

Open Board Meeting

April 30, 2015

**Board Member J. Mark McWatters
Statement on the Associational Common Bond Final Rule**

Although it is my understanding that NCUA has undertaken to revise the current “field of membership” (FOM) rules so as to provide the credit union community with much needed regulatory relief, that aspiration is not reflected in the Associational Common Bond Final Rule (Final Rule) before the Board today. If credit unions are in any manner abusing the Associational Common Bond FOM rules, as presently in effect, NCUA should promptly, aggressively, and decisively address those breaches under the Federal Credit Union Act and existing NCUA promulgated regulations. NCUA should, in accordance with objective, transparent, and well-recognized standards of due process, investigate and cause any “bad apples” to cease and desist any activity that is contrary to the Federal Credit Union Act and the Associational Common Bond FOM rules and regulations as in effect today. The Final Rule—except for the regulatory relief offered in the preapproval process—accomplishes little except to increase the regulatory burden on the vast bulk of credit unions that remain in full compliance with the letter and the spirit of the Associational Common Bond rules.¹

In dissenting from the adoption of the Final Rule, I wish to offer my thoughts concerning additional regulatory relief for the credit union community that is not incorporated in the Final Rule.²

¹ Consistent with this perspective, the Chair sent a letter to the credit union community in September 2013 stating in part:

The Federal Credit Union Act provides NCUA with a broad array of supervisory and administrative tools to enforce the law and rules. Depending on the degree of non-compliance, NCUA may initiate a supervisory contact, require a federal credit union to divest an associational group from its field of membership, and/or issue a Cease and Desist order.

The tool NCUA chooses will depend on a variety of factors including the severity of a particular violation, available methods to rectify a violation, and the extent of a federal credit union’s cooperation.

Upholding the membership standards of every federal credit union is essential to maintaining the integrity of the federal credit union system.¹

If this statement is accurate – and I believe it is accurate – then I question why NCUA needs to burden the credit union community with yet more FOM regulation.

² Section 109 of the Federal Credit Union Act (FCUA) provides for three types of federal credit union (FCU) charters: (i) single common bond (occupational or associational), (ii) multiple common bond (multiple groups), and (iii) community. 12 U.S.C. 1759(b). The NCUA Chartering and Field of Membership Manual (Chartering Manual) provides that a single common bond FCU consists of one group having a common bond of occupation or association, and a multiple common bond FCU consists of more than one group, each of which has a common bond of occupation or association. 12 CFR part 701,

1. Threshold Requirement. For purposes of qualifying for membership in a federal credit union under the current FOM rules, NCUA determines if a group satisfies the Associational Common Bond requirements by applying a “totality of the circumstances test” (Totality of the Circumstances Test), which centers on a detailed multi-factor analysis.³ Under the Final Rule (as well as the Associational Common Bond April 2014 Proposed Rule (Proposed Rule)), NCUA has undertaken to incorporate a new burdensome “threshold requirement” (Threshold Requirement) that credit unions must satisfy *before* they are permitted to run the gauntlet of the Totality of the Circumstances Test.⁴

The Threshold Requirement prohibits the addition of an association to a federal credit union’s FOM unless the association was not formed for the “primary purpose” of expanding the federal credit union’s membership. The “primary purpose” requirement appears subjective and duplicative of the more objective and transparent elements of the Totality of the Circumstances Test. Those who operate federal credit unions most assuredly appreciate that this requirement injects yet more uncertainty and time delay into the FOM regulatory process. One of the key goals of true regulatory relief is to lessen uncertainty and the ability of the regulator to operate in a less than transparent and fully accountable manner.

Appendix B (Chapter 2, Section I.A.1). A community FCU consists of persons or organizations within a well-defined local community, neighborhood, or rural district. A single associational common bond credit union consists of natural persons and/or non-natural persons whose members participate in activities developing common loyalties, mutual benefits, and mutual interests. 12 CFR part 701, Appendix B (Chapter 2, Section III.A.1). A multiple associational common bond credit union may be chartered to serve a combination of distinct, definable single associational common bonds. Each such group in a multiple associational common bond credit union must have its own occupational and associational common bond. These groups must fall within a reasonable geographic proximity of the credit union and each individual group (select group) must fall within the service area of one of the FCU’s service facilities. A select group is considered within a FCU’s service area when a majority of the persons in that select group live, work, or gather regularly within the service area, the service group’s headquarters is located within the service area, or the group’s “paid from” or “supervised from” location is within the service area. A multiple common bond credit union may not include a trade, industry, or professional single occupational common bond or expand using single common bond criteria. 12 CFR part 701, Appendix B (Chapter 2, Section IV.A.1). Final Rule, pages 5, 6 and 7.

³ The seven factors are: (i) whether members pay dues, (ii) whether members participate in the furtherance of the goals of the association, (iii) whether the members have voting rights, (iv) whether the association maintains a membership list, (v) whether the association sponsors other activities, (vi) the association’s membership eligibility requirements, and (vii) the frequency of meetings. 12 CFR part 701, Appendix B (Chapter 2, Section III.A.1).

⁴ The new regulatory hurdle, the so-called “threshold requirement,” provides in part:

As a threshold matter, when reviewing an application to include an association in a federal credit union’s field of membership, NCUA will determine if the association has been formed *primarily for the purpose* of expanding credit union membership. (Emphasis added.) 12 CFR part 701, Appendix B (Chapter 2, Section III.A.1.a).

2. Corporate Separateness. The Final Rule (as well as the Proposed Rule) also increases the regulatory burden associated with the Totality of the Circumstances Test by adding an additional factor of “corporate separateness” to the mix. Adding the new item of “corporate separateness” to the Totality of the Circumstances Test confuses substance and form and accomplishes little except to increase the cost of incorporating an association into a federal credit union’s FOM.

3. Pre-Approved Associations. Although the Final Rule expands the list of groups pre-approved for Associational Common Bond status,⁵ notable omissions remain.⁶ In my view, the pre-approved list should also include—subject to reasonable and transparent limitations—any section 501(c)(3) nonprofit organization, as well as any other legitimate association that has operated for not less than five years. The expansion of the pre-approved list to include these organizations would constitute true regulatory relief for the credit union community.

4. Quality Assurance Review and Removal Process. The quality assurance review and removal process contained in the Final Rule raises due process concerns. I remain troubled by any such rule that does not incorporate resilient standards of objective transparency, a meaningful period for a federal credit union to cure or remedy any non-compliance issue after written and timely notice from NCUA, and a formal rule-based and fair minded process by which a federal credit union may appeal any adverse determination by NCUA. The Final Rule states that quality assurance review and removal “are intended to protect the integrity of NCUA’s FOM requirements, not disrupt a federal credit union’s ability to serve its members or hamper a federal credit union’s ability to thrive.”⁷ Without the incorporation of meaningful due process standards into the Final Rule or, at a minimum, into regulatory guidance, these words offer modest comfort to the credit union community.

5. Geographic Limitations. The Final Rule provides that NCUA was not “seeking to impose geographic limitation on associational groups, similar to the geographic

⁵ The Final Rule adds the following pre-approved groups: parent teacher associations, chamber of commerce groups, athletic booster clubs, fraternal organizations or civic groups, and organizations promoting social interaction or educational initiatives. 12 CFR part 701, Appendix B (Chapter 2, Section III.A.1.b).

⁶ For example, by excluding health clubs, such as the YMCA, the Agency appears insensitive to the common loyalties, mutual benefits, and mutual interests that people who jointly engage in athletic endeavors and physical conditioning develop. To the aspiring athlete, or the weekend warrior, a health club often offers the comforting environment of a fraternal organization or civic club where common loyalties, mutual benefits, and mutual interests most assuredly thrive and prosper.

Fortunately, the Agency avoided the mistake of excluding from the pre-approved list alumni organizations that permit non-alumni to join. In many college towns such as Austin, Tuscaloosa, and Columbus alumni and non-alumni enthusiastically support the local university. Excluding alumni groups that accept the latter serves no purpose, has no rational basis, and appears arbitrary and elitist.

⁷ Final Rule, page 25.

limitation placed on multiple common-bond FCUs” and that the “Board reiterates that the Chartering Manual clearly states that single associational common bond federal credit unions do not have geographic limitation.”⁸ Nevertheless, in my view, it is imperative that NCUA address the geographic limitation and reasonable proximity rules applicable to multiple common bond credit unions.⁹ Today, a common bond may form, develop, and prosper among both disparate and homogenous groups over an iPhone or other device in a seamless manner regardless of the physical location of the participants.¹⁰ NCUA’s failure to act on the antiquated geographic limitation and reasonable proximity rules will place federal credit unions at a distinct competitive disadvantage to their peers.¹¹

Thank you.

⁸ Final Rule, page 27. 12 CFR part 701, Appendix B (Chapter 2, Section III.A.1).

⁹ FCUA 109(f)(1)(B).

¹⁰ On a related matters and as I noted in my GAC speech, it is critical that all credit unions embrace the structure and delivery of financial services as demanded by today’s marketplace.

¹¹ The existing rules are more appropriate for the Flintstones when we live in the era of the Jetsons. NCUA should not penalize FCUs that seek to operate their financial institutions in the 21st Century and avoid old-school thinking and outmoded technology.