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National Association of Federally-Insured Credit Unions

May 21, 2018

Monica Jackson
Office of the Executive Secretary
Bureau of Consumer Financial Protection
1700 G Street, NW
Washington, DC 20552

RE: Request for Information Regarding the Bureau's Supervision Program
(Docket No. CFPB-2018-0004)

Dear Ms. Jackson:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), the only national trade association focusing exclusively on federal issues affecting the nation's federally-insured credit unions, I am writing in response to the Bureau of Consumer Financial Protection's (Bureau) request for information regarding its supervision program.

General Comments

NAFCU believes that the Bureau's supervision and examination authority over credit unions with more than \$10 billion in total assets creates needless administrative burdens and results in a fragmented examination process. As credit unions approach the \$10 billion dollar threshold, compliance costs dramatically rise to accommodate the Bureau's supervisory oversight. Furthermore, the cost of getting compliance right can be extraordinarily expensive. One NAFCU member reported spending over \$10 million to comprehensively prepare for Bureau examinations, a price that includes the purchase of new computer systems and a significant expansion in staff. For state chartered, federally insured credit unions, the Bureau's supervisory jurisdiction results in three layers of examination that span state and federal agencies, causing significant disruption to credit union operations. In essence, the establishment of new compliance infrastructure to meet the Bureau's inappropriately tailored expectations is likely to detract from investment in new products or services that would be of greater value to members. Accordingly, NAFCU believes that the Bureau should exempt credit unions from the provisions of section 1025 of *The Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank Act), and allow the National Credit Union Administration (NCUA) to supervise federally insured credit unions (FICUs) of all asset sizes.

Credit unions, by virtue of their member-owned structure, democratic control, and volunteer boards, strive to maintain the highest standards of compliance because they are directly accountable to their membership. At the consumer protection level, credit unions present minimal risks, and have rightfully earned their reputation as consumer-friendly institutions dedicated to improving their members' financial wellbeing. As a result, Bureau oversight only

distracts from credit unions' core mission of service, and needlessly duplicates the supervisory functions of the NCUA, credit unions' historical regulator and an agency that has demonstrated ample capacity to examine and enforce federal consumer financial law. Consolidation of supervisory authority with the NCUA would help achieve more efficient examinations and conserve Bureau resources, which would be better spent policing the largest and riskiest actors in the financial marketplace.

The Bureau should exempt credit unions from its supervisory jurisdiction and transfer examination responsibilities to the National Credit Union Administration (NCUA).

Section 1025 of the Dodd-Frank Act vests the Bureau with the authority to supervise credit unions with more than \$10 billion in total assets. In addition, section 1025(b)(1) of the Dodd-Frank Act grants the Bureau exclusive authority to conduct examinations of such credit unions for the purposes of assessing compliance with federal consumer finance laws, obtaining information about associated compliance systems, and detecting associated risks to consumers. Despite these provisions, the Bureau has legal authority to exempt credit unions from its supervisory jurisdiction—either by practical delegation of its supervisory functions to the NCUA or by exercise of the Bureau's broad exemption authority under section 1022(b)(3).

Although the Bureau possesses exclusive authority to conduct examinations, section 1025(b)(2) provides that the Bureau "shall coordinate its supervisory activities with the supervisory activities conducted by prudential regulators." Furthermore, section 1025(b)(3) provides that in exercising its supervisory function, the Bureau shall, to the fullest extent possible, use reports that have been provided to federal agencies. These provisions, when read together, permit the Bureau to delegate its examination and supervision functions to the NCUA if it so chooses.

The Bureau may also exempt by regulation any class of covered person "from any provision of" Title X of the Dodd-Frank Act pursuant to its authority under section 1022(b)(3)(A). NAFCU believes that exempting credit unions from the provisions contained in section 1025 would be the best way to reduce unnecessary administrative and regulatory burdens, free up the Bureau's resources to examine the largest and most complex financial institutions, and enable more consistent and cost-effective examination at the NCUA.

FICUs of all asset-sizes should be examined and supervised by the NCUA. The Chairman of the NCUA Board agrees. In a letter to the Bureau's previous director, Richard Cordray, Chairman McWatters asked that the agency consider "exempting federally insured credit unions [...] from the examination and enforcement provisions of section 1025 of the Consumer Financial Protection Act of 2010 (CFPA)."¹ Furthermore, Chairman McWatters noted that consolidating examination and enforcement functions at the NCUA for FICUs with more than \$10 billion in assets would be a "small shift in burden." Of the more than 5,500 FICUs operating today, only seven have \$10 billion or more in assets as of March 2018.

In exercising its exemption authority under Section 1022(b), the Bureau must take into account three factors: (1) the total assets of the class of covered persons; (2) the volume of transactions

¹ Mark J McWatters, CREDIT UNION EXAMINATION AND ENFORCEMENT (July 6, 2017), 2, available at <https://www.ncua.gov/newsroom/Documents/mcwatters-letter-to-CFPB-credit-union-examination-enforcement.pdf>.

involving consumer financial products or services in which the class of covered persons engages; and (3) existing provisions of law which are applicable to the consumer financial product or service and the extent to which such provisions provide consumers with adequate protections. NAFCU and the NCUA² find that upon consideration of these factors, an exemption for FICUs is warranted.

First, the total assets of FICUs currently subject to the Bureau supervisory jurisdiction are dwarfed by that of other depository institutions. In fact, the total assets in the credit union industry continue to be eclipsed by the individual total assets of any of the four largest U.S. banks. The Bureau forgoing direct supervision and examination of seven credit unions hardly impacts the extent of its jurisdiction or capacity to regulate consumer financial products or services throughout the broader economy.

Second, NAFCU believes that any assessment concerning the volume of transactions should be contextualized in terms of the historical conduct of credit unions. As member-owned and democratically controlled institutions, credit unions have consistently demonstrated that they present minimal consumer risks. Credit unions are connected to their communities in ways that large, national banks are not and are directly invested in their members' financial well-being.³ Furthermore, the Bureau's former director—along with its legislative architect—have, on various occasions, publicly stated that if all lenders had behaved the way credit unions had, there likely would not have been a financial crisis.⁴ The former director's assessment of credit unions rings true today:

"[Credit unions] were not underwriting the bad loans that brought down the housing market. Instead, you continued to uphold sound underwriting standards even though you lost customers and market share to irresponsible lenders who did not play by the rules. And you sounded the alarm well before the growing irregularities in the mortgage market caused the credit crunch that sank the economy."⁵

NAFCU believes that the Bureau's supervisory authority over seven large credit unions adds no benefit to the industry's preexisting culture of compliance and member-focused service. In addition, a credit union exemption from section 1025 would neither deprive the Bureau of its rulemaking authority nor limit the ability of the NCUA to supervise compliance with and enforcement of consumer financial regulations. Thus, there is little reason for the Bureau to insist on direct oversight.

² See *id.* at 3.

³ See Prepared Remarks of CFPB Director Richard Cordray at the White House Conference on Aging Regional Forum (April 27, 2015), available at <https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-the-Bureau-director-richard-cordray-at-the-white-house-conference-on-aging-regional-forum/>.

⁴ See Prepared Remarks of CFPB Director Richard Cordray at the National Credit Union Administration Webinar, (Feb. 10, 2015), available at <https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-the-Bureau-director-richard-cordray-at-the-national-credit-union-administration-webinar/>; see Remarks by Senator Elizabeth Warren on the Re-Nomination of Rich Cordray to be Director of the Consumer Financial Protection Bureau (July 15, 2013), available at <https://www.warren.senate.gov/newsroom/press-releases/remarks-by-senator-elizabeth-warren-on-the-re-nomination-of-rich-cordray-to-be-director-of-the-consumer-financial-protection-bureau>.

⁵ Cordray, *supra*, note 4.

Third, exempting credit unions from section 1025 would not result in any regulatory gaps or loss of oversight; instead, the Bureau would be returning supervisory functions to the agency most qualified to examine credit unions. As stated previously, the NCUA is best equipped to examine FICUs of all asset sizes and can do so more efficiently than the Bureau. Moreover, the Bureau would not—by granting such an exemption—abdicate any of its general rulemaking authority or contravene any requirement that FICUs be examined for compliance.

In sum, NAFCU believes that an exemption from section 1025 is supported under each of the three factors listed in section 1022(b). Not only would such an exemption reduce the burdens associated with a parallel examination process, it would ensure that examinations are consistent with the NCUA's more informed understanding of the credit union risk landscape.

However, should the Bureau decline to exempt credit unions from section 1025, NAFCU believes there are also technical changes that can ease burdens and achieve a fairer examination process.

The Bureau should adopt more reasonable timeframes for collecting information and documents from a supervised entity prior to the commencement of an examination.

As set forth in the Supervision and Examination Manual (Examination Manual), the Bureau's current policy for scoping information requests is to give supervised credit unions, "whenever feasible," approximately 60 days advance notice before the commencement of an onsite examination.⁶ However, the Bureau does not specify when the actual request must be provided or answered, and permits the examiner in charge (EIC) to send requests with any deadline that "generally ensures" the supervised entity has sufficient time to provide a response.

Due to the lack of any concrete timeframes, examinations may be conducted in a less than efficient manner, particularly when the judgment of the EIC overestimates the supervised credit union's capacity to provide comprehensive responses in a short period of time. Furthermore, having less than 60 days to respond to requests that are often complex or involve assembly of unconventional data often results in disruption to a credit union's operations. Accordingly, NAFCU believes that the Bureau should provide at least 60 days advance notice for the purpose of scoping its information request, and also permit a supervised credit union to respond within 60 days of actually receiving the request.

The Bureau should promote a more flexible examination appeals process that provides more meaningful relief.

The Bureau's current supervisory appeals policy states that the filing of an appeal will not prevent the agency from pursuing an enforcement action. NAFCU believes that the appeals process may be underutilized as a result of this significant caveat, which does not relieve the supervised entity of future enforcement risk. Furthermore, the Bureau states that the appeals process does not relieve a supervised entity from complying with supervisory decisions and actions during the appeals process. While the Bureau may temporarily suspend a requirement to

⁶ See CFPB, Supervision and Examination Manual – Examinations, 5 (June 2017), *available at* https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201706_the_Bureau_supervision-and-examination-manual.pdf

comply with supervisory actions or decisions at its discretion, there is no established process or set of standards for requesting the Bureau's forbearance during the pendency of the appeal.

NAFCU believes that the Bureau's decision to adopt opaque mechanisms to guide its supervisory appeals process introduces unnecessary uncertainty and creates a strong disincentive for institutions to avail themselves of what should be a useful tool for addressing erroneous exam findings. Accordingly, NAFCU recommends that the Bureau adopt a policy recognizing that a successful appeal of a supervisory determination should foreclose subsequent enforcement action based upon the appealed determination or finding. The Bureau should also adopt transparent procedures for entities who are seeking temporary relief from supervisory action during the pendency of their appeal.

The Bureau should adopt more reliable mechanisms for factoring complaint data into examinations.

The Bureau's current policy for assessing risks related to unfair, deceptive, or abusive acts and practices (UDAAP) permits examiners to consider consumer complaints, despite the fact that consumer complaints are not fully verified. While the Bureau's Examination Manual states that examiners should consider the "context and reliability of complaints," it also advises examiners to flag issues when "consumers repeatedly complain" about an institution's product or service.⁷ In addition, the Examination Manual notes that even relatively minor complaints should be treated seriously. For example, the Bureau advises examiners to treat complaints alleging misunderstanding of terms and conditions as a "red flag."⁸ The Examination Manual further states that consumer complaints alleging misunderstanding "may provide a window into the perspective of the reasonable consumer."⁹ Yet the Bureau has never defined a reasonable misunderstanding, which grants examiners considerable discretion to inflate the importance of individual complaints in order to demand lengthy and burdensome document production.

NAFCU believes that exam scoping should be based on objective criteria and verifiable information. Accordingly, the Bureau should avoid assigning "red flags" to particular complaint trends before it has fully verified all the facts in the underlying complaint narratives. Treating repeat complaints or misunderstandings as inherently suspicious overstates the reliability of a complaint system that is, by its very nature, designed to invite subjective criticism. NAFCU intends to provide additional comments on the role of the consumer complaint database in separate comments, but believes the Bureau should reconsider its current "red flag" methodology. Additionally, NAFCU recommends that the Bureau fully verify the facts in complaints that it relies upon for examination scoping purposes

Updates to the Bureau's Examination Manual should be accompanied by *Federal Register* notices and official redlines.

Given the length and breadth of the Bureau's Examination Manual, changes to its contents should be accompanied with a redline document to provide supervised institutions with the ability to see

⁷ See *id.* at 10.

⁸ See *id.* at 9.

⁹ *Id.*

exactly how particular policies have changed. The Bureau should also endeavor to publish its examination playbooks as they are updated. This would improve the transparency of the agency's examination processes which are not covered in the Examination Manual.

The Bureau should favor supervisory processes over enforcement actions, and provide entities with a more reasonable timeframe to respond to potential action and request for response (PARR) letters.

The Bureau currently uses PARR letters to inform supervised entities of legal violations that could potentially result in supervisory or enforcement action. Upon receipt of a PARR letter, the entity is given the chance to respond with pertinent information relative to the preliminary findings, which are derived from examination review materials.¹⁰ The Bureau's current policy regarding PARR letters is to focus on "significant violations of Federal consumer financial law," but letters may include discussion of "non-routine questions of law," including unfair, deceptive, or abusive acts or practices.¹¹

To promote the resolution of identified concerns through the supervisory process, the Bureau should be required to issue PARR letters before it commences an enforcement action. NAFCU also recommends that PARR letters invite the supervised party to meet and discuss alleged violations with senior officials. Such a policy would provide supervised entities with a reasonable opportunity to address the Bureau's concerns without the disruption and publicity that accompany an enforcement action. Furthermore, given that the Bureau has developed the scope of UDAAP through enforcement actions, supervised entities may not be aware of the Bureau's evolving and potentially novel interpretations of the law. Consequently, NAFCU believes that it is only fair to give parties a meaningful chance to clarify the facts or resolve alleged violations before they are raised in a notice of charges. The Bureau should also provide parties with at least 30 days to address identified violations in a PARR letter and freely grant requests for extensions of time.

Conclusion

NAFCU appreciates the opportunity to provide comments on this request for information regarding the Bureau's supervision program. If you have any questions or concerns, please do not hesitate to contact me at amorris@nafc.org or (703) 842-2266.

Sincerely,



Andrew Morris
Regulatory Affairs Counsel

¹⁰ See CFPB, SEFL Integration 3.2, Examination Playbook.

¹¹ See *id.*