September 28, 1995

Opinion O-95-5 (Redacted version)

"A"

VIA FACSIMILE

Subject: Response to Comment Letters on "B"
Interpretation No. 95-1

Dear "A":

Thank you for your letter dated September 6, 1995, on behalf of several "C" credit unions, providing comment on the conversion of "B" to a state charter. We also received comment letters on the conversion from a number of other credit unions in that area. I have provided below a brief background on this situation, followed by a summary of each of the primary comments and our response to each comment. In the interest of saving time, I have furnished a copy of this letter to each of the other commenters rather than prepare separate letters.

As explained below, we have concluded that the field of membership rules do not apply to the conversion of "B". We approved the conversion, which was completed on September 20, 1995.

General Background

"B" essentially had the community of the city of "C" in its field of membership ("FOM"), subject to a FOM Bylaw restriction (the "Bylaw restriction") that the following persons were not eligible for membership in "B":

> Persons eligible for primary membership in another occupational or associational credit union maintaining an office in the ["C" community] as of August 6, 1975.

"B" desired to delete the Bylaw restriction, effective upon its conversion to a state charter.

The Washington Credit Union Act (Chapter 31.12 RCW) permits each credit union to serve occupational groups, associational groups, and community groups in its approved FOM. RCW 31.12.05. State credit unions are not limited to serving one type of group. WAC 419-72-012. The rules of the Division of Credit Unions("DCU") on approval of FOMs are set forth in Chapter 419-72 WAC, most recently amended in May 1995 ("FOM rules"). WAC 419-72-065 deals with approval of inclusion of a community group in a credit union's FOM.

We received several comments concerning the effect that the deletion of "B" Bylaw restriction would have on competition among "C"-area credit unions. Part of our statutory mandate is to ensure that credit unions as a movement remain "viable and competitive in this state." RCW 31.12.015. We also view it as part of our mandate to allow credit unions, through the FOM application process, to serve more citizens of the state of Washington.

Many credit unions have told us that in order to thrive, they must grow through the addition of new groups to their FOM. The addition of occupational, associational, and community groups pursuant to the Credit Union Act inevitably increases competition among credit unions (and all financial institutions). However, we believe that credit unions, including small credit unions, can flourish in a competitive environment.

More specific to the "B" situation, under the FOM rules, a state credit union with a community FOM can accept as members those persons in the community who are in the occupational or associational FOM of another credit union. It is not unusual these days for individuals to be eligible to join several credit unions. These so-called "overlaps" between a community FOM on one hand and an occupational or associational FOM on the other are permitted for state credit unions. Compare WAC 419-17-065 with –025(3) and –050(3). Nonetheless, we encourage credit unions to work cooperatively to resolve these overlapping situations.

However, "B" is prohibited from conducting a direct marketing campaign targeted at occupational or associational groups in the "C" community that are within the FOM of another credit union. See copy of enclosed opinion letter, and the second sentence of WAC 419-72-065(8). Complaints regarding practices that violate this prohibition should be forwarded in writing to my attention. We will contact the credit union committing the practice and may undertake an audit if necessary.

Comment Summary and Response

1. Comment: If "B" were to apply for their present FOM today, it would not be granted by the DCU or NCUA. The "B" request is beyond what DCU has approved in the past.

Response: It is true that we would not approve an application today to add a community group the size of "C", even with the Bylaw restriction, if it exceeded the 75,000 population limit for approval. However, this was not a case where a credit union was adding a community group to its FOM. "B" was already serving the "C" community, as approved by the NCUA in 1975. Our Credit union Act clearly permits state credit unions to have community FOMs. Therefore, it was not necessary for "B" to apply for our approval under the FOM rules to add a community to its FOM. RCW 31.12.045; WAC 419-72-010. Upon conversion of a credit union from federal to state charter, the shareholders and members of the state credit union. RCW 31.12.715(2).

Moreover, notwithstanding any provision of state law, state chartered credit unions have all the powers and authorities enjoyed by federal credit unions as of December 21, 1993. RCW 31.12.136 (commonly referred to as the "parity provision"). "B" community FOM was approved in accordance with authorities that were possessed by federal credit unions at that time (1975) and that have been possessed by federal credit unions continuously since that time. "B" therefore is permitted to maintain its community FOM based on the parity provision.

The only aspect of the conversion which could arguable have triggered an FOM issue was the deletion of the Bylaw restriction which, as discussed below, is not subject to the FOM rules generally.

2. Comment: The problem is the removal of the Bylaw restriction. The total number of persons eligible for membership in "B" with the Deletion of the Bylaw restriction is well over 100,000, in excess of current limits established by the Division for approval of community FOMs. The deletion of the Bylaws restriction should be considered as a separate, stand-alone FOM application.

Response: State chartered credit unions with a community FOM, unlike their federal counterparts, are not required to include in their FOM Bylaws a restriction similar to "B" Bylaw restriction. Consequently, the FOM rules were not intended to apply to the deletion of a bylaw restriction such as "B" Bylaw restriction, let alone in the context of a federal credit union's conversation to a state charter.

The deletion of "B" Bylaw restriction presented a case of first impression. We were called upon to determine if and how the FOM rules applied in this circumstance. We determined that the deletion of the Bylaw restriction is not in form or substance the equivalent of adding a new community to a credit union's FOM. Therefore, the deletion of the Bylaw restriction is not subject to the FOM rules. However, we did determine that certain of the documentation requirements set forth in WAC 419-72-065 should apply to the deletion of the Bylaw restriction:

1. WAC 419-72-065(1): the request for approval of the Bylaw change must include the name of the credit union,
2. –065(2): The credit union must furnish evidence of compliance with the notice and voting requirements for a Bylaw change under RCW 31.12.115,
3. The second sentence of –065(8): The credit union must include documentation that it will not conduct certain direct marketing targeted to other occupational and associational groups, discussed above, and
4. -065(9): The credit union must document that it provided notice of the Bylaw change to certain other credit unions, discussed below.

If (for the sake of argument) we viewed the deletion of the Bylaw restriction as the basis for a stand-alone application for a community FOM, the "community" at issue would be the group created by the deletion of the Bylaw restriction, and not the entire community without the Bylaw restriction. You have stated that the current population of "C" is roughly 100,000. Therefore, it is highly unlikely that the population of the "community" created solely by the deletion of the Bylaw restriction would exceed the 75,000 limit for FOM approval.

3. Comment: The boundaries of the city of "C" are always changing.

Response: The boundaries of "C" may change from time to time. However, we permit a state credit union to use the boundaries of various governmental units to define the boundaries of its community FOM, for example, city, town, and school district limits. WAC 419-72-065. As these boundaries change, more or fewer people may be eligible for membership in the credit union. Of course, even those communities with fixed boundaries may be subject to significant population growth. Consequently, we look at current population when determining whether a community is within the population limits for FOM approval.

Moreover, "B" may continue to include the city of "C" within its FOM based on the parity provision.

<u>4. Comment:</u> "B" bylaws are poorly written and outside the guidelines of WAC 419-72-65, and include such nebulous terms as "students attending public schools" which clearly are not part of the WAC section.

Response: While the wording of "B" FOM Bylaws may be improved, they are not so vague as to be deficient under the FOM rules.

Moreover, "B" may continue to include students attending public schools in its FOM based on the parity provision.

<u>5. Comment:</u> The bylaw amendment will threaten the viability of existing credit unions.

<u>Response:</u> This is a factor in approving FOMs, pursuant to WAC 419-72-075(7). However, as noted above, the FOM rules do not generally apply to the deletion of the Bylaw restriction.

Moreover, without hard evidence demonstrating that the deletion of the Bylaw restriction presented an immediate threat to the viability of a specific credit union, we did not have safety and soundness concerns for another credit union that would have affected our decision whether to approve the conversion of "B".

<u>6. Comment:</u> We do not appreciate the deceptive way that "B" attempted to ignore the notice requirement, and started advertising that everyone can join "B" before the approval of their application.

<u>Response:</u> As noted above, the FOM rules do not generally apply to deletion of the Bylaw restriction. However, we determined that notice was appropriate and required that notice be given in the manner provided in WAC 419-72-065(9). Subsection (9) doe not expressly require that the notice include a copy of the working changes to the FOM Bylaw. Therefore, we believe that the August 10, 1995 notice letter to credit unions from "B", which described the deletion of the Bylaw restriction, was adequate and not deceptive. However, in the interest of satisfying the concerns over notice, we did send out a copy of the revised Bylaw working to the credit unions that received the August 10 notice.

The pre-conversion advertising we saw indicated in essence that "B" was making a change that would allow all the residents of "C" to join. It did not state that all residents could join at that time. We have spoken with "B" and they have assured us

that they did not accept anybody for membership prior to the conversion who was eligible only by virtue of the deletion of the Bylaw restriction.

7. Comment: "B" is attempting to get what it cannot through a federal charter.

Response: The beauty of the dual chartering system is that it pressures each regulator to stay reasonably competitive, thereby providing choice and leverage to credit unions, to their clear advantage. In respect to FOMs, state charters currently have a broader set of powers than federal charters.

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I trust this letter explains our position on the conversion of "B" FCU and the deletion of "B"'s Bylaw restriction.

Sincerely,

J. Parker Cann
Acting Assistant Director