

Understanding Regulations

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Credit Union Laws and Regulations



Laws and Regulations

- **Federal Laws** – introduced as a bill. Becomes a law in one of three ways:
 - President signs the bill into law.
 - President doesn't sign within 10 days and doesn't return it to the House or Senate with objections.
 - Congress overrides the Presidential veto by a 2/3 majority vote.
- **State Laws** - similar to Federal Process.
- **Regulations** – clarify the laws that are passed. Help to ensure that all financial institutions adhere to the same guidelines in the same ways.



- **Bylaws** – *contract between the credit union and its members. Bylaws usually set forth the organizational structure of the credit union, membership requirements and business practices.*
- **Regulatory Opinion Letters** – usually in response to a specific scenario posed by the credit union.
- **Letters to Credit Unions** – provides general guidance on an issue the agency deems important or clarifies certain issues.



Who's responsible for what?

- **Board Members** – charged with setting the direction of the credit union (strategic planning, approving policies, etc.).
- **Management** – responsible for the day to day operations of the credit union and keeping on top of regulatory changes, making recommendations for policy changes when needed.
- **Regulators** – supervise, regulate, examine and sometimes insure credit unions. *The Regulator's purpose is to ensure the safety and soundness of the credit union and protect funds on deposit.*



- Policy – is an operating principle, a statement on how the credit union will conduct business.
 - Approved by the Board.
- Procedure – outlines the steps necessary to accomplish the policy.
 - Management drafts and approves procedures that implement the Board approved policies.



Prompt Corrective Action (PCA)

- Prompt Corrective Action (PCA) – sets forth disciplinary actions that must be taken when a credit union’s net worth falls to certain levels.
 - Net worth below 7% - major disciplinary action may be implemented. Disciplinary action may restrict asset growth or member business loans.
 - Net worth below 5% or less – additional actions may be necessary in cooperation with the NCUA and State Regulator if applicable. This may include the removal of Directors or Senior Management. Regulator approval for new branches, acquisition, new business, restrict CUSO activities, or limit dividends.

*Net worth is the amount which a credit union’s assets exceeds its liabilities. Net worth ratio is the net worth divided by total assets and is determined quarterly.



Prompt Corrective Action (PCA)

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TABLE 1 -- STATUTORY NET WORTH CATEGORY CLASSIFICATION

<i>A credit union's net worth category is . . .</i>	<i>if its net worth ratio is . . .</i>	<i>and subject to the following condition(s) . . .</i>
"Well Capitalized"	7% or above	And if "complex," meets applicable risk-based net worth requirement (RBNW)
"Adequately Capitalized"	6% to 6.99%	And if "complex," meets applicable RBNW
"Undercapitalized"	4% to 5.99%	Or if "complex," fails applicable RBNW
"Significantly Undercapitalized"	2% to 3.99%	Or if "undercapitalized" at less than 5% net worth ratio, fails to timely submit or materially implement a net worth restoration plan
"Critically Undercapitalized"	Less than 2%	None



Bank Bribery Act

- Prohibits any credit union official (employee officer, director, committee member, agent, or attorney) from giving, receiving or soliciting anything of value with the intent to influence or reward that official.
- Your credit union may have a Code of Ethics or Code of Conduct that addresses this. This code or policy should address a list of exceptions or acceptable gifts as outlined by the NCUA.
Exceptions to policy may be granted on a case by case basis after determining that the conflict or gift does not pose a threat to the safety or integrity of the credit union.



Supervisory Committee Audits and Verifications

- All federally insured credit unions are required to obtain an annual supervisory committee audit (usually delegated and conducted by a state licensed independent auditor in accordance with Generally Accepted Accounting Standards (GAAS)).
- The supervisory committee is also responsible for the verification of accounts, this can also be delegated to a licensed auditor according to GAAS.



Bond and Insurance Coverage

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- Fidelity Bonds - cover fraud and dishonesty by any credit union employee, director, officer, and supervisory committee or credit committee member.
- All credit unions are required to have insurance coverage in addition to the fidelity bond.
- Failure to maintain adequate bond and insurance coverage may result in cancellation of the credit union's share insurance.



Security Program

- Every federally insured credit union is required to maintain a security program. The program should:
 - Protect the credit union from robberies, burglaries, larcenies, and embezzlement;
 - Ensure the security and confidentiality of member records;
 - Protect against unauthorized access to or use of member records;
 - Assist in the identification of persons who commit or attempt such actions or crimes; and
 - Prevent destruction of vital records.



Bank Secrecy Act (BSA)

- The BSA requires credit unions to develop and maintain records regarding certain transactions. Credit unions must file reports on currency transactions that exceed certain limits or when the credit union notices suspicious activity on an account.
 - Currency Transaction Report (CTR) – filed if cash transaction are over \$10K
 - Suspicious Activity Report (SAR) – filed when suspicious activity is identified.



- The Board is required to approve the BSA Compliance Program. At a minimum, the program should have the following:
 - System of internal controls to ensure compliance.
 - Designation of a BSA Officer.
 - Provide for an ongoing training program.
 - Provide for independent testing for compliance.



Incidental Powers

- Incidental Power is
 - an activity that is necessary or requisite to enable the credit union to effectively carry on its business;
 - is convenient or useful in carrying out the mission or business of credit unions consistent with the Federal Credit Union Act;
 - is the function equivalent or logical outgrowth of activities that are part of the mission or business of credit unions;
 - and involves risk similar to those already assumed as part of the business of credit unions.

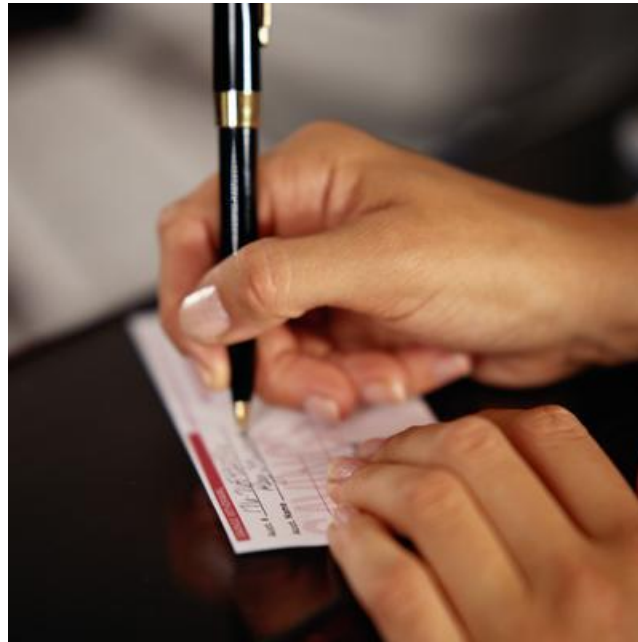


Incidental Powers

- Financial Institutions continue to evolve, members wants and needs for financial services have also changed. Credit unions are able to meet member demands by offering products and services through the incidental powers regulation.
 - Electronic Financial Services
 - Equipment and Employees
 - Financial Counseling Services
 - Loan Related Products
 - Marketing



Deposit Regulations



- Requires certain disclosures be given to members when opening accounts or on request. Disclosures contain:
 - Rates
 - Fees
 - Other terms and conditions relating to the credit union's account
- *This regulation applies to all credit unions (regardless of insurance)* and provides consistency across all types of financial institutions so consumers can make informed deposit decisions based on uniform calculations and disclosures.



Privacy – Information Sharing

- Financial Institutions are required to disclose to consumers what information they collect, what information is shared and with whom the information is shared.
- Examples of information sharing:
 - ATM transactions, credit card use and check clearing – information is shared to perform transactions for members.
 - Search warrants, subpoenas, filing information returns with the IRS or state tax authority.
 - CUSO, such as brokerage services.
- *The Board should require that all vendor contracts have a confidentiality clause that specifies permissible uses for member information provided by the credit union.*



- Regulation CC governs the guidelines for check holds.
- Credit Unions must adopt a Regulation CC or Funds Availability policy and disclose this policy to members.
- The policy outlines how long the credit union intends to hold funds deposited in member accounts before the funds can be withdrawn or used to write checks.



Reserve Requirements

- The Federal Reserve requires depository institutions to maintain reserve accounts that can be called on to cover checks outstanding in the case the institution becomes insolvent.
- Reserve requirements are based on the amount of money in transaction accounts, such as checking accounts.
- Other accounts referred to as Regulation D accounts, limit transactions (6) – Money Market Accounts.



Electronic Funds Transfer

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- Any transfer of funds initiated through an electronic terminal, telephone, computer, or magnetic tape that orders, authorizes or instructs the credit union to deposit or withdraw from a member's account is considered an electronic fund transfer (EFT).
- *This includes transactions conducted through point-of-sale terminals used in retail stores, ATMs, direct deposits or withdrawals (including payroll deduction), and audio response and debit card transactions.*



Share Insurance for Federally Insured Credit Unions

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- Federal share insurance gives NCUA the authority to examine federally-insured state-licensed or chartered credit unions for safety and soundness.
- Being federally insured means that member accounts are backed by the full faith and credit of the US Government.
- “Federally insured by NCUA” in advertisements.



Lending Regulations



Equal Credit and Fair Lending

- Regulation B implements the Equal Credit Opportunity Act and Fair Housing Act which strictly prohibit discrimination against applicants who fall into certain protected classes.
- Classes are: race, color, religion, national origin, sex, marital status, age, receipt of income from public assistance and the exercise of an applicant's rights under the Consumer Credit Protection Act.
- Regarding housing related loans, the Fair Housing Act also protects applicants from discrimination on familial status (children under the age of 18) or handicap.



- Covered lenders record certain information about dwelling related applications and loans and update the Loan Application Register (LAR) quarterly.
- Data is reviewed by consumer groups and examiners to determine if a lender may be discriminating against applicants in protected classes.



Consumer Leasing

- Consumer Credit Protection and Regulation M protect consumers who lease personal property (usually auto leases for Credit Unions).
 - Ensures consumers receive meaningful disclosures that allow them to compare lease terms among companies.
 - Limits the amount of a balloon payment at lease end.
 - Provides for accurate disclosure of lease information in advertisements.



- *Regulation Z implements the Truth in Lending Act (TILA). TILA was designed to promote the informed use of consumer credit by requiring specific disclosures regarding:*
 - The terms and cost of credit
 - The right to rescind (applies to certain loan transactions secured by principal dwelling)
 - The calculation of loan interest.



NCUA Lending Regulations

- **Incentives** – certain employees can be paid commissions or incentives (except senior management) in connection with a loan if the Board has adopted written policies, established internal controls for the program and reviews annually.
- **Non-preferential Treatment** – Loans made to the Board, supervisory committee and credit committee members and their family (same household) or business partners must be made on same terms and conditions available to the general membership.
- **Written Lending Policies** – Adequate documentation and protection of security interest, capacity to repay and determination of value.



Member Business Loans (MBLs)

- MBL – a loan primarily for commercial or corporate use, business investment property or venture, or agricultural purpose not meeting the exemptions below.
- **Exemptions:**
 - Loan amount (aggregated with all other business purpose loans by same member or group of members) does not exceed \$50,000.
 - The loan is secured by a lien on the member's principal dwelling.
 - The loan is secured by shares.
 - The loan is guaranteed by a federal or state entity (for example, the Small Business Administration or similar program.).



Appraisal Regulations

- All federally insured credit unions are subject to NCUA's appraisal regulation.
- Regulation requires the credit union to have a written appraisal for loans secured by real property.
- There are several exemptions including loans of less than \$250,000.
- Credit unions that make real estate loans that could be sold in the future on the secondary market are subject to the appraisal requirements set by institutional investors such as Fannie Mae and Freddie Mac.



- All federally insured credit unions are subject to NCUA requirements to obtain a flood hazard determination on applications to make, extend, renew or increase loans secured by a building attached to real property.
- If the credit union determines that the property is located in a flood hazard area, the loan cannot be made until the borrower obtains flood insurance.



Homeowners Protection Act

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- Credit unions and other lenders sometimes require Private Mortgage Insurance (PMI) on certain loans when the amount is high (above 80 or 90%) compared to the value of the property.
- The Homeowners Protection Act requires specific termination procedures and notices regarding the rights of the borrower with regard to cancellation of PMI.



Real Estate Settlement Procedures Act (RESPA)

- RESPA contains numerous disclosures, accounting, and notice requirements to alert consumers to the true cost of a mortgage loan.
- Credit unions are required to provide:
 - A good faith estimate of the fees and charges.
 - A booklet produced by HUD about mortgage loan costs and charges.
 - A settlement statement at the time the loan is funded that specifies the fees and charges the borrower paid or financed in connection with the loan.



Servicemembers' Civil Relief Act

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- Entering active duty in the military provides a member with certain benefits under law.
- Member must show that military service created a “material effect” on the member’s circumstances in question.
 - Member has the ability to have their interest rate lowered on their debt incurred prior to entering active duty to 6%.
 - Eviction action may be delayed and repossessions and foreclosures may not go forward against the member on active duty.



Miscellaneous Regulations



Credit Union Service Organizations (CUSOs)

- CUSOs are formed by credit unions, sometimes with non-credit union parties to provide services primarily to credit unions or credit union members.
- The CUSO is a separate legal entity, with a separate board of directors and separate accounting.
- Independence is important so that problems or liabilities of the CUSO cannot revert to the credit union.



- State and federal credit unions that serve predominately low income members may apply to the program for a loan (up to \$300,000).
- Credit unions can use these funds – repayable in 5 years, to provide basic financial and related services to residents and stimulate economic activities in their communities.



- Federally insured credit unions are required to maintain a records preservation program to identify, store, and reconstruct vital records in the event that the credit union's records are destroyed.
- Vital records are considered permanent records and consist of members' share and loan accounts, credit union financial reports, including assets, liability accounts, and bank reconcilements, and a list of the credit union's financial institutions, insurance policies and investments.



Credit Union Conversions

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- Federal or state chartered? Credit unions have the option of switching charters.
 - Board of directors must approve.
 - Membership must vote.
 - New regulator reviews the credit union's business plan to assess whether the conversion will benefit members and prospective members.
- Credit union to mutual savings bank.
 - NCUA regulations part 708a.



- Once a merger partner is selected, the boards of both credit unions must give preliminary approval.
- Merger plan must be developed – requirements for the merger plans are set out in federal regulations or by the state regulator.
- Membership votes at the annual meeting or a special meeting called for that purpose.



Liquidation

- **Voluntary liquidation** – usually occurs when there is a lack of adequate leadership, management or member support (usually a merger partner is sought out).
- **Involuntary liquidation** – ordered by the credit union's regulator. Usually at this point all possibilities for merger or assumption by another credit union have been pursued.



Compliance Program

- *The credit union Compliance Program should emphasize a commitment to observe the laws, rules and regulations that affect the credit union's operations.*
- Compliance Programs vary based on the size and complexity of the credit union's program.
- Individuals responsible for compliance should have sufficient authority to report to senior management, including the president or CEO.



- The Compliance Officer should:
 - Review new products and services.
 - Train staff or assist in the development of training programs to ensure compliance.
 - Monitor changes in laws and regulations.
 - Develop, review and modify policies and procedures.
 - Review forms, marketing materials and electronic services.



Questions?

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- What questions do you have?
- Thank you for participating!!!!

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