



## Chartering New Credit Unions

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New credit union chartering is a very time consuming, demanding, and worthwhile activity both for the individuals seeking the charter or license and the body or agency granting the charter. The goals of any organizational body in charge of credit union chartering should be to:

- encourage the formation of credit unions in accordance with existing law and rules and regulations;
- promote the formation of economically feasible, safe and sound financial institutions that will remain a going concern well into the future;
- promote savings and grant access to credit for credit union members; and
- make quality credit union service available for all eligible people.

**Types of Charters** – Generally credit unions can be formed based on an occupational, associational, or community charter. The occupational charter usually includes all persons and entities that share the identified occupational common bond or are employed by a common employer. Depending on local law, an associational common bond may include in its charter, regardless of location, all-natural person members, non-natural person members, and employees of a recognized association whose members participate in activities that generate mutual benefits and interests. Community charters are usually based on a well-defined local community, neighborhood, or rural area. Individuals who live, work, attend school, or worship in the designated area would be eligible for membership.

**Founders of the Credit Union** – Credit unions are generally organized by persons who volunteer their time and resources and are responsible for determining the interest, commitment, and economic advisability of forming a credit union. This requires considerable time and effort. Persons interested in organizing a credit union should contact the chartering organization to inquire about the requirements and receive the documentation needed to apply for a credit union charter.

The founders of a credit union should be of legal age and eligible for membership within the proposed credit union. The number of founding members must be at least the minimum amount identified by the chartering body. Each founding member should be required to purchase at least the minimum amount of ownership shares required for membership. The founding members will elect from among themselves, until the first annual general meeting, officials to fill the positions of the board of directors, supervisory committee and credit committee, unless the credit committee is appointed by the board of directors who should designate the committee members upon being appointed to the board. Each elected or appointed official should be required to review a job description that specifically outlines their duties and responsibilities and discusses the necessary prerequisites to fulfill the job requirements. Founding members who will serve in an

official capacity shall confirm in writing their voluntary membership and that they have agreed to fulfill duties relative to their position.

Each founding member shall have a business and personal reputation beyond reproach. The following individuals are always unsuitable to be credit union officials:

- persons who have committed crimes against property or violated legislation while conducting their activity;
- former financial institution or legal entity general managers, board members, credit or supervisory committee members that caused, as a result of their actions, an institution's insolvency or a legal entities' bankruptcy;
- persons whose management style and/or business ethics are considered to be questionable or dishonorable and/or dangerous resulting in losses at other financial institutions; and
- persons who have had criminal charges brought against them.

**Member Support** – The charter applicant should be able to demonstrate that membership support is sufficient to ensure viability. Therefore, the chartering body should have strict entry requirements for new credit unions. Currently regulations addressing entry requirements are minimal in most countries. It is not uncommon to have 20 or fewer individuals starting a credit union with only a small amount of capital. This has led to a large number of institutions that can not offer their members the services they want and are unable to compete financially because they do not have the economies of scale. Licensing such institutions that can not demonstrate sustainability is a mistake and a burden on the agency in charge of regulation and supervision. Prior to licensing any credit union, the chartering body should be satisfied that the institution would be viable.

**Required Capital Formation prior to Chartering** – As previously stated, it is currently not unusual for very small groups of individuals to receive credit union charters because entry requirements are minimal to non-existent. If minimum capital formation requirements are not established for chartering then few, if any newly chartered credit unions, will have the ability to meet member needs because the credit union will not have the funds necessary to meet loan demand and offer the services desired.

Capital formation and entry requirements are the most important requirements for the formation of sustainable financial intermediaries. The minimum allowable capital amount should be clearly identified as an amount that must be collected by the founding members prior to chartering. Initially the funds that are needed to apply for a charter will come from the ownership share deposits made by the members and donations. Upon receiving a charter, then the credit union will be subject to institutional capital requirements as other existing credit unions are. This regulation normally specifies that a credit union should maintain an institutional capital to total assets ratio of at least 10%. Institutional capital is defined as regulatory reserves, other reserves, monetary donations and grants, undivided earnings, and year to date net income that has not been closed to undivided earnings. Ownership shares should not be included as institutional capital. These shares are withdrawable upon membership termination and can be used to secure a

loan. Shares should only be considered capital if they can not be withdrawn under any circumstances by members and the funds are available to absorb losses.

**Required Documentation for Chartering** – Required documentation for a charter application will vary from country to country, however, the following written documentation is usually required:

- Completed application for charter as provided by the chartering body that usually includes the following information:
  - the name and location of the proposed credit union;
  - the proposed field of membership;
  - the names and addresses of the founding members along with the number of ownership shares purchased by each member;
  - the total amount of ownership share capital as of the formation of the credit union;
  - the names, positions, and number of officials that will make up the board, credit and supervisory committees;
  - the type of facility in which the credit union will be located; and
  - the services to be offered when the credit union opens for business.
- Proposed bylaws that were either modified model bylaws provided by the chartering body or drafted independently by the founding members;
- Resumes or educational and employment information for the members of the board, credit and supervisory committees, and the proposed general manager;
- Signed and dated job descriptions by each elected or appointed official that outlines the duties and responsibilities necessary to fulfill their job requirements;
- Proposed organizational chart detailing the positions within the credit union and the proposed individuals that will fill the positions;
- Proposed credit, collections, capital accumulation, investment, and personnel policies; and
- A business plan.

**Economic Advisability/Business Plan** – Prior to chartering a credit union, the chartering body should assure that the institution will be viable and that it will not materially affect existing credit unions. In general, the success of any credit union depends on:

- the character and quality of daily management and the officials;
- the depth of member support; and
- the present and projected market conditions.

Groups applying for a charter should be required to prove their economic viability through a business plan that is supported by written assumptions, survey results, and initial membership numbers that meet the required minimum. The business plan is the union between the ideas, goals, and objectives of the founding members with financial numbers. The business plan has three main objectives:

- It documents support for the credit union. This support may be in the form of letters of commitment, survey results, and pledges from potential members pertaining to the amount of savings and shares that they would most likely place in the credit union.

- It describes what the credit union intends to do and how and when it proposes to meet the goals and objectives.
- The plan demonstrates that these goals are achievable. The financial projections should show that the credit union could generate sufficient income to cover the cost of providing services, paying interest on member deposits, and building up financial reserves.

At a minimum the business plan should include the following information:

1. The mission statement;
2. Analysis of market conditions – economic prospects for the potential membership group, information on the other financial institutions currently serving the area, current availability of financial services from other credit unions and financial institutions;
3. Summary of survey results;
4. Financial services needed/desired;
5. Financial services to be provided;
6. How and when the services will be implemented;
7. Staffing of the credit union and background information on key employees;
8. Operating facilities – office space, equipment, supplies, insurance coverage, etc.;
9. Type of management information system to be used;
10. Operating budget for year one and two including the written assumptions used to draft the budget;
11. Pro forma balance sheet for year one and two including the written assumptions used to draft the pro forma;
12. Goals for savings, loans, and number of members;
13. Goals for operating independently – i.e. without subsidies or grant funds;
14. Source of funds to pay expenses during initial months of operations; and
15. Evidence of sponsor support if subsidies are critical to the success of the credit union.

Sometimes the business planning process produces a red flag or warning signal such as:

- the credit union would not be self-sustaining;
- the credit union lacks support from the potential membership;
- the desired services to be offered appear too costly and should be scaled back at the onset of operations; and/or
- the founders are unable to decide on one common vision for the credit union.

These red flags are very important and should be addressed prior to applying for a charter or the chartering process discontinued because the chances of the credit union remaining a going concern are significantly reduced.

**Requirements for the Management Information System** – If it is financially possible, new credit unions should start operations with an automated management information system. The selected hardware and software should be:

- suitable for credit union operations;
- able to handle the anticipated level of operations;
- able to provide transparent accounting information that is comparable to similar institutions;

- able to produce internal control and required regulatory reports;
- understandable to management and the employees; and
- supported by adequate formal training and maintained by the providers of the hardware and software.

If it is not possible to begin credit union operations with an automated system, credit unions should use a manual accounting and record keeping system that has been approved by the chartering body. Whatever the type of system that is used, automated or manual the issues that should not be overlooked are:

- the system generates information as prescribed by the chartering and/or regulatory body so that reported information is reliable and comparable to other credit unions;
- the employees receive adequate training so that errors do not compromise the integrity of the information; and
- the protection of data is adequate so that it can not be destroyed by natural elements or manipulated by employees or other individuals.

**Chartering Body Procedures** – Once the chartering body receives a complete charter application package, an acknowledgement of receipt should be sent to the founding members. The chartering body should have the right to request additional information or documents that are deemed necessary to make a decision on chartering the proposed credit union.

An employee of the chartering body will review the application package and verify its accuracy and reasonableness. The employee will inquire into the financial management experience and the suitability and commitment of the proposed officials and employees, and will make an assessment of economic advisability through a detailed review of the business plan. The business plan should be assessed for:

- realistic projections;
- attainable goals;
- adequate service;
- sufficient start-up capital; and
- sufficient time commitments by the proposed officials and employees.

Any concerns that the chartering body may have after the review process should be discussed with the prospective credit union officials. All concerns should be resolved prior to granting the charter; these resolution efforts may delay the processing and granting of the charter.

Approval of a charter should be based on the qualitative evaluation and assessment of the:

- probability of financial and operational success;
- reputation and background information of the founders and the elected and appointed officials;
- professional qualifications of the general manager and other key employees;
- evaluation of the business plan;
- adequacy of start-up capital; and

- suitability of the proposed credit union location, premises, and equipment.

Under normal circumstances, assuming that the chartering body receives all of the necessary documentation completed as prescribed, the charter should be granted in no more than 60 calendar days from the receipt of the documentation. When a proposed credit union is approved for operations and receives a charter, operations should begin within one year from the date the charter was issued.

All chartering documentation should be maintained in a file specific to the chartered credit union. At a minimum, the file should contain the following:

- the approved application for chartering;
- the approved bylaws;
- the names, addresses, account numbers, and ownership share balances of the founding members;
- the business plan;
- decision of the chartering body to license the credit union; and
- the charter or license that grants the credit union the right to operate.

The chartering body should also have the right to deny charters. Charters are usually denied for the following reasons:

- non-submission of all the documents needed for chartering;
- non-compliance of submitted documentation with requirements set forth in law and applicable rules and regulations;
- inadequacy of start-up capital;
- economic non-viability of the business plan; and
- individuals proposed as officials and/or operational management are found to be under criminal investigation, have been convicted of a crime, are liable for, or associated with, losses at other financial institutions, or are generally unsuitable to carry out the duties and responsibilities of their proposed position.

If the chartering application is denied, the chartering body should, within one month, send a written notice of denial to the applicant and give the reason(s) for denial. If the founding members of the proposed credit union can address and correct all the reasons that caused the denial, they should be able to re-apply for a license at any time. If the founding members feel that they are being treated unfairly by the chartering body they should have the right to appeal the decision to a court.

**Pre-Licensing On-Site Contact** - Prior to granting a license, an employee of the chartering body should perform an on-site visit to meet with the founders and any other individuals having an interest in the proposed credit union to assess the viability and to establish rapport with the founders. The chartering body employee should discuss the role of the chartering body, its expectations regarding the operations of the credit union, and determine that everything is in place to commence credit union operations. All of the observations noted should be placed in writing and made a part of the credit union's permanent file. This information should be used for any follow-up visits.

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