

Legislative Analysis



REVISIONS TO CREDIT UNION ACT

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<http://www.house.mi.gov/hfa>

House Bill 5017 as enacted
Public Act 152 of 2016
Sponsor: Rep. Anthony G. Forlini

Analysis available at
<http://www.legislature.mi.gov>

House Bill 5018 as enacted
Public Act 153 of 2016
Sponsor: Rep. Peter Pettalia

House Bill 5020 as enacted
Public Act 155 of 2016
Sponsor: Rep. Lana Theis

House Bill 5019 as enacted
Public Act 154 of 2016
Sponsor: Rep. Paul Clemente

House Bill 5021 as enacted
Public Act 156 of 2016
Sponsor: Rep. Tom Barrett

House Committee: Financial Services
Senate Committee: Banking and Financial Institutions
Revised 3-28-19

SUMMARY:

House Bills 5017 to 5021 make general amendments to the Credit Union Act, the act that provides for the organization, operation, regulation, and supervision of credit unions.

In each bill in the package, the term “commissioner” is replaced by “director” in provisions reflecting the creation of the Department of Financial and Insurance Services (DIFS). Among other things, the bills do the following:

House Bill 5017 establishes the Credit Union Regulatory Fund and makes numerous changes to the regulation of credit unions, as well as modernizing defined terms.

House Bill 5018 addresses the supervision of domestic credit unions and bylaws.

House Bill 5019 addresses the authority to organize or invest in service organizations that provide trust and other services.

House Bill 5020 revises the examination process by the department.

House Bill 5021 deals with credit union mergers.

The bills took effect September 7, 2016, and are described in greater detail below.

House Bill 5017

Regulatory Fund

House Bill 5017 creates the Credit Union Regulatory Fund. The fund consists of fees, civil or administrative fines, and any other money collected under the act (except for fines imposed for violation of section 217); money appropriated to the fund; donations to the fund from any source; and interest and earnings from fund investments. Money in the fund at the end of a

fiscal year remains in the fund and does not revert to the state's general fund. Upon appropriation, DIFS is to use the money in the fund only for credit union regulatory purposes. DIFS is the administrator of the fund for auditing purposes. The state treasurer directs the investment of the fund.

Delegation of Board Duties

Under the act, the board of a credit union is required to perform certain duties. The bill says that if a credit union board delegates a duty to the general manager or chief executive officer, and either one acts pursuant to that delegation, the general manager or chief executive officer must provide a summary of the actions taken to the credit union board at the next regularly scheduled meeting of the credit union board.

In addition, the bill newly allows the delegation of the following: establishing the minimum individual shareholdings of members; acquiring, selling, or encumbering real property; borrowing money; fixing the amount of surety bonds for all officers and employees who handle money; and specifying forms and procedures for applications for membership and setting criteria for use in determining whether to accept an applicant into membership.

Reimbursement and Insurance for Board Members, etc.

The act says, generally, that board and committee members shall not receive compensation for their service. Under the bill, a domestic credit union may provide reasonable life, health, accident, disability, or similar insurance protection, and reimbursement for reasonable expenses that are incidental to the performance of official business of the credit union, to board members, associate board members, supervisory committee members, and credit committee members, as well as to members of other committees that perform significant ongoing functions related to credit union operations.

Board Meetings

Under the bill, the board of a domestic credit union must meet at least six times in each calendar year and at least every other month. The board must meet in person or by means of electronic communication devices that enable all participants in a meeting to communicate with each other.

Associate Board Members

In addition to the credit union board members currently required under the act, the board of a domestic credit union may appoint one or more associate board members. All of the following apply concerning associate board members:

- A credit union board in its discretion determines whether to appoint associate board members, the number of associate board members, if any, and their duties. The credit union board has authority concerning the appointment and removal of individuals as associate board members.
- A credit union board may not appoint an individual as an associate board member who does not meet the eligibility requirements described in the act for board members.
- An individual appointed as an associate board member serves in an ex officio capacity. An associate board member may participate in meetings of a credit union board, but only in an advisory capacity; has no authority to vote or act as a board member; and is not considered a board member for purposes of the act.

- An associate board member must sign a confidentiality agreement to ensure that any information concerning the credit union remains confidential. Disclosure of confidential information by an associate board member without approval of the director is a violation of the act.

Board Member Oath

The bill specifies that the oath taken when a board member is first elected or appointed to the credit union board, to diligently and honestly perform the duties of the office and not knowingly violate any provisions of the act, remains in effect as long as the board member remains in office.

Supervisory Committee Vacancies

The bill specifies that an individual appointed to fill a vacancy on the supervisory committee serves for the remainder of the term of the vacant position.

Termination of Membership

The bill allows the general manager or chief executive officer of a domestic credit union (rather than, as previously, the board), or a designee, to suspend some or all services to a member, or terminate the membership of any person that causes loss to a credit union; commits fraud or another misdeed against the credit union; engages in inappropriate behavior involving another individual, such as physical or verbal abuse of another member or an employee. (These last two are new offenses in the act.)

A member that has services suspended or a person that has its membership terminated may appeal the suspension or termination to the credit union board within 90 days after the date of the suspension or termination. The credit union board has final authority to resolve an appeal.

Domestic Credit Union Powers

The act allowed a credit union to purchase the assets of another domestic credit union and, with state approval, assume any of the liabilities of another credit union. The bill instead allows the purchase of assets and assumption of liabilities of another “depository institution.”

Under the bill, an agreement to acquire and hold buildings or land jointly with other credit unions or financial organizations requires prior approval of the director. The director must act on a completed application within 30 days after it is filed.

The act specifies that a domestic credit union’s investments or contractual obligations, direct, indirect, or contingent, in land and buildings may not exceed 5% of its assets without the approval of the commissioner. Under the bill, prior approval is not required if all of the following are met:

- Pro forma projections over the next three years are reasonably estimated to provide positive earnings and document the ability of the credit union to meet its short- and long-term liquidity obligations.
- The director determines that the credit union is well capitalized.
- The credit union has not been the subject of a cease and desist order or placed in receivership or conservatorship by the director within the preceding three years.
- The director determines that the credit union is in overall sound and fundamentally sound condition.

The act allows domestic credit unions to make charitable contributions, if the individual contributions and the aggregate amount of the contributions are reasonable. The bill also allows a credit union to establish charitable donation accounts if those accounts meet the requirements of the federal National Credit Union Administration Act. Investment yields generated in a charitable donation account must be used for charitable donations. The credit union must notify the director before it establishes a charitable account.

The bill allows a credit union to do any of the following in an underserved area or for someone who does not have an established relationship with a financial institution: provide financial counseling; provide educational scholarships; and invest in interest rate derivatives for mitigating portfolio risk. The credit union must notify the DIFS director at least 60 days before it begins a program to invest in interest derivatives. A domestic credit union must conduct such an investment program in a safe and sound manner. Any investment in interest rate derivatives must meet standards for an obligation specified in the act.

Automated Information Processing Services

Under the act, a domestic credit utilizing automated information processing services of a vendor must enter into a written contract agreement for those service. The bill eliminates the extensive provisions in the act governing such contracts and instead says that any vendor or subcontractor that has access to confidential member information is subject to regulation and examination by the director.

Domestic Credit Union Insurance Program

Under the bill, before a domestic credit union makes an insurance program available to its members, it must conduct a reasonable due diligence review of the product. The credit union must provide the director access to any files that are relevant to that review on request. (This replaces similar language in the act.)

Loans to Officers and Management

The act says the credit union may not make a loan or extend a line of credit if an official or senior management employee will receive a commission, fee, or compensation other than salary if the loan or line of credit is approved. Under the bill, this provision does not limit or prohibit arrangements that compensate employees who are not senior management employees based on the volume of loans generate by those employees. The bill also says that the DIFS director may not impose any additional limitations on the authority of a domestic credit union to review a loan application of, or approve or deny a loan to, an official of the credit union that do not apply to member loans generally.

Borrowing Limit

Under the bill, a credit union may not loan an amount that exceeds 25% of the credit union's unimpaired capital to a borrower. Previously, this provision referred to \$20,000 or 25% of its net worth, whichever was greater. However, the following apply for purposes of this section:

- If the director determines at any time that the interests of a group of more than one person are so interrelated that they should be considered as a unit for which credit is extended, the total loans and extensions of credit and leases of person of that group are combined and considered loans and extensions of credit and leases to one borrower.
- A credit union does not violate the section solely because the indebtedness of a group exceeds the percentage limitation at the time of a determination by the director that the

indebtedness of that group must be combined. However, it is a violation of this section if the credit union does not do one of the following:

- If required by the director, within a ***reasonable time***, dispose of a sufficient amount of the indebtedness of the group so that the amount of the remaining indebtedness is within the percentage limitation. ***Reasonable time*** means a period of time that the director determines reasonable and, if the credit union is making a reasonable effort to dispose of the excess indebtedness in a manner designed to avoid a loss of any portion of that excess indebtedness, is a period of at least 180 days.
- If permitted by the director, if the credit union is well capitalized, establish a reserve in the amount that the group's indebtedness exceeds the percentage limitation rather than disposing of the excess amount.

Non-Member Borrowers and Co-Signers

As additional security for a loan transaction with a borrower, a credit union may permit a person that is not a member to act as an additional borrower or a cosigner or guarantor of the loan.

Investments that Become Impermissible

The bill says that if a domestic credit union invests funds in a security, obligation, or other instrument that at the time is permitted under the act, but the investment subsequently becomes impermissible because of a change in circumstances or law, and the director finds that continuing to hold the investment will have an adverse effect on the safety and soundness of the credit union, then the director may require the credit union to develop a reasonable plan for the divestiture of the investment.

Sale or Pledge of Member Obligations

Under the act, a credit union may sell all or part of an obligation of a member if the sale meets the conditions of the sale policy adopted by the credit union board and if the board approves the sale. The bill allows senior management employees to approve the sale if the board has delegated such authority in a written board policy.

A domestic credit union may pledge all or any part of an obligation of a member. The bill requires such a pledge to meet the conditions of the pledge policy adopted by the board and the pledge to be approved by senior management employees to whom the board has, in written board policy, delegated the authority to approve pledges. If one or more pledges are approved by a senior management employee, he or she must provide a summary of the pledges to the credit union board at the next regularly scheduled board meeting.

Branch Location and Employee Titles

A credit union must provide written notice to the director seven days before the change of its principal location. If the name of the title of an official senior management employee changes, the credit union must provide it to the director within seven days after the change.

Definition of "Branch"

The bill specifies that the term "branch" does not include elementary, middle, or high schools where an employee or agent of a credit union only accepts deposits; electronic funds transfer facilities that are made available to two or more depository institutions; a loan production office; or a mobile office.

House Bill 5018

The act allowed a credit union to conduct its business solely by mail or through electronic communication without having a physical location where members transact business with the credit union if the commissioner gave prior approval.

The bill allows this if the credit union gives prior written notice.

House Bill 5019

Under the act, a domestic credit union may organize, invest in, or loan money to one or more credit union service organizations that engage in providing certain products or services to credit unions as specified in the act. House Bill 5019 also applies to service organizations that engage in investment administration and other services related to small business equity interests or venture capital fund investments if all of the following are met:

- The target small business for a specific equity investment is a member of at least one of the credit unions that have an ownership or investment interest in the credit union service organization; has its principal office in this state; and either more than 50% of its assets are in this state or more than 50% of its employees are employed in this state.
- Any venture capital fund established or funded by the credit union service organization provides an amount equal to at least 51% of its available funds to member small businesses that have their principal offices in this state or more than 50% of their employees employed in this state.
- A credit union's aggregate investment in the credit union service organization that is offering small business equity and venture capital investment services does not exceed 10% of the credit union's net worth.
- None of the officers or directors of the credit union that have an ownership interest or an investment in a credit union service organization hold an equity position in any small business financed by that credit union service organization.
- A credit union that is an owner or investor in the credit union service organization must ensure that it has enacted and complies with policy guidelines for outstanding obligations, which the bill delineates in detail.

Under the act, a domestic credit union may organize, invest in or loan money to one or more credit union organizations that engage in providing products and services as specified in the act. House Bill 5017 further allows trust services if either of the following is met:

- The credit union service organization is a state bank or state foreign bank with trust powers under the Banking Code, is a savings bank with trust powers under the Savings Bank Act, or is authorized to act as a fiduciary in Michigan under the Banking Code.
- The credit union service organization is providing the trust services as a host bank under an agreement described in the Banking Code.

Under the act, a credit union service organization must agree in writing to obtain an audit from a certified public accountant at least annually and provide a copy of each audit report to the domestic credit union. House Bill 5019 says that this provision does not apply to a credit union service organization that is consolidated for financial reporting purposes if the consolidated audit program is sufficient to provide reasonable and appropriate coverage to sufficiently test the credit union service organization's financial records.

The bill defines the following terms as follows:

Equity interests means limited partnership interests and other equity investments in which liability is limited to the amount of the investment, but does not include general partnership interests or other interests that involve general liability. The term could include subordinated or convertible debt.

Small business means a corporation, partnership, limited liability company, proprietorship, or other entity formed under the laws of the United States, or a state, district, or other territory of the United States that meets the appropriate United States Small Business Administration (SBA) definition of small business and that is principally engaged in the development or exploitation of inventions, technological improvements, new processes, or other products that previously were not generally available in this state or in making other investments that provide an economic benefit to this state.

Venture capital fund means a limited liability entity formed under the laws of the United States, or a state, district, or territory of the United States whose principal business is or will be making investments in and providing significant managerial assistance to businesses that meet the SBA definition of small business.

House Bill 5020

Under the act, the commissioner or an authorized agent must examine the condition and affairs of each domestic credit union, and may examine the condition and affairs of any subsidiary of a domestic credit union, not less frequently than once every 18 months.

The bill says that any document, material, or information (“information”) related to an examination under the act is confidential by law and privileged, is not subject to the Freedom of Information Act, is not subject to subpoena, and is not subject to discovery or admissible in evidence in any private civil action. However, the director may use the information to further any supervisory activity or legal action brought as part of his or her duties. The director, or any person that received information while acting under the director’s authority, may not, and cannot be required to, testify in any private civil action concerning confidential information.

To assist in the performance of his or her duties, the director may do any of the following:

- Share information, including confidential information, with state, federal, and international regulatory agencies or law enforcement authorities, provided that the recipient agrees to maintain the confidentiality and privileged status of the information.
- Receive information, including otherwise confidential information, from regulatory and law enforcement officials of other foreign or domestic jurisdictions. The director must maintain as confidential or privileged any information received with notice or the understanding that the information received is confidential or privileged under the laws of the jurisdiction that is the source of the information.
- Enter into agreements governing the sharing and use of information that are consistent with the act.

The disclosure of any information to the director, or the sharing of information, is not a waiver of any privilege applicable to or claim of confidentiality in the information.

The bill allows the director to release final, adjudicated actions that are open to public inspection under the Freedom of Information Act to a database or other clearinghouse service maintained by the National Credit Union Administration or its affiliates or subsidiaries.

A person to which confidential and privileged information is disclosed may not further disseminate that confidential and privileged information.

Any person on which a demand for production of confidential and privileged information is made, whether by subpoena, order, or other judicial or administrative process, must withhold production of the confidential and privileged information and must notify the director of the demand. If the director is notified of such a demand, the director may intervene for the purpose of enforcing the limitations of these provisions or seeking the withdrawal or termination of the attempt to compel production of the confidential and privileged information.

Any request for discovery or disclosure of confidential and privileged information, whether by subpoena, order, or other judicial or administrative process, must be made to the director, and the director must determine within seven days whether to disclose the information. If the director determines not to disclose the information, the decision is subject to judicial review.

The judicial review of a decision of the director may include in camera review of the confidential and privileged information. After such review, a court may order disclosure only of the portions that are relevant and otherwise unobtainable by the requesting party. The director may immediately appeal any court order that compels disclosure of confidential and privileged information, and the order is automatically stayed pending the appeal.

In a report or an addendum of the report of the examination, the director or an authorized agent may suggest best practices or other improvements in the operation of the credit union that are not required by law or required to address the safety and soundness of the domestic credit union. The manner in which a credit union addresses issues concerning the operation of a domestic credit union are within the discretion of the credit union, except as required by law or to address a concern over the safety and soundness. The director may not take action against a domestic credit union based on a failure or refusal to follow a best practice or other suggested improvement that is suggested informally or in an addendum to a report of examination.

By September 7, 2017, the director must issue guidance to promote consistency and due process in the examination process, including at least establishing guidelines that define the scope of the examination process and clarify how issues will be resolved.

House Bill 5021

Under the act, two or more domestic credit unions may merge into one of the credit unions or into a newly formed domestic credit union if certain conditions are met. The act requires the members of each constituent credit union to approve the plan of merger at a special membership meeting or by mail ballot. If the vote is held at a special meeting, the credit union board must provide each member with written notice of the meeting at least 10 days and not more than 30 days before the meeting. The bill instead requires notice at least 7 days and not more than 30 days before the meeting.

The bill also eliminates a provision that prohibited the director from accepting a certificate of merger if an effective date was specified that was more than 90 days after the date of filing.

FISCAL IMPACT:

The bills would not have a significant fiscal impact on DIFS for the following reasons:

- Most of the amendments to the act within the bills would not affect the implementation, administration, or enforcement of the act, and those that would, would likely only nominally impact DIFS expenditures (e.g., costs of promulgating new rules, publishing new guidance, revising standardized forms, training staff about changes).
- The “base fee” that the act authorizes DIFS to establish and that is utilized to calculate the annual operating fees levied on credit unions is currently within statutory limitations (\$2.10 in FY 2015, subject to a maximum of \$3.50); accordingly, any increases in DIFS expenditures could be sufficiently offset with revenue generated via increased annual operating fees.

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■ This analysis was prepared by nonpartisan House Fiscal Agency staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.