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Credit Union Membership Act Implementation: Legal Issues

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M. Maureen Murphy
Legislative Attorney
American Law Division

ABSTRACT

Regulations implementing the Credit Union Membership Act of 1998 are being challenged in court as impermissively expansive. This report examines the background and issues of this litigation. For further information on the background and ramifications of these regulations *see* CRS Report RL30028, *"Commercial Banks vs. Credit Unions: Operations and Legislative Issues"* (January 14, 1999).

Credit Union Membership Act Implementation: Legal Issues

Summary

In early 1998, the Supreme Court interpreted the Federal Credit Union Act to require that a single common bond must unite members of a federal credit union organized on the basis of an occupational common bond. In August 1998, Congress enacted the Credit Union Membership Act, P.L. 105-219, that permits and sets standards for multiple group federal credit unions. In December 1998, the National Credit Union Administration (NCUA) issued regulations implementing this legislation. Shortly thereafter, the American Bankers Association petitioned the U.S. District Court for the District of Columbia to enjoin enforcement of these regulations. ABA could not show irreparable injury and likelihood to win on the merits and was denied a preliminary injunction on March 10, 1999. ABA argued that the regulations are contrary to Congressional intent and will mean irreparable injury for banking competitors of federal credit unions. The case will now go to trial on the issue of granting a permanent injunction with the date of decision unpredictable. While Congressional attention was focused on this issue on February 3, 1999, with House Banking Committee's Subcommittee on Financial Institutions and Consumer Credit hearings, no legislation has been introduced.

The main issues concern whether the statutory directives to favor chartering single credit unions rather than adding groups to existing credit unions and generally requiring groups over 3,000 to be separately chartered have been properly interpreted by NCUA. In the hearings and presumably in the lawsuit, ABA charges that the regulations undermine Congressional intent with the result that the credit union industry will be able to consolidate and expand. Another point of contention revolves around whether "local community" as interpreted by NCUA to include rural and metropolitan jurisdictions of 300,000 or less is a reasonable interpretation of the statutory language considering the statutory purpose of requiring actual interaction among members as a component of the common bond of a community credit union. Also contested is NCUA's readings of the terms, "household," and "immediate family," which ABA argues are expansive.

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Background[1]

On February 25, 1998, in *National Credit Union Administration v. First National Bank & Trust Co.*,__ U.S. __, 119 S.Ct. 60, the Supreme Court interpreted the Federal Credit Union Act, 12 U.S.C. §§ 1751 - 1759k, to require that a single common bond must unite members of a federal credit union organized on the basis of an occupational common bond. In August 1998, Congress enacted the Credit Union Membership Act, P.L. 105-219, that permits and sets standards for multiple group federal credit unions. In December 1998, the National Credit Union Administration (NCUA) issued regulations implementing this legislation.[2] The American Bankers Association petitioned the U.S. District Court for the District of Columbia to enjoin enforcement of these regulations.[3] ABA could not show irreparable injury and likelihood to win on the merits and was denied a preliminary injunction on March 10, 1999. ABA argued that the regulations are contrary to Congressional intent and will mean irreparable injury for banking competitors of federal credit unions. The case will now go to trial on the issue of granting a permanent injunction. Congressional attention was focused on this issue on February 3, 1999, when the House Banking Committee's Subcommittee on Financial Institutions and Consumer Credit held hearings on the issue.

In *National Credit Union Administration v. First National Bank & Trust*, the Supreme Court rejected NCUA's policy of permitting multiple groups having separate common bonds to be joined in a single credit union, finding it contrary to the unambiguous language of a provision of the Federal Credit Union Act. That provision, which has since been amended, limited federal credit union membership to "groups having a common bond of occupation or association, or to groups within a well-defined neighborhood, community or rural district." 12 U.S. C. § 1759. Since the Court found the provision unambiguous, the second prong of the test used in *Chevron U.S.A, Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984) was not applied. Under *Chevron*, in interpreting a statute, a court looks first to whether the language is unambiguous. If the language is clear, then that is how the statute must be interpreted. Only when the court finds ambiguity is there a need to resort to

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[1] For further information on the background and ramifications of these regulations *see* CRS Report RL30028, *"Commercial Banks vs. Credit Unions: Operations and Legislative Issues"* (January 14, 1999).

[2] 63 *Fed. Reg.* 71998 (December 30, 1998).

[3] *American Bankers Association v. National Credit Union Administration* (D.D.C., 99-0042).

legislative history and a requirement to defer to a reasonable interpretation of the administrative agency charged with enforcing or interpreting the statute.

The 1998 Supreme Court decision placed many federal credit unions in jeopardy. Without legislation the court might have required them to divest of any groups other than their original organizing group and not to add new members from any but the original group. To remedy the situation, Congress passed the Credit Union Membership Access Act. This legislation preserves existing multiple group, occupational bond federal credit unions. It contains instructions to NCUA with respect to future applications by groups to become or be joined with a multiple group credit union, *i.e.*, NCUA is to charter single groups where possible, or to require the group to join a credit union "within reasonable proximity" to the group. A standard for affiliations is set in terms of size of group being annexed: groups of more than 3,000 should generally not be permitted to affiliate with an existing credit union. Multiple group credit unions may extend their membership to persons and organizations located within areas underserved by other depository institutions. NCUA's regulations interpreting these statutory provisions are at issue in the 1999 ABA case, which may well be decided on *Chevron* grounds.

The Credit Union Membership Access Act

The Credit Union Membership Access Act sets forth three categories or fields of membership under which a federal credit union may be organized: (1) single associational or occupational common bond credit union; (2) multiple common bond credit union; and (3) community credit union.

The single common bond credit union has "[o]ne group that has a common bond of occupation or association." 12 U.S.C. § 1759(b)(1).

The multiple common bond credit union has more than one group, each of which has a common bond of occupation or association. As a general rule, each of these groups must have had no more than 3,000 members at the time it was first included. 12 U.S.C. §§ 1759(b)(3) and (d)(1). Inclusion of groups having more than 3,000 members is permissible under any of a series of exceptions:

> (1) One exception permits adding persons from an underserved area or neighborhood.[4]
>
> (2) Another exception applies to any group that the NCUA determines not to be viable.[5]

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[4] This includes any person in an underserved area that meets the criteria established for an "investment area" under the Community Development Banking and Financial Institutions Act of 1994, in which the credit union establishes and maintains an office or facility. 12 U.S.C. § 1759(c)(2).

[5] This includes any group that NCUA determines not capable of being a separate credit union for lack of sufficient resources; failure to have various criteria important for success, such as age and income diversity; or unlikely to operate a safe and sound credit union. 12 U.S.C. §

(continued...)

(3) Another exception applies to any group transferred in connection with a supervisory merger.[6]

Essentially, the statute provides that, other than for supervisory mergers and additions from underserved areas, only groups of 3,000 or more that are not economically viable may be added to another group or groups in a multiple group credit union. The statute requires NCUA to issue guidelines and regulations establishing the criteria to accomplish this.[7]

The statute further provides that the NCUA, where practicable and consistent with safety and soundness, encourage the formation of separate credit unions; if that is not possible in a given situation, then it must require the group to be included in a credit union that is reasonably proximate unless questions of impracticality or safety and soundness are implicated.[8] Under the legislation, moreover, the NCUA is prohibited from approving any application to add a group unless it makes various determinations that are directed at assuring the credit union's safety and soundness and, thus, the integrity of the share insurance fund. The required determinations are: (1) that the credit union has not engaged in an unsafe or unsound practice within the preceding year; (2) the credit union is adequately capitalized; (3) the credit union has the financial and administrative capability to serve the proposed group; (4) any potential harm to other credit unions by the expansion is outweighed by the public good realized in meeting the needs of the group being added; (5) and the credit union has met any additional requirements that the NCUA has required by regulation.[9]

The statute also provides that any regulation defining "immediate family or household," for credit union membership purposes, and any regulation defining "well-defined local community, neighborhood, or rural district," for purposes of defining a community credit union is to be treated as a major rule, thus, delaying implementation for 60 days.[10]

The Regulations

Generally. On December 17 and December 22, 1998, the NCUA approved final rules and issued Interpretative Ruling and Policy Statement IRPS 99-1, its Field of Membership Manual, governing Federal Credit Union Chartering. Testimony at February 3, 1999 hearings before the House Banking Committee's Subcommittee on Financial Institutions and Consumer Credit raised various concerns as to whether

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[5](...continued)
1759(d)(2)(A).

[6] 12 U.S.C. § 1759(d)(2)(B). A grandfather provision authorizes groups transferred through voluntary mergers approved prior to October 25, 1996. 12 U.S.C. § 1759(d)(2)(C).

[7] 12 U.S.C. § 1759(d)(3).

[8] 12 U.S.C. § 1759(f)(1.

[9] 12 U.S.C. § 1759(f)(2)

[10] *See* 5 U.S.C. § 801 *et seq*. The 60-day period expired on March 5, 1999, without legislation having been enacted.

those regulations conform with the intent of Congress. Issues raised included questions as to whether the regulations furthered statutory policies with respect to chartering separate credit unions and adding groups to reasonably proximate credit unions; and whether NCUA's definitions of "community," "immediate family," and "household," furthered the goals of the statute.

Numerical Limit of 3,000 on Groups That May Be Added. One of the points discussed was whether the procedures established by the NCUA for adding select groups to existing credit unions or combining groups in initially chartering multiple group credit unions comply with the statutory requirement that NCUA "encourage the formation of separately chartered credit unions wherever practicable and consistent with reasonable standards for safe and sound operation of the credit union." 12 U.S.C. § 1759(f). Criticism has been directed at NCUA's approaches to determining: economic viability of groups seeking a credit union charter, the geographic proximity requirements for adding new groups, and the application of the statutory numerical limitation of 3,000 for groups seeking to be added to an existing credit union.[11] NCUA has taken the position that the size of the group seeking a charter often indicates economic viability, which it terms "economic advisability." In the regulations, it set 3,000 members as the mark of presumptive viability and declared that an applicant with less than 3,000 members may have to provide more evidence of viability, such as a pledge of continued financial support by the employer or sponsor, than a group of 3,000 or more. This figure of 3,000 members was an increase from a previous figure of 500.[12] To critics setting a floor of 3,000 as a benchmark of group viability seems at variance with the statutory's ceiling of 3,000 for adding to existing groups. In announcing the promulgation of the regulations, NCUA advanced the 3,000 threshold as "consistent with congressional intent as well as NCUA experience," and as "not intended to undermine the statutory requirement

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[11] Testifying for the American Bankers Association at a February 3, 1999, hearing before the House Banking Committee's Subcommittee on Financial Institutions and Consumer Credit, Harley D. Bergmeyer, charged that NCUA's rule is violative of Congressional intent:

> Last year, this Subcommittee set up a straight-forward approach to multiple-bond and community credit unions, which was incorporated in the final law. This approach was predicated on three inter-related concepts, each designed to give preference to smaller, locally controlled credit unions. First, NCUA should encourage single common bond credit unions whenever possible. To strengthen this directive, Congress permitted only groups with fewer than 3,000 to join another credit union except under prescribed extenuating circumstances. Second, if a new common bond were, in fact, added to an existing credit union, the combination should be with a credit union located within *reasonable proximity*. Third, the word "*local*" was added to the standard for *community* credit unions. Despite these clear directives from Congress, NCUA's rule disregards this preference for smaller, locally-controlled credit unions, and is biased toward large credit unions, whether local or not.

Testimony of Harley D. Bergmeyer, [http://www.house.gov/banking/2399aba.htm] (emphasis in original) (hereinafter, ABA Testimony).

[12] IRPS 94-1, 59 *Fed. Reg.* 29066 (June 3, 1994).

to encourage the formation of new credit unions."[13] One reason advanced by NCUA for the increase was that today's technology requires both start-up costs and sophisticated skills for credit union employees that are less likely to be found in small groups.[14]

While a numerical limit of 3,000 is set as the general rule permitting a group to join another credit union not having the same common bond, the statute authorizes exceptions and requires that NCUA issue guidelines for approving additions of groups of 3,000 or more.[15] NCUA seems to have espoused a balancing test that considers the 3,000 numerical limit in the context of safety and soundness concerns.[16] The NCUA guidelines require a more detailed analysis for groups of 3,000 or more members. The credit union must demonstrate that the formation of a separate credit union is not practical and that the group lacks volunteer and other resources to operate an economically viable credit union under NCUA standards. Also required is identification of the new group's eligibility for membership in any other credit union, whether it has other credit union service available, and information on the proximity of the group to the petitioning credit union's service facilities.

The Proximity Test for Adding Groups. The statute requires that NCUA "include the group in a credit union within reasonable proximity to the location of the group wherever practicable and consistent with reasonable standards for the safe and sound operation of the credit union." The Senate Report accompanying this legislation states that:

> This section provides for the NCUA to encourage the formation of separately chartered credit unions wherever possible, consistent with safety and soundness, instead of including an additional group within an existing credit union's field of membership. If the formation of a separate credit union by such group is not practicable or consistent with safety and soundness standards, then the inclusion of that group is required to be in a credit union within reasonable proximity to the location of the group.[17]

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[13] 63 *Fed. Reg.* 71998, 72001.

[14] Dennis Dollar, Testimony Before the House Committee on Banking and Financial Services, Subcommittee on Financial Institutions and Consumer Services, on the Implementation of the Credit Union Membership Act, February 3, 1999 (Available in LEXIS, BANKING Library, CURNWS File).

[15] 12 U.S.C. § 1759(d)(1).

[16] NCUA stated:

> As the legislation directs, the Board will encourage the formation of separately chartered credit unions if it is prudent and economically advisable. Important factors in making this determination, however, are the desire of the group and the sponsor support. In other words, to ignore the group's administrative capability may lead to unnecessary supervisory problems in the future.
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> 63 *Fed. Reg.* 71998, 72002.

[17] S.Rept. 105-193, at 7-8.

The regulations, however, do not set forth procedures directly implementing the reasonable proximity requirement. For example, there is nothing that indicates that NCUA will consider whether an addition of a group to a credit union fulfills the reasonably proximate standard or whether the new group should be referred to a closer credit union. What is included is one general statement that:

> NCUA will attempt to assist any group in chartering a credit union or joining an existing credit union. If the group is not eligible for federal credit union service, NCUA will refer the group to the appropriate state supervisory authority where different requirements may apply.[18]

NCUA does not ask for any information about other nearby credit unions or reasons for not choosing to join them. In testimony, the credit union trade organization, the National Association of Federal Credit Unions, indicated that the idea that NCUA would be a matchmaker for groups seeking to join credit unions does not coincide with the reality of the credit union application process.[19] That the statute requires matchmaking in some instances seems to be the position that ABA has taken in its lawsuit. A piece of legislative history that may be relevant appears in the Senate Report accompanying the final version of the legislation, which declares: "[t]he Committee does not intend for these exceptions to provide the Board with broad discretion to permit larger groups to be included in other credit unions. These exceptions are intended to apply where the Board has sufficient evidence to support a finding that the creation of a separately chartered credit union, or the continued operation of an existing credit union presents safety and soundness concerns."[20]

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[18] 63 *Fed. Reg.* 71998, 72002.

[19] The testimony of J. Raymond Curtin, Before the House Comm. On Banking and Financial Services Subcomm on Financial Institutions and Consumer Credit (February 3, 1999) [http://www.house.gov/banking/2399nafc.htm], included the following assertion:

> The statute does not impose upon NCUA an affirmative obligation to serve as a 'clearing house' for applications submitted by groups that would like to obtain credit unions services but are unable to meet the necessary requirements to obtain a credit union charter in their own right. It may be a useful function for NCUA to perform, but it is not a statutorily mandated function. The nearly fifteen years of experience NCUA and the credit union community had in dealing with the extension of credit union services to groups through multiple group field of membership policy NCUA had in place prior to the Court's decision in the AT&T Family Federal Credit Union case suggests that the function of 'matching' groups seeking credit union services with credit unions interested in offering services to a larger membership base can best be accomplished in the marketplace itself....The 'match' between a select employee group and a credit union involves a number of factors, some of which are tangible and others that are intangible. The underlying need is a recognition on the part of both parties that, indeed, the 'match' is a 'good fit' for both.

[20] S.Rept. 105-193, 105th Cong., 2d Sess. 7 (1998).

One other factor that enters the equation is that usually proposals emerge from existing credit unions and groups that have already decided to join forces rather than from groups asking NCUA to find a match. Recognizing this, perhaps, NCUA includes among the elements considered is the desire of the group to be part of the credit union. Each application for adding a group, therefore, must be accompanied by a letter that indicates the group's desire to be added.[21]

Definitions of "Local Community". Another point of contention is the regulation's approach to interpreting the statutory requirement that a community credit union consist of "[p]ersons or organizations within a well-defined *local* community, neighborhood, or rural district." 12 U.S.C. § 1759(b)(3) (emphasis added). The 1998 law added the qualifying adjective, "local." It did so in the context of statutory findings that include the following language, "To promote thrift and credit extension, a meaningful affinity and bond among members, manifested by a commonality of routine interaction, shared and related work experiences, interests, or activities, or the maintenance of an otherwise well-understood sense of cohesion or identity is essential to the fulfillment of the public mission of credit unions."[22] The ABA contends that by this amendment, Congress intended to limit the reach of the noun, "community," and, thereby, reinforce a preference for small credit unions. It argues that NCUA took a more expansive reading that is biased in favor of large credit unions.[23] NCUA set up a three-part requirement for a community charter: (1) clearly defined geographic boundaries; (2) "well-defined local, community, neighborhood, or rural district," and (3) residents having common interests or interaction.[24] In describing the meaning of "local community, neighborhood, or rural district," NCUA referenced a number of factors: interaction, common interests, as well as population and geographic size. With respect to geographic size, however, it offered a presumption and minimal documentation requirements for establishing that "an ethnic neighborhood, a rural area, a city, and a county with 300,000 or less residents will generally have sufficient interaction and/or common interests to meet community charter requirements."[25] While larger population areas might be able to qualify, more documentation would be required of them.[26]

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[21] 63 *Fed. Reg.* 71998, 72033, Multiple Common Bond Amendments IV.B.3.

[22] P.L. 105-219, § 2(3), 112 *Stat.* 913, 914 (Aug. 7, 1998).

[23] ABA cites an example: "the prior rule required 'interaction' among individuals to qualify as a "community" for a community credit union. The rule now adds another option, requiring that individuals demonstrate either interaction or 'common interest.' ABA Testimony.

[24] 63 *Fed.Reg.* 71998, 72037, Community Charter Requirements, V.A.1.

[25] *63 Fed. Reg.* 71998, 72037, Community Charter Requirements, V.A.2.

[26] A single political subdivision with a population of 300,000 or less would only be required to show how the area meets the standards for community interaction or interests. Other communities would have to document their status as a local community, such as defined political jurisdictions, shopping areas, community clubs, community newspapers, maps designating the area, common characteristics of residents, or other documentation showing interaction and common interests. 63 *Fed. Reg.* 71998, 72038, V.A. 2.

Definition of "Immediate Family" or "Household" Member. In addition to members of the group having a common bond, the 1998 law provided that "[n]o individual shall be eligible for membership in a credit union on the basis of the relationship of the individual to another person who is eligible for membership in the credit union, unless the individual is a member of the immediate family or household (as those terms are defined by the Board, by regulation) of the other persons. NCUA's definition of "household," and "immediate family member" have been criticized as too expansive. The regulation defines "household" as "[p]ersons living in the same residence maintaining a single economic unit."[27] "Immediate family member" is defined as "[a] spouse, child, sibling, parent, grandparent, or grandchild. This includes stepparents, stepchildren, stepsiblings, and adoptive relationships."[28] Previously, NCUA permitted credit unions to define their common bond to include various persons sharing a relationship with the common bond group. There was no provision for members of a household. There was, however, a provision "members of their immediate families," that may have been interpreted to include unrelated persons living in a single household. It offered a general definition and did not require actual membership by the group member for a family member's eligibility.

> 'Members of their immediate families' may generally be defined as deemed appropriate by a Federal credit union when including this group among those to be served. To be made effective, however, the Federal credit union's board of directors must approve the definition by resolution, and include it in Article XVIII, Section 2, of its bylaws. The single exception is for those Federal credit unions serving student groups: only those 'members of the immediate families' of students who actually join the Federal credit union may be included. NCUA defines this secondary group for student groups as follows: 'Members of the immediate families of students who are members of this credit union.'[29]

Legislation

Although the House Banking Committee's Subcommittee on Financial Institutions and Consumer Credit held hearings on NCUA implementation of the Credit Union Membership Act on February 3, no legislation has been introduced in the 106th Congress. The district court's refusal to grant ABA a preliminary injunction means that until full trial of the issues and decision, the date of which is difficult to predict, NCUA, under its regulations, will be able to permit expansions that ABA views as illegal and competitively damaging. Even after a full trial, the court may require that ABA or competing credit unions challenge individual NCUA actions rather than the entire packet of regulations.[30]

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[27] 63 *Fed. Reg.* 719998, 12046, Appendix A—Glossary.

[28] *Id.*

[29] IRPS 89-1, II A.5, 54 *Fed. Reg.* 31165(July 27, 1989).

[30] For background on the legislation in the 105th Congress in the wake of the Supreme Court decision in *National Credit Union v. First Union National Bank & Trust*, see CRS Report No. 98-162, "Credit Union Common Bond Ruling," by M. Maureen Murphy; CRS Report 97-548, "Should Credit Unions Be Taxed?," by James Bickley; and CRS Report 97-267, "Multiple-Group Federal Credit Unions," by Pauline Smale.