Subject: Comparative Analysis of the State and Federal Charter

General Comments

There are advantages and disadvantages to being a state or federally chartered credit union. In the Go West region, the advantages of being a state charter generally outweigh the benefits of the federal charter. To illustrate this point state charters hold far more assets, and have grown there liabilities and assets at a much quicker rate than federal counterparts.

Below is a breakdown of assets in the five GoWest states with both federal and state charters.

State charters – 139 state charters, 88% of assets.

Federal charters – 127 federal charters, 12% of assets.

Should Wyoming credit unions choose to pursue the creation of a charter they would work together to define the parameters that reflect the values of the state. For example, Wyoming might consider protecting borrowers from ESG requirements while Federal lawmakers might enact legislation encouraging financial institutions to adopt ESG legislation.

Legislators and the state bank regulator have expressed interest in creating a state charter which would create more state control, and local jobs. Wyoming also has a strong lobbying base as they have the highest percentage of citizens that work for credit unions in the nation.

Federal Charter Advantages - Some of the advantages to being a Federally chartered credit union include:

Consistent regulations – Being under federal oversight means that federally chartered credit unions have the NCUA as a single regulator and insurer. This is particularly valuable for multi-state federal credit unions. For state charters with operations in multiple states it can be challenging and costly to navigate differences in state laws. We have seen that credit unions with operations in more than 5 states tend to prefer the federal charter. The National Association of State Credit Union Regulators recognizes this threat to the state system and is working on a modern interstate agreement that will help facilitate interstate operations for state charters.

Tax Advantages – Federal credit unions have the benefit of being chartered as instrumentalities of the United States under internal revenue code 501 c1. State chartered credit unions are chartered under 501 c14 of the internal revenue code. The 501 c 1 designation provides greater tax benefit than the 501 c14. FCUs do not have to file 990s or any tax returns, they do not have to pay sales, lodging and some other taxes. The savings can add up for example a FCU that purchases all of the building material for a new building could save as much as 10% in some states, additionally one large credit union estimated that they save nearly $200k in lodging costs by requiring staff to use their federal tax exemption when traveling. However, at least one state Montana confers all the tax benefits of Fed charters to state charters.

State Charter Advantages – The state charter is more attractive in GoWest states.

General benefits – State chartered credit unions in the GoWest Region have greater flexibility in terms of operational, lending, investments, membership, optionality, powers and other unique provisions. Additionally, state-chartered credit unions in the GoWest Region generally report that state supervisory authorities provide tailored supervision, quicker response times, and often remind the Federal insurer who the primary regulator is during exams. The GoWest CUA has demonstrated a strong track record of working with state legislatures to modernize statutes typically every two years as well as update regulations. The FCUA on the other hand was last comprehensively updated in 1998 with the passage of CUMAA.

Parity – One of the biggest advantages of the state charter is the ability to utilize parity to ensure that state charters can do anything that federal charters can do. The best example of a state parity provision is automatic federal parity and the ability to ask the prudential regulator for provisions from other state credit union acts or bank acts which allows state credit unions to compete on an even playing field with other financial services providers.

Field of Membership – Many state credit union acts include broad FOM provisions including the ability to mix and match types of charters, expand relatively easily into other states. Some states even have explicit nationwide FOM with no restrictions. For example, PenFed got their nationwide FOM by taking a troubled New York state chartered credit union that had a legacy nationwide FOM. Because they were in troubled condition PenFed was able to absorb the state charters FOM. State acts tend to be more flexible in allowing merging credit unions to combine FOMs in mergers regardless of troubled condition. Federal Charters converting to state charters often times are allowed to retain their Fed FOM and add permissible state FOMs in mergers.

Private Insurance – Some states offer the ability for a credit union to choose private share insurance eliminating the need to follow NCUA 741 regulations and removing the NCUA completely from oversight. Until recently one state allowed credit unions to self-insure which meant that the exam was solely a consumer compliance exam rather than a safety and soundness exam.

Assessments – In GoWest states assessments are typically 30 percent less than the operating fees that FCU's pay and as assets have grown GoWest has worked to reduce assessments.

Incidental Powers – Many states have crafted incidental powers provisions that provide broad autonomy to execute non enumerated powers. Federal credit unions are restricted to a prescriptive list of incidental powers.

Governance and Operations – State charters have significant governance advantages over federal charters examples include:

- **Bylaws** – Some state charters allow for credit unions to create and maintain their own unique bylaws and bylaw amendments do not have to be approved by regulators. FCU's have a mandated set of very prescriptive bylaws. Because FCU bylaws are in some instances beholden to out-of-date statutes the NCUA has not been able to fully modernize their bylaws. For example, the statute prohibits compensation of directors. However, NCUA board members and a number of senior NCUA staff have supported director compensation.

  Examples Flexible Bylaws provisions:
  - Amendments allowed without regulatory approval
  - Broader membership
  - Joint membership
  - Clear expulsion provisions
  - Virtual annual meetings and greater meeting flexibility
  - Higher bar for calling special membership meetings and greater flexibility to hold virtually
  - Greater flexibility on what constitutes a quorum
  - Eliminate requirement to have a supervisory or audit committee
  - Greater flexibility to remove directors
  - Ability to compensate directors
  - Greater flexibility on defining duties of the board and delegable duties
  - proxy voting allowed
  - election flexibility
  - Board combinations in mergers

- **Membership Share** – Some state charters do not require membership shares. This allows credit unions to use other types of accounts to qualify a member. For example, an individual can get a loan and that loan account works as the membership account. Credit unions that have deployed this have reported that it has resulted in increased demand for products and services as it simplifies the customer experience.

- **Definitions** – Good state acts have modernized definitions sections. For example, state acts may allow for domestic partnerships and committed intimate relationships to count as family for purposes of membership. A state act may have broader definition for qualifying for low-income designations.

Lending

- **General**
    - **Interest rate cap** - Most states do not set an artificial interest rate cap. The Fed is currently 18%. 28% (all in) on small dollar loans.
    - **Unsecured lending** – Many states allow unsecured lending with no restrictions on maturity or the amount of an unsecured loan. At the Federal level there are 15-year maturity restrictions on unsecured loans.
    - **Subordinated lending –** Many states do not restrict the terms of subordinated loans where the Fed restricts subordinated lending to 20 years.
    - **Unimproved property loans –** Many states do not restrict the terms on unimproved property loans.
    - **Loans to CU officials –** Many state acts permit higher limitations on loans to CU officials or do not restrict loans to CU officials. At the Federal level it is $20 K unless board approved.
    - **Concentration limits –** Many states have very few restrictions on concentration limits.
    - **Participations –** Many state acts have greater permissibility around the amount of participations that can be purchased.

- **Commercial**

    - **Flexible State MBL rules** - A handful of states have adopted there own MBL rules that are interpreted by the states often times with less restrictions than at the Federal level for example Washington has language that allows the state regulator to grant an exception to the cap.

- **Pre-payment penalties allowed** - Many states allow credit unions to charge prepayment penalties on commercial loans which is not allowed at the Federal level. State credit unions report that this is critical to being able to compete for MBLs.

Investments

- **Permissibility** – the best state acts specifically authorize broad investment authorities including the ability to invest in any permissible investment that is allowable for any other financial institution operating in the state.

- **Equity investments –** Some state acts allow for equity investments in Non-Cusos, including VC funds, privately held businesses, and publicly traded companies. The most expansive state act allows a credit union to purchase a bank through equity.

- **CUSO limitations** - Federal Credit Unions have a limited ability to make CUSO investments. Many states authorize much higher CUSO investment limits, for example Washington allows up to 10% of net-worth.

Exams and Regulatory Oversight

- **Approvals** – The best state acts have very few requirements for regulatory approvals. Instead, they allow credit unions to use notifications or are deemed approved unless the regulatory agency determines there is a safety and soundness concern.
  Examples include: Branching which can be a simple notification, Interstate Branching – which in some state acts is as simple as following the procedures outlined in host state. Bylaw updates which in some act can be done autonomously.

- **Credit Union Oversight** – Many state regulatory agencies have boards and commissions that exercise some oversight over regulatory agencies.