Calendar No. 384

105TH CONGRESS 2d Session } SENATE { REPORT 105–193

CREDIT UNION MEMBERSHIP ACCESS ACT

MAY 21, 1998.—Ordered to be printed

Mr. D'AMATO, from the Committee on Banking, Housing, and Urban Affairs, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany H.R. 1151]

The Committee on Banking, Housing, and Urban Affairs, to which was referred the bill (H.R. 1151), having considered the same, reports favorably thereon with an amendment and recommends that the bill as amended do pass.

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INTRODUCTION

On April 30, 1998, the Senate Committee on Banking, Housing, and Urban Affairs (the "Committee") marked up and ordered to be reported a committee substitute for H.R. 1151, the "Credit Union Membership Access Act," a bill to amend the Federal Credit Union Act to clarify existing law with regard to the field of membership of Federal credit unions, to preserve the integrity and purpose of

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Federal credit unions, to enhance supervisory oversight of federally insured credit unions, and for other purposes. The Committee reports the bill favorably with an amendment in the nature of a substitute, and recommends that the bill as amended do pass.

HISTORY OF THE LEGISLATION

On April 20, 1998, H.R. 1151, the "Credit Union Membership Access Act" was referred to the Committee after passage in the House of Representatives on April 1, 1998 by a vote of 411 to 8. The Committee held two hearings on the impact of the Supreme Court decision of February 25, 1998, *National Credit Union Administration* v. *First National Bank & Trust Co. et al.,* 118 S. Ct. 927 (1998), on federal credit unions. At the first hearing, on March 26, 1998 the Committee received testimony from John D. Hawke, Under Secretary for Domestic Finance at the Department of Treasury and Richard S. Carnell, Assistant Secretary for Financial Institutions at the Department of Treasury; Norman E. D'Amours, Chairman, Yolanda Townsend Wheat and Dennis Dollar, Board Members of the National Credit Union Administration ("NCUA"); and Bruce O. Jolly, Esquire, of Shook, Hardy & Bacon in Washington, D.C.

At the second hearing, on April 2, 1998, the Committee received testimony from Congressman Steven C. LaTourette and Congressman Paul E. Kanjorski; Michael S. Vadala who testified on behalf of National Association of Federal Credit Unions, Peggy Lents who testified on behalf of Credit Union National Association, Reid K. Pollard who testified on behalf of Independent Bankers Association of America, Neil Mahoney who testified on behalf of America's Community Bankers, and R. Scott Jones who testified on behalf of American Bankers Association.

On April 30, 1998, the Committee met in Executive Session to markup H.R. 1151. The Committee considered and adopted, without objection, an amendment in the nature of a substitute that was offered by Chairman D'Amato and Ranking Member Sarbanes that incorporated amendments by other Committee members. During the markup, the Committee adopted, by voice vote, an amendment concerning the conversion of insured credit unions to mutual savings banks or savings associations, offered by Senator Shelby for himself and Senator Bennett. Senator Gramm offered an amendment to strike Section 204 of Title II, the section of the bill requiring NCUA to periodically assess the record of credit unions in providing affordable credit union services to all individuals of modest means (including low- and moderate-income individuals) within the credit union's field of membership. Senator Shelby then offered a second degree amendment to the amendment offered by Senator Gramm. Senator Shelby's amendment would have exempted small banks from Community Reinvestment Act requirements. The second degree amendment failed by a vote of 9 to 9. Senators D'Amato, Sarbanes, Dodd, Kerry, Bryan, Boxer, Moseley-Braun, Johnson and Reed voted against the amendment. Senators Gramm, Shelby, Mack, Faircloth, Bennett, Grams, Allard, Enzi, and Hagel voted in favor of the amendment. Senator Gramm then withdrew his amendment.

The Committee then voted 16–2 to report H.R. 1151 to the Senate for consideration. Senators Mack and Hagel voted against the motion to report the bill from the Committee.

PURPOSE AND SUMMARY OF LEGISLATION

The purpose of H.R. 1151, the Credit Union Membership Access Act, as reported from the Committee, is to amend existing law with regard to the field of membership of federal credit unions, to preserve the integrity and purpose of federal credit unions and to enhance supervisory oversight of federally insured credit unions.

Credit unions are the only federally insured depository institutions not currently subject to capital requirements and a system of prompt corrective action. H.R. 1151 incorporates recommendations from the Treasury Department's 1997 study of credit unions and establishes capital standards and a system of prompt corrective action for federally insured credit unions that takes into account that credit unions are not-for-profit, member owned cooperatives that do not issue capital stock and must rely on retained earnings to build net worth. The bill significantly strengthens the prudential safeguards applicable to federally insured credit unions and makes the credit union system safer, sounder and more resilient.

SUMMARY OF LEGISLATION

TITLE I

Title I of the bill establishes three distinct types of common bond membership field categories for federal credit unions: single common-bond, multiple common-bond, and community credit unions. For multiple common-bond credit unions, each separate group must have its own common bond of occupation or association and less than 3,000 members at the time the group joins an existing credit union. The NCUA Board ("Board") shall encourage the formation of a separately chartered credit union instead of approving an additional group within the field of membership of an existing multiple common-bond or single common-bond credit union. Before a credit union adds a new group to its field of membership, the Board must determine in writing that the credit union meets specific criteria. If NCUA determines that the formation of a separate credit union is not practicable or consistent with the criteria, the NCUA is required to include the group in the field of membership of a credit union in reasonable proximity to the group where practicable and consistent with safety and soundness.

For multiple common-bond credit unions, there are exceptions to the numerical limit for including additional groups within the field of membership. Groups with 3,000 or more members are eligible to join an existing credit union if the NCUA determines in writing in accordance with guidelines and regulations required by the bill that the group would not be financially viable and is unlikely to succeed as a new single common-bond credit union. Another exception involves transactions for supervisory reasons.

Title I contains a grandfather provision for all persons and organizations who could be forced out of credit unions as a result of the February 25, 1998 Supreme Court decision. The title grandfathers all current members as well as current groups contained within the field of membership of a federal credit union as of the date of enactment of this legislation. The grandfather provision also permits such groups to continue adding new members. In addition, persons or organizations located in an area underserved by financial institutions may be included in the field of membership of a multiple common-bond credit union which will establish and maintain an office or facility in that underserved area.

This Title also addresses membership eligibility for family or household members. The section provides that membership in federal credit unions based on relationship shall be limited to individuals who are members of the "immediate family or household" of eligible members. The NCUA is directed to define these terms by regulation.

Title I provides that once a person becomes a member of a credit union, that person may remain a member until the person chooses to withdraw from the membership of the credit union.

Title I also includes a requirement that NCUA, by regulation, establish a definition for the term "well defined local community, neighborhood, or rural district" that will apply to applications to form a new credit union or alter or expand the field of membership of an existing community credit union.

TITLE II

Title II provides that the accounting principles used for reports or statements of insured credit unions required to be filed with the NCUA are to be uniform and consistent with generally accepted accounting principles. Insured credit unions with less than $10 million in total assets are exempt from this requirement unless otherwise directed by the NCUA or a State credit union supervisor. Credit unions with $500 million or more in total assets must obtain annual audits performed in accordance with generally accepted auditing standards by an independent certified public accountant or public accountant licensed by the appropriate State or jurisdiction. If a credit union with assets of more than $10 million, but less than $500 million, elects to conduct an audit using an independent auditor who is compensated, the audit must be performed in a manner that is consistent with the accountancy laws of the appropriate State or jurisdiction, including licensing requirements.

Title II provides that insured credit unions may convert to a mutual savings bank or mutual savings association without the prior approval of the NCUA. Credit unions that propose to convert to a mutual savings bank or mutual savings association must submit notices to each member eligible to vote at 90, 60, and 30 days before the member vote on conversion. Approval of the proposed conversion requires the affirmative vote of a majority of the members who vote on the proposal. The vote on a conversion proposal is administered by the NCUA and verified by the Federal or State regulatory agency that would have jurisdiction after the conversion. If either the NCUA or the other regulatory agency disapproves of the voting methods or procedures, the vote must be re-taken. In addition, the title limits the compensation of directors and senior management officials of converted credit unions to director's fees and compensation and other benefits paid in the ordinary course of business in connection with the conversion from a credit union to a mutual savings bank or mutual savings association.

Title II places, for the first time, significant restrictions on member business loans of federally insured credit unions. The total amount of outstanding member business loans of an insured credit union cannot exceed the lesser of 1.75 times the minimum net worth required for a well capitalized credit union (7 percent net worth ratio), or 1.75 times the actual net worth of the credit union. Insured credit unions that have a total amount of outstanding member business loans exceeding the limit on the date of enactment, are required to come into compliance with these restrictions within three years. This title provides exceptions for insured credit unions that are chartered for, or that have a history of primarily making member business loans to their members, such as members who are of a specialized vocation, for example: fishermen, farmers, truck drivers and taxi cab drivers. Credit unions that serve predominantly low income members or that are community development financial institutions are exempted. In addition, member business loan exemptions are codified as they appear in NCUA regulations currently in effect, including loans totaling $50,000 or less to any one borrower or associated member. Credit unions that exceed the member business loan limit are given three years to come into compliance with these limits.

Title II reaffirms that insured credit unions have a continuing obligation to meet the financial services needs of persons of modest means, including low- and moderate-income individuals. The NCUA is required to review each credit union's record of meeting the financial service needs of its entire field of membership. Title II establishes new appointment criteria for NCUA Board membership.

TITLE III

Title III establishes a new system of prompt corrective action and capital requirements for insured credit unions and requires an alternative prompt corrective action system for new credit unions. The section defines five net worth categories and allows for adjusting net worth levels if Federal banking agencies increase or decrease required minimum levels for other institutions. The section also prescribes net worth retention requirements and net worth restoration plans. The section repeals section 116 of the Federal Credit Union Act.

The section requires the NCUA to take prompt corrective action to resolve the problems of insured credit unions. The NCUA is required to report to Congress on the implementation of regulations for prompt corrective action and how the regulations differ from section 38 of the Federal Deposit Insurance Act and the reasons for these differences.

Title III prohibits credit unions that become undercapitalized from making new commercial loans that would result in an increase of the total amount of member business loans outstanding at that credit union. The prohibition remains in effect until the credit union becomes adequately capitalized.

Title III also affects the reporting of and calculation of the National Credit Union Share Insurance Fund equity ratio, available assets ratio, and standby premium charge.

TITLE IV

Title IV requires a study and report on differing regulatory treatment between credit unions and other federally insured depository institutions, including a review of the potential effect of applying Federal tax laws to credit unions. Title IV also requires review and report of regulations and policies to reduce unnecessary costs and the paperwork burden for insured depository institutions. The title also requires a report with recommendations to reduce and simplify the tax burden for small banks.

SECTION-BY-SECTION ANALYSIS

Section 1. Short title

Section 1 designates the act as the "Credit Union Membership Act" (the Act).

Section 2. Findings

Section 2 lists five Congressional findings related to the credit union movement and its beginning, the public purposes of credit unions, and the importance of the common bond requirement. The section also addresses findings regarding the nature of credit unions and their tax exempt status as well as the need for improved safety and soundness.

TITLE I—CREDIT UNION MEMBERSHIP

Section 101. Fields of membership

Section 101 provides that the membership of federal credit unions shall be limited to the three following categories: single common-bond, multiple common-bond, and community credit unions. Single common-bond credit unions shall consist of one group that has a single common bond of occupation or association. Multiple common-bond credit unions shall consist of more than one group, each of which has (within such group) a common bond of occupation or association, and the number of members of which does not exceed 3,000 persons at the time the group is included in the field of membership of the credit union. The 3,000 person limitation applies only to the size of the group at the time of their inclusion within the field of membership of a credit union. The limit is not intended to restrict the growth of such groups after they are added to the credit union. Multiple common bonds are designated as such in response to the Supreme Court's February 25, 1998 decision on the common bond issue in *National Credit Union Administration* v. *First National Bank & Trust Co., et al.,* 118 S. Ct. 927 (1998).

The Committee has determined that it is appropriate to amend existing law and specifically authorize multiple common bond federal credit unions, subject to additional group size and geographical expansion limits. The current law regarding community credit unions is modified by providing that these institutions shall consist of persons or organizations within a well-defined *local* community, neighborhood, or rural district.

This section also grandfathers all persons or organizations who are members of Federal credit unions on the date of enactment of the Act. Furthermore, any individual member of a group that is part of a credit union shall continue to be eligible to become a member of that credit union and any new member of such group is also eligible. The successor to any particular organization or business entity that belongs to a credit union shall be allowed to continue its membership.

An additional exception exists for persons or organizations within a local community, neighborhood or rural district that is underserved by other depository institutions. These persons or organizations may join an existing credit union provided that the credit union establishes a service facility in that area. The term "facility" is meant as it is defined by the NCUA. An automatic teller machine or similar device does not qualify as a service facility.

The 3,000 member limitation is intended as the maximum size of an additional group that can be eligible to be included within an existing credit union, unless a specified exemption applies. The NCUA may permit groups with over 3,000 members to join an existing credit union after the Board determines in writing that the group lacks sufficient financial resources, volunteers or operational capacity to establish and operate a new single common-bond credit union, or if the group would be unlikely to operate a safe and sound credit union. The Board may merge or consolidate a group with over 3,000 members into another credit union for supervisory reasons. In addition, a narrow exception applies to any group transferred in connection with a voluntary merger which was approved by the NCUA prior to October 25, 1996.

The 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 creation of a separately chartered credit union, or the continued operation of an existing credit union presents safety and soundness concerns.

This section also provides that membership eligibility is extended only to individuals who are members of an "immediate family or household" of a credit union member. The NCUA is directed to define these terms by regulation. Until the regulation becomes effective, the current NCUA policy with respect to immediate family members will remain in effect. In addition, once a member joins a credit union, that person or organization may remain a member until they choose to withdraw, unless credit unions use provisions in current law to remove them.

Section 102. Criteria for approval of expansion of membership of multiple common-bond credit unions

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.

Section 102 requires multiple common-bond credit unions and single common-bond credit unions to apply to NCUA each time they choose to add a new group to their field of membership. The NCUA must determine in writing that specific approval criteria have been met. Specifically, the NCUA must find that a multiple common-bond credit union has not engaged in any unsafe or unsound practice that is material for a year before applying to add the new group; the credit union is adequately capitalized; the credit union has the administrative capability and financial resources to serve the new group; the credit union has been evaluated as satisfactorily providing affordable services to all individuals of modest means within its field of membership; and that the probable beneficial effect of the expansion clearly outweighs in the public interest, any potential harm to other insured credit unions. Credit unions seeking to add new groups must also meet any other requirements prescribed by the Board by regulation.

Section 103. Geographical guidelines for community credit unions

Section 103 requires the Board to define by regulation the criteria it will use in determining the meaning of the term "well-defined local community, neighborhood, or rural district" for purposes of evaluating charter applications by community credit unions. The term shall only apply to applications for new credit unions and applications to alter the membership of existing credit unions submitted after the date of enactment.

TITLE II—REGULATION OF CREDIT UNIONS

Section 201. Financial statement and audit requirements

Section 201 provides that accounting principles applicable to reports or statements required to be filed with the Board shall be uniform and consistent with generally accepted accounting principles, unless the Board determines that such application is not appropriate, in which case the Board may prescribe principles that are no less stringent than generally accepted accounting principles. Credit unions with assets below $10 million are exempt from this provision, unless the Board or an appropriate State supervisor prescribes otherwise. This section requires insured credit unions with $500 million or more in assets to have an annual independent audit of their financial statements performed in accordance with generally accepted accounting principles by an independent certified public accountant or public accountant licensed by the appropriate State or jurisdiction to perform such services. This section also requires that accountancy laws of the appropriate State or jurisdiction, including licensing requirements, are to be followed when any credit union with assets greater than $10 million and less than $500 million, chooses to conduct a voluntary audit for any purpose using an independent auditor who is compensated for his or her audit services.

Section 202. Conversion of insured credit unions

Section 202 authorizes the conversion of insured credit unions to mutual savings banks or mutual savings associations without the prior approval of the Board. The proposal for such conversion shall be first approved by a majority of the directors of the credit union who shall set a date for a vote by members of the credit union either at a meeting on that date or by written ballot. Approval of the proposal for conversion shall be by the affirmative vote of a majority of the members of the credit union who vote. The first notice of the proposal shall be given to each member who is eligible to vote, 90 days prior to the date of the vote on conversion. Additional notices must be given to each member eligible to vote, 60 days prior to the vote and again at 30 days prior to the vote. The Board may require an insured credit union that proposes to convert to a mutual savings bank or mutual savings association to submit a notice of its intent to convert during the 90 day period before the completion of the conversion. Upon completion of the conversion, the credit union will no longer be subject to any provisions of the Federal Credit Union Act. The vote on the conversion proposal by the members of the credit union shall be administered by the NCUA and verified by the Federal or State regulatory agency that would have jurisdiction over the institution after the conversion. If either the NCUA or that regulatory agency disapproves of the methods or procedures of the vote, it will be repeated.

Section 202 also limits the economic compensation of any director or senior management official of an insured credit union that converts to a mutual savings bank or mutual savings association to director fees and compensation and other benefits paid in the ordinary course of business in connection with the conversion from a credit union to a mutual savings bank or mutual savings association. The term “senior management official” is defined for purposes of this section and includes a chief executive officer, an assistant chief executive officer, a chief financial officer, and any other senior executive officer as defined by the appropriate Federal banking agency pursuant to section 32(f) of the Federal Deposit Insurance Act.

In addition, this section requires the NCUA to promulgate rules, within 6 months of enactment, applicable to charter conversions that are consistent with rules promulgated by other financial regulators including the Office of Thrift Supervision and the Office of the Comptroller of the Currency. The rules for charter conversions by insured credit unions must be no more or less restrictive than those rules that apply to charter conversions by other financial institutions. In the case of conversions after the enactment of this act, but prior to the promulgation of rules for this section by the NCUA, the Committee intends for the NCUA to evaluate and review such conversions in a manner consistent with the provisions of section 202.

Section 203. Limitation on member business loans

In new section 107A(a) the Committee has imposed substantial new restrictions on commercial business lending by insured credit unions. Those restrictions are intended to ensure that credit unions continue to fulfill their specified mission of meeting the credit and savings needs of consumers, especially persons of modest means, through an emphasis on consumer rather than business loans. The Committee action will prevent significant amounts of credit union resources from being allocated in the future to large commercial loans that may present additional safety and soundness concerns for credit unions, and that could potentially increase the risk of taxpayer losses through the National Credit Union Share Insurance Fund ("Fund").

The intent of the Committee in this section is to further clarify and define business lending by insured credit unions. While the Committee acknowledges that consumer loans make up nearly 99 percent of all credit union lending, the Committee appreciates the necessity to minimize additional risk to the safety and soundness of insured credit unions through the extensive growth of commercial lending activity. An exception was included to recognize the expertise developed in specialized credit unions, such as those that serve members of specific vocations, the religious community and members of the agricultural community.

Section 203 provides that no insured credit union may make any member business loan that would result in a total amount of such loans outstanding at that credit union at any one time that exceeds the lesser of (1) 1.75 times the actual net worth of the credit union, or (2) 1.75 times the minimum net worth required for a well capitalized credit union as described in new section 216(c)(1)(A) of title III. There are exceptions from the limit on member business loans for insured credit unions that are chartered for the purpose of, or that have a history of primarily making member business loans to members, as determined by the Board; or for insured credit unions that serve predominantly low-income members; or for credit unions that are community development financial institutions as defined in section 103 of the Community Development Banking and Financial Institutions Act of 1994.

The Committee intends for the Board to interpret the exceptions under new section 107A(b), to permit worthy projects access to affordable credit union financing. Loans for such purposes as agriculture, self-employment, small business establishment, large up-front investment or maintenance of equipment such as fishing or shrimp boats, taxi cab medallions, tractor trailers, or church construction should not be unduly constricted as a result of the Board's actions.

This section defines a member business loan as any loan, line of credit, or letter of credit the proceeds of which will be used for a commercial, corporate or other business investment property or venture, or agricultural purpose. The definition codifies current NCUA exceptions at 12 CFR 701.21.

In addition, section 203 defines the term "net worth" with respect to an insured credit union to be the credit union's retained earnings balance as determined under generally accepted accounting principles. With respect to insured credit unions that serve predominantly low-income members, in addition to the earnings balance, net worth includes secondary capital accounts that are uninsured and subordinate to all other claims against the credit union. The term "associated member" is defined by this section as any member having a shared ownership, investment, or other pecuniary interest in a business or commercial endeavor with the borrower. Section 203 also requires insured credit unions whose total member business loans exceed the permitted amount to come into compliance with these business loan restrictions within three years.

Section 204. Serving persons of modest means within the field of membership of credit unions

Section 204 reaffirms the continuing and affirmative obligation of insured credit unions to meet the financial services needs of persons of modest means, consistent with safe and sound operation. The section also requires the Board, after consultation with the State credit union supervisors, to prescribe criteria, within one year of the date of enactment, for periodically reviewing the record of each insured credit union in providing affordable credit union services to all individuals of modest means, including those with low- and moderate-incomes, within the field of membership of such credit union, and to make the results of such review publicly available.

This section also requires the NCUA to prescribe additional criteria for annually evaluating the record of any insured credit union organized to serve a well defined local community, neighborhood, or rural district in meeting the credit needs and credit union service needs of its entire field of membership. The Board shall also prescribe procedures for remedying the failure of any community credit union to meet the credit needs of its entire field of membership. Such remedies would include the disapproval of any application by such credit union to expand its field of membership.

The NCUA, in evaluating insured credit unions under this section, shall focus on the actual performance of such credit union and not impose burdensome paperwork or record keeping requirements. In its annual report to Congress for the first five years following enactment the NCUA Board shall include a report on the progress of implementing this section.

Section 205. National Credit Union Administration Board membership

Section 205 establishes new criteria for membership and appointment of the NCUA Board. The section directs the President, in appointing members to the Board, to consider individuals who are especially qualified to serve on the Board, by virtue of their education, training, or experience relating to a broad range of financial services, financial services regulation, or financial policy. Not more than one member of the Board may be appointed to the Board from among individuals who, at the time of such appointment, are, or have recently been, involved with any insured credit union as a committee member, director, officer, employee, or other institution-affiliated party.

Section 206. Report and review requirement for certain regulations

Section 206 provides that any regulation prescribed by the Board to define or amend the definition of "immediate family or household" and to define or amend the definition of "well-defined local community, neighborhood, or rural district" shall be treated as a major rule for purposes of chapter 8 of title 5 of the U.S. Code.

TITLE III—CAPITALIZATION AND NET WORTH OF CREDIT UNIONS

Section 301. Prompt and corrective action

This section adds a new section 216 to the Federal Credit Union Act, establishing a system of prompt corrective action for federally insured credit unions. Under this system, as a credit union's net worth declines below minimum requirements, the credit union faces progressively more stringent safeguards. The goal is to resolve net worth deficiencies promptly, before they become more serious, and in any event before they cause losses to the National Credit Union Share Insurance Fund ("Fund'). New section 216 is intended to ensure that federally insured credit unions and the NCUA have incentives compatible with the interests of the Fund. It also sets forth the NCUA's duty to take prompt corrective action to resolve the problems of federally insured credit unions to avoid or minimize loss to the Fund.

New section 216 is modeled on section 38 of the Federal Deposit Insurance Act, which has applied to all FDIC-insured depository institutions since 1992. (12 U.S.C. §1831o.) New section 216 is specifically tailored to credit unions as not-for-profit, member-owned cooperatives.

New section 216(b) of the bill requires the NCUA to prescribe, by regulation, a system of prompt corrective action for federally insured credit unions that is consistent with the specific restrictions and requirements of new section 216 and comparable to section 38 of the Federal Deposit Insurance Act. "Comparable" here means parallel in substance (though not necessarily identical in detail) and equivalent in rigor. The NCUA must design the system of prompt corrective action to take into account that credit unions are not-for-profit cooperatives that (1) do not issue capital stock, (2) must rely on retained earnings to build net worth, and (3) have boards of directors that consist primarily of volunteers.

New section 216(b)(2) requires the NCUA to prescribe, by regulation, a system of prompt corrective action for new credit unions, which shall apply in lieu of the system applicable to federally insured credit unions generally. This alternative system of prompt corrective action must (1) carry out the purpose of section 216; (2) recognize that credit unions (as cooperatives that do not issue capital stock) initially have no net worth, and give new credit unions reasonable time to accumulate net worth; (3) create adequate incentives for new credit unions to become adequately capitalized by the time that they reach the age or asset size at which the regular prompt corrective action system becomes applicable; (4) impose appropriate restrictions and requirements on new credit unions that do not make sufficient progress towards becoming adequately capitalized; and (5) prevent evasion of the purpose of this section (such as would occur, for example, if a long-established credit union sought to avoid this section by merging with a smaller new credit union and then calling itself a new credit union).

This section classifies federally insured credit unions into one or more of five categories, based on their net worth. These categories are—well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized.

This section provides that for a credit union to be "well capitalized," it must have a net worth ratio of at least 7 percent. To be "adequately capitalized," a credit union must have a net worth ratio of at least 6 percent. In addition, in order to be well capitalized or adequately capitalized, a complex credit union must meet any applicable risk-based net worth requirement prescribed in this section.

A credit union with less than 6 percent net worth is "undercapitalized." In addition, a complex credit union is undercapitalized if it fails to meet any applicable risk-based net worth requirement.

A credit union is "significantly undercapitalized" if it has a net worth ratio of less than 4 percent. A credit union is also "significantly undercapitalized" if it has a net worth ratio of less than 5 percent and it (1) fails to submit an acceptable net worth restoration plan within the time allowed under section 216(f), or (2) materially fails to implement a plan accepted by the NCUA.

A credit union is "critically undercapitalized" if it has less than 2 percent net worth (or such higher level, not exceeding 3 percent, as the NCUA may prescribe by regulation).

These net worth categories overlap to some degree, as they do under section 38(b)(1) of the Federal Deposit Insurance Act. A significantly undercapitalized or critically undercapitalized credit union is also, by definition, undercapitalized (in that it has less than 6 percent net worth). A critically undercapitalized credit union is also significantly undercapitalized (in that it has less than 4 percent net worth). Accordingly, the rules for undercapitalized credit unions also apply to a significantly undercapitalized or critically undercapitalized credit union, and the rules for significantly undercapitalized credit unions also apply to a critically undercapitalized credit union.

The NCUA has some discretion to adjust the relevant net worth ratios for the four net worth categories in light of changes in the capital standards applicable to FDIC-insured depository institutions. Section 38(c) of the Federal Deposit Insurance Act requires all such institutions to meet two capital standards: a leverage limit, which the federal banking agencies have set at 4 percent of total assets; and a risk-based capital requirement, which the agencies have set at 8 percent of risk-adjusted assets. If the federal banking agencies increase or decrease the required minimum level for the leverage limit, the NCUA may, if two conditions are satisfied, correspondingly increase or decrease the net worth ratios for a credit union to be well capitalized, adequately capitalized, undercapitalized, or significantly undercapitalized. To make such an adjustment, the NCUA must first determine, in consultation with the federal banking agencies, that the reason why the banking agencies increased or decreased in the required minimum level for the leverage limit also justifies the proposed adjustment in net worth ratios for credit unions. The NCUA must also determine that the resulting net worth ratios for credit unions are sufficient to carry out the purpose of new section 216. The adjustment in a net worth ratio cannot exceed the difference between 4 percent of total assets (the current required minimum level for the leverage limit) and the required minimum level most recently established by the federal banking agencies. Thus, for example, if the federal banking agencies were to decrease the required minimum level for the leverage limit to 3.5 percent, the NCUA could (if the two conditions were satisfied) decrease any or all of the 7, 6, 5, and 4 percent net worth ratios by 0.5 percentage point (4.0 percent minus 3.5 percent). Likewise, if the federal banking agencies were to increase the required minimum level to 4.4 percent, the NCUA could (if the two conditions were satisfied) increase the 7, 6, 5, and 4 percent net worth ratios by 0.4 percentage point (4.4 percent minus 4.0 percent). If the NCUA increases any net worth ratio for credit unions, it must give credit unions reasonable time to meet the increased ratio.

New section 216(d) requires the NCUA, by regulation, to prescribe a risk-based net worth requirement for federally insured credit unions that are complex, as defined by the NCUA. For purposes of section 216(d), "complex" refers to credit unions' portfolios of assets and liabilities; it does not involve credit unions' field of membership. The NCUA must design the risk-based net worth requirement to take into account any material risks against which the 6 percent net worth ratio required for an insured credit union to be adequately capitalized may not provide adequate protection. Thus the NCUA should, for example, consider whether the 6 percent requirement provides adequate protection against interest-rate risk and other market risks, credit risk, and the risks posed by contingent liabilities, as well as other relevant risks. The design of the risk-based net worth requirement should reflect a reasoned judgment about the actual risks involved.

Other provisions of section 301 are intended to encourage the NCUA, in designing the risk-based capital requirement, to seek and receive broad input—to help assure that the requirement is workable, fair, and effective. Section 301(d)(2)(A) requires the NCUA Board to publish an advance notice of proposed rulemaking not later than 180 days after the date of enactment. Section 301(c) requires the Board to consult with the Secretary of the Treasury, the federal banking agencies, and state credit union supervisors. Although section 301 does not set a deadline for publishing in the Federal Register proposed regulations implementing the risk-based net worth requirement, it nonetheless contemplates that the Board would publish such regulations for public comment, as required by the Administrative Procedure Act. 5 U.S.C. §552(a). Section 301(d)(2)(B) gives the Board a full two years to promulgate final regulations for risk-based capital requirement—six months longer than under section 216 generally. And to accommodate the extended rulemaking process, section 301(e)(2) provides for the effective date of the risk-based capital requirement to be January 1, 2001.

New section 216(e)(1) requires a federally insured credit union that is not well capitalized, (i.e., is adequately capitalized, undercapitalized, significantly undercapitalized, or critically under-capitalized) to set aside as net worth a certain percentage of its annual gross income. The amount to be set aside annually shall equal not less than 0.4 percent of a credit union's total assets. This earnings-retention requirement is the only prompt corrective action rule applicable to credit unions that are adequately capitalized, but not well capitalized. This subsection replaces the earnings-retention requirement now in section 116 of the Federal Credit Union Act (12 U.S.C. §1762), and section 301(g) of the bill repeals section 116.

Under new section 216(e)(2), the NCUA may, case by case, decrease the 0.4 percent requirement if the facts justify two determinations by the NCUA. First, the NCUA must determine that the decrease in the requirement is necessary to avoid curtailing a credit union's dividends to such a degree that the credit union would suffer a significant redemption of shares. And second, the NCUA must determine that the decrease would further the purpose of new section 216. The NCUA may not decrease the requirement below zero, and must periodically review any decrease that is in effect.

Furthermore, new section 216(f) requires an insured credit union that becomes undercapitalized to submit a timely and acceptable net worth restoration plan to the NCUA. The section requires the credit union to confront its problems in a timely manner, and to develop and submit an acceptable net worth restoration plan for remedial action. The NCUA's staff must, upon timely request by an insured credit union with total assets of less than $10 million, assist the credit union in preparing a net worth restoration plan.

The NCUA must, by regulation, establish deadlines that give insured credit unions reasonable time to submit net worth restoration plans and that require the NCUA to act on net worth restoration plans expeditiously. If a credit union fails to submit a net worth restoration plan within the time allowed, the NCUA must promptly notify the credit union of that failure, and give the credit union a reasonable opportunity to submit a plan.

If a credit union submits a timely plan but the NCUA determines that the plan is not acceptable, the NCUA must promptly notify the credit union of why the plan is not acceptable, and give the credit union a reasonable opportunity to submit a revised plan. The NCUA may accept a credit union's net worth restoration plan only if the NCUA determines that the plan is based on realistic assumptions and is likely to succeed in restoring the credit union's net worth.

New section 216(g) provides that an undercapitalized federally insured credit union shall not generally permit its average total assets to increase unless (1) the NCUA has accepted the credit union's net worth restoration plan; (2) any increase in total assets is consistent with the plan; and (3) the credit union's net worth ratio increases at a rate consistent with the plan. The term "generally" allows the NCUA to make carefully delineated exceptions to the asset-growth restrictions if the exceptions are consistent with the purpose of new section 216. The requirement that the credit union's net worth ratio increase at a rate consistent with the plan is intended to help assure that growth strengthens the credit union rather than exacerbates its problems.

In addition, an undercapitalized federally insured credit union is prohibited in this section from making new commercial loans that would result in a increase in the total amount of member business loans outstanding at that credit union. The prohibition remains in effect until the credit union becomes adequately capitalized.

Because book-value net worth is a lagging indicator of problems, section 38(g) of the Federal Deposit Insurance Act (in tandem with section 8(b)(8) of that Act) permits the appropriate federal banking agency, under certain circumstances, to treat an FDIC-insured depository institution as if it were in the next lower net worth category (or, if the institution is well capitalized, to reclassify it as adequately capitalized). The agency may take such action if the depository institution, when most recently examined, received an unsatisfactory rating for any of the noncapital components of its examination rating and has not corrected the deficiency.

New section 216(h) imposes two restrictions on the NCUA's exercise of authority under regulations comparable to section 38(g) of the Federal Deposit Insurance Act. First, the NCUA cannot treat a credit union as if it were in a lower net worth category (or reclassify a credit union into a lower net worth category) for reasons not pertaining to the safety and soundness of that credit union. Second, the NCUA cannot delegate its authority to treat a credit union as if it were in a lower net worth category (or reclassify the credit union into such a category).

New section 216(i) requires the NCUA, within 90 days after a federally insured credit union becomes critically undercapitalized, to either (1) appoint a conservator or liquidating agent for the credit union; or (2) take such other action as the NCUA determines would better achieve the purpose of section 216, after documenting why the action would better achieve that purpose. A determination to take alternative action expires after 180 days, and the NCUA must then renew the determination or appoint a conservator or liquidating agent.

The NCUA must generally appoint a liquidating agent for a credit union that remains critically undercapitalized on average during the calendar quarter beginning 18 months after the credit union became critically undercapitalized, unless the Board determines that the credit union (a) has substantially complied with an approved net worth restoration plan requiring consistent improvement in the credit union's net worth, and (b) has positive net income or an upward trend in earnings that the NCUA projects as sustainable; and the Board certifies that the critically undercapitalized credit union is viable and not expected to fail.

The NCUA Board generally cannot delegate its authority under new section 216(i). But in the case of credit unions that have less than $5 million in total assets, the Board may delegate such authority if the Board permits the credit union to appeal any adverse action to the Board.

Under section 38(k) of the Federal Deposit Insurance Act, if an FDIC-insured depository institution causes a material loss to the deposit insurance fund, the appropriate federal banking agency's inspector general must review the agency's supervision of the institution and make a written report to the agency. For purposes of determining whether the Fund has incurred a material loss with respect to a federally insured credit union—such that the inspector general of the NCUA must make a report—a loss is material if it exceeds the sum of $10 million and an amount equal to 10 percent of the credit union's total assets at the time the NCUA initiated assistance under section 208 of the Federal Credit Union Act or was appointed liquidating agent.

New section 216(k) specifies that material supervisory determinations made under section 216 (including decisions to require prompt corrective action) made by NCUA officials other than the Board may be appealed to the Board pursuant to the independent internal appellate process required under section 309 of the Riegle Community Development and Regulatory Improvement Act of 1994 (or, if the Board so specifies, pursuant to separate procedures specified by regulation).

Under new section 216(l), the NCUA must consult and seek to work cooperatively with state credit union supervisors. In addition, when evaluating any net worth restoration plan submitted by a state-chartered, federally insured credit union, the NCUA must seek the views of the state credit union supervisor.

As the NCUA Board decides whether to appoint a conservator or liquidating agent for a state-chartered, federally insured credit union, several specific restrictions and requirements apply. The Board must seek the views of the state credit union supervisor, and give the supervisor an opportunity to take the proposed action. The Board must, upon timely request by the supervisor, promptly give the supervisor a written statement of the reasons for the proposed action, and reasonable time to respond to that statement. If the supervisor makes a timely written response disagreeing with the proposed action and giving reasons for that disagreement, the NCUA Board cannot appoint a conservator or liquidating agent for the credit union unless the Board, after considering the supervisor's views, has made two determinations: first, that the Share Insurance Fund faces a significant risk of loss if a conservator or liquidating agent is not appointed for the credit union; and second, that the appointment is necessary to reduce the risk or magnitude of the loss. The NCUA Board cannot delegate either of those determinations.

Other provisions of the bill also clarify state credit union supervisors' role. Section 301(c) of the bill requires the NCUA, in developing regulations to implement new section 216, to consult with state credit union supervisors. Moreover, as specified in new section 216(n), section 216 does not limit state credit union supervisors' authority to take action in addition to (but not in derogation of) that required under section 216.

New section 216(m) exempts an insured corporate credit union from section 216(a). To qualify for the exemption, the entity in question must (1) operate primarily for the purpose of serving credit unions, and (2) permit individuals to be members only to the extent that applicable law requires that such persons own shares (e.g., directors' qualifying shares).

New section 216(n) does not limit any authority of the NCUA or a state to take action in addition to that required under section 216. Thus, for example, section 216 in no way limits any existing authority of the NCUA to deal with problems in their incipiency, before they manifest themselves in net worth deficiencies. Nor, for example, does it limit a state credit union supervisor's authority to appoint a conservator or liquidating agent for a state-chartered, federally insured credit union or to accept such an appointment from the NCUA.

New section 216(o) defines "Federal banking agency," "net worth," "net worth ratio," and "new credit union." "Federal banking agency" means the Comptroller of the Currency, the Director of the Office of Thrift Supervision, the Federal Reserve Board, and the FDIC. (12 U.S.C. § 1813(z))

A credit union's "net worth" is its retained earnings, as determined under generally accepted accounting principles. Under those principles, a credit union subtracts its allowance for loan losses from total assets in the course of calculating net worth. In the case of a low income credit union, "net worth" also includes uninsured secondary capital accounts that are subordinate to all other claims against the credit union, including the claims of creditors, shareholders, and the Share Insurance Fund.

A credit union's "net worth ratio" is the ratio of the credit union's net worth to the credit union's total assets.

A "new credit union" is a federally insured credit union that has been in operation for less than 10 years, and has not more than $10 million in total assets. A credit union ceases to be new when it reaches either the age or the asset-size threshold, whichever comes first.

Section 301(b) of the bill makes changes in laws relating to conservatorship or liquidation of federally insured credit unions that are necessary to effectuate prompt corrective action. Section 301(b) derives from section 133 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), which made similar amendments to effectuate prompt corrective action under section 38 of the Federal Deposit Insurance Act. Pub. L. No. 102–242, § 133, 105 Stat. 2236, 2270–73 (1991).

Section 301(b) expands the grounds for appointing a conservator or liquidating agent for a federally insured credit union. First, the Board is authorized to take such action when a credit union is significantly undercapitalized and has no reasonable prospect of becoming adequately capitalized. This ground permits the NCUA to act before such a credit union's net worth and franchise value erode further. Second, the Board is authorized to take such action when the credit union is critically undercapitalized. Section 301(b) codifies the two new grounds in sections 206(h)(1) (conservatorship) and 207(a) (liquidation) of the Federal Credit Union Act. (12 U.S.C. §§ 1786(h)(1), 1787(a))

Section 301(c) provides that the Board shall consult with the Secretary of the Treasury, the Federal banking agencies, and State credit union supervisors in developing regulations to implement new section 216 of the Federal Credit Union Act.

Section 301(d) requires the Board to publish in the Federal Register, within 270 days after the date of enactment, proposed regulations implementing the provisions of new section 216 other than the risk-based capital requirement. Furthermore, the Board must promulgate final implementing regulations within 18 months after the date of enactment. In the case of the risk-based net worth requirement, the Board must publish in the Federal Register an advance notice of proposed rulemaking within 180 days after the date of enactment. The Board shall promulgate final regulations for risk-based net worth requirement within two years after the date of enactment.

Section 301(e) provides that new section 216 as provided by this bill shall become effective two years after the date of enactment of the Act, except for the risk-based net worth requirement as provided for in new section 216(d) which becomes effective on January 1, 2001.

Section 301(f) requires the NCUA to submit a report to Congress—when publishing proposed regulations, or promulgating final regulations to implement new section 216 (other than the risk-based net worth requirement)—that specifically explains (1) how the regulations carry out section 216(b)(2) (relating to the cooperative character of credit unions); and (2) how the regulations differ from section 38 of the Federal Deposit Insurance Act, and the reasons for such differences.

Section 301(g) specifies that the NCUA can enforce orders issued under new section 216 of the Federal Credit Union Act. New section 216(e) supersedes the earnings-retention requirement now in section 116 of the Federal Credit Union Act. (12 U.S.C. § 1762) Accordingly, section 301(g) of the bill repeals section 116.

Section 302. National Credit Union Share Insurance Fund equity ratio, available assets ratio, and standby premium charge

Section 302 makes a series of amendments to section 202 of the Federal Credit Union Act (12 U.S.C. § 1782) in order to further strengthen the Share Insurance Fund. The amendments include six key changes (which, together with other aspects of section 302, are discussed more fully below). The first requires more timely and accurate calculation of the Fund's "equity ratio"—i.e., the ratio of the Fund's reserves to the total amount of the shares (deposits) that the Fund insures. The second requires a federally insured credit union with more than $50 million in total assets to adjust its 1 percent deposit in the Fund semi-annually. The third does not permit distributions to dissipate the Fund's reserves when the Fund's "available-assets ratio"—i.e., the ratio of high-quality, liquid net reserves to the total shares that the Fund insures—falls below 1 percent. The fourth, in place of the current rule that fixes any insurance premium at 1⁄12 of 1 percent of insured shares, gives the NCUA discretion to adjust the premium rate according to the Fund's financial needs. The fifth imposes a premium if the Fund's equity ratio falls below 1.2 percent, in keeping with the NCUA's longstanding practice. The sixth gives the NCUA discretion to let interest on the Fund's reserves increase the Fund's equity ratio to 1.5 percent.

Section 302(a)(1) of the bill amends section 202(b)(1) of the Federal Credit Union Act to require an insured credit union with more than $50 million in total assets to make a certified statement semi-annually. Section 202(b) of the Federal Credit Union Act currently requires each insured credit union to file annually a certified statement containing information about the credit union's insured shares and the credit union's own 1 percent deposit in the Share Insurance Fund. This information enables the credit union and the NCUA to calculate adjustments needed in the 1 percent deposit.

In addition, section 302(a)(1) contains an exception for newly insured credit unions that became insured during the reporting period. This provision is implicit in the phrasing of current section 202(b)(1) (requiring certified statements only from "each insured credit union which became insured prior to the beginning of that year").

Section 302(a)(2) of the bill amends section 202(c)(1)(A)(iii) of the Federal Credit Union Act to require an insured credit union with more than $50 million in total assets to adjust its 1 percent deposit in the Fund semi-annually. Section 202(c)(1)(A)(iii) of the Federal Credit Union Act currently requires an insured credit union to adjust its 1 percent deposit in the Share Insurance Fund annually. Credit unions with more than $50 million in assets hold the vast majority of insured shares. Requiring such credit unions to adjust their 1 percent deposit semi-annually will ensure that the 1 percent deposit accounts in a timely fashion for such credit unions' insured share growth.

Section 302(a)(3) of the bill amends section 202(c)(2) of the Federal Credit Union Act to give the NCUA discretion to adjust the premium rate according to the Share Insurance Fund's financial needs. Section 202(c)(2) of the Federal Credit Union Act currently gives the NCUA discretion to require each insured credit union to pay an insurance premium, and fixes the premium rate at 1⁄12 of 1 percent of the credit union's insured shares. Furthermore under amended section 202(c)(2), the NCUA may assess a premium only if (1) the Fund's equity ratio is less than 1.3 percent; and (2) the premium does not exceed the amount necessary to restore the equity ratio to 1.3 percent. If the Fund's equity ratio is less than 1.2 percent, the NCUA is required to assess a premium to restore the equity ratio to (and maintain it at) 1.2 percent. This provision in effect partially codifies the NCUA's longstanding practice of not permitting the Fund's equity ratio to fall below 1.25 percent.

Section 302(a)(3) of the bill also amends section 202(c)(3) of the Federal Credit Union Act, which governs distributions (often referred to as dividends) from the Share Insurance Fund. The NCUA is required under amendments to section 202(c)(3) to make a pro rata distribution to insured credit unions after each calendar year if, as of the end of that calendar year: (1) any loans to the Fund from the federal government, and any interest on those loans, have been repaid; (2) the Fund's equity ratio exceeds the normal operating level; and (3) the Fund's available assets ratio exceeds 1.0 percent. If these three conditions are satisfied, the NCUA is required to distribute the maximum possible amount that (1) does not reduce the Fund's equity ratio below the normal operating level; and (2) does not reduce the Fund's available assets ratio below 1.0 percent.

Section 302(a)(3) also directs the NCUA, in calculating the Fund's equity ratio and available assets ratio for purposes of the pro rata distribution, to use credit unions' certified statements from the final reporting period of the year in question to determine the total amount of shares that the Fund insures. Section 302(a)(4) requires the Board to use the most current and accurate data reasonably available. The term "reasonably available" is intended to strike a balance between the costs and benefits of obtaining more current and accurate data.

The provisions of 302(a)(3) differ from current law in (1) not requiring the NCUA to make distributions that would reduce the Fund's available assets ratio below 1 percent; (2) avoiding any possible implication that the NCUA must or should pay any distribution before the end of the year in question, even at the cost of basing the distribution on outdated data; and (3) requiring the NCUA to use data from credit unions' most recent certified statements in calculating the relevant Fund ratios. It also changes "insurance year" to "calendar year." Current law defines the "insurance year" as the calendar year unless the NCUA prescribes otherwise. In fact, the Fund operates on a calendar year basis.

Section 302(a)(5) of the bill recodifies the definitions in section 202(h) of the Federal Credit Union Act, adding definitions of "available assets ratio," "equity ratio" and "insured shares," setting new parameters for the "normal operating level."

The Fund's "available assets ratio" means the ratio of (1) the sum of the Fund's cash and the market value of the Fund's unencumbered securities investments under section 203(c), minus the Fund's direct liabilities and any contingent liabilities for which no provision for losses has been made, to (2) the aggregate amount of the insured shares in all insured credit unions.

The Fund's "equity ratio" means the ratio of (1) the amount of the Fund's capitalization, including insured credit unions' 1 percent capitalization deposits and the Fund's retained earnings balance (net of the Fund's direct liabilities and contingent liabilities for which no provision for losses has been made), to (2) the aggregate amount of the insured shares in all insured credit unions.

The definition of "insured shares" is substantively identical to that in current law.

Current law defines the Fund's "normal operating level" as "an amount equal to 1.3 per centum of the aggregate amount of the insured shares in all insured credit unions, or such lower level as the Board may determine." Section 302(a)(5) defines the "normal operating level" as an equity ratio specified by the NCUA, which must be between 1.2 percent and 1.5 percent. This revised definition (1) gives the NCUA discretion to let interest on the Fund's reserves increase the Fund's equity ratio to 1.5 percent; and (2) prevents the NCUA from making distributions from the Fund if the equity ratio is less than 1.2 percent. It is shorter than the current definition because the term "equity ratio" incorporates the concept of "the aggregate amount of the insured shares in all insured credit unions," which therefore need not be repeated in the definition of "normal operating level."

Although the revised definition permits the Fund's equity ratio to rise above 1.3 percent, such an increase cannot occur through premiums. Under new section 202(c)(2)(B) of the Federal Credit Union Act, the NCUA can assess a premium only if the equity ratio is less than 1.3 percent, and then only in the amount necessary to restore the equity ratio to 1.3 percent.

Section 302 becomes effective on January 1 of the first calendar year beginning more than 180 days after the date of enactment of this Act.

Section 303. Access to liquidity

Section 303 adds two new subsections to section 204 of the Federal Credit Union Act. (12 U.S.C. § 1784) New section 204(f) requires the NCUA to (1) periodically assess the potential liquidity needs of each federally insured credit union, and the options that the credit union has available for meeting those needs; and (2) periodically assess the potential liquidity needs of insured credit unions as a group, and the options that those credit unions have available for meeting their liquidity needs. New section 204(g) requires the NCUA to make available to the Federal Reserve banks (subject to appropriate assurances of confidentiality) information relevant to making discount-window advances to federally insured credit unions, including the NCUA's reports of examination.

TITLE IV—MISCELLANEOUS PROVISIONS

Section 401. Study and report on differing regulatory treatment

Section 401 requires the Secretary of the Treasury to conduct a study of the differences between credit unions and other federally insured financial institutions, including regulatory differences, and including the potential effects of applying Federal laws and Federal tax laws to credit unions in the same manner as such laws are applied to other federally insured financial institutions. This section also requires the Secretary to report to Congress within 1 year after enactment on the results of the study.

Section 402. Review of regulations and paperwork reductions

Section 402 amends section 303 of the Riegle Community Development and Regulatory Act of 1994 which required a two year review of regulations by each of the banking agencies for the purpose of streamlining rules and regulations. This section requires that each Federal banking agency and the NCUA conduct a review of the regulations and written policies of each such agency for the purposes of streamlining and modifying these regulations to improve efficiency, reduce unnecessary costs, reduce the paperwork burden for insured depository institutions, and to remove inconsistencies, outmoded and duplicative requirements. The review is to be conducted during the 1-year period following the date of enactment.

Section 403. Treasury report on reduced taxation and viability of small banks

Section 403 requires the Secretary of the Treasury to submit a report to Congress, within one year of the date of enactment, containing recommendations for legislative and administrative action that the Secretary deems appropriate that would reduce and simplify the tax burden for insured depository institutions with less than $1 billion in assets and banks having total assets of not less than $1 billion and not more than $10 billion. The report shall include any other recommendations that the Secretary deems appropriate to preserve the viability and growth of small banks in the United States.

Regulatory Impact Statement

This legislation was designed to strengthen the safety and soundness of federally insured credit unions at the least possible loss to the National Credit Union Share Insurance Fund, while allowing the multiple common-bond field of membership category along with limitations on commercial lending by credit unions. Because H.R. 1151 seeks to strengthen the safety and soundness of insured credit unions by providing express and specific regulatory guidance, the Committee believes that this legislation will have a minimal regulatory impact.

Congressional Budget Office Cost Estimate

Senate rule XXVI, section 11(b) of the Standing Rules of the Senate, and section 403 of the Congressional Budget Impoundment and Control Act, require that each committee report on a bill containing a statement estimating the cost of the proposed legislation, which was prepared by the Congressional Budget Office. This statement has been requested from the Congressional Budget Office, but it was not available at the date of filing this report. When the information is made available to the Committee, it will be placed in the Congressional Record.

Changes in Existing Law

In the opinion of the Committee, it is necessary to dispense with the requirement of subsection 12 of rule XXVI of the Standing Rules of the Senate in order to expedite the business of the Senate.

ADDITIONAL VIEWS OF SENATOR HAGEL

During the Committee's negotiations on H.R. 1151 there was considerable discussion over the role of credit unions in commercial lending. I believe the language does not adequately ensure that credit unions remain focused on their primary mission—consumer lending.

H.R. 1151 needs to ensure that credit unions remain strong, healthy, and committed to serving their members. Unfortunately it fails to do so. Since passage of the Federal Credit Union Act in the early 1930s, credit unions have been an important provider of basic financial services to the millions of Americans who rely on them for checking, savings, and small consumer loans. We need to make sure credit unions retain the special membership services that set them apart from banks and other financial institutions so they can fulfill their core mission of consumer lending and serving members' basic financial needs.

I'm concerned that, as currently written, H.R. 1151 would have unintended negative consequences for credit union members and taxpayers. The legislation is risky for credit union members who rely on their credit union for small, consumer loans because it would allow credit unions to shift their focus from consumer service to large-scale commercial lending. Congress should place limits on commercial lending by credit unions—and those limits should be real.

The Banking Committee attempted to address this problem by including a cap on credit unions' commercial lending activities—but unfortunately the limit is far too weak. First, the cap in the bill stands at 1.75 times the minimum net worth required for a well capitalized credit union. If a credit union were to reach this cap, it would represent more commercial lending than is generally done by the average community bank. Clearly, this would represent a shift away from its primary mission of consumer lending

Second, H.R. 1151 doesn't count loans to one borrower that total under $50,000 toward the commercial lending cap. Even if I were comfortable with the 1.75 times net worth cap, the under $50,000 loophole renders the cap meaningless. Unfortunately, this loophole reflects current NCUA policy. I question the wisdom of the regulator's current policy.

It is a generally accepted notion that commercial lending is riskier than consumer lending. It is crucial for the regulator and the public to be aware of the risk profile of the loan portfolio of each and every credit union. All loans that go for supporting commercial ventures, no matter how small these loans are, should be counted as such.

In sum, while the Committee-passed version of H.R. 1151 contains important improvements to the safety and soundness of the credit union industry, in the area of commercial lending the bill raises the risk to taxpayers and depositors. Have we really forgotten the disastrous lesson of the 1980s, when Congress and thrift regulators permitted the savings and loan institutions to stray from their primary mission and allowed riskier lending activities? Taxpayers continue to pay heavily for that mistake. It is my intention to address these concerns once the bill reaches the Senate floor.

CHUCK HAGEL.

ADDITIONAL VIEWS OF SENATORS GRAMM, SHELBY, MACK, FAIRCLOTH, BENNETT, GRAMS, ALLARD, ENZI, AND HAGEL

The legislation, as reported by the Committee, fails to change certain provisions of the bill as adopted by the House, costly mandates that are contrary to the very concept of credit unions. These would for the first time treat credit unions as public utilities and impose upon them unfunded mandates similar to the Community Reinvestment Act (CRA) requirements imposed on banks. We believe that these mandates should be removed from the bill.

Some have described these provisions as "CRA-lite." When CRA was first imposed upon banks, it was described as a light burden, merely encouraging banks to do what they should do. Unfortunately, and predictably, these reassurances turned out to be false, and the burden has been anything but light. We see no reason to believe that history would not repeat itself were this burden also imposed on credit unions.

At best, these provisions are inconsistent with the nature of credit unions and would result in expensive and wasteful record-keeping and examination costs. More significantly, because they fundamentally change the nature of credit unions, the CRA-style provisions would ensnare credit unions in a regulatory trap from which they could only find temporary release by financing the agendas of non-members at the expense of members.

Credit unions are financial cooperatives organized by private individuals to assist the members of the cooperative to save and invest, so it is hard to imagine forcing them to begin serving needs of non-members. But these CRA-style provisions in the bill would treat credit unions like public utilities, compelled by law to provide financial services to favored persons identified by the government. This mandate would require that these cooperatives of equal members give special treatment to some who would become more equal than others, or it would insist that credit unions use their resources to serve the wants of those who are not members at all. Frankly, these CRA-style provisions of the bill would likely lead to both outcomes, and neither one is acceptable to us.

Here is just one example of how the CRA-style provisions of the bill would likely operate. Suppose that a credit union wants to expand its field of membership, as allowed under the bill. That credit union would first have to prove to the regulators that it is already providing, in a "satisfactory" and "affordable" manner, credit union services to all individuals of modest means within the credit union's field of membership. The credit union verifies that it is offering loans at prime rate to all of its members. Offering? No, that would not qualify. The credit union has to be providing, and prime rate may not be affordable for some of these people. And what about those people of "modest means" who are eligible for membership but have not yet joined? After all, credit unions are not usually successful in enrolling more than a third of the people in their field of membership. The mandate, though, would require that the credit union serve all those people, whether members of the credit union or not, whether they have put money into a credit union or not. The requirement, in short, is open-ended and pernicious, leaving credit unions at the mercy of regulators and the activist groups that have already made such a practice of using CRA against community banks. These provisions should be stricken from the bill.

In addition, we believe that rather than imposing new CRA mandates on credit unions, the burden of CRA should be lifted from the shoulders of small, community banks. CRA preempts the free market lending criteria of the small community banks. CRA is nothing less than government mandated credit allocation, the form of credit allocation that has proven disastrous most recently in east Asia. It is ridiculous to assume that small community banks would not serve local financial needs. That is their franchise, their bread and butter. The CRA mandates impose on community banks an intrusive regulatory structure in the name of ensuring that these banks do what they would do anyway.

These regulatory burdens do not come cheap. According to a new Federal Reserve study, entitled "The Cost of Banking Regulation: A Review of the Evidence," regulatory costs account for up to "13 percent of noninterest expenses" of banks. In addition, the study concluded that "(A)verage compliance costs for regulations are substantially greater for banks at low levels of output than for banks at moderate or high levels of output." In other words, compliance costs are higher for small banks than for large banks.

For these reasons, we supported in committee an amendment to exempt community banks, with less than $250 million in assets, from the Community Reinvestment Act. That amendment was not adopted, with a tie vote of nine to nine. We believe that it would be wise to review this issue when the bill is brought before the full Senate.

PHIL GRAMM.
RICHARD SHELBY.
CONNIE MACK.
LAUCH FAIRCLOTH.
ROBERT F. BENNETT.
ROD GRAMS.
WAYNE ALLARD.
MIKE ENZI.
CHUCK HAGEL.

ADDITIONAL VIEWS OF SENATOR ENZI

Commercial lending has generally been considered riskier business than consumer lending. From this notion comes the premise of restricting the amount of lending that can be used for commercial purposes. Even though H.R.1151 limits commercial lending activity, the restriction in my belief is dubious at best.

Currently, the regulator of federally chartered credit unions, NCUA, does not designate an extension of credit which is less than $50,000 as a commercial or "member business" loan. If H.R. 1151 as passed by the Committee becomes law, NCUA's rule exempting any credit union loan less than $50,000 as being defined as a member business loan would be codified. I am concerned about the consequences this action may bring.

I place great emphasis and value on the accuracy of records of financial institutions. If a credit union does not count a loan which is less than $50,000 as a member business loan, even though the loan is used 100 percent for commercial purposes, it will never be known exactly how much of its loan portfolio is used for commercial purposes. The most stringent safety and soundness provisions are ineffective if accurate recordkeeping practices do not exist.

I feel it is of utmost importance to require all member business loans, at any amount, to be designated as such. Our markets and financial institutions perform best when there is transparency and accuracy of information. The United States has become the model for financial markets, in part because of the transparent accounting methods required of publicly traded companies. I believe credit unions should be obligated to be transparent in their loan activities. Credit unions should be required to accurately define every loan.

MICHAEL B. ENZI.

ADDITIONAL VIEWS OF SENATOR REED

I am supportive of the substitute amendment to H.R. 1151 adopted by the Committee. Yet, I also have several concerns about the commercial lending provisions included in the bill.

As a general matter, I support the ability of credit unions to engage in commercial lending. I am keenly aware that for some members, credit union loans are the only available sources of capital for business investment. However, such lending can significantly increase the risk profile of credit unions. This is evidenced by recent National Credit Union Administration (NCUA) data which illustrates that the delinquency rate on credit union business loans (3.1 percent) is more than three times the delinquency rate on credit unions' overall loan portfolio (0.97 percent). More importantly, in 1991, my home state of Rhode Island experienced a credit union crisis that resulted from the failure of a state-chartered private deposit insurance corporation. This crisis affected one in five citizens and was predicated in part on excessive and risky commercial lending by insured institutions. Indeed, 13 of the state's credit unions were permanently closed, and the state had to seek federal assistance to repay depositors.

In view of these facts, I believe that commercial lending by credit unions should be limited. As such, I supported provisions in H.R. 1151 that imposed an aggregate cap on commercial lending by credit unions of 12.25 percent of outstanding loans. However, I am concerned that this cap is too permissive and could have adverse safety and soundness implications in the future.

First, the 12.25 percent commercial lending cap in the bill is significantly higher than the level of commercial lending that credit unions are currently engaged in. According to NCUA Call Report data, federal credit unions' commercial loans totaled 0.75 percent of outstanding loans at the end of 1997. In view of this fact, it is apparent that the commercial lending cap in the bill does not bear a rational relationship to the actual levels of commercial lending by credit unions. In fact, by establishing a statutory commercial lending cap that is substantially higher than existing commercial loan levels, Congress may encourage credit unions to engage in additional commercial lending. Also, given the limited experience of credit unions in commercial lending, I am concerned about their ability to underwrite commercial loans in a safe and sound manner. Finally, I am concerned that loans under $50,000 would not be counted toward the 12.25 percent cap. As a result, it is possible that credit unions could engage in commercial lending to a much greater extent than the limit imposed in the bill.

When H.R. 1151 is debated on the floor and in conference, I would hope that my colleagues give serious consideration to these concerns and would limit commercial lending to an amount that bears a closer relationship to existing levels.

JACK REED.

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