

7535-01-U

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Organization and Operations of Federal Credit Unions

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is amending its field of membership rules regarding service to underserved areas to limit underserved area additions to multiple common-bond credit unions and revise facility requirements for underserved areas. These amendments are being made after a comprehensive review of chartering policy based upon NCUA's experience addressing field of membership issues and the uncertainty resulting from recent litigation challenging service to underserved areas in Utah and the current ambiguity in the Federal Credit Union Act on this issue. This final rule will ensure continued reliable and efficient service to federal credit union members located in approved underserved areas and continue to allow multiple common-bond credit unions to add underserved areas to their charters. The final rule generally adopts the amendments as proposed. In

addition, the final rule retains the definition of service facility as a credit union owned facility where shares are accepted for members' accounts, loan applications are accepted, and loans are disbursed.

DATES: Effective July 28, 2006.

FOR FURTHER INFORMATION CONTACT: Michael J. McKenna, Deputy General Counsel, John K. Ianno, Senior Trial Attorney, or Regina Metz, Staff Attorney, Office of General Counsel, 1775 Duke Street, Alexandria, Virginia 22314 or telephone (703) 518-6540.

SUPPLEMENTARY INFORMATION

A. Background

NCUA's chartering and field of membership policy is set out in NCUA's Chartering and Field of Membership Manual (Chartering Manual), Interpretive Ruling and Policy Statement 03-1. 68 FR 18333, Apr. 15, 2003. The policy is incorporated by reference in NCUA's regulations at 12 CFR 701.1. On December 29, 2005, the NCUA Board issued a moratorium suspending that portion of its chartering policy allowing non-multiple-common-bond credit unions to add new underserved areas. After establishing a moratorium, the NCUA conducted a comprehensive review of its underserved area policy.

On January 19, 2006, the NCUA Board approved a proposed rule regarding service to underserved areas. 71 FR 4530, Jan. 27, 2006. The NCUA proposed two amendments that would apply only prospectively. The first proposed change was to limit the addition of new underserved areas to only multiple common-bond credit unions. The second proposed change was to the definition and location of the service facility. When adding underserved areas, NCUA proposed requiring a physical presence in the underserved areas to assure better service to members in these locations and deleting the choice of a credit union owned electronic facility with certain functions as a service facility.

B. Comments

NCUA welcomed general comments on the proposed rule and also on all aspects of NCUA's rules on credit unions serving underserved areas. In addition to seeking general comments on the proposed rule, the Board specifically sought comments on a series of questions related to the impact of the proposed changes on consumers and credit unions. The comments were intended to assist the Board in understanding what, if any, impact the proposed changes would have on credit unions that have expended resources investing in underserved areas. The Board is concerned that there is both financial and reputation risk if credit unions, previously authorized to operate in underserved areas, are prohibited from continuing to do so. The Board is also concerned that the proposed changes could limit the ability of credit unions to grow and expand services into underserved areas and provide needed financial assistance to

consumers of modest means who do not currently have access to low cost financial services and undermine the viability of the federal credit union charter.

NCUA received 49 comment letters in response to the proposed rule: 31 from federal credit unions, one from a state-chartered credit union, 12 from credit union trade organizations, three from bank trade organizations, one from an individual, and one from an institute. Most credit union commenters opposed the proposal and support the status quo. One commenter believes the proposal contradicts congressional intent by only allowing multiple common-bond credit unions to add underserved areas. In contrast, some credit union commenters appreciated NCUA's concerns and supported the proposal. Whether opposed to or in favor of the proposal, most credit union commenters support a legislative solution amending the Federal Credit Union Act to expressly state that all federal credit unions may add underserved areas. Bank trade group commenters generally supported the proposal and, in some cases, recommended further requirements for credit unions serving underserved areas.

The NCUA Board asked for specific comments on the following five questions.

- 1) NCUA's authority to permit expansions into underserved areas for all three federal charter types.

With the exception of the bank trade groups, almost all commenters expressed the opinion that NCUA has the authority to allow all three charter types to add underserved areas. Six commenters support the continuation of the moratorium and understand the basis for NCUA's proposal in this area given the current litigation. Almost all credit union commenters suggest that NCUA seek a statutory change to the Federal Credit Union Act in order to insert express language authorizing this activity.

Credit unions are leaders among financial institutions in providing affordable financial services to persons within their specific field of membership, including people of modest means. The Board is committed to assuring that credit unions have the regulatory tools necessary to perform this important role. One of the primary purposes of the Credit Union Membership Access Act (CUMAA) was to codify the legality of multiple common-bond credit unions. CUMAA also reflects Congress' intent to clarify that this new charter type was authorized to add underserved areas. Unfortunately, the statutory language does not expressly provide that authority to the other two charter types although there is legislative history that indicates Congress intended that all types of federal credit unions should be able to add underserved areas. This absence of specific statutory language, when considered together with the specific authorization for multiple common-bond credit unions, creates uncertainty about the continued authority of non-multiple common-bond credit unions to serve underserved areas. Though most commenters argued that the Board has the authority to authorize the other

charter types to serve underserved areas, they provided no persuasive argument to address the issue created by the absence of any specific statutory language. In addition, recently the American Bankers Association and others have filed litigation challenging the authority of a non-multiple common-bond credit union to serve underserved areas in Utah.

In light of this uncertainty, the Board is amending its chartering policies to allow only multiple common-bond credit unions to serve underserved areas pending clarification of the language contained in the Federal Credit Union Act that authorizes the addition of underserved areas. The amendments to the chartering policy will apply only prospectively. The NCUA Board agrees a statutory change is necessary.

2) The impact of limiting expansions into underserved areas to only multiple common-bond credit unions.

Several credit union commenters described the negative impact on both credit unions and consumers of limiting underserved expansions to multiple common bond credit unions. Commenters wrote that low-income individuals and those who most need credit union service will receive less service. A couple of commenters wrote that there will be less competition. One commenter said there will be a negative impact on the dual chartering system and that some federal credit unions will convert to state charters.

The Board agrees that restricting further expansions has the potential to limit the availability of credit union services to some consumers. Nevertheless, the Board has concluded that there are many opportunities for continued growth and expanded service to consumers within existing fields of membership, even with a change to chartering policies limiting prospective addition of underserved areas to multiple common-bond credit unions. The Board concludes that the ambiguity arising from the statute as well as the current litigation outweighs the potential harm to credit unions and potential members.

3) Whether, if only multiple common bond credit unions are permitted to add underserved areas, they should be permitted to retain these areas in the event they change charter type.

Almost all credit union commenters who commented on this issue support permitting multiple common-bond credit unions to retain their underserved areas if they change charter types. The banking trade group commenters oppose credit unions retaining the areas.

Given that the final rule will not permit non-multiple common-bond credit unions to serve underserved areas, the Board concludes that, upon conversion to another charter type, the restrictions applicable to the new charter type must apply. Therefore, a multiple common-bond credit union converting to either a

single common-bond or community charter would be required to give up its underserved areas. The credit union could continue to serve its existing members. This approach is faithful to the requirements of this final rule which prospectively permits only multiple common-bond credit unions to serve underserved areas. It is also consistent with the approach taken when a multiple common-bond credit union converts to a community credit union. In those circumstances, a credit union must comply with the requirements of the new charter type and relinquish its select employee groups.

The Board is aware that certain unpredictable factors, such as economic downturns and plant closings, could cause a multiple common-bond credit union to convert its charter type. While the loss of underserved areas in these circumstances may seem harsh, the Board concludes that the credit union must balance the potential impact of the loss with other factors relevant to a decision on its charter type. Part of the consideration regarding whether a charter change makes good business sense should necessarily include the fact that, once a multiple common-bond credit union changes its charter, it will lose its underserved areas.

4) The type and extent of existing investment by non-multiple common bond credit unions in underserved areas including for example, capital investment, loans, share deposits, and other programs targeting low income people.

The Credit Union National Association, a credit union trade group, provided a comprehensive list of investments by non-multiple common-bond credit unions in underserved areas. Credit unions described investments in branch offices and ATMs, their involvement through loans, deposit products, services, and community involvement and charitable services in underserved areas. This information is discussed further in connection with question 5 below.

5) The impact to members of underserved areas, and non-multiple common-bond credit unions, of restrictions on the addition of new members in underserved areas they are currently serving.

Almost all credit union commenters on this question believe the restrictions would have a negative impact. A few credit unions wrote they might have to close branches and would suffer economic loss. Several credit unions requested they be “grandfathered” so that they can continue to add new members from the underserved areas they currently serve.

The information provided establishes that many credit unions have invested significant funds, totaling in excess of 400 million dollars, and other resources into serving more than 800 underserved areas. This investment includes the establishment of hundreds of branches in and near underserved areas. Activity by credit unions in these areas indicates the significance of their services to their

financial well being and the needs of their membership. It includes billions of dollars in loans and share deposits.

Generally, regulations are prospective in nature. Bowen v. Georgetown Hospital, 488 U.S. 204, 216 (1988) (Scalia, J., concurring). In considering the equities of applying a rule retroactively courts will consider such factors as the degree of hardship parties would experience, whether reliance on past regulation was justifiable and any statutory interest in retroactive application of the new rule. See, e.g., Consolidated Freightways v. N.L.R.B., 892 F.2d 1052, 1058 (D.C. Cir. 1989) citing Tennessee Gas Pipeline Co. v. FERC, 606 F.2d 1094, 1115, 1116 n.77 (D.C. Cir. 1979), cert. denied, 445 U.S. 920 (1980).

Application of these principles to this rule demonstrate that the equities favor prospective application.

The comments received demonstrate that there has been significant financial investment by credit unions in reliance on NCUA's existing rule. These investments were made with the expectation that service would be available to all potential members in the underserved areas. Prohibiting the addition of new members would limit growth in these areas, expose the institutions to significant hardship through increased financial and reputation risk, and could cause safety and soundness concerns. Existing members would also suffer as a result of the

diminished services that would result if further membership growth was prohibited.

It is also clear that reliance by credit unions on NCUA's regulation permitting these expansions was justified. NCUA has authorized all federal credit unions, regardless of charter type, to add underserved areas since 1994. Prior to the passage of the CUMAA in 1998 these areas were referred to as underserved communities.

With the passage of CUMAA, NCUA made significant changes to its chartering policies but again reiterated that all charter types were permitted to add underserved areas. In the preamble to the regulatory changes implementing CUMAA, the Board noted that the new legislation specifically authorized flexible policies regarding multiple common-bond credit unions providing service to underserved areas. At that time we also encouraged all credit unions to continue service to poor and disadvantaged areas and indicated that previous policy permitting all charter types to serve underserved areas would continue. IRPS 99-1, 63 FR 71998, 72016 (Dec. 30, 1998). Credit unions reasonably relied on these policy statements by this Board.

In short, investment by credit unions in underserved areas has occurred in reliance on long-standing NCUA policies that authorized and indeed encouraged such activity. Members in underserved areas have benefited from low cost

financial services made available as a result of these efforts. They have become members in reliance upon NCUA policy that authorized credit union expansion into these areas. Credit unions that have invested in these areas have done so based on economic assumptions that included continued growth in membership. If continued growth is no longer possible, credit unions will be unable to sustain the current level of services provided in these areas. This could result in diminished or lost services to existing members.

On balance therefore, the Board concludes that the equities support only prospective application of this rule. Credit unions, regardless of charter type, that were serving underserved areas at the time the proposed rule was issued should be permitted to continue to serve those areas to include adding new members. To require them to do otherwise, given their reasonable reliance on NCUA's policy as well as their substantial investments, would cause substantial harm to the credit unions, their members, and potential members in the underserved area.

Regarding the service facility location, many commenters opposed NCUA's proposal to require a physical presence in the underserved area and recommend keeping the status quo. Some opposing commenters believe NCUA has the authority to require a credit union to locate a service facility in or near an underserved area. Some commenters believe the location of a branch is a business decision for the credit union to decide. Some commenters believe

NCUA should focus on the level of service to the underserved area, not whether the branch is within the area, and one commenter noted that the Community Reinvestment Act does not require branches in an area and allows banks to provide service via ATMs and computers. Another commenter supported a specified distance from the underserved area to the service facility's location rather than requiring it to be in the underserved area.

A commenter wrote that the service facility should not have to be in an underserved area within two years if there is public transportation to the service facility or is an acceptable distance from the underserved area. The same commenter suggested the proposed definition of local community should be revised to be 50 miles for heavily populated urban areas and 200 miles for lightly populated rural areas. The commenter believes common interests and interaction should be removed as they are no longer valid or necessary due to credit reports.

Several commenters supported the service facility requirement as proposed, requiring a service facility be within the underserved area. A couple of commenters specifically mentioned that a physical presence ensures a credit union is serving the area.

A banking trade group commenter wrote that NCUA should require credit unions serving underserved areas to establish a service facility in that area within one

year. Another banking trade group wrote that NCUA should require a credit union to establish the service facility in the area upon approval of the expansion.

The NCUA Board finds that a service facility physically located in the underserved area assures better service to members in these locations. A credit union can build a better relationship and understanding of the needs of the community by having a physical presence in the area. By doing so the credit union will be better able to assess the needs of the underserved area and provide needed services to its members. NCUA believes requiring establishment of a service facility within two years of the credit union's addition of the area is reasonable and is retaining it. In addition, the Board has decided to retain as an option for an acceptable type of service facility within the underserved area, a credit union owned facility where shares are accepted for member accounts, loan applications are accepted, and loans are disbursed.

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a regulation may have on a substantial number of small credit unions (primarily those under \$10 million in assets). The final amendments will not have a significant economic impact on a substantial number of small credit unions and therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

The Office of Management and Budget control numbers assigned to Section 701.1 are 3133-0015 and 3133-0116. NCUA has determined that the amendments will not increase paperwork requirements and a paperwork reduction analysis is not required.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999 - - Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act of 1999, Pub. L. 105-277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104-121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedure Act. 5 U.S.C. 551. NCUA is recommending the Office of Management and Budget determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 701

Credit, Credit unions, Reporting and record keeping requirements

By the National Credit Union Administration Board on June 22, 2006

Mary Rupp

Secretary of the Board

For the reasons stated in the preamble, the National Credit Union Administration amends 12 CFR Part 701 as follows:

PART 701-ORGANIZATION AND OPERATION OF FEDERAL CREDIT UNIONS

1. The authority citation for part 701 continues to read as follows:

Authority: 12 U.S.C. 1752(5), 1755, 1756, 1757, 1759, 1761a, 1761b, 1766, 1767, 1782, 1784, 1787, 1789. Section 701.6 is also authorized by 15 U.S.C. 3717. Section 701.31 is also authorized by 15 U.S.C. 1601, et seq., 42 U.S.C. 1981 and 3601-3610. Section 701.35 is also authorized by 12 U.S.C. 4311-4312.

2. Section 701.1 is revised to read as follows:

§ 701.1 Federal credit union chartering, field of membership modifications, and conversions.

National Credit Union Administration policies concerning chartering, field of membership modifications, and conversions are set forth in Interpretive Ruling and Policy Statement 03-1, Chartering and Field of Membership Manual, as amended by IRPS 06-1, Copies may be obtained on NCUA's website, www.ncua.gov, or by contacting NCUA at the address found in Section 790.2(c) of this chapter.

(Approved by the Office of Management and Budget under control number 3133-0015 and 3133-0116.)

Note: The text of the IRPS 06-1 does not appear in the Code of Federal Regulations.

3. IRPS 03-1, Chapter 3, Section III.A is revised to read as follows:

A multiple common-bond federal credit union may include in its field of membership, without regard to location, communities satisfying the definition of underserved areas in the Federal Credit Union Act. Adding an underserved area will not change the charter type of the multiple common-bond federal credit union. More than one multiple common-bond federal credit union can serve the same underserved area. The Federal Credit Union Act defines an underserved area as a local community, neighborhood, or rural district that is an “investment area” as defined in Section 103(16) of the Community Development Banking and Financial Institutions Act of 1994.

For an underserved area, the well-defined local community, neighborhood, or rural district requirement is met if:

- The area to be served is in a recognized single political jurisdiction, i.e., a city, county, or their political equivalent, or any contiguous portion thereof;

- The area to be served is in multiple contiguous political jurisdictions, i.e. a city, county, or their political equivalent, or any contiguous portion thereof and if the population of the requested well-defined area does not exceed 500,000; or
- The area to be served is a Metropolitan Statistical Area (MSA) or its equivalent, or a portion thereof, where the population of the MSA or its equivalent does not exceed 1,000,000.

If the area to be served does not meet the MSA or multiple political jurisdiction requirements outlined above, the application must include documentation to support that it is a well-defined local community, neighborhood, or rural district.

For an underserved area, an investment area includes any of the following, as reported in the most recently completed decennial census or equivalent government data:

- An area that wholly consists of or is wholly located within an Empowerment Zone or Enterprise Community designated under section 1391 of the Internal Revenue Code (26 U.S.C. 1391);

- An area where the percentage of the population living in poverty is at least 20 percent;
- An area in a Metropolitan Area where the median family income is at or below 80 percent of the Metropolitan Area median family income or the national Metropolitan Area median family income, whichever is greater;
- An area outside of a Metropolitan Area, where the median family income is at or below 80 percent of the statewide non-Metropolitan Area median family income or the national non-Metropolitan Area median family income, whichever is greater;
- An area where the unemployment rate is at least 1.5 times the national average;
- An area meeting the criteria for economic distress that may be established by the Community Development Financial Institutions Fund (CDFI) of the United States Department of the Treasury.

In addition, the local community, neighborhood, or rural district must be underserved, based on data considered by the NCUA Board and the Federal banking agencies.

Once an underserved area is added to a federal credit union's field of membership, the credit union must establish and maintain an office or service facility in the community within two years. A service facility is defined as a place where shares are accepted for members' accounts, loan applications are accepted and loans are disbursed. This definition includes a credit union owned branch, a shared branch, a mobile branch, an office operated on a regularly scheduled weekly basis, or a credit union owned facility that meets, at a minimum, these requirements. This definition does not include an ATM or the credit union's Internet web site.

The federal credit union adding the underserved community must document that the community meets the definition for serving underserved areas in the Federal Credit Union Act. Adding an underserved community does not change the charter type of a multiple common-bond federal credit union. In order to receive the benefits afforded to low-income designated credit unions, such as expanded use of nonmember deposits and access to the Community Development Revolving Loan Program for Credit Unions, a credit union must receive low-income designation pursuant to 12 C.F.R. §701.34.

A federal credit union that desires to include an underserved community in its field of membership must first develop a business plan specifying how it will serve the community. The business plan, at a minimum, must identify the credit and depository needs of the community and detail how the credit union plans to

serve those needs. The credit union will be expected to review the business plan regularly to determine if the community is being adequately served. The regional director may require periodic service status reports from a credit union about the underserved area to ensure that the needs of the community are being met as well as requiring such reports before NCUA allows a multiple common-bond federal credit union to add an additional underserved area.