

THE CREDIT UNION REFLECTION



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COMMISSIONER FACE EXTOLS BENEFITS OF STATE CHARTER

In a recent speech to the Legislative Forum of the Virginia Credit Union League, Commissioner Joe Face outlined the Bureau's plans to make a state charter even more the "charter of choice" in Virginia. NCUA has approved several initiatives in 2001, and state chartered credit unions have discussed with the Bureau parity with federally chartered credit unions on these issues. The Bureau has determined that state chartered credit unions already have some of the powers the NCUA has given the credit unions it regulates. The Bureau has always recognized the need to keep the state charter competitive so that state chartered credit unions are not disadvantaged.

Mr. Face first mentioned as an advantage of being a state-chartered credit union the value credit unions place on their personal relationship with their regulators. In large institutions and regulatory agencies it is difficult sometimes to find a responsible person to talk to about your problem. The Bureau is accessible, and Bureau management and employees are willing to listen and to help.

He also pointed out that state regulators are many times more willing to work with troubled institutions. As an example, he reported on the conservatorship at The Nansemond CU in Suffolk. After two years of management by the Bureau this credit union is well on the road to recovery. Return of management to the membership and its elected board is anticipated soon. With the problems at this credit union, it would have been easy to merge it two years ago. But the Bureau saw--and was sensitive to--a community need, and worked to restore the credit union.



Mr. Face also observed that a federal charter tends to be a “one size fits all” approach designed to encompass the needs of the entire country. The assumption is that what works in Des Moines will work in Roanoke. But these two locations are vastly different, and different regulatory approaches are needed. The state regulatory system recognizes that, and customizes its approach to regulation to find unique resolutions to problems.

Regardless of Mr. Face’s personal preferences, as chief regulator for Virginia state-chartered financial institutions, he is obligated to enforce the laws. In that role he noted the Bureau has been finding requests to be in compliance with the law, and the Bureau has a nearly perfect record in approval of small employee group (SEG) requests over the two years the new law has been in effect. The record on community field of membership approvals has been equally as good. New SEGs and community charters are adding tens of thousands of new potential members to individual credit unions. He thought this presented an opportunity for healthy competition. In the end, the consumer benefits the most from competition.

Mr. Face noted a couple of distinctions between the Bureau and the NCUA. The Bureau does not set public policy. This is the job of the Virginia General Assembly, which has not asked the Bureau to promote credit unions or any other financial service provider. The Bureau is charged with protecting the deposits of the citizens of the Commonwealth. Mr. Face asserted that an agency that is charged with regulating, insuring, and promoting one industry cannot perform all three roles adequately. The regulatory conflicts become more pronounced as credit unions get bigger.

After the passage of H.R.1151, the Bureau brought together the credit union and banking industries to hammer out new field of membership legislation. This legislation was an improvement and gave Virginia state-chartered credit unions parity. Mr. Face used this example to commit that “if changes need to be made to improve state law, the Bureau and the VCUL can work together to facilitate those changes in the General Assembly.”

Mr. Face noted the flurry of changes and growth in the credit union industry in the past few years. “The credit union movement is a vital part of the financial services business and has a tremendous role in the delivery of financial services and products both nationally and here in the Commonwealth of Virginia,” he stated. There are 73 state-chartered credit unions in Virginia with total assets just under \$3 billion dollars and serving just under 550,000 Virginians. Assets continue to grow, at a 8.6% pace this year. However, the number of credit unions continues to decline as smaller credit unions merge with large credit unions that provide more products and services.

Competition among financial service providers has gotten tougher. It has become more difficult to distinguish the differences between financial institutions. Charter enhancements provided by NCUA’s new regulations make competition even tougher. Mr. Face noted that one of these perceived enhancements is risk-based supervision. He stated that the Bureau has been performing this type of examination for a number of years, and that it originally came from bank regulation. It works better for large financial institutions than small ones, as regulators have found it helpful “to get their arms around” these behemoth institutions. Risk-based supervision in the largest of these institutions means continuous examination and on-site examiners twelve months a year.

Mr. Face observed that competition has evolved, and that credit unions are now even competing with each other for members. This competition will become keener as larger credit unions expand by taking in SEGs or converting to community fields of membership. Credit union managers are well advised to develop strategies to compete with all financial service providers. While there has been a hot debate between the banking and credit union industries in recent years, Mr. Face stated “the larger battle to be won (is) to retain your members who are constantly being courted by other financial service providers.”

RESERVE TRANSFER REQUIREMENT TO CHANGE



State-chartered credit unions have been required to comply with Section 6.1-225.58 of the Code of Virginia. This Section requires reserve transfers when the percentage of reserves to risk assets falls below prescribed levels.

The Credit Union Membership Access Act (H.R.1151) of 1998 enacted a requirement that all federally insured credit unions comply with Prompt Corrective Action (PCA). PCA evaluates a credit union's "net worth" instead of its "capital" as was evaluated previously. The basic difference between net worth and capital is that the Allowance for Loan Loss account is not included in net worth. Various categories of net worth are defined in Part 702 of NCUA's Rules and Regulations. Credit unions with net worth greater than 7.0% are defined as "well capitalized," and they do not have to make reserve transfers. If a credit union's net worth falls below 7.0%, a reserve transfer is the first remedy (there may be others depending on which "under capitalized" category the credit union is in). This PCA required reserve transfer is 1/10 of one percent of the credit union's total assets for the current quarter, and is to be made quarterly until the credit union is "well capitalized."

Virginia state-chartered credit unions that have a net worth ratio above 7.0% are disadvantaged because the Code of Virginia may require a reserve transfer to be made while PCA does not. Also, "undercapitalized" credit unions in all probability will have a higher Code-required reserve transfer than they are required to make under PCA.

After review of this problem, the Bureau has drafted a Regulation, "Regular reserve accounts." This regulation requires Virginia state-chartered credit unions to establish and maintain a regular reserve account in accordance with applicable provisions of Part 702 of NCUA's Rules and Regulations, and regardless of subdivisions 1, 2, and 3 of Section 6.1-225.58 of the Code. This regulation will be published in the Virginia Register the first week of October 2001, and there will be a thirty day public comment period. It may be reviewed on the Bureau's website at <http://www.state.va.us/scc/caseinfo/banking/b010204.htm>

When this regulation is finally approved, Virginia state-chartered credit unions will no longer be required to make reserve transfers unless they are required to do so under the provisions of PCA. The sections of the Code of Virginia that address reserves will also be updated by legislation to do the necessary "housecleaning." The ultimate outcome is that Virginia state-chartered credit unions will no longer be disadvantaged because of PCA in regard to reserve transfers.

FIELD OF MEMBERSHIP CHANGES

During the second and third quarters of 2001 the Bureau approved 51 small employee groups (SEGs) to be added to the fields of membership of six credit unions. At the end of the third quarter one expansion request was filed but in the middle of a published comment period because of its size. A total of 7,184 new potential credit union members were approved during the two quarters. The average group size was about 140. Since legislation to permit SEG expansion went into effect on July 1, 1999 there have been 150 SEGs approved for total new potential membership of 26,677. The average group size is about 178.

There were no community field of membership approvals during the second and third quarters. However, two requests for community fields of membership were being reviewed as of quarter end. Subject to some technical changes in the statement of their field of membership, the Commissioner will grant approval to New Horizon CU's conversion to a community field of membership. Their community will be the Dulles Corridor in Northern Virginia, with clear, defined boundaries established. The revised estimated population of this community is 260,057. Shenandoah County CU's request for a community field of membership is also being reviewed. The population of Shenandoah County is about 35,000.

BUREAU'S SENIOR COUNSEL RETIRES



Senior Counsel Bill Schutt retired October 1, 2001 after more than 27 years with the State Corporation Commission. A Richmond native, Bill was graduated from Davidson College with a Bachelors Degree in History. After a two-year tour in the U.S. Army, Bill attended the T.C. Williams School of Law at the University of Richmond, where he earned a Juris Doctor degree. Prior to joining the SCC, Bill spent a couple of years working at the law firm of former SCC Judge Junie Bradshaw.

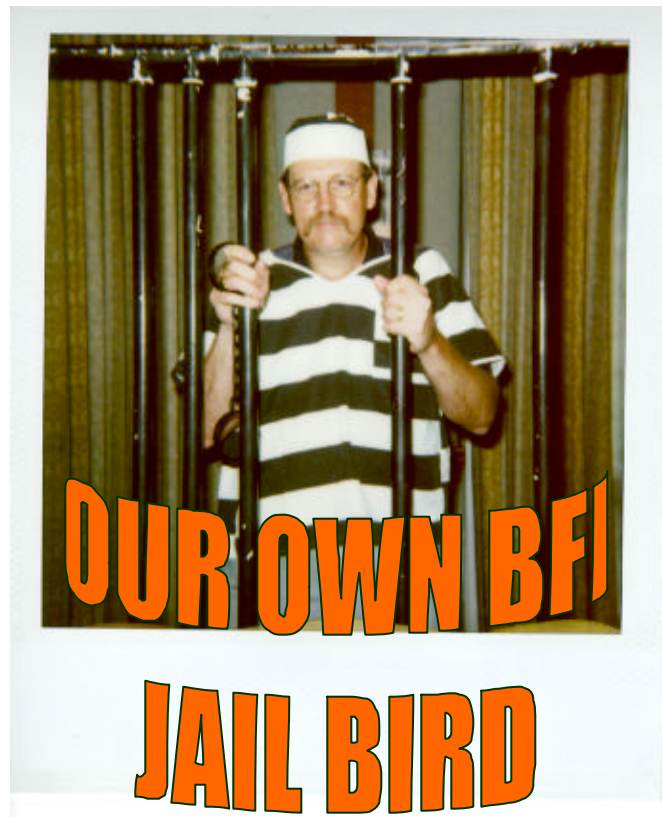
One of the highlights of Bill's career came shortly before announcing his retirement. He was involved in the preparation of a petition Commissioner Joe Face and other defendants filed in the United States Supreme Court in June in the case of NHEMA (National Home Equity Mortgage Association) v. Face, et. al. The petition sought review of rulings by two lower federal courts that federal law preempts Virginia's laws limiting

the prepayment penalty lenders can charge on alternative home mortgage loans. Unfortunately, in October 2001 the Supreme Court denied certiorari on the case.

Bill was actively involved in advising the Commissioner on credit union field of membership and other issues. His duties included managing legal issues for the Bureau for all the financial institutions the Bureau regulates. Bill says the best thing he liked about working for the State Corporation Commission was the people.

In retirement Bill wants to “try to find some useful work around town...(that will) make a difference in some people’s lives.” Bill and his wife Genie have two daughters and a son. He enjoys tennis, singing, and reading. The Bureau certainly wishes our friend Bill Schutt all the best in retirement!

MARTHA STEWART SAYS: “IT’S A GOOD THING”



“BEHIND BARS FOR GOOD!”

September 25, 2001 was a day of excitement, and employees waited to watch this magic moment. Deputy Commissioner George Latham was locked up to raise money for The Muscular Dystrophy Association. He would like to thank all his friends and employees for their contributions toward his making “bail” and to such a wonderful charity. Mr. Latham raised for the MDA \$551.00. He is out of jail now, but next year is coming. Maybe he can stay just a little longer for this great cause.



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