

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE MINNESOTA DEPARTMENT OF COMMERCE

In the Matter of the
THE
Proposed Rule Relating
LAW JUDGE
to Credit Unions

REPORT-OF
ADMINISTRATIVE

The above-entitled matter came on for hearing before Peter C. Erickson, Administrative Law Judge from the State Office of Administrative Hearings, on September 18, 1989 at the Minnesota Department of Commerce, Metro Square Building, St. Paul, Minnesota.

Appearing on behalf of the Department of Commerce was Assistant Attorney General Gregory P. Huwe, 1100 Bremer Tower, Seventh Place and Minnesota Street, St. Paul, Minnesota 55101, and Deputy Commissioner of Commerce James Miller. The record closed, as explained more fully below, on September 28, 1989.

The Department must wait at least five working days before taking any final action on the rule; during that period, this Report must be made available to all interested persons upon request.

Pursuant to the provisions of Minn. Stat. § 14.15, subd. 3 and 4, this Report has been submitted to the Chief Administrative Law Judge for his approval. If the Chief Administrative Law Judge approves the adverse findings of this Report, he will advise the Department of actions which will correct the defects and the Department may not adopt the rule until the Chief Administrative Law Judge determines that the defects have been corrected. However, in those instances where the Chief Administrative Law Judge identifies defects which relate to the issues of need or reasonableness, the Department may either adopt the Chief Administrative Law Judge's suggested actions to cure the defects or, in the alternative, if the Department does not elect to adopt the suggested

actions, it must submit the proposed rule to the Legislative Commission to Review Administrative Rules for the Commission's advice and comment.

If the Department elects to adopt the suggested actions of the Chief Administrative Law Judge and makes no other changes and the Chief Administrative Law Judge determines that the defects have been corrected, then the Department may proceed to adopt the rule and submit it to the Revisor of Statutes for a review of the form. If the Department makes changes in the rule other than those suggested by the Administrative Law Judge and the Chief Administrative Law Judge, then it shall submit the rule, with the complete record, to the Chief Administrative Law Judge for a review of the changes before adopting it and submitting it to the Revisor of Statutes.

When the Department files the rule with the Secretary of State, it shall give notice on the day of filing to all persons who requested that they be informed of the filing.

Based upon all the testimony, exhibits and written comments, the Administrative Law Judge makes the following:

FINDINGS QF FACT

Procedural-Requirements

1. On July 27, 1989, the Department filed the following documents with the Chief Administrative Law Judge:

- (a) A copy of the proposed rule certified by the Revisor of Statutes.
- (b) The Order for Hearing.
- (c) The Notice of Hearing proposed to be issued.
- (d) A Statement of the number of persons expected to attend the hearing and estimated length of the Agency's presentation.
- (e) The Statement of Need and Reasonableness.

2. On July 24, 1989, a Notice of Hearing and a copy of the proposed rule was published at 14 State Register 149.

3. On July 20, 1989, the Department mailed the Notice of Hearing to all persons and associations who had registered their names with the Department for the purpose of receiving such notice.

4. On July 27, 1989, the Department filed the following documents with the Administrative Law Judge:

- (a) The Notice of Hearing as mailed.
- (b) The Agency's certification that its mailing list was accurate and complete.
- (c) The Affidavit of Mailing the Notice to all persons on the Agency's list.
- (d) The names of Department personnel who will represent the Agency at the hearing together with the names of any other witnesses solicited by the Agency to appear on its behalf.
- (e) A copy of the State Register containing the proposed rule.
- (f) A copy of the State Register containing a Notice of Intent to Solicit Outside Opinion regarding the proposed rule relating to credit unions published on June 22, 1987 at 11 State Register 2339.

The documents were available for inspection at the Office of Administrative Hearings from the date of filing to the date of the hearing.

5. Due to an error in the mailing of the original Notice of Hearing, which set the hearing for August 23, 1989, it was necessary to reschedule the hearing. On July 28, 1989, the Commissioner issued a Notice of Hearing Date Change, announcing that the hearing had been rescheduled to September 18, 1989. This was published in the State Register on August 7 at 14 State Register 291 and mailed to all persons on the Department's list on August 14, 1989.

6. The period for submission of written comments and statements remained open until September 25, 1989. The three-day response period lasted until September 28, at which time the record closed for all purposes.

-History and Background

7. Although the State has regulated credit unions since 1925, the events leading up to this rule did not really begin until 1983. Prior to 1983, there was no minimum number of persons who had to agree to join a credit union. Minn. Stat. § 52.01 (1982) provided that any seven residents of the State could apply to the Commissioner of Banks for permission to organize a credit union. Section 52.05 of the 1982 statutes required that credit union organizations be limited to groups, "of both large and small membership", having a common bond of occupation, or association, or to residents within a well-defined neighborhood, community, or rural district.

8. In 1983, the statutes were amended in a number of ways. First of all, the Commissioner was directed to consider whether or not the proposed organization of a credit union would be "economically feasible" in determining whether or not to grant permission to organize a credit union. In addition, in 1983, the Legislature provided that any 25 residents of the State representing a group could apply to the Commissioner, advise him of the common bond of the group and its number of potential members, and ask for a determination of whether it was feasible for the group to form a credit union. If the Commissioner determined it was not feasible because the number of potential members was too small, then he was to certify the applicant group as eligible to petition for membership in an existing credit union, subject to the existing credit union accepting the group into its membership. Between 1983 and 1987, more than 100 small group petitions were considered. More than 90% of these were occupational groups.

9. In 1987, the Legislature again amended the statutory provisions relating to members and formation of credit unions. It directed the Commissioner to adopt rules to implement the subdivision relating to small groups (Minn. Stat. § 52.05, subd. 2). The Legislature specified that the rules must provide that groups with a potential membership of less than 1,500 would be considered too small to be feasible, absent a compelling reason to the

contrary; and groups with a potential membership in excess of 1,500 would be considered in light of all the circumstances relevant to the objectives of the subdivision and, finally, that all group applications, with certain exceptions, would be considered separately from any consideration of the membership of existing credit unions. In other words, a small group with a common bond different from that of an existing credit union could still be allowed to join the existing credit union -- the common bonds of the small group and the existing credit union do not have to be identical, or even overlapping.

10. Pursuant to the legislative directive to adopt rules, the Commissioner published a Notice of Intent to Solicit Outside Opinion in June of 1987 and first proposed rules in November of 1987 (see 12 State Register 9292, November 2, 1987). However, these were withdrawn on November 30, 1987, after certain credit unions indicated that they would object to the proposed rules. Approximately a year later, on September 26, 1988, the Commissioner proposed a new set of rules, but they, too, were withdrawn after credit union opposition surfaced on October 17, 1988. 13 State Register 689 and 975. Finally, on April 17, 1989, the Commissioner proposed a third set of rules. 13 State Register 2480. These drew a sufficient number of requests for a public hearing so that the Commissioner determined to proceed with the hearing which is the subject of this Report.

11. The proposed rule is very brief, consisting of a single rule (proposed Part 2675.6400) having six subdivisions. Only one part of the proposed rule drew any adverse comment. That was the very last paragraph, which is subpart 6.B. The remainder of the rule was uncontested, and without further discussion it is found that the Department has justified the need for and reasonableness of its adoption. This Report will focus upon proposed subpart 6.B.

12. The proposed rule defines a "select group" as one that has a common bond but cannot feasibly form and maintain a credit union with its own membership, and desires to join an existing credit union. The uncontested subparts of the rule provide for an application procedure, and other procedural mechanisms for the Commissioner's approval or disapproval of an application for "select group" status. Subpart 6 of the proposed rule reads as follows:

[Subsequent action by an existing credit union.] For an existing credit union to qualify for approval of a bylaw amendment to include an eligible select group in its field of membership, in addition to the requirements in Minnesota Statutes, 52.02, the existing credit union must be capable of serving the eligible select group, and the commissioner may require:

- A. the existing credit union and representatives of the eligible group to agree on and submit a plan of operation to facilitate servicing of the members of the eligible select group for the commissioner's consideration on a case-by-case basis; and
- B. a statement that solicitations will not be directed at individuals to join the select group as a condition for membership in the credit union.

It was this last provision, relating to solicitations, which drew comments and criticisms, and triggered the hearing.

13. The impetus for the proposed rule prohibiting solicitation is the fear that an existing credit union could use the "select group" mechanism to obtain a "wide open" field of membership, and attract members (and their deposits and loan business) from a much larger pool than they could otherwise draw from if limited to the original "common bond". An actual example, drawn

from the hearing record, will illustrate this. The St. Paul Postal Employees Credit Union applied to have the Miller Scholarship Fund (a scholarship fund for postal employees' children) included in its field of membership under the "small group" provisions. The Miller Fund membership at the time of the request was 400 members. After it was approved by the Commissioner, the St. Paul Postal Employees Credit Union published an invitation for anyone to join the Miller Scholarship Fund (and, therefore, become eligible for membership in the credit union) by contributing \$1.00 to the fund. The credit union's Winter 1987 Newsletter, "Dollars & Cents", contained the following:

SPREAD THE GOOD NEWS . . . EVERYONE IS NOW ELIGIBLE TO JOIN!

Due to a recent change in the credit union by-laws, EVERYONE is now eligible to join St. Paul Postal Employees Credit Union! That includes your friends, relatives, neighbors, and fellow employees. The only requirement to join this credit union is a one-time \$1.00 contribution to the John Miller Scholarship Fund. The John Miller Scholarship Fund provides educational scholarships to children of postal employees. Your contribution is TAX DEDUCTIBLE! So help SPREAD THE WORD to everyone you know. Encourage them to stop in, sign up, and enjoy the many benefits your credit union has to offer!!

14. The Minnesota Association of Credit Unions argued that such an arrangement strikes at the heart of the "common bond" requirement, and threatens to undermine the very purpose for which the "parent" credit union was originally formed. Using a postal employees' credit union as an example, the Association argued that such an employees' credit union would be expected to gear its services and operations to postal employees and their families. If a postal strike were to occur, or if there were a massive layoff or cutback in the Postal Service, the credit union would be expected to be sensitive to that situation and assist its members in arranging financial support. It would not be unusual for such an employees' credit union to grant extensions on payment schedules to its members under such circumstances. Those kinds of services would be threatened, however, if a "small group" were allowed to be used as a vehicle to bring in vast numbers of non-employee members. Ultimately, it is likely that they would control the credit union and if a postal strike or layoff were to occur, they would have no reason to grant extensions or other considerations to affected employees. What had started out as an institution to provide specific services to a specific group would end up just like a bank or other institution serving the general public -- it could not be expected to give any special consideration to its founders. Because of this, and because of a desire to protect their members from solicitation by overly-aggressive

credit unions, the Association favors the rule as proposed, which would prohibit the solicitation of individuals to join a select group.

15. The proposed rule is opposed by the Minnesota League of Credit Unions. The League is not opposed to any of the other provisions in the proposed rule except subpart 6.B. The League alleges:

a. The Commissioner does not have statutory authority to regulate solicitations or advertising;

b. The credit unions and their members have constitutionally guaranteed rights of freedom of speech and freedom of assembly;

c. The proposed rule is arbitrary and capricious since it would only apply to credit unions adding a select

group after the effective date of these rules, not those which have already added a select group before the effective date; and

d. The Department's Statement of Need and Reasonableness fails to present the arguments in favor of the proposed subpart.

Each of these arguments will be discussed below.

16. The Department is relying upon two statutes to support its authority to adopt these rules. The first is Minn. Stat. § 45.023, which reads as follows:

The commissioner of commerce may adopt, amend, suspend, or repeal rules, including emergency rules, in accordance with chapter 14, and as otherwise provided by law, whenever necessary or proper in discharging the commissioner's official responsibilities.

Minn. Stat. § 52.05, subd. 2, amended in 1987, provides in pertinent part as follows:

The commissioner shall adopt rules to implement this subdivision. These rules must provide that . . .

Following are the three conditions discussed earlier in describing the 1987 amendment.

17. The listing of three items which the rule must contain does not prevent the Commissioner from including other matters. If it did, there would be no reason to grant the Commissioner rulemaking authority, as the three items would already have been spelled out by the Legislature and there would be no need for a rule. Therefore, the fact that solicitation or advertising is not mentioned as one of the three items required to be included in the rule does not mean that the Commissioner has exceeded his statutory authority. The provision of section 45.023 is dramatically broad -- it empowers the Commissioner to adopt rules "whenever necessary or proper in discharging the Commissioner's official responsibilities." One of the Commissioner's responsibilities, as set forth in Minn. Stat. § 52.06, is the supervision of credit unions. An examination of all of chapter 52 leaves no doubt but that the Commissioner is the sole "policeman" of state chartered credit unions. It

is the Commissioner who is empowered to issue cease and desist orders.
It is
the Commissioner who is empowered to suspend a credit union's operation
or
instigate an investigation and review by the advisory task force. It
is the
Commissioner who is empowered to apply to the district court for the
appointment
of a receiver. Finally, it is the Commissioner who is empowered to
accept and
rule on applications for new credit unions or for new select groups and
determine whether there is an adequate common bond. It is, therefore,
within
the Commissioner's broad statutory authority to adopt rules to protect
the

concept of "common bond" from subversion from an open field solicitation. The Administrative Law Judge finds that the Commissioner does have statutory authority to adopt the proposed subpart.

18. The League's second assertion is that the proposed rule violates constitutionally guaranteed rights of freedom of speech and freedom of assembly.

The solicitation is "commercial speech", which can be regulated by the government so long as certain restrictions are met. In the case of *Central Hudson Gas &-Electric- Corporation v. Public Service Commission-of New York*, 447 U.S. 557, 100 S. Ct. 2343, 65 L.Ed.2d 341 (1980), the Supreme Court set forth a four-part test to determine the constitutionality of restrictions on commercial speech. The four parts of the test are:

- (1) whether the commercial speech in question deals with a lawful activity and is not misleading. If the activity is both lawful and the speech is not misleading, then the government's power is more limited;
- (2) whether the governmental interest asserted in support of the restriction is substantial;
- (3) whether the restriction imposed directly advances the governmental interest asserted; and
- (4) whether the restriction goes no further than necessary to serve the governmental interest.

Central Hudson, 447 U.S. at 564.

In a more recent case, the court backed away from the last of these requirements, which had come to be known as the "least restrictive" test. In the case of *Board of Trustees of the State University of New York v. Fox*, - U.S. - , 106 L.Ed.2d 388, 109 S. Ct. 3028, 57 U.S.L.W ' 5015 (June 29, 1989), the court indicated that requiring the absolutely least restrictive approach was inconsistent with past decisions, and was too difficult to apply. The court stated:

In sum, while we have insisted that the "free flow of commercial information is valuable enough to justify imposing on would-be regulators, the cost of distinguishing . . . the harmless from the harmful"

(citations omitted), we have not gone so far as to impose upon them the burden of demonstrating that the distinguishment is 100% complete, or that the manner of restriction is absolutely the least severe that will achieve the desired end. What our decisions require is a "fit" between the legislature's ends and the means chosen to accomplish those ends, a fit that is not necessarily perfect, but reasonable, that represents not necessarily the single best disposition but one whose scope is "in

proportion to the interest served,"; that employs not necessarily the least restrictive means but . . . a means narrowly tailored to achieve the desired objective. Within those bounds, we leave it to governmental decision-makers to judge what manner of regulation may best be employed.

Therefore, the government may restrict commercial speech, such as the solicitation of individuals to join a select group in order to allow them to become members of a credit union, so long as it meets the four Central-Hudson tests, as modified by Fox. The first three Central Hudson tests are met. A question arises, however, with regard to the fourth -- is the Commissioner's proposed rule "narrowly tailored" to achieve the desired objective? The objective is to protect the "common bond" quality of a credit union from unnecessary dilution by those who would try to use the "select group" mechanism to appeal to the broad public at large. The language of the rule itself permits the Commission to require from an existing credit union a statement that solicitations will not be directed at individuals to join the select group.

Implicit in the rule, although not explicitly stated, is the idea that the restriction is aimed at the existing credit union as an entity, and not at its individual members. As the Department stated in its September 22, 1989 post-hearing submission to the Administrative Law Judge:

The rule thus has no impact on the right of credit union members to meet with and speak to whomever they please about any subject they please.

This was submitted in response to charges from the League that individual members have a right to encourage others to become members of a credit union, and to freely associate with whomever they choose. The Administrative Law Judge agrees with the Department, but urges the Department to consider eliminating any question by modifying the language of the proposed rule subpart. The subpart should make it clear that what is being prohibited is the solicitation by the existing credit union, and not by individual members. While the current language is not defective for the reason claimed by the

League, the Department is urged to modify the rule as suggested.

For the reasons set forth above, the Judge finds that the proposed rule does not infringe upon protected commercial speech beyond the bounds allowed by the Fox case, and that it may be adopted without violating either the Federal or State Constitutions.

19. The League next argues that the proposed rule is arbitrary and capricious since it would only apply to credit unions adding a select group after the effective date of these rules, and not to those which have already added a select group before the effective date. While the League is correct in describing the practical effects of the proposed rule, those effects cannot be said to be arbitrary and capricious. Almost every regulatory enactment, whether by the Legislature or by an agency, does have disparate impacts upon those who were able to act before its effective date, and those who were not. See, Monk &

Excelsior v. Minnesota State Board of Health 302 Minn. 502, 22 N.W. 2d 821 (1985); state by Spannus v. Hopf, 323 N.W.2d 746 (Minn. 1982); Welsand v.-State Qf Minn.-R.R. & W. Com'n, 88 N.W.2d 834 (Minn. 1958). For a discussion of "grandfather" rights, see, No Power Line Inc. v. Minnesota Environmental, Quality Council, 262 N.W.2d 312 (Minn. 1977). The Judge finds that the proposed rule is not arbitrary and capricious.

20. The League's final argument is that the rule must be rejected because the Department's Statement of Need and Reasonableness is deficient in its justification for the proposed rule subsection. The Statement of Need and Reasonableness limits its justification to one sentence:

Further, it would be determined that the procedure is not used to defeat the existing statutory limitations for credit unions' field of membership.

At the hearing, Deputy Commissioner Miller expanded upon this by stating that the rules were needed and reasonable because (a) they had been reviewed by the Credit Union Advisory Task Force, and supported by it; (b) that this problem was not just speculative -- he described the circumstances surrounding the St. Paul Postal Employees' Credit Union/Miller Scholarship Fund incident; (c) that the Legislature never intended to allow this vehicle to be used to solicit the general public; (d) that the proposed rule does not impact existing credit unions' primary field of membership -- that they apply only to select groups added by the procedures established under the rules.

After Miller completed his presentation, the Administrative Law Judge offered anybody the opportunity to ask questions of him, but none elected to do so. Instead, the hearing proceeded to take comments from the public. The first person to speak was Thomas E. Haider, staff attorney for the Minnesota League of Credit Unions. Mr. Haider appeared with an 11-page typewritten memorandum setting forth the League's position on subpart 6.B. Clearly, he was not surprised by Miller's testimony. At no time during the hearing did he

request a recess (as provided in the rules, which he was clearly aware of) to allow him time to prepare a response to the Department's arguments in favor of the rule. In fact, in his final post-hearing submission, he stated that the League does not believe it is necessary to recess the hearing because it had identified, in testimony and in previous memoranda, more serious reasons why the rule ought to be rejected. The other trade organization, the Minnesota Association of Credit Unions, also appeared at the hearing with a prepared statement and testified in support of the proposed rule, focusing entirely on the proposed subpart 6.B. and the St. Paul Postal Employees' Credit Union situation. It was not surprised by anything which was raised at the hearing, as they did not submit any post-hearing material.

21. It is concluded that the Department's Statement of Need and Reasonableness -- albeit minimal -- did not prejudice any person in this particular case, and as Mr. Haider himself admits, no purpose would be served by recessing the hearing process at this point in order to "cure" the deficient Statement of Need and Reasonableness. Under these circumstances, there is no reason to take any action concerning this issue. The Department has demonstrated the need for and reasonableness of the proposed rule.

22. Subpart 6 of the proposed rule is defective, however, because it grants unbridled discretion to the Commissioner to impose requirements upon credit unions without standards to guide him. It provides that the Commissioner may require the submission of a plan of operation and the Commissioner may require a statement that solicitations will not be directed at individuals to join the select group. Will the Commissioner require these in all cases, only some, or none? When will he require them, and when will he not? The law in this State has become relatively clear over the years:

Discretionary power may be delegated to administrative officers "[i]f the law furnishes a reasonably clear policy or standard of action which controls and guides the administrative officers in ascertaining the operative facts to which the law applies, so that the law takes effect upon these facts by virtue of its own terms, and not according to the whim or caprice of the administrative officers."

Accordingly, in a rule that grants discretionary authority to the administrative officer, the issue is whether the rule furnishes a "reasonably clear policy or standard of action". . . . An unauthorized unspecific and ambiguous rule allows the administrative officer to create and apply qualification criteria without fulfilling the APA rule-making procedures. Such ad hoc rule-making power is invalid.

Beck, Bakken & Muck, Minnesota Administrative Procedure (St. Paul: 1987) § 24.4, citing from Lee v. Delmont, 228 Minn. 101, 113, 36 N.W.2d 530, 538 (1949).

In order to cure this defect the word "may" must be replaced with the word "shall" or "must", or, in the alternative, the Commissioner must fashion criteria to guide his discretion. In light of the difficulty of fashioning such criteria without creating a "substantial change", the agency is advised to make the simple language change suggested above.

23. The language of the rule itself is not as clear as it could be. It permits the Commissioner to require a statement (presumably from the existing credit union) that solicitations will not be directed at individuals to join

the select group "as a condition for membership in the credit union".
This language initially suggests that the Commissioner is seeking an assurance that persons desiring to join the credit union would not be solicited to join the select group. In other words, the language initially suggests that the Commissioner is seeking a commitment that (to use the previous example) a postal employee (otherwise qualified to join a postal employees' credit union) will not be forced to contribute to the scholarship fund as an Additional condition of joining the credit union. While that is not the interpretation intended by the Department, it is an interpretation that could be drawn from reading the rule. It is recommended, therefore, that the Department consider alternate language to more clearly express what is intended. Such language could read as follows:

- B. a statement that the existing credit union will not solicit individuals to join the select group.

Based upon the foregoing Findings of Fact, the Administrative Law Judge makes the following:

CONCLUSIONS

1. That the Department gave proper notice of the hearing in this matter.
2. That the Department has fulfilled the procedural requirements of Minn. Stat. §§ 14.14, subs. 1, 1a and 14.14, subd. 2, and all other procedural requirements of law or rule.
3. That the Department has demonstrated its statutory authority to adopt the proposed rules and has fulfilled all other substantive requirements of law or rule within the meaning of Minn. Stat. §§ 14.05, subd. 1, 14.15, subd. 3 and 14.50 (i)(ii), except as noted at Finding 22.
4. That the Department has documented the need for and reasonableness of its proposed rules with an affirmative presentation of facts in the record within the meaning of Minn. Stat. §§ 14.14, subd. 2 and 14.50 (iii).
5. That the Administrative Law Judge has suggested action to correct the defects cited in Conclusion 3 as noted at Finding 22.
6. That due to Conclusion 3, this Report has been submitted to the Chief Administrative Law Judge for his approval pursuant to Minn. Stat. § 14.15, subd. 3.
7. That any Findings which might properly be termed Conclusions and any Conclusions which might properly be termed Findings are hereby adopted as such.
8. That a finding or conclusion of need and reasonableness in regard to any particular rule subsection does not preclude and should not discourage the Department from further modification of the proposed rules based upon an examination of the public comments, provided that no substantial change is made

from the proposed rules as originally published, and provided that the rule finally adopted is based upon facts appearing in this rule hearing record.

Based upon the foregoing Conclusions, the Administrative Law Judge makes the following:

RECOMMENDATION

It is hereby recommended that the proposed rule be adopted except where specifically otherwise noted above.

Dated this day of October, 1989.

Law Judge

Peter C. Erickson Administrative