



CUNA & Affiliates

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**WRITTEN TESTIMONY
OF
CHRIS LOSETH
PRESIDENT & CEO, POTLATCH NO.1 FEDERAL CREDIT UNION
AND
CHAIRMAN, IDAHO CREDIT UNION LEAGUE GOVERNMENT AFFAIRS
COMMITTEE
ON BEHALF OF THE
CREDIT UNION NATIONAL ASSOCIATION
ON
“THE CONSIDERATION OF REGULATORY RELIEF PROPOSALS”
BEFORE THE
SENATE BANKING, HOUSING AND URBAN AFFAIRS COMMITTEE

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Chairman Shelby, Ranking Member Sarbanes, Senator Crapo, and other members of the Committee, on behalf of the Credit Union National Association (CUNA), I appreciate this opportunity to come before you and express the association's views on legislation to help alleviate the regulatory burden under which all insured financial institutions operate today.

CUNA is the largest credit union advocacy organization, representing over 90% of our nation's approximately 9,000 state and federal credit unions and their 86 million members.

I am Chris Loseth, President & CEO of Potlatch No.1 Federal Credit Union and Chairman of the Idaho Credit Union League's Government Affairs Committee. Potlatch No.1 Federal Credit Union is a low-income community chartered credit union, serving a total of thirteen counties -- eleven in Idaho and two in Washington. Five of these counties are included in our low-income community charter, while the other eight counties were added through the Underserved Community designation.

The average unemployment rate in the counties we serve (through March of 2005) is 8.1% (with the high being 14.6%). We are very aware of these circumstances and offer several programs to assist our members when they need us most. For example, we offer checking accounts that have no minimum balance requirement, no monthly fees or transactional fees. We also offer debit cards with no monthly fees or transactional fees. Our ATM's charge no fees to our members. According to Callahan and Associates, a national rating service, we rank in the 93rd percentile for checking account penetration, and in the 92nd percentile for checking accounts outstanding among credit unions in the U.S. for March 2005.

Our lending services also have no loan set up fees, no application fees, no annual fees, and are priced competitively in the market place for the benefit of our members. We rank in the 94th percentile for loans outstanding and in the 90th percentile for our loan to share ratio among credit unions in the U.S. (Callahan and Associates, March 2005).

Potlatch No.1 Federal Credit Union offers members free financial counseling through our trained staff, financial literacy classes on a range of topics for our members, and provides volunteers to teach in the local elementary, junior and senior high schools and local colleges to help further financial literacy education. We offer free AD&D insurance to our members, free life savings insurance, free notary services, and low balance certificates of deposit. We also do not have fees for low balance savings accounts, check cashing, and a many other common nuisance fees that many financial institutions charge.

Our credit union's ability to continue serving the financial needs of our current members and our potential members who need access to our services in Northern Idaho and Eastern Washington will be significantly reduced *without* the regulatory relief this Committee is addressing.

CUNA is pleased that the Committee is moving forward with its efforts to provide regulatory relief of unneeded and costly burdens. Some might suggest that the Credit Union Membership Access of 1998¹ (CUMAA) was the credit union version of regulatory relief. While that law did provide relief from an onerous Supreme Court decision, it also imposed several new, stringent regulations on credit unions, which, in spite of assertions to the contrary, are the most stringently regulated of insured financial institutions.

Credit Unions Are Distinct Financial Institutions

Among its numerous provisions, the CUMAA required the U.S. Department of the Treasury to evaluate the differences between credit unions and other types of federally insured financial institutions, including any differences in the regulation of credit unions and banks.

The study, "Comparing Credit Unions with Other Depository Institutions," found that while "credit unions have certain characteristics in common with banks and thrifts, (e.g., the intermediation function), they are clearly distinguishable from these other depository institutions in their structure and operational characteristics."

¹ Pub. L. No. 105-219 Sec. 401; 112 Stat. 913 (1998); 12 USC 1752a note and 1757a note

These qualities, catalogued by the U.S. Treasury in its 2001 study, had been previously incorporated into the congressional findings of the Federal Credit Union Act² when CUMAA was adopted in 1998.

Recognition and appreciation of such attributes is critical to the understanding of credit unions, as Congress made it clear when it amended the Federal Credit Union Act in 1998 that it is these characteristics that form the foundation on which the federal tax exemption for credit unions rests. As Congress determined when it passed CUMAA:

“Credit unions, unlike many other participants in the financial services market, are exempt from Federal and most State taxes because they are:

1. member-owned,
2. democratically operated,
3. not-for profit organizations,
4. generally managed by volunteer boards of directors, and
5. because they have the specified mission of meeting the credit and savings needs of consumers, especially persons of modest means.”

While other institutions, such as mutual thrifts, may meet one or two of these standards or display some of these differences, other credit union distinctions listed here do not necessarily apply. As Treasury noted in its study, “Many banks or thrifts exhibit one or more of ...(these) characteristics, but only credit unions exhibit all five together.”³

² P. L. 105-219, Sec. 2, 112 Stat. 913

³ U.S. Dept. of the Treasury, *Comparing Credit Unions with Other Depository Institutions*, (Wash. DC: 2001.)

Other 1998 congressional findings in CUMAA also emphasize the unique nature of credit unions:

- (1) “The American credit union movement began as a cooperative effort to serve the productive and provident credit needs of individuals of modest means.”
- (2) “Credit unions continue to fulfill this public purpose and current members and membership groups should not face divestiture from the financial services institution of their choice as a result of recent court action.”

Since their inception, credit unions continue to share these unique attributes, separating them from other depository institutions. Despite the frequent attempts of detractors to present credit unions in a false light and label them as other types of institutions, the distinct characteristics of credit unions have been recognized in statute and in analytical reports from the U.S. Treasury and others. Further, despite repeated attempts, legal challenges brought by banking groups against the National Credit Union Administration’s (NCUA) field of membership policies under CUMAA have not proved fruitful.

As unique institutions, credit unions today stand distinctly in need of regulatory relief.

Credit Unions’ Regulatory Burden Is Real And Relief Is Imperative

As cooperative financial institutions, credit unions have not been shielded from the mounting regulatory responsibilities facing insured depositories in this country.

Last year, Federal Deposit Insurance Corporation (FDIC) Vice Chairman John M. Reich said in testimony before the House Subcommittee on Financial Institutions and Consumer Credit, “regulatory burden is a problem for all banks.” His statement is accurate as far as it goes.

Regulatory burden is an issue for all financial institutions generally, and credit unions in particular. Indeed, credit unions **are the most heavily regulated of all financial institutions.** This dubious distinction is the result of several factors, which include:

- Credit unions operate under virtually the same consumer protection rules, such as Truth-Lending, Equal Credit Opportunity, Home Mortgage Disclosure, Real Estate Settlement Procedures Act, Truth-in-Savings, Expedited Funds Availability Act, USA Patriot Act, Bank Secrecy, safety and soundness including prompt corrective action (PCA) regulations reviewed by Treasury, and other rules that apply to banks. Credit unions will also have to comply with developing rules under the Fair and Accurate Credit Transactions (FACT) Act and the Check 21 statutory requirements. A list of the 137 rules that federal credit unions must follow is attached.

In addition:

- (1) Credit unions are the only type of financial institution that have restrictions on whom they may serve;
- (2) Credit unions are the only group of financial institutions that must comply with a federal usury ceiling;

- (3) Credit unions may not raise capital in the marketplace but must rely on retained earnings to build equity;
- (4) Credit unions are the only group of financial institutions that must meet statutory net worth requirements;
- (5) Credit unions face severe limitations on member business lending;
- (6) Credit unions have limitations on loan maturities;
- (7) Credit unions have stringent limitations on investments;
- (8) Credit unions have not been granted new statutory powers, as banks have under Gramm-Leach Bliley; and
- (9) Credit unions' operations and governance are inflexible because many aspects are fixed in statute.

Most importantly for credit unions, time and other resources spent on meeting regulatory requirements are resources that would otherwise be devoted to serving their members – which is, after all, their primary objective.

With Few Exceptions, Credit Unions Must Comply with Virtually All Bank Rules

Despite unfounded banker charges to the contrary, federally insured credit unions bear an extraordinary regulatory burden that is comparable to that of banks in most areas and much more restrictive in others.

As the Treasury's 2001 study comparing credit unions with other institutions concluded, "Significant differences (in the general safety and soundness regulation of banks and credit unions, parenthesis added) have existed in the past, but have been gradually disappearing." The Treasury

study cited PCA and net worth requirements for credit unions as a major regulatory difference that was removed in 1998.

Treasury further noted that their “relative small size and restricted fields of membership” notwithstanding, “federally insured credit unions operate under bank statutes and rules virtually identical to those applicable to banks and thrifts.”

Credit Unions Must Comply With Substantial Requirements Banks Don’t Have to Follow

In addition to following rules applicable to the banking industry, credit unions operate under considerable statutory and regulatory requirements that do not apply to other types of financial institutions.

As Treasury’s study pointed out, credit union statutory net worth requirements direct federally insured credit unions to maintain a minimum of 6% net worth to total assets in order to meet the definition of an adequately capitalized credit union. Well-capitalized credit unions must meet a 7% net worth ratio. “(T)his exceeds the 4% Tier 1 level ratio applicable for banks and thrifts (and is statutory as opposed to regulatory),” Treasury stated. Complex credit unions have additional net worth requirements.

Treasury’s analysis also pointed to the fact that **“federal credit unions have more limited powers than national banks and federal saving associations. Most notably, federal credit unions face stricter limitations on their (member business) ...lending and securities activities.** In addition, a usury ceiling prevents them from charging more than 18% on any loan, and the term of many types of loans may not extend beyond twelve years.”

Credit unions also have statutory and regulatory restrictions as to whom they may serve. Federal credit unions' fields of membership must meet the common bond requirements that apply to an associational, occupational, multi-group or community credit union. Thus, unlike banks and thrifts, which may serve anyone regardless of where they live or work, a credit union may only offer its services to individuals within its field of membership.

Credit unions operate under heavily constrained investment authority as well. A federal credit union may invest in government securities and other investments only as provided under the Federal Credit Union Act and authorized by NCUA.

Credit unions also must comply with limitations on lending, including member business lending. A federal credit unions' member business loan (MBL) may not exceed the lesser of 1.75 times its net worth or 12.25 percent of total assets, unless the credit union is chartered to make such loans, has a history of making such loans or has been designated as a community development credit union. By comparison, banks have no specific limits on commercial lending and thrifts may place up to 20% of their total assets in commercial loans.

It is useful to note that there are other limitations on credit unions' member business lending that do not apply to commercial banks. A credit union's MBLs must generally meet 12-year maturity limits and can only be made to members. Credit union MBLs have significant collateral and while not required, often carry the personal guarantee of the borrower.

Commercial banks have a variety of mechanisms through which they can raise funds, including through deposit-taking or borrowing funds in the capital markets. In marked contrast, credit unions

may only build equity by retaining earnings. A credit union's retained earnings are collectively owned by all of the credit unions' members, as opposed to a bank that is owned by a limited number of stockholders or in some cases, by a finite number of individuals or family members.

Thus, a major distinction between credit unions and commercial banks is that credit unions operate under a number of specific, operational regulations that do not apply to banks. Bank trade associations attempt to mislead Congress when they erroneously argue that credit unions have evolved into banks. The restrictions on credit union operations and the limitations on their activities drive a stake into the heart of that argument.

Unlike Banks, Credit Unions Have Not Received New Statutory Powers

Not only have credit unions not received new statutory powers as banks have, severe regulatory constraints on member business lending and under PCA have been imposed on credit unions for the last several years.

An important study regarding the regulation of credit unions was published in 2003 under the auspices of the Filene Research Institute and addresses the regulatory advantages banks have over credit unions.

Authored by Associate Professor of Economics William E. Jackson, III, Kenan-Flagler Business School, University of North Carolina at Chapel Hill and entitled, "The Future of Credit Unions: Public Policy Issues,"⁴ the study looked at the efforts of Congress over the last two decades to

⁴ Jackson, III, William E., University of North Carolina-Chapel Hill. *The Future of Credit Unions: Public Policy Issues, 2003.*

provide regulatory relief for traditional depository institutions and whether more relief for credit unions is reasonable and appropriate.

The study reviewed sources of funding, investments, and the ownership structure of banks, thrifts and credit unions and found that the operational differences among these types of institutions are “distinctive.” It observed that since 1980, Congress has enacted a number of statutory provisions that have noticeably changed the regulatory environment in which banks and thrifts conduct business, such as by deregulating liabilities; removing restrictions on interstate branching; and expanding the list of activities permissible for financial holding companies.

For example, the Gramm-Leach-Bliley Act of 1999 expanded the statutory definition of the kinds of products and services in which banks may engage. Under the Act, banking institutions may engage in activities that are merely “financial in nature” as opposed to those that are “closely related to banking.” The bank regulators have the authority to determine what is permissible as “financial in nature.” Credit unions were not included in this sweeping, statutory expansion of bank powers. However, while they received neither benefits nor new powers under the Gramm-Leach-Bliley Act, credit unions were included in the substantial requirements under the Act regarding privacy, including requirements to communicate their member privacy protection policies to members on an annual basis.

The credit union study noted, “Credit unions face stricter limitations on their lending and investing activities” than other institutions bear. “In general, credit unions have received less deregulation than either banks or thrifts,” the study concluded.

Pending Credit Union Regulatory Improvements Legislation That CUNA Supports

CUNA strongly supports H.R. 2317, the Credit Union Regulatory Improvements Act (CURIA), which was recently introduced by Representatives Royce and Kanjorski in the House of Representatives. In the 108th Congress, CUNA had also endorsed the House-passed Regulatory Relief Act, which was approved by the House of Representatives on March 18, 2004, by a vote of 392-25.

In our view, these bills provide an excellent starting point for the Senate Banking, Housing and Urban Affairs Committee as it considers real reforms that will provide regulatory relief to credit unions and other institutions.

While CUNA also supports other statutory changes, we first want to focus on amendments to the Federal Credit Union Act--all of which CUNA has endorsed--that are contained in the newly introduced H.R. 2317.

H.R. 2317—The Credit Union Regulatory Improvements Act

Although this legislation goes beyond what was included in the Regulatory Relief measure that passed the House last year, it nevertheless provides a sound foundation for this Committee's consideration of some fundamental problems facing credit unions today and we ask you to take a close look at these proposed changes as incorporated in CURIA. This portion of my testimony will describe the different sections of CURIA, followed by an explanation of why CUNA strongly supports the proposed and necessary changes.

H.R. 2317, THE CREDIT UNION REGULATORY IMPROVEMENTS ACT OF 2005--

SECTION-BY-SECTION DESCRIPTION

TITLE I: CAPITAL REFORM

CUNA strongly supports this title, which reforms the system of PCA for credit unions by establishing a dual ratio requirement: a pure leverage ratio and a net worth to risk-asset ratio. The resulting system would be comparable to the system of PCA in effect for FDIC insured institutions while taking into account the unique operating characteristics of cooperative credit unions.

Section 101. Amendments to Net Worth Categories

The Federal Credit Union Act specifies net worth ratios that, along with a risk-based net worth requirement, determine a credit union's net worth category. This section would continue to specify net worth requirements, but at levels more appropriate for credit unions and comparable to those currently in effect for banking institutions.

Section 102. Amendments Relating to Risk-Based Net Worth Categories

Currently, federally insured credit unions that are considered "complex" must meet a risk-based net worth requirement. This section would require all credit unions to meet a risk-based net worth requirement, and directs the NCUA Board to design the risk-based requirement appropriate to credit unions in a manner more comparable to risk standards for FDIC-insured institutions.

Section 103. Treatment Based on Other Criteria

Current risk-based net worth requirements for credit unions incorporate measures of interest-rate risk as well as credit risk. The comparable standards for risk-based capital requirements for FDIC

insured institutions of Section 102 deal only with credit risk. This section would permit delegation to NCUA's regional directors the authority to lower by one level a credit union's net worth category for reasons of interest rate risk only that is not captured in the risk-based ratios.

Section 104. Definitions Relating to Net Worth

Net worth, for purposes of PCA, is currently defined as a credit union's retained earnings balance under generally accepted accounting principles. The Financial Accounting Standards Board (FASB) is finalizing guidance on the accounting treatment of mergers of cooperatives that would create a new component of net worth, in addition to retained earnings, after a credit union merger. The unintended effect of the FASB rule will be to no longer permit a continuing credit union to include the merging credit union's net worth in its PCA calculations. This section addresses that anomaly and defines net worth for purposes of PCA to include the new component for post-merger credit unions.

It was our understanding that FASB intended to apply the standard to credit unions beginning in early 2006, following a comment period, but now may be putting application of the standard off until the beginning of 2007. Such a change, we believe, will have the unintended consequence of discouraging, if not eliminating, voluntary mergers that, absent FASB's policy, would be advantageous to credit union members involved. In addition, FASB's application of its proposal to credit unions will mean that a credit union's net worth would typically be understated by the amount of the fair value of the merging credit union's retained earnings.

This result is not in the public interest. That is why CUNA, along with the NCUA and others, supports a technical correction that would amend the Federal Credit Union Act to make it clear that

net worth equity, including acquired earnings of a merged credit union as determined under GAAP, and as authorized by the NCUA Board, would be acceptable. Senior legal staff at FASB have indicated support for a legislative approach, and we urge the Committee to likewise support such an effort, well in advance of the effective date so credit unions will have certainty regarding the accounting treatment of mergers.

Legislation was introduced by Representative Bachus to address this issue in H.R. 1042, the “Net Worth Amendment of Credit Unions Act,” which passed the House of Representatives on June 13, 2005 by voice vote. The language to correct this issue is identical in H.R. 1042 and H.R. 2317.

Also in this section, the definition of secondary capital for low-income credit unions is expanded to include certain limitations on its use by those credit unions. The definition of the net worth ratio is modified to exclude a credit union’s share insurance fund deposit from the numerator and denominator of the ratio, and the ratio of net worth to risk-assets is defined, also to exclude a credit union’s share insurance fund deposit from the numerator.

Section 105. Amendments Relating to Net Worth Restoration Plans

Section 105 would provide the NCUA Board with the authority to permit a marginally undercapitalized credit union to operate without a net-worth restoration plan if the Board determines that the situation is growth-related and likely to be short term.

This section would also modify the required actions of the Board in the case of critically undercapitalized credit unions in several ways. First, it would authorize the Board to issue an order to a critically undercapitalized credit union. Second, the timing of the period before appointment of

a liquidating agent could be shortened. Third, the section would clarify the coordination requirement with state officials in the case of state-chartered credit unions.

The following is a detailed discussion of the need for and logic of PCA reform.

HISTORY OF CREDIT UNION PCA

The PCA section of CUMAA established for the first time “capital” or “net worth” requirements for credit unions. Prior to that time, credit unions were subject to a requirement to add to their regular reserves, depending on the ratio of those reserves to “risk-assets” (then defined as loans and long-term investments). The purpose of Section 1790d (PCA) of the Act is “to resolve the problems of insured credit unions at the least possible long-term loss to the Fund.” The CUMAA instructs the NCUA to implement regulations that establish a system of PCA for credit unions that is consistent with the PCA regime for banks and thrifts under the Federal Deposit Insurance Corporation Improvement Act (FDICIA) but that takes into account the unique cooperative nature of credit unions.

There are, however, a number of ways that credit union PCA under CUMAA differs from PCA as it applies to banks and thrifts under FDICIA. Chief among these is that the net worth levels that determine a credit union’s net worth classification are specified in the Act rather than being established by regulation as is the case for banks and thrifts. Further, the levels of the net worth ratio for a credit union to be classified “well” or “adequately” capitalized are two percentage points (200 basis points) above those currently in place for banks and thrifts, even though credit unions’ activities are far more circumscribed than those of banks. In addition, the system of risk-based net worth requirements for credit unions is structured very differently from the Basel-based system in

place for banks and thrifts. For example, the Basel system is credit-risk based while credit union risk-based net worth requirements explicitly account for the difficult-to-quantify interest rate risk. In PCA as implemented under FDICIA, interest rate risk is instead dealt with through examination and supervision.

NEED FOR REFORM OF CREDIT UNION PCA

Net worth requirements were not the original purpose of the CUMAA. The genesis of the Act was the Supreme Court's field of membership decision of 1998 that prohibited NCUA from approving credit union fields of membership comprising more than one group. Since its adoption seven years ago, NCUA and credit unions have had sufficient time to experience PCA requirements. Therefore, it is not surprising that there should be a need for some modifications to PCA now that the NCUA and the credit union movement have been operating under PCA for several years.

There are two basic problems with the current PCA system.

- **HIGH BASIC CREDIT UNION CAPITAL REQUIREMENTS.** Credit unions have significantly higher capital requirements than do banks, even though the credit union National Credit Union Share Insurance Fund (NCUSIF) has an enviable record compared to other federal deposit insurance funds. Indeed, because credit unions' cooperative structure creates a systemic incentive against excessive risk taking, it has been argued that credit unions actually require less capital to meet potential losses than do other depository institutions.

- **RISK BASED SYSTEM IS IMPRECISE.** The current system of risk-based net worth requirements for credit unions provides an imprecise treatment of risk. It is only when a portfolio

reaches a relatively high concentration of assets that it signals greater risk and the need for additional net worth. This unartful system weakens the measurement of the NCUSIF's exposure to risk, and provides blurred incentives to credit unions on how to arrange their balance sheets so as to minimize risk. A Basel-type method of applying different weights to asset types based on the asset's risk profile would permit a more precise accounting for risk than does the current credit union system, thus improving the flow of actionable information regarding net worth adequacy to both regulators and credit unions.

Taken together, these problems have created an unnecessary constraint on healthy, well-managed credit unions. Credit unions agree that any credit union with net worth ratios well below those required to be adequately capitalized should be subject to prompt and stringent corrective action. There is no desire to shield such credit unions from PCA; they are indeed the appropriate targets of PCA. Because credit unions themselves fund the NCUSIF, they are keenly aware that they are the ones that pay when a credit union fails. Therefore, CUNA strongly supports a rigorous safety and soundness regulatory regime for credit unions that is anchored by meaningful and appropriate net worth requirements that drive the credit union system's PCA requirements.

Under the current system of PCA, there are many credit unions that have more than enough capital to operate in a safe and sound manner, but that feel constrained in serving their members because potential reductions in their net worth category can result from growth in member deposits, even when uninduced by the credit union. The current law stipulates that a credit union with a 6% net worth ratio is "adequately" capitalized. Considering the risk exposure of the vast majority of credit unions and the history of their federal share insurance fund, 6% is more than adequate net worth. However, as a result of the effect of potential growth on a credit union's net worth ratio under the

present system of PCA, a very well run, very healthy, very safe and sound credit union feels regulatory constraints operating with a 6% net worth ratio. Without access to external capital markets, credit unions may only rely on retained earnings to build net worth. Thus, a spurt of growth brought on by members' desire to save more at their credit union can quickly lower a credit union's net worth ratio, even if the credit union maintains a healthy net income rate.

We are not here describing credit unions that aggressively and imprudently go after growth, just for growth's sake. Rather, any credit union can be hit with sharp and unexpected increases in member deposits, which are the primary source of asset growth for credit unions. This can happen whenever credit union members face rising concerns either about their own economic or employment outlook (as in a recession) or about the safety of other financial investments they may hold (as when the stock market falls). The resulting cautionary deposit building or flight to safety translates into large swings in deposit inflows without any additional effort by the credit union to attract deposits. As an example, total credit union savings growth rose from 6% in 2000 to over 15% in 2001 despite the fact that credit unions lowered deposit interest rates sharply throughout the year. The year 2001 produced both a recession and falling stock market, and was topped off with the consumer confidence weakening effects of September 11th.

Credit union concern about the impact of uninduced growth on net worth ratios goes far beyond those credit unions that are close to the 6% cutoff for being considered adequately capitalized. Again, because of the conservative management style that is the product of their cooperative structure, most credit unions wish always to be classified as "well" rather than "adequately" capitalized. In order to do that, they must maintain a significant cushion above the 7% level required to be "well" capitalized so as not to fall below 7% after a period of rapid growth. A typical

target is to have a 200 basis point cushion above the 7% standard. Thus, in effect, the PCA regulation, which was intended to ensure that credit unions maintain a 6% adequately capitalized ratio, has created powerful incentives to induce credit unions to hold net worth ratios roughly 50% higher than that level, far in excess of the risk in their portfolios. The PCA regulation in its present form thus drives credit unions to operate at “overcapitalized” levels, reducing their ability to provide benefits to their members, and forcing them instead to earn unnecessarily high levels of net income to build and maintain net worth.

There are two ways to resolve these problems with the current system of PCA. One would be to permit credit unions to issue some form of secondary capital in a way that both provides additional protection to the NCUSIF and does not upset the unique cooperative ownership structure of credit unions. CUNA believes that credit unions should have greater access to such secondary capital. However, this bill does not provide access to secondary capital.

The other solution is reform of PCA requirements themselves. Reform of PCA should have two primary goals. First, CUNA believes any reform should preserve the requirement that regulators must take prompt and forceful supervisory actions against credit unions that become seriously undercapitalized, maintaining the very strong incentives for credit unions to avoid becoming undercapitalized. This is essential to achieving the purpose of minimizing losses to the NCUSIF. Second, a reformed PCA should not force well-capitalized credit unions to feel the need to establish a large buffer over minimum net worth requirements so that they become overcapitalized.

H.R. 2317 would reform PCA in a manner consistent with these two requirements by transforming the system into one with net worth requirements comparable to those in effect for FDIC insured

institutions, and that is much more explicitly based on risk measurement by incorporating a Basel-type risk structure.

Under H.R. 2317, a credit union's PCA capitalization classification would be determined on the basis of two ratios: the net worth ratio and the ratio of net worth to risk assets. The net worth ratio would be defined as net worth less the credit union's deposit in the NCUSIF, divided by total assets less the NCUSIF deposit. The ratio of net worth to risk assets would be defined as net worth minus the NCUSIF deposit divided by risk assets, where risk assets would be designed in a manner comparable to the Basel system in effect for banks of similar size to credit unions. The tables below show the ratio cutoff points for the various net worth classifications. A credit union would have to meet both ratio classifications, and if different, the lower of the two classifications would apply. For example, a credit union classified as "well capitalized" by its net worth ratio, but "undercapitalized" by its ratio of net worth to risk assets would be considered undercapitalized.

Net Worth Categories	Net Worth Ratio	Ratio of Net Worth to Risk Assets
Well Capitalized	5% or greater	8% or greater
Adequately Capitalized	4% to < 5%	8% or greater
Undercapitalized	3% to < 4%	6% to 8%
Signif. Undercapitalized	2% to < 3%	< 6%
Critically Undercapitalized	<2%	NA

The net worth cutoff points specified in H.R. 2317 are substantially similar to those currently in effect for FDIC insured institutions, yet, the ratios would have the effect of being more stringent on

credit unions for two reasons. First, not all of an individual credit union's net worth is included in the numerator of the ratio; the NCUSIF deposit is first subtracted. Second, a portion of banks' net worth can be met by secondary or Tier II capital. All but low-income credit unions have no access to secondary capital, so all credit union net worth is equivalent to banks' Tier I capital, which has more characteristics of pure capital than does Tier II.

H.R. 2317 would require NCUA to design a risk-based net worth requirement based on comparable standards applied to FDIC insured institutions. The outlook for those standards as they will apply to banks is currently under review by the federal banking regulators. Federal banking regulators have indicated that when Basel II takes affect for the very largest U.S. banks (approximately 25 banks and thrifts), some modifications to Basel I for all other U.S. banks will be implemented.

The exact nature of the changes to Basel I for the vast bulk of U.S. banks and thrifts is as yet unclear, although U.S. banking regulators have stated they do not intend to permit smaller U.S. banks to be disadvantaged compared to the largest banks when Basel II lowers net worth requirements for the very large institutions. Thus, it will be the modified version of Basel I in place for smaller banks that will be the standard under which NCUA will construct a risk weighting system for credit unions. Since it will be Basel based, it will focus on credit risk, leaving the treatment of interest rate risk to the supervisory process. The new credit union risk-based system will provide a much more precise measure of balance sheet risk than the current risk-based net worth requirement.

H.R. 2317 will improve the risk-based components of PCA and place greater emphasis on the risk-based measures, while lowering to the same level in effect for banks, the pure net worth ratio

requirements for a credit union to be classified as adequately capitalized. CUNA believes that in addition to relying on improved risk measurements, a reduction of the pure net worth levels to be classified as well- or adequately-capitalized is justified for the following reasons:

1. One of the original justifications for higher credit union PCA net worth requirements (higher than for banks) was the 1% NCUSIF deposit. While FASB and NCUA have both affirmed that the 1% NCUSIF deposit is an asset and thus part of net worth, as a result of the unique funding mechanism of the NCUSIF (it has been funded solely by credit unions), the 1% deposit appears on the books of both the NCUSIF and insured credit unions. H.R. 2317 has addressed this issue by defining the net worth ratio as net worth less the 1% NCUSIF deposit divided by assets less the 1% deposit. Thus, to be adequately capitalized, a credit union must hold net worth equal to about 5.7% (on average) of its assets to meet the 5% net worth requirement. This means that the discretionary and mandatory supervisory actions of PCA will be applied at higher levels of individual credit union capitalization than for similarly situated banks and thrifts.

2. Another reason given for credit unions' higher net worth requirements is their lack of access to capital markets. Credit unions' only source of net worth is the retention of earnings, which is a time consuming process. The idea was that since credit unions cannot access capital markets, they should hold more capital to begin with so that they have it available in time of need. There is some merit to this notion, but a problem with this logic is that it suggests that a poorly capitalized bank can easily access the capital markets. However, if a bank's capital ratio falls substantially due to losses, investors are likely to be wary of providing additional capital to it. Other institutions similarly have limited access to capital markets when they have experienced substantial losses.

Thus, the lack of effective access to outside capital in times of financial stress might not really distinguish credit unions from banks or other depository institutions as much as it might appear.

3. The other reason that a credit union's net worth ratio might fall – rapid asset growth – does not require higher net worth requirements for credit unions either. Asset growth (which comes from savings deposits) can be substantially influenced by a credit union's dividend policies. Under the current PCA system, lowering dividend rates creates the dual effects of retarding growth and boosting net income, both of which raise net worth ratios which would not occur had dividend rates been lowered. H.R. 2317 would permit a credit union to protect a reasonable net worth ratio with appropriate dividend rate cutting rather than being required to hold additional net worth.

There is substantial evidence that credit unions actually require less net worth than do for-profit financial institutions in order to provide protection to the deposit insurance system.⁵ Credit unions, because of their very cooperative nature, take on less risk than do for-profit financial institutions. Because credit union boards and management are not enticed to act by stock ownership and options, the moral hazard problem of deposit insurance has much less room for play in credit unions than in other insured depository institutions. Evidence of the effects of this conservative financial management by credit unions is found in the fact that average credit union ratios for net worth, net income and credit quality have shown dramatically less volatility over that past two decades than

⁵ See *The Federal Deposit Insurance Fund that Didn't Put a Bite on U.S. Taxpayers*, Edward J. Kane and Robert Hendershott, *Journal of Banking and Finance*, Volume 20, September 1996, pp.1305-1327. Kane and Hendershott summarize their paper as “the paper analyzes how differences in incentive structure constrain the attractiveness of interest-rate speculation and other risk-taking opportunities to managers and regulators of credit unions.” See also *Differences in Bank and Credit Union Capital Needs*, David M. Smith and Stephen A. Woodbury (Filene Research Institute, Madison, WI. 2001) Smith and Woodbury find that credit unions have lower loan delinquencies and net-charge off rates than do banks, and that charge-offs at credit unions are only two-thirds as sensitive to macroeconomic shocks as they are at banks. They also explain that because of the governance structure in credit unions “economic theory predicts that credit unions would take less risk than banks.” (p. 5)

comparable statistics for banks and thrifts. Similarly, the equity ratio of the NCUSIF has been remarkably stable, between 1.2% and 1.3%, of insured shares while other federal deposit funds have seen huge swings, and even insolvency. This is hardly evidence supporting the need of more capital in credit unions than in banks and thrifts.

Reforming PCA as provided in H.R. 2317 would preserve and strengthen the essential share-insurance fund protection of PCA and would more closely tie a credit union's net worth requirements to its exposure to risk – the reason for holding net worth in the first place. It would also permit adequately and well-capitalized credit unions to operate in a manner devoted more to member service and less to the unnecessary accumulation of net worth.

TITLE II: ECONOMIC GROWTH

Section 201. Limits on Member Business Loans

This section eliminates the current asset limit on MBLs at a credit union from the lesser of 1.75 times actual net worth or 1.75% times net worth required for a well-capitalized credit union and replaces it with a flat rate of 20 percent of the total assets of a credit union. This provision therefore facilitates member business lending without jeopardizing safety and soundness at participating credit unions.

Section 202. Definition of Member Business Loans

This section would amend the current definition of a MBL to facilitate such loans by giving the NCUA the authority to exclude loans of \$100,000 or less as de minimus, rather than the current limit of \$50,000.

Section 203. Restrictions on Member Business Loans

This section would modify language in the Federal Credit Union Act that currently prohibits a credit union from making any new MBLs if its net worth falls below 6 percent. This change will permit the NCUA to determine if such a policy is appropriate and to oversee all MBLs granted by an undercapitalized institution.

Section 204. Member business loan exclusion for loans to non-profit religious organizations

This section excludes loans or loan participations by federal credit unions to non-profit religious organizations from the MBL limit contained in the Federal Credit Union Act, which is 12.25% of the credit union's total assets. This amendment would offer some relief in this area by allowing federal credit unions to make MBLs to religious-based organizations without concern about the statutory limit that now covers such loans. While the limit would be eliminated, such loans would still be subject to other regulatory requirements, such as those relating to safety and soundness.

We believe that this is really a technical amendment designed to correct an oversight during passage of CUMAA. The law currently provides exceptions to the MBL caps for credit unions with a history of primarily making such loans. Congress simply overlooked other credit unions that purchase parts of these loans, or participate in them. This provision would clarify that oversight and ensure that these organizations can continue meeting the needs of their members and the greater community at large and ensuring that loans are available for religious buildings as well as their relief efforts.

Section 205. Credit Unions Authorized to Lease Space in Buildings with Credit Union Offices in Underserved Areas

This section enhances the ability of credit unions to assist distressed communities with their economic revitalization efforts. It would allow a credit union to lease space in a building or on property in an underserved area on which it maintains a physical presence to other parties on a more permanent basis. It would permit a federal credit union to acquire, construct, or refurbish a building in an underserved community, then lease out excess space in that building.

Having described briefly how CURIA would address credit union member business lending concerns, I would like to provide the Subcommittee with a detailed rationale for these needed changes.

HELPING SMALL BUSINESS

Title II, Section 203 of CUMAA established limits on credit union MBL activity. There were no statutory limits on credit union member business lending prior to 1998. The CUMAA-imposed limits are expressed as a 1.75 multiple of net worth, but only net worth up to the amount required to be classified as well capitalized (i.e., 7%) can be counted. Hence the limit is $(1.75 \times .07)$ or 12.25% of assets.

NEED FOR REFORM OF CREDIT UNION MBL LIMITS

Small businesses are the engine of economic growth – accounting for about one-half of private non-farm economic activity in the U.S. annually. Their ability to access capital is paramount. But this access is seriously constrained by the double-whammy of banking industry consolidation and the CUMAA-imposed limitations on credit union MBLs. Recent research published by the Small

Business Administration reveals that small businesses receive less credit on average in regions with a large share of deposits held by the largest banks. FDIC statistics show that the largest 100 banking institutions now control nearly two-thirds of banking industry assets nationally. In 1992 the largest 100 banking institutions held just 45% of banking industry assets. Thus, CUMAA severely restricts small business access to credit outside the banking industry at a time when small firms are finding increasing difficulty in accessing credit within the banking industry.

Basic problems with the current MBL limits are:

- **THE LIMITS ARE ARBITRARY AND UNNECESSARILY RESTRICTIVE.** Insured commercial banks have no comparable business lending portfolio concentration limitations. Other financial institutions, savings and loans, for example, have portfolio concentration limitations, but those limitations are substantially less restrictive than the limits placed on credit unions in CUMAA.
- **THE 12.25% LIMIT DISCOURAGES ENTRY INTO THE MBL BUSINESS.** Even though very few credit unions are approaching the 12.25% ceiling, the very existence of that ceiling discourages credit unions from entering the field of member business lending. Credit unions must meet strict regulatory requirements before implementing an MBL program, including the addition of experienced staff. Many are concerned that the costs of meeting these requirements cannot be recovered with a limit of only 12.25% of assets. For example, in today's market, a typical experienced mid-level commercial loan officer would receive total compensation of approximately \$100,000. The substantial costs associated with hiring an experienced lender, combined with funding costs and overhead and startup costs (e.g., data processing systems, furniture and equipment, printing, postage, telephone, occupancy, credit reports and other operating expenses)

make member business lending unviable at most credit unions given the current 12.25% limitation. In fact, assuming credit unions could carry salary expense of 2% of portfolio, 76% of CUs couldn't afford to be active member business lenders even if they had portfolios that were equal in size to the current 12.25% of asset maximum. Alternatively, assuming credit unions could carry salary expense of 4% of portfolio, 63% of CUs couldn't afford to be active member business lenders even if they had portfolios that were equal in size to the current 12.25% of asset maximum.

- **THE LIMITS ARE NOT BASED ON SAFETY AND SOUNDNESS CONSIDERATIONS.** There is no safety and soundness reason that net worth above 7% cannot also support business lending. If all net worth could be counted, the actual limit would average between 18% and 19% of total assets rather than 12.25% of total assets.

- **THE MBL DEFINITIONS CREATE DISINCENTIVES THAT HURT SMALL BUSINESSES.** The current \$50,000 cutoff for defining an MBL is too low and creates a disincentive for credit unions to make loans to smaller businesses. Permitting the cutoff to rise to \$100,000 would open up a significant source of credit to small businesses. These "small" business purpose loans are so small as to be unattractive to many larger lenders. Simply inflation adjusting the \$50,000 cutoff, which was initially established in 1993 and hasn't been adjusted since that time, would result in an approximate 33% increase in the cutoff to over \$65,000.

While some bankers call credit union member business lending "mission creep" this is simply a preposterous fiction. Credit union member business lending is not new -- since their inception credit unions have offered business-related loans to their members. Moreover, credit union member business lending shows a record of safety. According to a U.S. Treasury Department study, credit

union business lending is more regulated than commercial lending at other financial institutions. In addition, the Treasury found that “member business loans are generally less risky than commercial loans made by banks and thrifts because they generally require the personal guarantee of the borrower and the loans generally must be fully collateralized. Ongoing delinquencies – for credit unions, loans more than 60 days past due, and for banks and thrifts, loans more than 90 days past due – are lower for credit unions than for banks and thrifts. Credit unions’ mid-year 2000 loan charge-off rate of 0.03 percent was much lower than that for either commercial banks (0.60 percent) or savings institutions (0.58 percent).”

Not surprisingly, the Treasury also concluded that member business lending “does not pose material risk to the” National Credit Union Share Insurance Fund.

Updated statistics from full-year 2000 through 2003 indicate that the favorable relative performance of MBLs reported in the Treasury study has continued in recent years. Credit union MBL net chargeoffs have averaged just 0.08% over the four-year period since the Treasury study, while the comparable average net chargeoff rate at commercial banks was 1.28% and at savings institutions it was 1.11%. MBLs have even lower loss rates than other types of credit union lending, which themselves have relatively low loss experience.

Credit union member business lending represents a small fraction of total commercial loan activity in the United States. At mid-year 2004, the dollar amount of MBLs was less than one-half of one percent of the total commercial loans held by U.S. depositories. Credit union MBLs represent just 3.1% of the total of credit union loans outstanding and only 17.9% of U.S. credit unions offer

MBLs. According to credit union call report data collected by the NCUA, the median size of credit union MBLs granted in the first six months of 2004 was \$140,641.

Currently, only 11 credit unions in Idaho, out of a total of 68 (only 16%), offer MBLs to their members. The average size MBL is \$91,653. The total amount of business lending by credit unions in Idaho is **\$17.3 million**, while banking institutions in Idaho make **\$4.3 billion** in business loans. In Idaho, credit unions represent 0.4% of the market share for business lending, while banking institutions represent 99.6%; and, while credit union business loans represent only 0.66% of credit union assets, banking institutions' business loans represent 78.98% of bank assets.

Adjusting credit union MBL limits from 12.25% to 20% of assets, which is the equivalent to the business lending limit for savings institutions, would not cause these numbers to change dramatically.

This adjustment would help small business. As noted earlier, small businesses are the backbone of the US economy. The vast majority of employment growth occurs at small businesses. And small businesses account for roughly half of private non-farm gross domestic product in the U.S. each year.

Small businesses are in need of loans of all sizes, including those of less than \$100,000, which many have said banks are less willing to make.

Moreover, large banks tend to devote a smaller portion of their assets to loans to small businesses.

The continuing consolidation of the banking industry is leaving fewer smaller banks in many

markets. In fact, the largest 100 banking institutions accounted for 42% of banking industry assets in 1992. By year-end 2003, the largest 100 banking institutions accounted for 65% of banking industry assets – a 23-percentage point increase in market share in just eleven years.

This trend and its implications for small business credit availability are detailed in a recently released Small Business Administration paper. The findings reveal “credit access has been significantly reduced by banking consolidation...we believe this suggests that small businesses, especially those to which relationship lending is important, have a lower likelihood of using banks as a source of credit.”

In reforming credit union MBL limits, Congress will help to ensure a greater number of available sources of credit to small business. This will make it easier for small businesses to secure credit at lower prices, in turn making it easier for them to survive and thrive.

TITLE III: REGULATORY MODERNIZATION

Section 301. Leases of land on federal facilities for credit unions

This provision would permit military and civilian authorities responsible for buildings on federal property the discretion to extend to credit unions that finance the construction of credit union facilities on federal land real estate leases at minimal charge. Credit unions provide important financial benefits to military and civilian personnel, including those who live or work on federal property. This amendment would authorize an affected credit union, with the approval of the appropriate authorities, to structure lease arrangements to enable the credit union to channel more funds into lending programs and favorable savings rates for its members.

Section 302. Investments in securities by federal credit unions

The Federal Credit Union Act limitations on the investment authority of federal credit unions are anachronistic and curtail the ability of a credit union to respond to the needs of its members. The amendment provides additional investment authority to purchase for the credit union's own account certain investment securities. The total amount of the investment securities of any one obligor or maker could not exceed 10 percent of the credit union's unimpaired capital and surplus. The NCUA Board would have the authority to define appropriate investments under this provision, thus ensuring that new investment vehicles would meet high standards of safety and soundness and be consistent with credit union activities.

Section 303. Increase in general 12-year limitation of term of federal credit union loans

Currently, federal credit unions are authorized to make loans to members, to other credit unions, and to credit union service organizations. The Federal Credit Union Act imposes various restrictions on these authorities, including a 12-year maturity limit that is subject to limited exceptions. This section would allow loan maturities up to 15 years, or longer terms as permitted by the NCUA Board.

All Federal credit unions must comply with this limitation. We are very concerned that credit union members seeking to purchase certain consumer items, such as a mobile home, may seek financing elsewhere in which they could repay the loan over a longer period of time than 12 years. While we would prefer for NCUA to have authority to determine the maturity on loans, consistent with safety and soundness, a 15-year maturity is preferable to the current limit. Such an increase in the loan limit would help lower monthly payments for credit union borrowers and benefit credit unions as well as their members.

Section 304. Increase in one-percent investment limit in credit union service organizations

The Federal Credit Union Act authorizes federal credit unions to invest in organizations providing services to credit unions and credit union members. An individual federal credit union, however, may invest in aggregate no more than 1% of its shares and undivided earnings in these organizations, commonly known as credit union service organizations or CUSOs. The amendment raises the limit to 3% percent.

CUSOs provide a range of services to credit unions and allow them to offer products to their members that they might not otherwise be able to do, such as check clearing, financial planning and retirement planning. Utilizing services provided through a CUSO reduces risk to a credit union and allows it to take advantage of economies of scale and other efficiencies that help contain costs to the credit union's members. Further, as federal credit union participation in CUSOs is fully regulated by NCUA, the agency has access to the books and records of the CUSO in addition to its extensive supervisory role over credit unions.

The current limit on CUSO investments by federal credit unions is out-dated and limits the ability of credit unions to participate with these organizations to meet the range of members' needs for financial services. It requires credit unions to arbitrarily forego certain activities that would benefit members or use outside vendors in which the credit union has no institutional stake. While we feel the 1% limit should be eliminated or set by NCUA through the regulatory process, we appreciate that the increase to 3% will provide credit unions more options to investment in CUSOs to enhance their ability to serve their members.

CUNA also would support raising the borrowing limitation that currently restricts loans from credit unions to CUSOs to 1 percent. We believe the limit should be on par with the investment limit, which under this bill would be raised to 3 percent.

Section 305. Check-cashing and money-transfer services offered within the field of membership

Federal credit unions are currently authorized to provide check-cashing services to members and have limited authority to provide wire transfer services to individuals in the field of membership under certain conditions. The amendment would allow federal credit unions to provide check-cashing services to anyone eligible to become a member.

This amendment is fully consistent with President Bush's and Congressional initiatives to reach out to other underserved communities in this country, such as some Hispanic neighborhoods. Many of these individuals live from pay check to pay check and do not have established accounts, for a variety of reasons, including the fact that they do not have extra money to keep on deposit. We know of members who join one day, deposit their necessary share balance and come in the very next day and withdraw because they need the money. This is not mismanagement on their part. They just do not have another source of funds. And sometimes, a \$5.00 withdrawal means the difference between eating or not.

If we are able to cash checks and sell negotiable checks such as travelers checks, we could accomplish two things: save our staff time and effort opening new accounts for short term cash purposes which are soon closed and gain the loyalty and respect of the potential member so that when they are financially capable of establishing an account, they will look to the credit union,

which will also provide financial education and other support services. Take the example of one of our credit unions in Pueblo, which attracts migrant workers who live in that area for several months each year, many who return year after year. It is well known that this particular group is taken advantage of because of the language barrier. The Pueblo credit union has developed a group of bilingual members who are willing to act as translators when needed and several successful membership relationships have resulted.

Legislation that includes similar provisions is pending in both the House and Senate on this issue: the International Consumer Protection Act, introduced in the House (H.R. 928) by Representative Gutierrez and in the Senate (S. 31) by Senator Sarbanes. Additionally, the Expanded Access to Financial Services Act (H.R. 749), introduced by Representatives Gerlach and Sherman, contains identical language to this provision, and passed the House of Representatives on April 26, 2005, by voice vote. CUNA strongly supports all legislative efforts to pursue this provision and is grateful to Ranking Member Sarbanes for the introduction of his bill.

Section 306. Voluntary mergers involving multiple common bond credit unions

In voluntary mergers of multiple bond credit unions, NCUA has determined that the Federal Credit Union Act requires it to consider whether any employee group of over 3,000 in the merging credit union could sustain a separate credit union. This provision is unreasonable and arbitrarily limits the ability of two healthy multiple common bond federal credit unions from honing their financial resources to serve their members better.

The amendment is a big step forward in facilitating voluntary mergers, as other financial institutions are permitted to do. It provides that the numerical limitation does not apply in voluntary mergers.

Section 307. Conversions involving common bond credit unions

This section allows a multiple common bond credit union converting to or merging with a community charter credit union to retain all groups in its membership field prior to the conversion or merger. Currently, when a multiple group credit union converts to or merges with a community charter, a limited number of groups previously served may be outside of the boundaries set for the community credit union. Thus, new members within those groups would be ineligible for service from that credit union. The amendment would allow the new or continuing community credit union to provide service to all members of groups previously served.

Section 308. Credit union governance

This section gives federal credit union boards flexibility to expel a member who is disruptive to the operations of the credit union, including harassing personnel and creating safety concerns, without the need for a two-thirds vote of the membership present at a special meeting as required by current law. Federal credit unions are authorized to limit the length of service of their boards of directors to ensure broader representation from the membership. Finally, this section allows federal credit unions to reimburse board of director volunteers for wages they would otherwise forfeit by participating in credit union affairs.

There has been more than one occasion when some credit unions would have liked to have had the ability to expel a member for just cause. It is relatively rare that things occur that would cause credit unions to use such a provision. However, the safety of credit union personnel may be at stake. One instance I know of involved a credit union member who seemed to have a fixation on an employee and had made inappropriate comments. Another involved an older member who refused to take no for an answer from a young teller whom he persistently asked to date. We have

heard of an example at another credit union when one member actually told one of the tellers he would punch her if he ever saw her out in public. Most cases are not quite that extreme; however, we have had other reports from credit unions of unruly members who seem to enjoy causing a ruckus.

Credit unions should have the right to limit the length of service of their boards of directors as a means to ensure broader representation from the membership. Credit unions, rather than the federal government, should determine term limits for board members. Providing credit unions with this right does not raise supervisory concerns and should not, therefore, be denied by the federal government.

Credit unions are directed and operated by committed volunteers. Given the pressures of today's economy on many workers and the legal liability attendant to governing positions at credit unions, it is increasingly difficult to attract and maintain such individuals. Rather than needlessly discourage volunteer participation through artificial constraints, the Federal Credit Union Act should encourage such involvement by allowing volunteers to recoup wages they would otherwise forfeit by participating in credit union affairs.

Whether or not a volunteer attends a training session or conference is sometimes determined by whether or not that volunteer will have to miss work and not be paid.

Section 309. Providing NCUA with greater flexibility in responding to market conditions

Under this section, in determining whether to lift the usury ceiling for federal credit unions, NCUA will consider rising interest rates or whether prevailing interest rate levels threaten the safety and soundness of individual credit unions.

Section 310. Credit Union Conversion Voting Requirements

This section would change the Federal Credit Union Act from permitting conversions after only a majority of those members voting approve a conversion, to requiring a majority vote of at least 20 percent of the membership to approve a conversion.

Time and time again, Congress has made clear its support for credit unions, in order to assure consumers have viable choices in the financial marketplace. Yet, banking trade groups and other credit union detractors have indicated they would like to encourage credit union conversions, particularly those involving larger credit unions, in order that they may control the market, thereby limiting consumers' financial options.

Last year, the NCUA adopted new regulatory provisions to require credit unions seeking to change their ownership structure to provide additional disclosures to their members to insure they are adequately informed regarding the potential change and are fully aware of the consequences of such action. CUNA strongly supported this action because we feel members should know that their rights and ownership interests would change, particularly if the institution converts to a bank. In such a situation the institution would "morph" from one in which the members own and control its operations to an institution owned by a limited number of stockholders.

CUNA likewise supports the agency's ongoing efforts to ensure members are provided sufficient disclosures and opportunities to present opposing views in relation to a possible conversion.

Congress addressed conversions in CUMAA and reinforced that a credit union board which desires to convert must allow its members to vote on its conversion plan. CURIA would require a minimum level of participation in the vote -- at least 20% of the members -- for a conversion election to be valid. Currently, there is a requirement that only a majority of those voting approve the conversion. The legislation would prevent situations in which only a very small number of an institution's membership could successfully authorize such a conversion.

Recently, CUNA's Board adopted a set of principles related to credit union conversions, and we want to share its provisions with the Committee.

Principles Regarding Credit Union Conversions

- We support the right of member/owners to exercise their democratic control of their credit unions.
- The credit union charter currently provides the best vehicle for serving the financial needs of consumers. CUNA encourages credit unions that are considering conversions to make their decisions based solely on the best interests of their members.
- Full, plain language, disclosures are essential to furthering the democratic process.

- Credit union directors and managers have a fiduciary responsibility to present objective and honest information as well as reasonable business alternatives (e.g. mergers, liquidations)

- We believe that the net worth of the credit union belongs to the members and should remain with them. There should be no unjust enrichment to Directors and senior management upon later conversion to a bank.

- CUNA supports NCUA and state regulators in the full use of their current authority to ensure members understand the conversion process and that fiduciary duties of credit union boards are fully enforced.

Section 311. Exemption from pre-merger notification requirement of the Clayton Act

This section gives all federally insured credit unions the same exemption as banks and thrift institutions already have from pre-merger notification requirements and fees of the Federal Trade Commission.

Section 312. Treatment of credit unions as depository institutions under securities laws

This section gives federally insured credit unions exceptions, similar to those provided to banks, from broker-dealer and investment adviser registration requirements.

108th Congress: H.R. 1375—Financial Services Regulatory Relief Act (Credit Union Provisions)

Most of the provisions of H.R. 2317, as outlined above, were also included in last Congress's H.R. 1375. The single exception is the following section.

Section 301. Privately insured credit unions authorized to become members of a Federal Home

Loan Bank

CUNA supports this section which permits privately insured credit unions to apply to become members of a Federal Home Loan Bank. Currently, only federally insured credit unions may become members. The state regulator of a privately insured credit union applying for Federal Home Loan Bank membership would have to certify that the credit union meets the eligibility requirements for federal deposit insurance before it would qualify for membership in the Federal Home Loan Bank system.

Additional Legislative Amendments CUNA Supports

None of the following provisions have been included in CURIA, nor past versions of regulatory relief legislation, yet represent legitimate burdens faced by credit unions that are deserving of relief. We encourage the Committee to consider including them in any future legislation.

- **Allow community credit unions to continue adding members from groups that were part of the field of membership (FOM) before the credit union converted to a community charter but are now outside the community**

Prior to the adoption of amendments to the Federal Credit Union Act in 1998, community credit unions were able to add new members from groups that they had previously served but are outside of the community area the credit union serves. Currently, the credit union may serve members of record but not include additional members from those groups. CUNA supports legislation that would restore that capacity to credit unions.

- **Allow credit unions to serve underserved areas with an ATM**

The legislative history to the CUMAA indicates that federal credit unions should establish a brick and mortar branch or other facility rather than establishing an ATM to serve an underserved area. This directive makes it far less affordable for a number of credit unions to reach out even more to underserved areas. While credit unions serving underserved areas through an ATM should be as committed to the area as a credit union with another type of facility, this change would facilitate increased service to underserved areas.

- **Eliminate the requirement that only one NCUA Board member can have credit union experience**

Currently, only one member of the NCUA Board may have credit union experience. Such a limit does not apply to any of the other federal regulatory agencies and denies the NCUA Board and credit unions the experience that can greatly enhance their regulation. At a minimum, the law should be changed to permit **at least one** person with credit union experience on the NCUA Board.

- **Accounting Treatment of Loan Participations as Sales**

Many of our members currently engage in loan participations, either as the originating institution or as an investor, and FASB's project to review FASB Statement (FAS) No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, is of great concern

to us. Other financial institution groups, as well as federal financial regulators, have likewise raised serious questions about the need for and advisability of the proposed guidance.

For a variety of reasons, participations can be important financial and asset liability management tools. They are used increasingly by credit unions, as well as by other institutions, to control interest rate risk, credit risk, balance sheet growth, and maintain net worth ratios. Participations enable credit unions to utilize assets to make more credit available to their membership than they would be able to do without the use of loan participations.

FASB states that it is concerned that in a loan participation in which the borrower has shares or deposits at the originating institution, if that institution is liquidated, the participating institution would not be able to recover its pro rata portion of the members' shares/deposits within the originating institution that are "claimed" by the originating institution to setoff the portion of the debt owed to it. This outcome is highly unlikely and we are not aware that it has ever occurred in a credit union.

Nonetheless, FASB is considering amendments to Statement of Financial Accounting Standard 140 that would expressly state that because the right of setoff between the originating institution and the member/depositor/borrower exists (setting up the potential that the participating institution would not have any claim against the member/depositors' funds in the originating institution) the loan transaction does not meet the isolation requirements of FAS 140. Because of this concern, instead of transferring the portion of the loan participated off of its books as a sale, it is our understanding that the transaction would be reflected on the originating credit union's financial statements and records as a secured borrowing.

In order for participations to continue being treated as sales for accounting purposes, the amendments would further change the existing accounting standards by requiring an institution to transfer participations through a qualified special purpose entity (QSPE), if the transaction did not meet “True-Sale-At-Law” test. This is a needless and costly expense that would make it difficult for credit unions to use participation loans as a management tool. Further, it would drastically limit the ability of credit unions to provide low-cost, economical financing for their membership through loan participations.

There are sufficient safeguards already in place that address FASB’s concerns about isolating the loan participation asset from the reach of the originating credit union and its creditors in liquidation, without the need for changes to FAS 140 of the nature FASB is contemplating.

Conclusion

In summary, Mr. Chairman, we are grateful to the Committee for holding this important hearing. The Potlatch No.1 Federal Credit Union’s ability to continue serving the financial needs of our current members and our potential members who need access to our services in Northern Idaho and Eastern Washington will be significantly reduced without the regulatory relief this Committee is addressing. We strongly urge the Committee to act on this very important issue this year. And, we strongly urge the Committee to make sure that the provisions in CURIA are a part of any Congressional action to provide financial institutions regulatory relief. We strongly believe that our future will be determined by our ability to provide relief in these important areas. Without this relief, many credit unions will be unable to respond to the financial needs of millions of Americans.



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THE REGULATORY BURDEN OF CREDIT UNIONS

**List of Rules Credit Unions Follow
Compiled by the
Credit Union National Association**

JUNE 2005

CREDIT UNIONS AS FINANCIAL INSTITUTIONS

National Credit Union Administration			
<i>NCUA is an independent federal agency that supervises and insures all federal credit union and insures most state-chartered credit union. It is entirely funded by credit unions and received no tax dollars</i>			
Subject	Description	Statute	Regulation
Advertising	Prescribes requirements on using the official federal share insurance sign and the official insurance statement and the accuracy of advertisements.	<i>12 USC 1785(a)</i>	<i>12 CFR 740</i>
Appraisals	Sets forth the real estate appraisal requirements for federally insured credit unions.	<i>12 USC 3341</i>	<i>12 CFR 722, 741.3(b)</i>
Audits and Verification	Sets for the responsibilities of federally insured credit unions concerning the review of credit union records and reports as well as the policies and control procedures to safeguard against error, carelessness, and fraud.	<i>12 USC 1761d, 1782(a)(6)</i>	<i>12 CFR 715</i>
Board of Director Changes	Sets forth conditions under which a federally insured credit union must notify NCUA in writing of any proposed changes in its board, committees, or executive staff.	<i>12 USC 1790a</i>	<i>12 CFR 701.14</i>
Borrowed Funds	Sets forth the limitations of federally insured credit unions to borrow from any source and regulatory conditions on borrowing from natural persons.	<i>12 USC 1757(9)</i>	<i>12 CFR 701.38, 741.5</i>
Capital Reserves	Establishes the amount of reserves that must be accumulated and maintained by federally insured credit unions.	<i>12 USC 1762</i>	<i>12 CFR 700.1, 702, 741.9</i>

Catastrophic Act Report	Requires federally insured credit unions to notify NCUA within five days of any natural disaster that affects the credit union's operations.	12 USC 1766	12 CFR 748
Community Development Revolving Loan Program	Implements a special loan program for low-income credit unions.	42 USC 9812, 12 USC 17726-1	12 CFR 705
Compensation of Officials and Indemnification	Sets forth the restrictions on the volunteer members of the federal credit union board receiving compensation and sets limits on their indemnification.	12 USC 1761(c)	12 CFR 701.33
Conversion of Insured Credit Unions	Establishes procedures for an insured credit union to convert to a mutual savings bank.	12 USC 1785(b)(2)	12 CFR 708a
Corporate Credit Unions	Establishes special rules for all credit unions organized to serve other credit unions.	12 USC 1757	12 CFR 704
Credit Practices	Defines unfair credit practices and unfair or deceptive cosigner practices for federal credit unions.	15 USC 57a(f)	12 CFR 706
Credit Union Service Organizations	Sets limits on federal credit unions' investments in and loans to organizations providing services to them and their members.	12 USC 1757(5)(D), (7)(I)	12 CFR 712
Criminal Referral report	Required federally insured credit unions to notify NCUA, the U.S. Attorney, and the FBI within seven business days when crimes or suspected crimes have occurred. Required credit unions to comply with record keeping and reporting requirements to help identify and prosecute money laundering.	12 USC 1786(q)	12 CFR 748 31 CFR 5311,5313
Discrimination in Real Estate Lending	Prohibits a federal credit union from discouraging a real estate loan application based on race, color, origin, religion, sex, disability, or familial status.	42 USC 3605	12 CFR 701.31
Dividends/Interest	Requires federal credit unions to make transfers to reserves	12 USC 1763	

Reporting	before declaring dividends.		
Employee Protection	Prohibits federally insured credit unions from discharging or discriminating against any employee who provides information to the federal government of any possible violation of a law or regulation.	<i>12 USC 1790b</i>	
Examinations	Requires federally insured credit unions to make periodic financial reports and be subject to regular examinations.	<i>12 USC 1756, 1784, 1789(8)</i>	<i>12 CFR 741.1, 741.6</i>
Fidelity Bond and Insurance Coverage	Requires federally insured credit unions to maintain fidelity bonds for employees and officials, and insurance to cover losses due to theft, vandalism, ect.	<i>12 USC 1761b</i>	<i>12 CFR 713</i>
Field of Membership and Chartering	Sets forth the practices and procedures concerning federal credit union chartering and field of membership modifications. Sets forth criteria for multiple common-bond credit unions and community credit unions.	<i>12 USC 1759</i>	<i>12 CFR 701.1, IRPS 99-1</i>
Fixed Assets	Sets forth the limitations on federal credit unions in regard to ownership of fixed assets.	<i>12 USC 1757(4)</i>	<i>12 CFR 701.36</i>
Flood Insurance	Sets forth guidelines for federally insured credit unions regarding flood insurance.	<i>42 USC 4012a, 4106</i>	<i>12 CFR 760</i>
Foreign Branching	Establishes the requirements for federally insured credit unions to branch outside the U.S.	<i>12 USC 1757, 1781</i>	<i>12 CFR 741.11</i>
Incidental Powers	Provides federal credit unions incidental powers necessary to carry out their business.	<i>12 USC 1757(17)</i>	<i>12 CFR 721</i>
Insurance and Group Purchasing Activities	Permits federal credit unions to make insurance and group purchasing plans involving outside vendors available to their membership under specified conditions.	<i>12 USC 1757(17)</i>	<i>12 CFR 721</i>
Investment and Deposit Activities	Sets forth the securities, deposits, and other obligations in which federal credit unions may invest.	<i>12 USC 1757(7), (8)</i>	<i>12 CFR 703</i>
Lending (General)	Sets forth the general requirements and limitations on loans to federal credit union members.	<i>12 USC 1757(5)</i>	<i>12 CFR 701.21</i>
Loan Limits to One	Restricts the amount of federal credit union funds that can be	<i>12 USC</i>	<i>12 CFR</i>

Borrower	loaned to one member to no more than 10% of a credit union's unimpaired shares and surplus.	1757(5)(A)(x)	701.21(c)(5)
Loan Participations	Establishes procedures a federal credit union must follow to participate in making loans with eligible organizations.	12 USC 1757(5)(E)	12 CFR 701.22
Loans to Directors and Committee Members	Sets forth the restrictions on loans and lines of credit to any member of the federal credit union board of directors, credit committee, or supervisory committee.	12 USC 1757(5)(A)(iv)	12 CFR 701.21(d)
Management Interlocks	Prohibits a management official of a credit union from also serving as a management official of another credit union if the credit unions are not affiliated and the credit unions exceed certain asset sizes or are located in the same local area.	12 USC 3201 et seq.	12 CFR 711
Member Business Loans	Defines "member business loan" and sets forth the requirements a federally insured credit union must meet to make such loans.	12 USC 1757(5), 1757a	12 CFR 701.21, 741.3 12 CFR 723
Mergers/Conversions	Prescribes the procedures for merging a federally insured credit union and the procedures and notice requirements for termination of, or conversions from, federal insurance.	12 USC 1785, 1786	12 CFR 708b IRPS 99-1
NCUA Board Membership	Establishes qualification for NCUA Board members.	12 USC 1752(b)	
Privacy	Requires credit unions to deliver privacy notices to members, outlines the procedures that credit unions must use when providing members with the right to opt out of certain information disclosures to third parties, and requires credit unions to establish safeguards for protecting the security of member information.	15 USC 6801 et seq.	12 CFR 716, 741,748
Prompt Corrective Action/Risk Based Net Worth Requirement	Establishes capital standards for credit unions, imposes consequences based on capitalization levels, and if necessary, authorizes supervisory action based on capital levels.	12 USC 1790d, 1787(a)	12 CFR 702
Public Unit and	Sets forth the limitations on federally insured credit unions	12 USC 1757(6)	12 CFR

Non-member Accounts	receiving funds from federal, state, and local governments and non-members.		701.32, 741.6
Purchase, Sale, and Pledge of Obligations	Sets forth procedures a federal credit union must follow to purchase, sell, or pledge assets.	12 USC 1757(13), (14)	12 CFR 701.23
Real Estate Lending	Sets for the rules for long-term mortgage lending by federal credit unions.	12 USC 1757(5)(A)(i)	12 CFR 701.21(g)
Records Preservation Program	Requires federally insured credit unions to maintain records preservation programs to identify, store, and reconstruct vital records.	12 USC 1766, 1789	12 CFR 749
Refunds of Loan Interest Payments	Sets forth the provisions under which a federal credit union may refund interest paid on loans.	12 USC 1761b(9)	12 CFR 701.24
Retirement Benefits	Establishes procedures a federal credit union must follow to provide reasonable retirement benefits for its employees and officers.	12 USC 1761b	12 CFR 701.19
Reg Flex	Provides regulatory flexibility to federal credit unions that maintain strong financial position.	12 USC 1766(a)	General Rulemaking
Service Contracts	Establishes the procedures a federal credit union must follow when entering into a contractual agreement with one or more credit unions or other organizations.	12 USC 1757(1)	12 CFR 701.26
Service Providers	Establishes that a credit union service provider is subject to regulation and examination by NCUA.	12 USC 1786a	
Share Insurance Coverage of Accounts	Describes the insurance coverage of various types of federally insured member accounts.	12 USC 1787(k)	12 CFR 745
Share Insurance Eligibility, Payments, and Responsibilities	Prescribes requirements of federal share insurance, the payment of insurance premiums and capitalization deposits, and enforcement sanctions.	12 USC 1781 et seq.	12 CFR 741
Trustees and	Sets forth the procedures for a federal credit union to act as	26 USC 408	12 CFR 724

Custodians of Certain Pension Plans	trustee or custodian of 401(k) pension plans and individual retirement accounts.		
Truth-in-Savings	Requires credit unions to disclose how dividends are calculated and what fees are assessed on savings accounts.	<i>12 USC 4301 et seq.</i>	<i>12 CFR 707</i>
Usury Limit	Limits the amount of interest a federal credit union can charge on a loan.	<i>12 USC 1757(5)(vi)</i>	<i>12 CFR 701.21(c)(7)</i>
Voluntary Liquidation	Prescribes the procedures a federal credit union must follow to voluntarily liquidate.	<i>12 USC 1766</i>	<i>12 CFR 710</i>

Federal Reserve System

The Federal Reserve System is an independent federal agency that executes monetary policy, oversees the national payments system, provides payment services, and implements major federal consumer protection laws.

Check-Holds/Check Collection	Governs check-hold policies and sets endorsement standards to expedite the check-clearing process.	12 USC 4001 et seq.	12 CFR 229 (Regulation CC)
Check Clearing in the 21 st Century Act	Establishes the rules and guidelines for substitute checks.	12 USC 5001	12 CFR 229 (Regulation C)
Commercial Payments via Automated Clearinghouses	Governs financial institutions' transaction and receipt of commercial ACH transaction through Federal Reserve Banks.	15 USC 1693(b)	12 CFR 205, 210 Fed. Reserve Op. Cir. #4
Consumer Lending	Governs the disclosure and advertising requirements when leasing property to consumers.	15 USC 1601 et seq.	12 CFR 213 (Regulation M)
Credit by Brokers and Dealers	Regulates certain stock purchase plans when a credit union assists its members in purchasing stock of the sponsor corporation.	15 USC 78a et seq.	12 CFR 220 (Regulation T)
Credit Secured by Negotiable Securities	Limits the amount of credit that credit unions can extend when the loan purpose is to purchase or carry securities and when the loan is secured by margin securities.	15 USC 78a et seq.	12 CFR 221 (Regulation U)
Discount Window	Establishes rules under which Federal Reserve Banks may extend credit to depository institutions and others.	12 USC 347a, b	12 CFR 201 (Regulation A)
Electronic Funds Transfer	Establishes the basic rights, liabilities, and responsibilities of consumers who use electronic money transfer services and of the credit unions that offer these services.	15 USC 1693 et seq.	12 CFR 205 (Regulation E)

Equal Credit Opportunity	Prohibits discrimination with respect to any credit transaction on the basis of sex, marital status, race, color, religion, national origin, and receipt of public assistance income.	<i>15 USC 1601 et seq., 1691</i>	<i>12 CFR 202 (Regulation B)</i>
Home Mortgage Disclosure	Requires credit unions to collect, report, and disclose data regarding home mortgage and home improvement loans, including the geographic location of where mortgage loans have been granted and denied.	<i>12 USC 2801 et seq.</i>	<i>12 CFR 203 (Regulation C)</i>
Payments Systems	Governs the collection of checks and other cash and non-cash items and the handling of returned checks by Federal Reserve Banks.	<i>12 USC 342, 360 12 USC 4001 et seq.</i>	<i>12 CFR 210 (Regulation J)</i>
Reserve Requirements	Sets monetary reserve requirements that covered credit unions must maintain at the Federal Reserve.	<i>12 USC 461 et seq.</i>	<i>12 CFR 204 (Regulation D)</i>
Truth-in-Lending	Requires credit unions to disclose terms and costs of consumer credit.	<i>15 USC 1601 et seq.</i>	<i>12 CFR 226 (Regulation Z)</i>

Internal Revenue Service

The IRS is a federal agency within the U.S. Treasury Department that administers and enforces the tax laws that include extensive information reporting.

Backup Withholding	Requires credit unions to obtain certified taxpayer identification numbers on W-9 forms or obtain W-8 form, and imposes backup withholding of 31% of an interest or dividend payment of a member under certain conditions.	26 USC 3406	26 CFR 35a.3406-2 et seq.
Depositing Funds Withheld	Governs how credit unions are to deposit funds with the U.S. government that are withheld due to backup withholding.	26 USC 7805	26 CFR 31.6302-3
Depositing Employee Funds Withheld	Governs how credit unions are to deposit income and other taxes withheld from employees' earning.	26 USC 7805	26 CFR 31.6302.1
Discharge of Indebtedness	Requires credit unions to file Form 1099-C to report the discharge of indebtedness for amounts of \$600 or more in a calendar year.	26 USC 6050P	26 CFR 1.6050P-1
Dividend/Interest Reporting	Requires credit unions to file a 1099-INT information return with members and with the IRS when making a payment of dividends of \$10 or more on an account.	26 USC 7805	26 CFR 1.6042-1
Employee Withholding	Requires employers to file Form W-2 to report wages paid to employees.	26 USC 7805, 6051	26 CFR 1.6041-2
Federal Insurance Contribution Act	Establishes the rates and computation of the FICA taxes than an employer must collect from each employee.	26 USC 3101 et seq.	26 CFR 31.3101 et seq.
Federal Unemployment Tax	Establishes the tax rates and computation of the unemployment tax.	26 USC 7805	26 CFR 31.3301 et seq.
Foreclosures and Abandonment of Security	Requires credit unions to file a Form 1099-A when acquiring an interest in any property that is security for a debt due to foreclosure or abandonment.	26 USC 7805	26 CFR 106050J-IT
Income Tax	Requires state-chartered credit unions to file a Form 990 annually.	26 USC 6104,	26 CFR

Return for Tax-Exempt Organizations		6033	1.6033-1
Individual Retirement Accounts	Prescribes rules relating to filing annually the Form 5498 and for handling distribution for IRAs. Establishes new "Roth" IRA.	26 USC 408, 408A	26 CFR 1.408, 1.408A
Magnetic Medic Reporting	Requires the general use of magnetic media for submitting Forms 1098 and the 1099 series to the IRS.	26 USC 6011(e)	26 CFR 301.6011-2
Mortgage Interest Reporting	Requires a credit union that receives at least \$600 of interest on most mortgages to file a Form 1098- information return annually.	26 USC 7805	26 CFR 1.6050H
Original Issue Discount Reporting	Requires credit unions, in certain cases where a certificate extends beyond one-year to file a Form 1099-OID information return in place of a 1099-INT return.	26 USC 1272	26 CFR 1.6049-1, 1.6050
Property Subject to Levy	Governs how credit union are to surrender funds to the IRS upon the receipt of a notice of levy.	26 USC 7805	26 CFR 301.6332
Real Estate Transaction Reporting	Generally requires credit unions to make a 1099-S information return with respect to a real estate transaction if no agent is involved with the sale.	26 USC 6045	26 CFR 1.6045-4
Record keeping Requirements for Employment Taxes	Sets forth the record keeping and return requirements for employers.	26 USC 7805	26 CFR 31.6001

U.S. Department Of The Treasury

The Department of the Treasury is a cabinet level agency responsible for formulating and executing domestic and international financial, economic, and tax policies

<p>Bank Secrecy Act, including USA PATRIOT Act</p>	<p>Sets forth the record keeping and reporting responsibilities for credit unions and other financial institutions to assist in the effort to combat money laundering, terrorism, tax evasion, and other criminal activity. Includes: Currency transaction reporting for each deposit, withdrawal, exchange of currency or other payment or transfer than involves a transaction in currency of more than \$10,000; Suspicious activity reporting for suspected money laundering activity, suspected structuring activity or other suspicious activity; Regulations issued to implement the USA PATRIOT Acts provisions regarding (1) identification and verification of any person who opens an account at a financial institution and (2) sharing of information between the government as well as among financial institutions themselves.</p>	<p>31 USC 5311-5322 12 USC 1786(q) 12 USC 1829b 12 USC 1951-1959</p>	<p>31 CFR 103 12 CFR 748</p>
<p>Book entry Transactions Involving Treasury Securities</p>	<p>Governs the purchase and sale of Treasury bonds, notes, and bills by individuals through financial institutions.</p>	<p>31 USC 3101 et seq. 12 USC 391</p>	<p>31 CFR 357</p>
<p>Counterfeit and Mutilates Currency</p>	<p>Governs the handling of counterfeit obligations presented at the credit union and the exchange of mutilated coin and paper currency.</p>	<p>18 USC 492 31 USC 321</p>	<p>31 CFR 403, 100 et seq</p>
<p>Federal Payments via Automated Clearinghouse</p>	<p>Governs the payment of federal government benefit and non-benefit proceeds made by the ACH method through the Federal Reserve to recipients who maintain accounts at financial institutions.</p>	<p>12 USC 391 31 USC 321</p>	<p>31 CFR 210</p>
<p>Fiscal Agents and Treasury</p>	<p>Governs the contractual terms of the agreement between a credit union and the Treasury Department in order to be designated to hold</p>	<p>12 USC 1767 31 USC 3122</p>	<p>12 CFR 701.37</p>

Tax Loan Depositories	government tax funds.		<i>31 CFR 203, 312</i>
Savings Bonds	Governs the manner in which an organization may qualify and act as a paying agent and issuing agent of Series EE US savings bonds.	<i>31 USC 3105</i>	<i>31 CFR 317</i>

Federal Trade Commission

The FTC is an independent federal agency with the primary responsibility to eliminate unfair or deceptive acts or practices affecting consumers

Credit Practices	Defines what constitutes unfair credit practices for state-chartered credit unions.	<i>15 USC 57a</i>	<i>16 CFR 444</i>
Fair Credit Reporting	Requires consumer-reporting agencies to provide information fairly and equitably to consumers with regard to the confidentiality, accuracy, and proper use of such information. Includes the Fair and Accurate Credit Transactions Act that includes identity theft protections and restrictions on information sharing.	<i>15 USC 1681 et seq.</i>	<i>16 CFR 600</i>
Fair Debt Collection	Prohibits a credit union that is collecting a debt for someone else from using any deceptive representation or deceptive means to collect or attempt to collect debts.	<i>15 USC 1692</i>	<i>16 CFR 901</i>
Holder-in-Due-Course	Restricts enforcement of contract terms when there is a business relationship between a seller of goods and services and a creditor financing the purchase.	<i>15 USC 41 et seq.</i>	<i>16 CFR 443</i>

NACHA – The Electronic Payments Association

NACHA is a private, non-profit association that writes the rules for the Automated Clearing House (ACH) system, which are known as the NACHA Operating Rules. These Operating Rules apply to all credit union that use the ACH system. Credit union that are capable of receiving ACH items into the accounts of their members are receiving depository financial institutions (RDFIs) and those that are capable of originating an ACH item are originating depository financial institutions (ODFIs). This section provides a reference to some provisions of the Operating Rules that affect credit unions participating in the ACH system. NACHA has Guidelines that supplement these “Operating Rules,” a NACHA publication.

Affidavits	The Operating Rules require a credit union to obtain an affidavit from a member before they re-credit a member’s account for an ACH item that the member alleges is unauthorized or improperly originated. IN those cases, when the credit union returns the ACH item to the ODFI, it warrants that the credit union has already obtained a signed affidavit.	<i>Operating Rules Article Seven, subsection 7.6.1-7.6.4, 7.7.1, 7.7.2</i>
Audits and Verification	The Operating Rules require credit unions in the ACH network and their ACH service providers to conduct annual audits of compliance with the Operating Rules. These requirements differ for ODFIs and RDFIs. The audits must be kept and available at NACHA’s request for six years from the date of the audit.	<i>Operating Rules Article One, subsection 1.2.1. Appendix Eight Guidelines Section II, subsection L, Guidelines Section II, Chapter IV RDFIs, subsection G</i>
Availability of Funds	Establishes when a RDFI must post ACH entries and make the funds from those entries available to members based on when entries are available to an RDFI.	<i>Operating Rules, Article Four, sections 4.3 and 4.4 Guidelines Section II, Chapter I, subsection J-2</i>
Returns	The ACH network allows the return of ACH entries and allows an ODFI to dishonor and contest a return.	<i>Operating Rules Article Five, section 5.1 and 5.2 Operating Rules Article Nine, section 9.3</i>

		<i>Operating Rules Appendix Five Guidelines Section II, Chapter I, subsection J-2 Guidelines Section II, Chapter I, subsection J-3 Section III, Chapter III</i>
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Other Federal Agencies Affecting Credit Union Operations

Americans with Disabilities Act- U.S. Department of Justice	Prohibits discrimination on the basis of disability, requires constructions of new buildings in compliance with the accessibility standards, and requires removal of physical barriers in existing facilities of alteration is readily available.	42 USC 12181	28 CFR 36
Anti-Discrimination Data Collection- U.S. Department of Housing and Urban Development	Requires credit unions participating in the HUD mortgage insurance programs, home improvement loan programs, GNMA mortgage purchase programs, or special mortgage assistance programs to maintain data on race, religion, nationality, and sex.	42 USC 3535(d)	24 CFR 107
Bankruptcy	Sets forth the requirements and procedures credit unions must follow when a member has filed bankruptcy including the automatic stay, proof of claim, and reaffirmation agreements.	11 USC 501 et seq	
Child Support Enforcement	Establishes responsibility for financial institutions to use data matches to provide states with the social security number, tax payer identification number and financial account information for parents who owe child support arrearages.	42 USC 666(a)(17)	
Credit Unions on Military Bases – U.S. Department of Defense	Provides general operating policies and procedures for credit unions operating on DOD installations.	10 USC 136	32 CFR 231a
Environmental Lender Liability	Sets forth guidelines under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) concerning responsibility for environmental cleanup of a foreclosed property.	42 USC 9601 et seq.	40 CFR 300 Subpart L
Electronic Records and Signatures	Establishes that electronic records and signatures may not be denied effect solely because they are not written. Provides default rules for electronic consumer disclosures and validated electronic records for checks that are used for record keeping	15 USC 7001 et seq.	

	and proof of payment, but not as payments instruments.		
Electronic Transfer Accounts	Establishes electronic transfer account that allows government benefit recipient to electronically receive benefits in credit union accounts.	<i>31 USC 3332</i>	<i>31 CFR 208 et seq.</i>
Food Stamps – U.S. Department of Agriculture	Establishes the criteria and procedures for the redemption of food stamps by qualified credit unions.	<i>7 USC 2001 et seq.</i>	<i>7 CFR 278.5</i>
Guaranteed Student Loans/PLUS Programs – U.S. Department of Education	Requires a credit union to disclose certain information to a borrower either before or at the time of the first disbursement of the student loan.	<i>20 USC 1078-2</i>	<i>34 CFR 682.205</i>
Privacy – Access by Various Federal Agencies to Credit Union Records	Governs the procedures that the Department of Treasury, U.S. Postal Service, and the Department of Defense must follow to gain access to credit union records.	<i>12 USC 3401 et seq</i>	<i>31 CFR 14 29 CFR 19 32 CFR 504 39 CFR 233</i>
Real Estate Settlement Procedures Act (RESPA/regulation X) – U.S. Department of Housing and Urban Development	Requires credit unions receiving loan applications for federally related mortgage loans to provide a copy of the special information booklet and an estimate of closing costs for settlement; requires loan originators and servicing organizations to disclose information on their practices of selling loan servicing; and requires disclosures relating to escrow accounts.	<i>12 USC 2601 et seq.</i>	<i>24 CFR 3500</i>
Signature Guarantees – Securities Exchange Commission	Provides the standard by which a credit union's signature guarantee regarding a stock transfer must be accepted by the stock transfer agent.	<i>15 USC 77c</i>	<i>17 CFR 240, 17Ad-15</i>
Soldiers' and Sailors' Civil Relief Act – U.S. Department of	Requires credit unions to reduce the interest rate on pre-existing loans of certain individuals upon entering military service, during their period of active duty.	<i>50 USC Appx 526</i>	

Defense			
Title I Property Improvement and Manufactures Home Loans – U.S. Department of Housing and Urban Development	Sets forth the requirements for participation in this programs insuring certain loans.	<i>12 USC 1701 et seq. 42 USC 3535(d)</i>	<i>24 CFR 201, 202</i>

Equal Employment Opportunity Commission

The EEOC is a federal agency that provides guidance and technical assistance to employees who suspect discrimination and to employers on equal employment laws.

Age Discrimination in Employment Act	Prohibits age discrimination in employment and requires credit union to keep records necessary for the administration of this law.	29 USC 621 et seq.	29 CFR 1627
Americans with Disabilities Act	Prohibits employers from discriminating against persons with disabilities who are otherwise qualified for employment, and requires employers to make reasonable accommodations to known disabilities.	42 USC 12101 et seq	29 CFR 1602, 1630
Equal Employment Opportunities – Civil Rights	Requires equal employment opportunity without regard to race, color, religion, sex, familial status, national origin, age, or disability.	42 USC 2000e	29 CFR 1601 et seq.

U.S. Department of Labor

The Department of Labor is a federal agency that promotes and develops policies relating to working conditions and employment opportunities for the benefit of U.S. wage earners

Affirmative Action Plans	Requires credit unions with more than 50 employees that are federal contractors to comply with affirmative action rules	29 USC 793, 794	41 CFR 60-741
Employee Retirement Income Security Act (ERISA)	Protects employees' rights to receive welfare and pension benefits, and includes detailed reporting, filing, and disclosure requirements.	29 USC 1001 et seq.	29 CFR 2509 et seq.
Employment Practices Record Keeping	Requires employers to make, keep, and preserve personnel records of employees, including wages, hours, and other conditions of employment.	29 USC 211	29 CRR 516
Family and Medical Leave	Requires employers with 50 or more employees to provide up to 12 weeks per year of unpaid, job-protected leave to eligible employees for family medical emergencies or to care for an infant.	29 USC 2601 et seq.	29 CFR 825
Group Health Plans	Requires employers to provide continuous group health coverage to certain individuals due to termination of employment.	29 USC 1161 et seq.	
Minimum Wage/Overtime	Establishes the minimum permissible wage per hour, and the maximum number of hours above which an employer must pay an employee not less than 1 ½ times regular wages.	29 USC 206, 207	29 CFR 500 et seq.
Occupational Safety and Health	Requires employers to provide employees a safe and non hazardous environment in which to work, and requires employers to keep records regarding activities relating to occupations safely and health as well as to report workplace injuries and illnesses.	29 USC 651 et seq.	29 CFR 1900 et seq.
Polygraph Protection	Prohibits employers from requiring an employee or prospective employee to take a lie detector test (with limited exceptions).	29 USC 2001 et seq.	29 CFR 801

Other Federal Employment Rules

<p>Bankruptcy Protection – U.S. Bankruptcy Code</p>	<p>Prohibits employers from discriminating against an employee/debtor with respect to employment.</p>	<p><i>11 USC 525(b)</i></p>	
<p>Employment of Aliens – U.S. Department of Justice/Immigration and Naturalization Service</p>	<p>Requires employers to verify employment eligibility of prospective employees by examining documentation and completing Form I-9.</p>	<p><i>8 USC 1324a</i></p>	<p><i>8 CFR 274a</i></p>
<p>Veteran's Reemployment Rights Act – U.S. Office of Personnel Management</p>	<p>Sets forth the rights and obligations of employees on connection with leaves of absence or restoration to duty following military duty.</p>	<p><i>28 USC 4301 et seq.</i></p>	<p><i>5 CFR 353</i></p>