

Freeborn's Credit Union Rules Report

by Brad R. Bergmooser

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Hello and Welcome to the First Installment of Freeborn's CU Rules Report.

In the constantly expanding legal and regulatory environment surrounding credit unions, we feel it's important to regularly update our clients on upcoming changes that could impact their operations. Whether your credit union is state or federally chartered, or federally or privately insured, Congress, the Illinois General Assembly, and state and federal administrative agencies are working tirelessly to redefine the rules you must follow on a daily basis to keep your business open.

The CU Rules Report will provide a "heads-up" on important topics that have recently become effective, or are being proposed by your friendly government official. No law or regulation operates in a silo that impacts only one portion of a credit union's operations, and Freeborn & Peters LLP is dedicated to being a full-service business partner. This information, in conjunction with the attorneys you work with at Freeborn, can help provide all the resources you need to make important everyday business decisions - from lending, to employment, and real estate to vendor relationships.

"Living in a world where no elected official or administrative agency wants to be outdone with regard to their authority to govern your financial institution, Freeborn is committed to keeping its clients ahead of the curve."

Charitable Donation Accounts

Have you heard about charitable donation accounts ("CDA")? NCUA implemented a rule, which was effective in December 2013, allowing credit unions to form a CDA and fund that account with otherwise impermissible investments. The rule applied to federally chartered credit unions, but Illinois law was amended in 2014 to allow state-chartered credit unions in the game. Based off of a credit union adopted policy, and subject to additional restrictions, a credit union can create a CDA and fund it with investments of its choosing so long as 51% of the yield is donated to charity. Credit unions are known for active community involvement, and can really benefit from the CDA structure. The investment flexibility could generate a much greater growth than the traditionally allowable investments, a bonus for the chosen charity or charities, and a bonus for the credit union - who can retain 49% of the CDA's yield. The policy created can be straightforward and succinct, and we can work with you to put a successful CDA program in place.

Fixed Assets

We can stick with investing and cover a recently *proposed* rule from NCUA. In attempting to deal with the aftermath of eliminating Regflex, NCUA is proposing to change its fixed asset rule. The general cap for federal credit unions on fixed asset (real estate and FF&E) is 5% of its shares and retained earnings. Since Regflex disappeared, waivers have been issued by NCUA for

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credit unions wanting to exceed this threshold. The proposed rule will allow federal credit unions, without waiver, to go beyond the 5% cap based off an adopted policy, board oversight and other internal controls. If this sounds too good to be true, it likely is. The commentary to the proposal goes into great detail discussing “NCUA’s Supervisory Review” of the credit union’s fixed asset ownership should it exceed 5% of shares and retained earnings. The basic result, should the rule be finalized, is that a credit union will need to prove to the NCUA examiner that its policy and procedure related to fixed asset ownership is “safe and sound” – which is highly subjective. What about state-chartered credit unions? Part 190.90 of the Illinois Administrative Code has something to say about fixed asset ownership and has yet to have any changes proposed. That rule has a more complex cap: the lesser of 70% of retained earnings or 6% of assets, but that amount can be exceeded if the credit union has a current net worth of the higher of 9% or 200 basis points above its risk based net worth level; a CAMEL of 1 or 2 for 2 consecutive exams; and a CEO in place for at least 2 years, but doesn’t contain the time limit restrictions for holding unimproved or unoccupied real estate found in the federal rule. Whether your credit union is state or federally chartered, both rules create ambiguity and potential examination issue – especially should NCUA’s proposal be finalized.

The CU Rules Report will be sent out periodically so our credit unions can plan, account for, and become compliant with any new rules, laws or other issues that may affect their business. Living in a world where no elected official or administrative agency wants to be outdone with regard to their authority to govern your financial institution, Freeborn is committed to keeping its clients ahead of the curve.

Thanks, and we’ll talk with you soon.

Brad

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