

# CRS Report for Congress

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## **Credit Union Regulatory Improvements Act of 2005 (CURIA)**

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### **Summary**

On May 12, 2005, regulatory modernization legislation for credit unions was introduced as H.R. 2317. The three titles of the Credit Union Regulatory Improvements Act (CURIA) would provide regulatory changes requested by credit union industry advocates. These changes would provide supervisory flexibility to the National Credit Union Administration (NCUA), the federal regulator for the credit union industry, enhance the ability of credit unions to provide loans to their members, and ease credit union regulatory burdens. For the last several years, credit union representatives have asked Congress to increase their ability to serve their members by addressing the growing costs of regulatory compliance and by providing additional flexibility through regulatory reform measures. Omnibus legislation (H.R. 3505) that would reduce existing regulatory requirements on all depository financial institutions has been reported by two House committees (Financial Services and Judiciary). The credit union specific provisions of H.R. 3505 incorporate many of the provisions of CURIA. H.R. 3505 does not address two major issues covered by H.R. 2317, prompt corrective action and member business loan restrictions. Credit union representatives are supportive of H.R. 3505 but are committed to the passage of all of the provisions of H.R. 2317. This report provides background on the legislation and congressional interest in regulatory relief, and will be updated as developments warrant.

### **Background**

The Credit Union Regulatory Improvements Act (CURIA) provides regulatory relief and reform for credit unions. The intent of this legislation is to modernize the prompt corrective action system for credit unions, make adjustments to their loan authority, and ease credit union regulatory burdens. H.R. 2317 was introduced on May 12, 2005; no further action has been taken on this bill. CURIA contains three titles. Title I provides the National Credit Union Administration (NCUA) more flexibility in operating the statutorily mandated prompt corrective action (PCA) system used to resolve problems in federally insured credit unions. The proposal would permit the NCUA to implement a

more risk-based approach. Title II amends the current restrictions on member business loans. The 12 sections of Title III address specific rule changes to update and streamline existing regulations. The regulatory relief provisions in Title III are similar to those passed by the House in 2004 (H.R. 1375, 108<sup>th</sup> Congress) and to those included in H.R. 3505. Credit union advocates say CURIA would ensure the financial strength of credit unions and enhance the services provided to credit union members. Opposition to the legislation was expressed by three banking trade associations in a letter to the Speaker of the House.<sup>1</sup> The letter states that the legislation would increase the powers of credit unions and raise serious safety and soundness concerns.

Two separate bills (H.R. 749 and H.R. 1042) already approved by the full House contain language included in CURIA. H.R. 749 would allow federally chartered credit unions to offer nonmember individuals access to a defined set of financial services and products. The credit union could offer money orders, check cashing, and money transfer services. The legislation passed the House on April 27, 2005. H.R. 1042 amends the statutory definition of net worth to address a potential problem raised by new merger guidance issued by the Financial Accounting Standards Board.

Although separate hearings have not been held on CURIA, the House Financial Services Committee's Subcommittee on Financial Institutions held a hearing on H.R. 3505 on October 18, 2005. Three additional hearings were held to review and consider regulatory relief proposals. These hearings provided a forum to offer new or updated proposals.<sup>2</sup> All four hearings featured testimony from federal regulators, trade associations, individual institutions, and consumer advocates. Since 2001, Congress has been working with regulators and industry representatives on legislative proposals to reduce existing regulatory requirements and the compliance burdens they place on depository financial institutions. The goal has been to identify outdated, duplicative, or ineffective regulations that are not justified by either the need to ensure safety and soundness or to provide consumer protection. This legislation would also counterbalance new responsibilities placed on banks and thrifts by the anti-money laundering and the anti-terrorist financing provisions of the 2001 USA PATRIOT Act (P.L. 107-56).

Witnesses at the hearings mainly addressed the institutions they represented or regulated. The National Credit Union Administration and credit union representatives testified at all four hearings. Testimony was supportive of H.R. 3505 but also encouraged Congress to either incorporate all of the provisions of H.R. 2317 (CURIA) into the omnibus regulatory relief legislation or pass the bill separately. Several witnesses representing banks and savings associations expressed opposition to the capital and lending authority provisions of CURIA that were not included in H.R. 3505. In general, their position is that credit unions should not be granted authorities, which could enhance their competitive strength, while continuing their exemption from federal income tax.<sup>3</sup>

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<sup>1</sup> The letter can be found at [<http://www.icba.org/>]; look under ICBA letters to Capitol Hill.

<sup>2</sup> The Senate Committee on Banking, Housing, and Urban Affairs held hearings on June 21, 2005 and Mar.1, 2006, and the House Financial Services' Subcommittee held a hearing on May 12, 2005.

<sup>3</sup> For a discussion of this issue, please see CRS Report 97-548, *Should Credit Unions Be Taxed?*, by James M. Bickley.

H.R. 3505 was reported by the House Financial Services Committee on December 17, 2005, and by the House Judiciary Committee on February 16, 2006 (H.Rept. 109-356 Part I and II). Senate legislation is expected to be introduced in the spring of 2006.

## **An Overview of the CURIA Titles**

The Credit Union Regulatory Improvements Act of 2005 (H.R. 2317) was introduced on May 12, 2005. The legislation had 109 co-sponsors by February 28, 2006. The following is an overview of the bill's three titles.

### **Title I — Capital Reform**

This title reforms the prompt corrective action (PCA) system for federally insured credit unions.<sup>4</sup> After six years of experience with this congressionally mandated system, the NCUA is seeking adjustments that provide supervisory flexibility and incorporate a more risk-based approach. The objective of PCA is to minimize the probability of credit union insolvency through early intervention by the federal regulator. PCA establishes a net worth ratio framework that requires progressively more stringent mandatory and discretionary regulatory actions for credit unions with low or declining net worth levels. (Net worth is all of the credit union's retained earnings.<sup>5</sup>)

CURIA would provide more flexibility to the current statutory requirements of the PCA system. The bill would reduce the standard net worth ratio requirement for credit unions to a level comparable to what is required of institutions insured by the Federal Deposit Insurance Corporation. The proposal includes a more risk-based approach to credit union capital standards. The legislation modifies the requirements for net worth restoration plans imposed by the NCUA. In addition, the statutory definition of net worth would be amended to address a potential problem raised by new merger guidance issued by the Financial Accounting Standards Board.

### **Title II — Economic Growth**

This title amends the authority of federal credit unions to make member business loans. Many of the financial services provided by credit unions are similar to those offered by banks and thrifts, but credit unions are distinguishable because of their cooperative framework and unique charter requirements. Individual credit unions are owned by their membership. Credit unions can make loans only to their members, to other credit unions, and to credit union organizations. This title would enhance credit union member service and help to maintain credit union competitiveness by making adjustments to the statutory restrictions on member business loans.

Currently the aggregate limit on a credit union's net member business loan balances is the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total

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<sup>4</sup> PCA standards were mandated by P.L. 105-219 (12 U.S.C. 1790d).

<sup>5</sup> Retained earnings normally includes undivided earnings, regular reserves and any other appropriations of undivided earnings designated by management or regulatory authorities.

assets. CURIA would replace this limitation with a flat rate of 20% of the total assets of a credit union. In addition, the legislation would exclude loans or loan participations to nonprofit religious organizations from the member business loan limit. The definition of a member business loan now excludes loan(s) that are equal to or less than \$50,000. CURIA would amend the definition to exclude loans of \$100,000 or less.

Provisions of this title would also enhance the ability of credit unions to assist the economic revitalization efforts of distressed communities. It would give a credit union operating in an underserved community more flexibility in regards to the leasing of space in a building or property in which the credit union maintains a physical presence. Currently, credit unions may lease space only if they have plans to take over the entire property.

### **Title III — Regulatory Modernization**

The provisions of this title are very similar to the legislation passed by the House in 2004 (H.R. 1375, 108<sup>th</sup> Congress). An overview of each of the 12 sections is provided below.

#### **Section 301. Leases of Land on Federal Facilities for Credit Unions**

This section would give authorities in charge of buildings erected on federal property the discretion to extend real estate leases at minimal charge to credit unions that finance the construction of credit union facilities on the federal land.

#### **Section 302. Investments in Securities by Federal Credit Unions**

The investment authority of federal credit unions is limited by statute to loans, government securities, deposits in other financial institutions, and certain other limited investments. This may place them at a competitive disadvantage with state-chartered credit unions and other depository financial institutions. This section would expand the investment options by permitting a federal credit union to purchase for its own account certain investment securities of a defined investment grade. The total amount of the investment securities of any one obligor or maker could not exceed 10% of an institution's net worth.

#### **Section 303. Increase in General 12-Year Limitation of Term of Federal Credit Union Loans to 15 Years**

Federal credit unions are authorized to make loans to members, other credit unions, and to credit union organizations. Loans are restricted by a statutory 12-year maturity limit with a few exceptions. This section would increase that maturity limit to 15 years, or to longer terms if permitted by the NCUA.

#### **Section 304. Increase in 1% Investment Limit in Credit Union Service Organizations**

Organizations that provide services to credit unions and credit union members are commonly known as credit union service organizations (CUSOs). An individual federal

credit union is authorized to invest in aggregate up to 1% of its shares<sup>6</sup> and undivided earnings in CUSOs. This section would raise the limit to 3%.

**Section 305. Check Cashing and Money Transfer Services Offered Within the Field of Membership<sup>7</sup>**

Federal credit unions are authorized to provide check cashing and money transfer services to their members. In an effort to meet the needs of individuals who are not account holders at mainstream depository financial institutions, this section would allow federal credit unions to provide these services to anyone eligible to become a member.

**Section 306. Voluntary Mergers Involving Multiple Common Bond<sup>8</sup> Credit Unions**

The groups forming a multiple common bond charter are restricted to 3,000 members under most circumstances. This numerical limitation has been a concern in voluntary mergers of multiple common bond credit unions. The National Credit Union Administration (NCUA) has required member groups resulting from the merger that are larger than 3,000 to spin off and form separate credit unions. This section would provide that this numerical limitation does not apply in voluntary mergers.

**Section 307. Conversions Involving Common Bond Credit Unions**

This section addresses voluntary mergers or conversions involving a single or multiple common bond credit union and a community credit union. (Credit union charters are granted by federal or state governments on the basis of a “common bond.” This requirement determines the field of membership, and is unique among depository financial institutions. The common bond for establishing a credit union might be occupational, associational, or community. There are three types of federal credit union charters: single common bond (occupational and associational), multiple common bond (more than one group each having a common bond of occupation or association), and community.) Community charters are required to be based on a single, geographically well-defined local community neighborhood, or rural district. This section would require the NCUA to establish the criteria to use to determine that a member group or other portion of a credit union’s existing membership, located outside the community base, can be satisfactorily served and remain within the newly constituted credit union’s field of membership.

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<sup>6</sup> Individual credit unions are owned by their membership. Members’ savings are referred to as shares and earn dividends instead of interest.

<sup>7</sup> For more information on section 305 (which is also separate legislation, H.R. 749), please see CRS Report RS22146, *Expanded Access to Financial Services Act*, by Pauline Smale.

<sup>8</sup> Credit union charters are granted by federal or state governments on the basis of a “common bond.” This requirement determines the field of membership, and is unique among depository financial institutions. The common bond for establishing a credit union might be occupational, associational, or community. There are three types of federal credit union charters: single common bond (occupational and associational), multiple common bond (more than one group each having a common bond of occupation or association), and community.

**Section 308. Credit Union Governance**

This section deals with three separate issues. It provides for the expulsion of a federal credit union member for a good cause<sup>9</sup> by a majority vote of the institution's board of directors. Currently, a two-thirds vote of the membership is required. It would give institutions the authority to limit the number of consecutive terms an individual could serve on the board of directors in an effort to encourage broader representation on the board. Finally, federal credit unions would be able to reimburse volunteer board members for wages they would otherwise forfeit by participating in credit union affairs.

**Section 309. Providing the National Credit Union Administration with Greater Flexibility in Responding to Market Conditions**

The rate of interest on loans made by a federal credit union may not exceed 15% under most circumstances. This section would permit the NCUA to consider whether rising interest rates or the prevailing interest rate levels threaten the safety and soundness of individual institutions when the agency debates lifting the usury ceiling.

**Section 310. Credit Union Conversion Voting Requirements**

This section deals with the process a credit union follows when it undertakes a charter conversion to become a mutual savings bank. The NCUA has expressed concern that the membership of the credit union needs to fully understand the effect a conversion may have and therefore the importance of the membership's vote on conversion. This section would require a majority vote of at least 20% of the membership to approve a conversion. Currently, the membership must approve the proposal to convert by the affirmative vote of a majority of those members who vote on the proposal.

**Section 311. Exemption from Pre-Merger Notification Requirement of the Clayton Act**

This section would give all federally insured credit unions the same exemption as banks and thrift institutions 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 would provide federally insured credit unions exceptions, similar to those provided banks, from broker-dealer and investment adviser registration requirements.

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<sup>9</sup> An example of good cause, provided by a credit union spokesman, is a member who is disruptive to the operations of the credit union, including harassing personnel and creating safety concerns.