

To: Opinion File

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 Director of Credit Unions

Subject: Summary of new Washington State Credit Union Act, Chapter 31.12
 RCW

Opinion no.: O-98-4

Summary of
New Washington State Credit Union Act
Chapter 31.12 RCW

Effective January 1, 1998

Table of Contents

Background Information4

 Introduction.....4

 Sections of the memo.....4

 Effective date of the new Act.....4

 Distribution of copies of new Act.....4

Bylaw Amendments Necessitated by Chapter 397.....5

 Administration by the Division.....5

 Delegation of authority to Division to approve.....5

 Grace period for bylaw compliance for examination purposes.....5

 Board of Directors.....5

 Delegation of duties5

 Qualifications5

 Vacancies5

 Indemnification6

 Members6

Expulsion/reinstatement.....	6
Conditions	6
Delegation	6
Meetings.....	6
Annual.....	6
Special.....	6
Voting by minors	6
Supervisory Committee.....	6
Directors on Committee.....	6
Qualifications of members	7
Vacancies	7

Section-by-Section Summary -

Significant Changes Effected by Chapter 397.....	8
Board of Directors; Committee Members; Officers	8
Compensation of directors and committee members	8
Duties of Board	8
Fiduciary duties of directors and officers.....	8
Oath.....	8
Officers	9
Qualifications of directors.....	9
Suspension by Board.....	9
Vacancies	9
Corporate Governance	9
Articles of Incorporation.....	9
Amendments	9
Information on directors and incorporators.....	9
Bylaws.....	9
Amendments	9
Indemnification	10
Definitions.....	10
Enforcement.....	10
Cease and desist orders	10
Conservatorship and receivership	10
Removal of directors, supervisory committee members, officers, and employees.....	10
Examination and supervision.....	11
Exam reports and other confidential information	11
GAAP requirements.....	11
General authority of the Director	11
Regular reports to the Director.....	11
Regular reserves	11
Members	11
Expulsion/reinstatement.....	11

Conditions for expulsion.....	11
Delegation.....	11
Process.....	11
Meetings.....	12
Annual.....	12
Special.....	12
Voting.....	12
Mergers.....	12
Out-of-state and foreign credit unions.....	12
Powers of credit unions.....	13
Generally.....	13
Investments.....	13
Loans.....	13
Loans-to-one-borrower limit.....	14
Real property.....	14
Statutory lien on member shares and deposits.....	14
Supervisory Committee.....	14
Directors on Committee.....	14
Duties.....	14
Attending Board meetings.....	14
No more reports on special member meetings.....	14
Qualifications.....	14
Suspension by Supervisory Committee.....	15
Vacancies.....	15

Sections Repealed by Chapter 39716

Disposition Chart for Former Sections of Chapter 31.12 RCW Re-numbered by Chapter 39717

New Washington State Credit Union Act

Background Information

Introduction. In 1997, the Washington State Legislature enacted extensive modernizing revisions to the Washington State Credit Union Act (Act), Chapter 31.12 of the Revised Code of Washington (RCW). These changes, enacted as Chapter 397 of the Laws of 1997, took effect on January 1, 1998, with a few exceptions, as discussed below.

In part, the new Act allows credit unions to exercise certain corporate governance powers, but only if they are set forth in the credit union's bylaws. In effect, these provisions require credit unions that wish to take advantage of these powers to amend their bylaws.

Sections of the memo. This memo addresses the following:

1. Bylaw amendments necessitated by Chapter 397.
2. Section-by-section summary of the new Act.
3. Sections repealed by Chapter 397.
4. Disposition of former sections re-numbered by Chapter 397.

Effective date of the new Act. The new Act took effect on January 1, 1998, except for

- RCW 31.12.428, concerning loan-to-one-borrower limits, which takes effect on July 1, 1998. Until July 1, 1998, pre-existing RCW 31.12.317 prescribes loan-to-one-borrower limits.
- RCW 31.12.569, concerning compliance with Generally Accepted Accounting Principles (GAAP) as identified by rule of the Division, which takes effect on January 1, 1999.

Distribution of copies of new Act. A copy of the new Act was previously mailed to all credit unions. Additional copies of the Act are available from Tina at the Division. She may be reached at (360) 902-8718, or by e-mail at tphilippsen@dfi.wa.gov. In addition, the new Act is available over the Internet at:

http://leginfo.leg.wa.gov/pub/rcw/title_31/chapter_012/

New Washington State Credit Union Act

Bylaw Amendments Necessitated by Chapter 397, Laws of 1997

Administration by the Division

Delegation of authority to Division to approve. Although the new Act and Division rules refer to action by the Director of the Department of Financial Institutions (Director), the Director has for the most part delegated his authority to the Assistant Director of the Division. Consequently, all correspondence, notices, applications, etc. which the statute requires to be submitted to the Director should be submitted instead to the Division for processing.

Grace period for bylaw compliance for examination purposes. Although the new Act took effect on January 1, 1998, the Division has taken the position that credit unions will not be criticized for failing to amend their bylaws as required by the new Act, until after June 30, 1998. However, for other purposes, such as delegating Board duties, or creating a member expulsion procedure, credit unions may wish to act as soon as possible to amend their bylaws. As you know, only FOM Bylaw amendments need the prior approval of the Division.

Board of Directors

Delegation of duties (RCW 31.12.255). The Board may delegate the duties listed in RCW 31.12.255(2). The delegation should be stated in the credit union's bylaws or a resolution adopted by the Board.

Qualifications (RCW 31.12.065, .235).

1. If a credit union wants to establish qualifications (other than statutory qualifications) for members to serve on the Board, it must provide for such in its bylaws.
2. If the credit union wants to allow officers and employees to serve on the Board, it must provide for such in its bylaws.

Vacancies (RCW 31.12.225). If the credit union wants to allow interim directors to serve only until the next annual membership meeting (rather than allowing them to serve out the unexpired term of the replaced director), it must provide for such in its bylaws.

Indemnification (RCW 31.12.065)

If provisions for the indemnification of directors, supervisory committee members, officers, and employees are not set forth in the credit union's articles of incorporation, they must be set forth in the bylaws.

Members

Expulsion/reinstatement

Conditions (RCW 31.12.255). The Board must establish the conditions for expulsion of members for cause. These conditions should be set forth in the bylaws or in a Board resolution.

Delegation (RCW 31.12.255, .388). The Board may delegate its authority to expel and reinstate members to a committee, officer, or employee of the credit union. The delegation should be set forth in the bylaws or in a Board resolution.

Meetings

Annual (RCW 31.12.185). The Board must approve rules of procedure for conduct of annual membership meetings. These rules should be adopted by reference in the credit union's bylaws or a Board resolution. Established rules of procedure should be utilized, such as *Robert's Rules of Order*.

Special (RCW 31.12.195).

1. If the credit union wants to allow special meetings to be held outside of the county in which the principal place of business of the credit union is located, it must provide for such in its bylaws.
2. If the credit union wants to allow the Board secretary to give notice of a special meeting more than 10 days after the request for the meeting is received, it must provide for such in its bylaws.
3. The Board must approve rules of procedure for conduct of special membership meetings. These rules should be adopted by reference in the credit union's bylaws or a Board resolution. Established rules of procedure should be utilized, such as *Robert's Rules of Order*.

Voting by minors (RCW 31.12.386). If the credit union wants to allow members younger than 18 to vote, it must provide for such in its bylaws.

Supervisory Committee

Directors on Committee (RCW 31.12.326). If the credit union wants to allow members to elect more than one director of the credit union to serve on the Supervisory Committee at the same time, it must provide for such in its bylaws.

Qualifications of members (RCW 31.12.065). If the credit union wants to establish qualifications (other than statutory qualifications) for members to serve on the Supervisory Committee, it must provide for such in its bylaws.

Vacancies (RCW 31.12.326). If the credit union wants to allow interim Supervisory Committee members to serve only until the next annual membership meeting (rather than allowing them to serve out the unexpired term of the replaced member), it must provide for such in its bylaws.

New Washington State Credit Union Act

Section-by-Section Summary - Significant Changes Effected by Chapter 397, Laws of 1997

Note: This summary explains only the significant wording changes in the new Act. This summary does not explain provisions of the old Act which were not amended and continue in effect.

Board of Directors; Committee Members; Officers

Compensation of directors and committee members (RCW 31.12.365).

1. The new Act continues to prohibit directors and committee members from receiving compensation. However, under the new Act directors and committee members may receive:
 - Incidental services provided to other employees generally; and
 - Gifts of minimal value. The Division has taken the position that gifts to individual directors and committee members from their credit union may not exceed \$50 in the aggregate each year.
2. A credit union may reimburse directors and their spouses for expenses related to the director's Board and committee duties.

Duties of Board (RCW 31.12.255).

1. The changes to this section clarify the delegable and non-delegable duties of the Board.
2. The Board may delegate authority for the expulsion and reinstatement of members.
3. This section was not intended as an exhaustive listing of all Board duties. The Board should use its prudent judgment in determining whether duties not listed in this section are delegable or non-delegable.

Fiduciary duties of directors and officers (RCW 31.12.267).

This section confirms the fiduciary duties of directors and officers. Credit union directors and officers (whether board officers or corporate officers) owe a fiduciary duty to the credit union. The wording of this section follows the description of the fiduciary duties of general business corporation directors and officers set forth in RCW 23B.08.300 and .420.

Oath (RCW 31.12.225). Directors, principal operating officers, and committee members no longer have to swear an oath of office.

Officers (RCW 31.12.265).

The Board must elect board officers and designate operating officers. Note the distinction between Board officers and corporate officers, as indicated in the definition section, RCW 31.12.005.

Qualifications of directors (RCW 31.12.235).

1. A credit union must set forth in its bylaws any qualifications (other than statutory qualifications) for individuals to serve on the Board.
2. Officers and employees of a credit union may serve on the credit union's Board, but only if the credit union's bylaws so provide. The officers and employees on the Board must constitute less than a majority of the full Board.

Suspension by Board (RCW 31.12.285).

The Board may for cause suspend a director or Supervisory Committee member until a membership meeting is held, but a two-thirds vote of the Board is no longer required to suspend. A simple majority of the Board will suffice.

Vacancies (RCW 31.12.225).

1. The Board must appoint an interim director to fill a vacancy on the Board, unless the interim director would serve a term of fewer than 90 days.
2. Interim directors serve out the unexpired term of the director they replace, unless the credit union's bylaws provide that interim directors may serve only until the next annual membership meeting.

Corporate Governance

Articles of Incorporation

Amendments (RCW 31.12.105). The Division must approve or deny applications for articles amendments within 60 days after receipt of the complete application.

Information on directors and incorporators (RCW 31.12.055). A credit union may delete its directors' and incorporators' occupations and addresses from its articles of incorporation.

Bylaws

Amendments (RCW 31.12.115).

1. The Board of Directors must approve a bylaw amendment by at least a majority vote. No longer is a two-thirds vote required. Certain other notice requirements for approval of bylaw amendments have been deleted.
2. The Division must approve or deny applications for FOM bylaw amendments within 60 days after receipt of the complete

application.

Indemnification (RCW 31.12.065). A credit union must set forth provisions on indemnification of directors, Supervisory Committee members, officers, and employees in its bylaws if they are not set forth in the credit union's articles of incorporation.

Definitions (RCW 31.12.005)

The following terms are redefined or defined for the first time:

- Board officer means an officer of the Board who is elected by the Board.
- Branch means a staffed, physical facility where deposits are taken. It does not include ATM machines.
- Capital means reserves, undivided earnings, and the allowance for loan loss. Note: This change is particularly important, because capital and net capital are used as benchmarks in several places in the Act.
- Insolvency.
- Loan means any loan, overdraft line of credit, extension of credit, or lease, in whole or in part.
- Material violation of law.
- Net capital means capital less the allowance for loan loss.
- Operating officer means an officer designated by the Board for conducting the business of the credit union.
- Principally or primarily means more than one-half.
- Unsafe or unsound condition.
- Unsafe or unsound practice.

Enforcement

Cease and desist orders (RCW 31.12.585). The changes to this section clarify the Division's authority to issue a notice of charges preliminary to the entry of a cease and desist order (C&D).

Conservatorship and receivership (RCW 31.12.637). This section establishes grounds for the Division to put a credit union under supervisory direction, or appoint a conservator or receiver for a credit union.

Removal of directors, supervisory committee members, officers, and employees (RCW 31.12.575). The Division may remove a credit union director, Supervisory Committee member, officer, or employee, if certain grounds exist. This section replaces the Division's existing authority to remove a director or principal operating officer.

Examination and supervision

Exam reports and other confidential information (RCW 31.12.565). Exam-type confidentiality is extended to:

- Exams of other state and federal regulators submitted to the Division; and
- Business plans and other proprietary information provided to the Division in connection with applications or notices to the Division. The applicant or notifying party must furnish the information in a separate binder marked “confidential” in order for the confidentiality provision to apply.

GAAP requirements (RCW 31.12.569). Credit unions must comply with generally accepted accounting principles (GAAP) as identified by rule of the Division. The Division may not put such rules into effect before January 1, 1999. The Division may take into consideration whether such rules should be phased in for small credit unions. However, this section was not intended to eliminate any current GAAP requirements established by the Division as a matter of safety and soundness (SFAS 115, allowance for loan loss, etc.).

General authority of the Director (RCW 31.12.516). The Director is granted broad administrative discretion to interpret the Act.

Regular reports to the Director (RCW 31.12.567). Credit unions must file financial reports with the Division at least semi-annually, consistent with current filing practice (5300S reports).

Regular reserves (RCW 31.12.445). The changes to this section confirm that the regular reserve requirements apply only to credit unions whose shares and deposits are not federally-insured, such as WCUSGA members. NCUA-insured credit unions must comply with the reserving requirements in NCUA rules at Part 741.

Members

Expulsion/reinstatement

Conditions for expulsion (RCW 31.12.255). The Board must establish the conditions for expulsion of members for cause. These conditions should be set forth in the bylaws or in a Board resolution.

Delegation (RCW 31.12.255, .388). The Board may delegate its authority to expel and reinstate members to a committee, officer, or employee of the credit union. The delegation should be set forth in the bylaws or in a Board resolution.

Process (RCW 31.12.388). The process for expulsion of a member, and the obligations of an expelled member, are clarified.

Meetings

Annual (RCW 31.12.185). A credit union must conduct its annual membership meetings in accordance with rules of procedure approved by the Board. These rules should be adopted by reference in the credit union's bylaws or a Board resolution. Established rules of procedure should be utilized, such as *Robert's Rules of Order*.

Special (RCW 31.12.195).

1. A credit union may conduct special membership meetings outside of the county in which the principal place of business of the credit union is located, but only if the credit union's bylaws so provide.
2. A credit union may allow the Board secretary to give notice of a special meeting more than 10 days after the request for the meeting is received, but only if the credit union's bylaws so provide.
3. A credit union must conduct its special membership meetings in accordance with rules of procedure approved by the Board. These rules should be adopted by reference in the credit union's bylaws or a Board resolution. Established rules of procedure should be utilized, such as *Robert's Rules of Order*.

Voting (RCW 31.12.386).

1. Credit union members may not vote by proxy at membership meetings.
2. The Board may permit members younger than 18 to vote, but only if the credit union's bylaws so provide.

Mergers (RCW 31.12.461)

The disappearing credit union in a merger may submit the merger proposal to its members at an annual or special membership meeting. Previously, the credit union had to submit the proposal for a vote at a special membership meeting.

Out-of-state and foreign credit unions (RCW 31.12.471)

1. Foreign credit unions (organized under the laws of other countries) may conduct business in Washington State, subject to the same requirements as out-of-state credit unions, with two additional requirements:
 - That a treaty with the country in which the foreign credit union is organized requires the Division to permit the credit union to conduct business here; and
 - That the foreign credit union has substantially the same characteristics as Washington State-chartered credit unions.
2. The Division may enter into agreements with out-of-state and foreign credit union regulators concerning the Washington laws that apply to such credit unions' Washington branches, and the laws of other states and countries that apply to branches of Washington credit unions in those states or countries.

Powers of credit unions

Generally (RCW 31.12.402).

1. In general, the powers of credit unions are clarified, and cross-references to sections dealing with specified powers have been added.
2. A credit union's outstanding aggregate borrowings may not exceed 50% of its total shares, deposits, and net capital.
3. A credit union may not sell all or substantially all of its assets without the prior approval of the Division. Previously, a credit union could not sell more than 10% of its assets without the prior approval of the Division.
4. The existing implied authority of credit unions is confirmed in several areas, including the authority to:
 - Procure for or sell to members group life, accident, health, and credit life and disability insurance.
 - Enter into agreements with other credit unions to foster their development.
 - Make charitable contributions in the communities in which they do business.

Investments (RCW 31.12.436).

1. Credit unions may invest in the listed investments, as long as they are deemed prudent by the Board.
2. The authority of credit unions to buy loans from other lenders is clarified. Note that NCUA rules at Part 741 restrict the purchase of certain loans by NCUA-insured credit unions.
3. A credit union may invest an amount up to 5% of its capital in organizations owned by the Washington Credit Union League.
4. A credit union may invest in credit union service organizations (CUSOs), whether or not the CUSO's ownership or membership is limited primarily to credit unions, as long as the primary purpose of the CUSO is to serve credit unions and their members. A credit union may invest in CUSOs an amount up to 2% of its assets (1% in CUSO stock; 1% in loans to the CUSO).
5. A credit union may invest in key person insurance, if the proceeds from the policy inure exclusively to the credit union.

Loans (RCW 31.12.426).

1. The requirement that credit unions document their loans in writing is eliminated. This change will allow for the use of document imaging and other technology. However, credit unions must ensure that loan documentation continues to be sufficient to support enforcement and collection of the loan, as well as review of the loan by the Division. Inadequate loan documentation may create safety and soundness issues.
2. Credit unions are no longer required to retain a percentage of loans that they sell.

Loans-to-one-borrower limit (RCW 31.12.428). Effective beginning July 1, 1998, a credit union cannot make a loan to a borrower if the aggregate of all loans (consumer and business) to the borrower will exceed an amount equal to 25% of the credit union's capital (a defined term). This provision applies only to loans made on or after July 1, 1998. There are certain exceptions to this limit - a credit union may make a loan to a borrower if the aggregate loans to the borrower do not exceed:

1. \$10,000; or
2. An amount which has been approved in advance by the Division.

Until July 1, 1998, the loans-to-one-borrower limit will continue to be 2.5% of assets. See pre-existing RCW 31.12.317.

Note that there is a separate loans-to-one-borrower limit on member business loans, which will continue in effect. See WAC 208-464-050. Consequently, member business loans must also satisfy this WAC limit.

Real property (RCW 31.12.438). The changes to this section confirm that a credit union may purchase property primarily for use in conducting its business. In addition, a credit union must put property purchased for future expansion into primary use within 3 years.

Statutory lien on member shares and deposits (RCW 31.12.416). The changes to this section confirm that credit unions have a statutory lien on shares and deposits for member obligations.

Supervisory Committee

Directors on Committee (RCW 31.12.326). A credit union's members may elect no more than one director of the credit union to serve on the Supervisory Committee at the same time, unless provided otherwise by the credit union's bylaws.

Duties

Attending Board meetings (RCW 31.1.335). At least one Supervisory Committee member may attend each Board meeting.

No more reports on special member meetings (RCW 31.12.195). Supervisory Committees no longer have to make a report to the Director of DFI on the outcome and conduct of special membership meetings.

Qualifications (RCW 31.12.065). A credit union must set forth in its bylaws any qualifications (other than statutory qualifications) for individuals to serve on the Supervisory Committee.

Suspension by Supervisory Committee (RCW 31.12.345).

The Supervisory Committee is no longer authorized to suspend officers.

Vacancies (RCW 31.12.326).

1. The Supervisory Committee must appoint an interim member to fill a vacancy on the Committee, unless the interim member would serve a term of fewer than 90 days.
2. Interim members serve out the unexpired term of the member they replace, unless the credit union's bylaws provide that interim members may serve only until the next annual membership meeting.

New Washington State Credit Union Act

Sections Repealed by Chapter 397, Laws of 1997

Section 88 of Chapter 397 repealed various RCW sections:

- RCW 31.12.095
- RCW 31.12.165 - However, the substance of this section was added to RCW 31.12.402.
- RCW 31.12.206 - This section permitted members to petition the Director of DFI to remove a majority of the Board.
- RCW 31.12.315 - This section required the credit committee or a loan officer to approve loan applications. Repeal will allow the prudent use of automated loan approval programs.
- RCW 31.12.355
- RCW 31.12.376 - In essence, this section defined “capital” to include all shares and deposits. The term has been redefined in the definition section (RCW 31.12.005) to include reserves, undivided earnings, and the allowance for loan loss.
- RCW 31.12.395 - However, the substance of this section was added to RCW 31.12.255.
- RCW 31.12.415
- RCW 31.12.455
- RCW 31.12.475 - However, the substance of this section was added to RCW 31.12.448.
- RCW 31.12.495 - However, the substance of this section was added to RCW 31.12.402.
- RCW 31.12.506 - This section limited operating expenses to a set percentage of assets.
- RCW 31.12.535 – However, the substance of this section was added to RCW 31.12.516.
- RCW 31.12.645 – However, the substance of this section was added to RCW 31.12.850.
- RCW 31.12.903
- RCW 31.12.904
- RCW 31.12.905
- RCW 43.320.125 – However, the substance of this section was added to RCW 31.12.516.

New Washington State Credit Union Act

Disposition Chart for Former Sections of Chapter 31.12 RCW Re-numbered by Chapter 397, Laws of 1997

<u>Old Chapter 31.12 Section</u> <u>(as of 12/31/97)</u>	<u>New Chapter 31.12 Section</u> <u>(as of 1/1/98)</u>
.037 .....	.407
.039 .....	.408
.045 .....	.382
.125 .....	.402
.136 .....	.404
.145 .....	.384
.155 .....	.386
.215 .....	.571
.295 .....	.388
.306 .....	.367
.317 .....	.428 (effective January 1, 1999)
.385 .....	.416
.406 .....	.426
.425 .....	.436
.435 .....	.438
.465 .....	.448
.485 .....	.418
.526 .....	.471
.635 .....	.850
.655 .....	.630
.665 .....	.633
.675 .....	.664
.685 .....	.667
.695 .....	.461
.705 .....	.464
.715 .....	.467
.720 .....	.890
.725 .....	.474
.735 .....	.860
.740 .....	.891