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Credit Union Membership Access Act: Background and Issues

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Summary

On February 25, 1998, the U.S. Supreme Court ruled in favor of the banking industry, invalidating the National Credit Union Administration's (NCUA) policy regarding multiple-group fields of membership for federal credit unions. Multiple-group federal credit unions (FCUs) and litigation challenging the structure and membership in these FCUs have been the focus of much media attention and congressional concern. After the decision, Congress moved quickly to pass legislation addressing the concerns of the credit union industry. On August 7, 1998, P.L. 105-219 the Credit Union Membership Access Act was enacted. The Act grandfathers all current FCUs and all current credit union members. The Act provides for future multiple-group formations subject to limitations that the NCUA must consider when authorizing charters. In addition, the statute contains provisions for stricter regulatory, supervisory and commercial lending requirements for credit unions. This report will not be updated.

Background

Credit unions differ from other depository financial institutions because of their cooperative framework and unique charter requirements. The original concept of a credit union was a cooperative organization formed for the purpose of promoting thrift among its members and providing them with a source of low-cost credit. Credit union charters are granted by federal or state governments. Federal charters have been available since 1934 when the Federal Credit Union Act (FCUA) was passed. All credit union charters are granted on the basis of a "common bond"; this requirement determines the field of membership, and is unique among depository financial institutions.

The FCUA outlines three categories of common bond: occupational, associational, and community. The NCUA is the federal regulator for credit unions. The NCUA has established guidelines and policies for all three types of common bond. An occupational group is defined as employment by the same enterprise. The associational membership is an organization, participation in whose activities develops common loyalties, mutual

benefits, and mutual interests. The community common bond bases members on persons who live or work within a well defined neighborhood, community or rural district.

Individual credit unions are owned by their membership. Members' savings are referred to as "shares," and earn dividends instead of interest. Credit union loan and investment powers are more restrictive than commercial banks. Credit unions can only make loans to their members, to other credit unions, and to credit union organizations. Credit unions can invest in government or government-guaranteed financial instruments. Because credit unions are considered financial cooperatives, the institutions are exempt from federal income tax. Individual members are taxed on their dividends.

The recent dispute about membership requirements evolved from a policy adopted in 1982 by the NCUA. In 1982, the NCUA issued an interpretive ruling and policy statement that provided flexibility to the field of membership requirements for federal credit unions. The NCUA's interpretation permitted membership in a FCU to consist of more than one distinct group so long as each group has its own common bond. The NCUA's action was taken in response to changing economic conditions and as part of an industry commitment to meet the needs of individuals seeking credit union service. This resulted in court cases with the banking industry. Bankers claim that credit unions have outgrown their founding principle and no longer deserve the competitive advantages of federal tax exemption and less stringent regulatory procedures.

In 1990, the American Bankers Association and several small North Carolina banks filed a lawsuit contesting the NCUA's approval of multiple-group field of membership for the AT&T Family Federal Credit Union. In July 1996, the U.S. Court of Appeals for the District of Columbia overturned a lower court's decision and ruled that "all members of a federal credit union must share one common bond." Under the terms of several subsequent orders, FCUs could not add new groups to their fields of membership, but the institutions were permitted to enroll new members into those established groups already being served.

On February 24, 1997, the U.S. Supreme Court agreed to hear the credit union case. The court heard arguments on October 6, 1997. The Justices spent most of the hearing focusing on whether the banks were the appropriate parties to challenge a regulation that was not addressed to them. On February 25, 1998, the Supreme Court ruled that federal occupation-based credit unions must consist of an occupational group having a single common bond. The majority also held that the banks had legal standing to mount a court challenge to the NCUA.[1]

Legislation in the 105th Congress

The 105th Congress monitored the developments in the court case and the ongoing controversy. Several bills were introduced in the first session and while oversight hearings were held no action was taken until after the Supreme Court decision. The 105th Congress was pressured by both the banking and the credit union industries to legislate solutions to

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[1] For more information on the litigation and the Supreme Court decision see: U.S. Library of Congress. Congressional Research Service. *NCUA v. First National Bank & Trust Co.-U.S.-(No. 96-843): Credit Union Common Bond Ruling,* by Maureen Murphy. CRS report 98-162A.

controversies arising from competition between the two. The banking industry wanted measures with provisions to tax credit unions on the federal level, and to stop the industry growth achieved by multiple-group FCUs. Credit union representatives lobbied for legislation that would simply clarify the language of the Federal Credit Union Act to leave no doubt concerning the FCU fields of membership including multiple-groups.[2] Congress acknowledged the conundrum, and debate on the issues was quite heated. The Supreme Court decision increased the pressure on Congress to deal legislatively with the issue of credit union membership.

Several bills were introduced during the first session of the 105th Congress and oversight hearings were held. The credit union industry backed H.R. 1151 (LaTourette and Kanjorski) a bill that would effectively codify the NCUA's policy regarding multiple-group fields of membership. H.R. 1151 gained over 200 co-sponsors.

After the Supreme Court ruling the House Banking Committee reworked the bill to provide a solution for credit unions and their customers while ensuring a policy of safety and soundness for the industry. An amended version of H.R. 1151 was passed by the House on April 1, 1998. Additional changes were added by the Senate and the final version passed the Senate on July 28, 1998. The Senate- approved H.R. 1151 cleared the House on August 4, 1998. The bill was signed into law into law August 7, 1998.

Credit Union Membership Access Act: P.L. 105-219

The *Credit Union Membership Access Act*, P.L. 105-219 includes provisions to grandfather all current common bond arrangements and all current credit union members. Multi-group FCUs would be permitted in the future, but groups would be restricted to 3,000 members under most circumstances.

Other key provisions of the Act address the regulation and supervision of credit unions. P.L. 105-219 places limits on commercial lending; business loans to members are limited to 12.25 percent of total assets. The Act establishes new capital standards for insured credit unions and requires independent audits for insured institutions with assets of $500 million or more. The capital standards are similar to those enacted for banks and thrifts. The Act authorizes and clarifies an insured credit union's conversion to a mutual savings banks or saving association without prior NCUA approval. In addition, the law requires the NCUA to promulgate rules regarding several issues of safety and soundness including a system of prompt corrective action for credit unions.

Finally, P.L. 105-219 requires the Treasury to conduct two studies. The first will compare the differences between the regulation of credit unions and other depository financial institutions, including credit union tax treatment. The second will study ways to assist small banks, including reducing their taxes.

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[2] U.S. Congress. House. Committee on Banking and Financial Services. Subcommittee on Financial Institutions and Consumer Credit. Issues Currently Facing the Credit Union Industry. Hearing, 105th Congress, 1st session. Feb. 26, 1997. Washington G.P.O., 1998. 371 p.

Reactions to P.L. 105-219

The credit union industry views P.L. 105-219 as the most significant change in federal law affecting credit unions since the 1970's. The credit union community was pleased by the swift legislative response to the issue of credit union membership, after the Supreme Court ruling. Credit union supporters feel the enactment of P.L. 105-219 will permit the industry to continue its commitment to meeting the needs of individuals seeking credit union service.[3]

The banking industry was strongly opposed to the original credit union bill and to the legislation as enacted. Representatives of the banking industry anticipate a rapid expansion of large "bank like" credit unions. These institutions can be expected to seek a role in all aspects of the financial services industry. In addition, bankers state the law does not adequately address issues of safety and soundness.

[3] House passes credit union bill; Clinton wastes no time in signing it. BNA's banking report, v.71, no.6, Aug. 10, 1998: 245-246.