, financing equipment purchases and looking for innovative solutions to the financing problems of not-for-profit agencies. For example, a local not-for-profit low-income housing development organization often had cash flow problems despite successful fund-raising efforts. The grants to carry out its projects were often delayed by bureaucratic problems which in turn caused costly delays in the organization's construction schedule. Because most of its grant funds were restricted to specific projects, funds on hand could not be used to alleviate the delays. Although credit union regulations prevented North Side from making a loan to a not-for-profit organization that was not fully secured by deposits, the credit union worked with the housing developer to solve its problem. Now the organization keeps most of its accounts at the credit union and borrows from the credit union against restricted grant funds to avoid project delays.

Another example of North Side's innovation is its response to a community-based organization's need to finance a new computer system in order to manage its services better. Working together, the organization and the credit union were able to get a local funder to deposit $10,000 in a certificate of deposit and allow the CD to be used as collataral for the community organization's loan to finance the computer system.

In response to a local church school's request for help in timely collection of tuition payments, North Side developed a loan program specifically designed to meet the needs of the school. The church opened an account with the Credit Union that was pledged as collateral for student tuition loans. Parents unable to pay tuition in September were referred to the Credit Union for a loan. This provided a means for low-income parents to make monthly payments on children's tuition without burdening the school with bookkeeping and collection problems.

Perhaps the most unique loan program developed by North Side is a very small initiative designed to help a local housing cooperative ensure an economic mix within its building. Three of the six units were set aside for low-income residents. However, the residents selected were not able to finance their $1,000 equity share. Conventional financial institutions would not consider this type of loan or borrower. North Side worked with the project developer to determine the creditworthiness of the borrowers and to ensure the credit union's right to use the unit as collateral for the loan. By making these loans, North Side helped its members to achieve the stability provided by home ownership.

Conclusion

Community development credit unions are a creative and democratic tool which low-income communities can use to increase the availability of financial services. They provide neighborhood residents with the means to satisfy immediate financial needs which would otherwise not be served. The innovative ways in which the North Side Community Federal Credit Union has used its resources also point out the great potential which this type of credit union has in fostering economic development in low-income urban neighborhoods. By linking up with other local institutions such as community-based organizations and schools, the North Side Community Federal Credit Union has increased the neighborhood's ability to address some of its social and economic problems. Through its lending it has strengthened the neighborhood's economic well-being.

As the North Side Community Federal Credit Union's case also shows, the lack of resources available to credit unions in low-income areas imposes limitations in how much they can do in their communities and how soon they can have a sizable impact. Limited resources impose not only economic but also organizational and educational constraints. For the North Side Community Federal Credit Union, the lack of resources meant a lack of professional management for many years, which in turn affected its Board's ability to address other important organizational concerns such as long-term planning and growth. This not only limited services to members, but also full realization of opportunities to have an impact on the community.

A community development credit union in a low-income area must therefore carefully and thoroughly utilize all available resources in order to succeed. It must first have a sponsor with enough resources to minimize the credit union's costs through donations of office space, staff time and other services. It must utilize all available free technical assistance. It must build and utilize a committed core of volunteers. And it must work to quickly build a base of membership and non-member deposits so that a professional staff and increased member services soon become possible. While not a small agenda, these pieces can fit together to form a credit union which will have a significant impact on the financial service needs of its members and its community.