

Conversion of a Non-Credit Union Entity to a Credit Union Charter

The National Credit Union Administration (NCUA) occasionally receives inquiries from financial entities, including banks, with questions about converting to a credit union charter. While unusual, such conversions may be possible for some financial entities. This document provides guidance on various issues that may arise when a non-credit union entity (NCE) is considering conversion to a credit union charter.

Credit unions may be either federally-chartered or state-chartered. NCUA charters federal credit unions (FCUs), and this document focuses for the most part on conversion to the FCU charter. This document does not address conversion from one credit union charter to another. This document also does not address conversions from the credit union charter to a non-credit union charter.

The words “I,” “me,” and “my” below refer to the owners of the NCE.

What is a credit union?

Credit unions are not-for-profit, member-owned, and member-controlled cooperatives organized to provide financial services to their members. The primary business of most credit unions is to provide their members a place to save and borrow at good rates, although credit unions may also provide their members with certain other financial services. Credit unions are either state-chartered or federally-chartered. NCUA, an independent agency in the executive branch of the federal government, charters all federal credit unions (FCUs) and provides account (deposit) insurance to all FCUs and most state-chartered credit unions.

By law, credit unions are limited to serving persons within certain fields of membership as established in the credit union’s chartering documents. Any person or organization within a credit union’s field of membership may join the credit union and so become a member. The field of membership concept, an important aspect of credit unions, is discussed in more detail below.

Credit unions are run by boards of directors who are elected from, and by, the credit union’s members. In FCUs, most directors must serve on a volunteer (uncompensated) basis.

What is the process for converting to a federal credit union?

In the past, NCUA has conducted NCE-to-FCU conversions by chartering a new credit union and immediately merging the existing NCE into the credit union. This means that for an NCE to convert to an FCU it must understand and comply with both NCUA chartering and NCUA merger policies, as well as other NCUA Rules and Regulations, and submit various documents to NCUA. The primary guidance on chartering is

contained in NCUA's Chartering and Field of Membership Manual and the primary guidance on mergers is contained in NCUA's Credit Union Merger and Conversion Manual.

Before completing any forms, NCEs should first contact the NCUA regional office that serves the state where the NCE is located. The regional office staff will advise NCEs whether a conversion is feasible, and advise the NCE of the information needed to process the conversion application. After analyzing the NCE's information NCUA will prepare a timeline with the NCE, outlining the various actions the NCE must take to obtain NCUA approval of the conversion transaction. If the NCE is granted a credit union charter, NCUA will issue a Letter of Understanding and Agreement to the new credit union outlining operational goals it must achieve.

A state-by-state list and contact information for NCUA's Regional Offices is available at www.ncua.gov/AboutNCUA/org/orgchart.htm.

Would my current regulator permit a conversion to a credit union?

NCUA believes national banks and federal savings associations have authority under federal law to convert to an FCU. State-chartered NCEs, including banks and savings associations, should consult their current regulator and applicable state law and regulations. Some important conversion issues, such as whether the conversion requires a vote of your current owners, must be addressed to your current regulator.

What are credit union "shares?"

Money deposited into a credit union by its members is called "shares." The credit union treats this money very much like a deposit at a bank. The member can withdraw his or her shares in full at any time (subject to a possible early withdrawal penalty if the share account is a term account). Shares accounts are also federally insured by the NCUA in a manner very similar to how the Federal Deposit Insurance Corporation (FDIC) insures bank deposits, up to at least \$100,000 (\$250,000 until December 31, 2013) or possibly more depending on how the member structures his or her shares. NCUA insurance, like FDIC insurance, is backed by the full faith and credit of the federal government. No member of a federally-insured credit union has ever lost a penny of shares insured by the NCUA.

To become a member of a credit union, a person must be within the field of membership and also deposit and maintain one share. The FCU can establish the amount, or "par value," of the share.

What is a "field of membership?"

By law, FCUs are limited to serving those persons and organizations in a defined field of membership who share a common bond. The common bond may be single occupational (i.e., based on similar employment), single associational (i.e., based on membership in a group such as a church or a labor union), multiple common bond (with each occupational or associational group having its own common bond) or community (i.e., based on presence within a defined geographic area). Non-credit union entities should consider whether their proposed field of membership meets the requirements of NCUA's Chartering and Field of Membership Manual.

Can I serve my existing customers after conversion to an FCU?

Likely, yes, an NCE's existing customers of record as of the conversion date could become members of an FCU, as long as they have a minimum deposit at the NCE at the time of conversion equal to or greater than the par value of one share. Following the conversion, however, the NCE will only be able to add new members who are within the FCU's field of membership and who subscribe to (deposit) at least one share. Some NCEs may have borrowers who do not have deposit accounts at the NCE and so who are not automatically eligible for membership upon conversion. NCUA will allow the NCE to maintain these loan accounts. Following conversion, however, the NCE may not provide these borrowers any new services, including any new loans or advances on their existing loans, unless the borrowers are within the field of membership and join the FCU by purchasing at least one share.

If I am organized in stock form, can I convert to an FCU?

A credit union is a financial cooperative organized in mutual form and owned equally by all its members. As such, credit unions do not issue stock. If an NCE currently has a stock form of ownership, it must consider how it would transition ownership from the stock holders to the members of the credit union. In addition, the FCU, like any organization, needs capital to operate. The conversion of an NCE to an FCU would require the NCE transfer enough of its capital to the FCU to provide the FCU with acceptable levels of capital. This could make it difficult to convert from a stock NCE to a credit union.

Do I have volunteers willing to serve as credit union directors?

Federal credit unions must have an odd number of directors, with at least five directors and no more than 15. By law, only one officer of the board of directors may be compensated as an FCU director. If permitted by the FCU's bylaws, some FCU directors may also serve as employees and be compensated as such, but no more than half the directors may also be employees.

Will I have to make changes to my lending practices upon conversion to an FCU?

All lending institutions, including credit unions, have legal and safety and soundness limits on their lending authority. Federal credit unions, for example, are generally prohibited from making business loans exceeding 12.25% of their net worth, and loans other than residential mortgages may not have maturities that exceed 15 years. FCUs are also subject to an interest rate ceiling, currently set at 18%, and FCUs may not put prepayment penalties in their loans.

An NCE that converts to an FCU may have to modify, or divest, loans that fail to meet these and other legal requirements, or that do not meet NCUA's standards for safety and soundness. The NCUA Regional Office, in consultation with the NCUA Office of General Counsel, will advise an NCE of any necessary divestitures as part of the conversion review and approval process.

Will I have to make changes to my investment portfolio upon conversion to an FCU?

All depository institutions, including credit unions, have restrictions on their investment authority. The FCU Act generally limits FCU investments to loans, government securities, deposits in other financial institutions, and a few other narrowly-defined investment categories. Federal credit unions, for example, generally may not hold corporate debt or equity securities.

An NCE that converts to an FCU may have to divest investments that fail to meet legal requirements, or that do not meet NCUA's standards for safety and soundness. The NCUA Regional Office, in consultation with the NCUA Office of General Counsel, will advise an NCE of any necessary divestitures as part of the conversion review and approval process.

Will I have to pay for federal share (deposit) insurance following conversion?

Share insurance protects members from loss in the event a credit union fails. All FCUs and most state-chartered credit unions have deposit insurance from the National Credit Union Share Insurance Fund (NCUSIF), administered by NCUA. The NCUSIF insures members to at least \$100,000 (\$250,000 until December 31, 2013), or possibly more depending on how the member structures his or her shares. NCUSIF coverage is similar to the coverage for banks offered by the FDIC to bank depositors. The NCUSIF insurance, like FDIC's insurance, is backed by the full faith and credit of the U.S. Government.

Every federally insured credit union must maintain an equity deposit in the NCUSIF equal to one percent of the credit union's insured shares. The amount of the required deposit is recalculated annually for credit unions with assets up to \$50 million and semi-

annually for credit unions with assets above \$50 million. NCUA may also levy additional premiums if necessary to maintain the NCUSIF's required equity ratio, and these premiums are calculated as a percentage of the credit union's insured shares.

In May, 2009, Congress authorized NCUA to establish a Temporary Corporate Credit Union Stabilization Fund (CCUSF). The NCUA may, through the CCUSF, borrow money from the U.S. Treasury to pay for certain expenses associated with NCUA's Corporate Credit Union Stabilization Program. To the extent the CCUSF borrows money, the borrowings must be repaid via assessments made by NCUA on federally-insured credit unions. An entity that converts to a federal credit union, or a federally-insured state chartered credit union, would be liable for these assessments in addition to any assessment made by the NCUSIF. The CCUSF is a temporary fund and will likely close no later than 2017.

Could I convert to a state-chartered credit union instead of an FCU?

Non-credit union entities may also want to investigate the possibility of becoming a state-chartered credit union, particularly if an entity currently has a state charter. An NCE considering conversion to a state-chartered credit union should contact the state's credit union regulator.

What other resources related to FCU conversions are available?

The following materials contain additional authority and guidance:

The Federal Credit Union Act, 12 U.S.C. §§1751-1795k, available at www.ncua.gov/Resources/RegulationsOpinionsLaws/fcu_act/fcu_act.pdf.

NCUA Regulations, 12 C.F.R. Parts 700-796, available at www.ncua.gov/Resources/RegulationsOpinionsLaws/Regulations.aspx. (Part 708b governs mergers).

NCUA's Express Chartering Procedure at www.ncua.gov/GenInfo/GuidesManuals/ecp/ecp.aspx.

NCUA Chartering and Field of Membership Manual, available at www.ncua.gov/Resources/RegulationsOpinionsLaws/charter_manual/charter_manual.aspx.

NCUA Credit Union Merger Manual, available at www.ncua.gov/GenInfo/GuidesManuals/merger/merger.aspx.

NCUA's Federal Credit Union Bylaws, available at
www.ncua.gov/GenInfo/GuidesManuals/bylaws/index.aspx.