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National Association of Federally-Insured Credit Unions

July 15, 2022

The Honorable Todd M. Harper, Chairman
The Honorable Kyle S. Hauptman, Vice Chairman
The Honorable Rodney E. Hood, Board Member
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

RE: Part 701.36 Amendment

Dear Chairman Harper, Vice Chairman Hauptman, and Board Member Hood:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing to urge the National Credit Union Administration (NCUA) to reevaluate and amend its regulations in Part 701.36 addressing federal credit union occupancy, planning, and disposal of acquired and abandoned premises and incidental powers. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 130 million consumers with personal and small business financial service products. The COVID-19 pandemic has changed the nature of work and had a profound impact on commercial office space utilization. NAFCU urges the NCUA to recognize the need that credit unions have, now more than ever, for flexibility in the occupancy and use of their premises. Specifically, NAFCU requests that the NCUA amend its Part 701.36 to reduce the requirement that credit unions occupy and use at least 50 percent of their premises, and instead require 25 percent occupancy and use. NAFCU appreciates your attention to this matter, and we hope that you will work with us to recognize the altered landscape of office usage and the benefits to safety and soundness that will follow from providing flexibility to credit unions in how they manage their properties.

Background

In order to ensure safety and soundness, and in accordance with the *Federal Credit Union Act* (FCU Act), federal credit unions (FCUs) are prohibited from investing in real estate for speculative purposes or otherwise engaging in real estate activities that do not generally support their financial services to members. In 2016, as part of the NCUA's Regulatory Modernization Initiative, the NCUA issued a final rule amending NCUA Rules and Regulations Part 701.36 governing FCU occupancy, planning, and disposal of acquired and abandoned premises and Part 721 regarding incidental powers.[1] The final rule eliminated a requirement in Part 701.36 (formerly known as the fixed assets rule) that an FCU must plan for, and eventually achieve, full occupancy of acquired premises.

Additionally, the final rule modified the definition of "partially occupy" in Part 701.36(b) to mean occupation and use, on a full-time basis, of at least 50 percent of a premises by a FCU or by a

[1] *See* 81 FR 93577; 12 CFR 701, 12 CFR 721 (2016).

combination of the FCU and a credit union service organization (CUSO) in which the FCU has a controlling interest. The final rule also amended the excess capacity provision in the NCUA's incidental powers rule, Part 721, to clarify that an FCU may lease or sell excess capacity in its facilities, but it need not anticipate that such excess capacity will be fully occupied by the FCU in the future.

In the final rule, the NCUA addressed comments that suggested the following changes:

- satisfaction of the 50 percent occupancy requirement should be "grandfathered" once initially achieved by the FCU.
- because mixed-use developments in urban areas sometimes require shared space, common areas and other shared fixtures and utilities should count toward the 50 percent partial occupancy requirement.
- the 50 percent occupancy threshold be removed or, alternatively, that the threshold be reduced to no more than 25 percent.

In response to these recommendations, the NCUA noted that the final rule would retain the waiver provisions for the partial occupancy requirement, which allow FCUs to request a waiver of either the 50 percent requirement or the six-year requirement. The NCUA stated that the waiver process is designed to allow the agency to evaluate unique circumstances, such as instances in which certain zoning laws affecting a particular property would support the NCUA accepting less than 50 percent occupancy or extending the time period for compliance. The NCUA expressed its belief that it was important to maintain the partial occupancy requirement to ensure safety and soundness, that the 50 percent standard would provide FCUs with a clear guideline for achieving compliance, and that the waiver provisions would ensure further flexibility when warranted.

If the NCUA Board were to apply the same logic to reevaluating Part 701.36 now as it did when amending Part 701.36 in 2016, it could reasonably find it appropriate to reduce the 50 percent occupancy and use requirement. The requirement that FCUs occupy and use, on a full-time basis, at least 50 percent of their premises was a reasonable safeguard against FCUs engaging in real estate speculation when it was introduced in 2016. However, the dynamic surrounding office space and in-person work has shifted dramatically in the intervening years, making the requirement much less reasonable today. Fifty percent occupancy and use was a subjective requirement in 2016, and it remains subjective now. The Board noted in its final rule that it had decided upon the 50 percent requirement because, when coupled with the option of waivers, the rule provided FCUs with flexibility, while ensuring safety and soundness.

In its final rule, the Board noted:

> "[T]he United States Supreme Court has emphasized that an 'initial agency interpretation is not instantly carved in stone,' and 'to engage in informed rulemaking, [an agency] must consider varying interpretations and the wisdom of its policy on a continuing basis,' indicating that an agency may change its interpretive position on the statutes it administers. The final rule is reasonable and

> eliminates the imposition of unnecessary hardship on FCUs whose growth potential and member service strategies may be hampered by the current rule."[2]

This line of reasoning is both correct and easily applicable to the current situation. Given the tremendous shifts experienced due to COVID-19, the Board should consider the "wisdom of its policy on a continuing basis." Part 701.36 imposes an unnecessary hardship on FCUs and hampers growth potential, member service strategies, and the increased safety and soundness that credit unions would experience from increased lease income. Reducing the occupancy requirement from 50 percent to 25 percent is a reasonable and warranted response to conditions currently facing the credit union industry.

Authority to Amend

As a foundational matter, it is important to note that the NCUA has the statutory authority to provide greater flexibility in the partial occupancy requirements of Part 701.36. Section 107(4) of the FCU Act authorizes an FCU to purchase, hold, and dispose of property necessary or incidental to its operations.[3] While NAFCU recognizes that the FCU Act prohibits an FCU from "engag[ing] in real estate activities that do not support the purpose [of providing financial services to its members]," we note that the statute does not prescribe specific occupancy requirements for permissible real estate holdings.[4]

Traditionally, the NCUA has interpreted this statutory language to mandate full occupancy within a specified period. In the years since Part 701.36 was amended, the NCUA has interpreted the statute to mandate at least partial occupancy of 50 percent. NAFCU and its members believe this interpretation is unnecessarily restrictive, as the FCU Act includes no express occupancy mandate on real estate that supports the purpose of providing financial services to credit union members. To further emphasize the subjective nature of the 50 percent standard, in the 2016 Final Rule, the Board noted that "the ability to request a waiver from the partial occupancy requirement is, in part, an acknowledgement that there may be circumstances where an FCU could prudently occupy a lesser percentage of the premises and still comply with the Act."[5]

Accordingly, we urge the agency to reduce the 50 percent partial occupancy requirement from the Part 701.36 to a 25 percent partial occupancy requirement. Easing this restriction would allow FCUs to stay competitive with other financial institutions in the current environment, which demands that institutions be able to provide their members with improvements, such as new products, services, and locations, and adopt new technologies in a timely fashion.

COVID-19 Impact

When the pandemic hit the U.S. hard in March 2020, millions of workers began working from home – an unprecedented and ongoing phenomenon facilitated by the rise of connectivity and

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[2] *See* 81 FR 93577; 12 CFR 701 (2016).
[3] *See* 12 U.S.C. § 1757(4) (1934).
[4] *See* 69 FR 58039, 58041.
[5] *See* 81 FR 93577; 12 CFR 701 (2016).

communication technologies. Before the pandemic, the conventional wisdom had been that offices were critical to productivity, culture, and winning the war for talent. Companies competed intensely for prime office space in major urban centers around the world, and many focused on solutions that were seen to promote collaboration. Now, more than two years since the start of the pandemic, organizations with strong in-person cultures have increasingly come to the realization that they have not lost a step with remote work. The use of Zoom, Microsoft Teams, Webex, or other video conferencing services has skyrocketed since the start of the COVID-19 pandemic. Similarly, organizations with limited technological capacity have found that these platforms are easy to adopt. COVID-19 has forced the majority of organizations in the country to adapt to these technologies and the result has been a near-universal success.

Estimates suggest that by April 2020, 62 percent of employed Americans were working at home during the crisis, compared with about 25 percent a couple of years ago.[6] NAFCU's Economic and CU Monitor Survey from April 2020 found that nearly every credit union (89 percent) reported adopting social distancing procedures, such as expanded telework policies, restrictions on non-essential travel, and enhanced cleaning.[7] Other data indicated that once restrictions were removed, and assuming that employers allowed the choice, most U.S. workers would work remotely as much as possible.[8] Many employees have emphasized the benefits of reduced commutes and greater flexibility in balancing their personal and professional lives.[9] Simultaneously, many employers are redefining what the "workspace" will look like and are reevaluating the need to have all employees in the office all the time. These considerations have resulted in individual organizations issuing return-to-work policies that employ in-person, remote, and hybrid work plans in varying configurations, however, as a whole, the number of in-person workers has been significantly reduced.

The Federal government has been similarly impacted and a workforce with a formerly strong in-person culture that generally reserved remote work for employees with seniority, is now supportive of legislation that would encourage federal agencies to expand their telework programs for the long-haul.[10] Most importantly, many credit unions have experienced a massive shift in the prevalence of remote work, a shift that most expect to be permanent. In NAFCU's 2021 State of the Industry survey, respondents were asked to report the percent of back-office staff workdays that were performed remotely prior to the COVID-19 pandemic as compared with their estimate of staff remote workdays two years in the future.[11] The results were startling, with 39 percent of respondents reporting 0 percent remote work and 43 percent reporting 0-5 percent remote work in the pre-COVID days. Conversely, 24 percent of respondents estimated 30-50 percent of staff

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[6] *See* Megan Brenan, Gallup, "US Workers Discovering Affinity for Remote Work," (April 3, 2020) *available at* https://news.gallup.com/poll/306695/workers-discovering-affinity-remote-work.aspx.
[7] NAFCU Economic and CU Monitor Survey, April 2020.
[8] *See* Mckinsey & Company, "Reimagining the office and work life after COVID-19" (June 8, 2020) *available at* https://www.mckinsey.com/business-functions/people-and-organizational-performance/our-insights/reimagining-the-office-and-work-life-after-covid-19.
[9] *Id*.
[10] *See* Federal News Network, "House committee pushes forward on encouraging federal telework expansion" (June 16, 2022) *available at* https://federalnewsnetwork.com/congress/2022/06/house-committee-pushes-forward-on-encouraging-federal-telework-expansion/
[11] NAFCU State of the Industry Survey, 2021.

workdays would be remote, and 15 percent estimated 20-30 percent remote work two years in the future.

As pandemic restrictions abate and workers fail to return to the office in pre-pandemic numbers, vast swathes of office space remain vacant throughout the country. This is true too of FCUs, many of which have realized that more work can be done remotely and that less office space is needed to conduct the functions of the credit union. It is understandable, then, that landlords, including FCUs, are being forced to be increasingly innovative in their struggle to fill these empty spaces. For example, The New York Times reports that office space is now the most frequent target for conversion to residential rental units, over hotels and factory space: "Converted offices make up about 25 percent of the more than 52,700 rental units slated to become available in 2022 in properties built for other purposes."[12] This relatively permanent conversion of office space into alternative uses hints at a stark reality that is coming into clearer focus for landlords and property owners: the "work from home" revolution is here to stay, and landlords and employers will need to adapt or face losses. For the thousands of FCUs that own brick and mortar locations, Part 701.36 imposes a significant, though subjective and easily remedied, barrier to their ability to adapt.

Even for those credit unions that have maintained pre-pandemic telework policies and office usage, the ability to lease more of their space would enhance their safety and soundness, while simultaneously providing financial access to underserved communities. Credit unions looking to expand and open new branches must weigh the cost of constructing new branches against the cost of purchasing existing construction and converting it to serve credit union members. As previously discussed, vacant office space and other properties are plentiful, while worldwide constraints on the supply of building materials and the sky-high cost of labor often make new construction prohibitive.[13][14] Purchasing existing construction is often the prudent decision for credit unions, but Part 701.36 places restraints on the properties that credit unions can consider purchasing. As the regulation currently exists, a credit union seeking to expand into a new community without building new construction must find a vacant commercial property large enough to accommodate credit union operations, but not so large that credit union operations occupy less than half of the property. This "goldilocks" scenario makes it difficult for credit unions to find a space that is just right and puts an unnecessary barrier in the way of increased financial inclusion. This is especially true in rural and underserved communities that have been consigned to "banking deserts" after the departure of big banks.

Credit unions have a strong desire to offer financial products and services in areas that lack access to them. If the 50 percent threshold were reduced, more credit unions would be able to enter rural and underserved areas, where many existing properties are vacant, and be able to offer financial

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[12] *See* New York Times, "'Living at the Office' Takes On a New Meaning During the Pandemic" (October 14, 2021) *available at* https://www.nytimes.com/2021/10/14/realestate/offices-hotels-converted-to-rental-apartments.html.
[13] *See* Wealth Management, "Hotel Developers Battle Rising Construction Costs to Build More Rooms" (June 27, 2022) *available at* https://www.wealthmanagement.com/lodging-hotel/hotel-developers-battle-rising-construction-costs-build-more-rooms.
[14] *See* YahooNews, "Rise in cost of materials, their accessibility hurdles for Clark County construction" (June 29, 2022) *available at* https://news.yahoo.com/rise-cost-materials-accessibility-hurdles-141000899.html.

access to these communities. Access to lending and other products would also stimulate the local economy and these credit unions would be able to lease more unused space, thereby creating credit union income and increasing the safety and soundness of the credit union itself.

If the NCUA were to reduce the requirement that FCUs must occupy and use at least 50 percent of their premises to 25 percent, credit unions would benefit from much needed flexibility. FCUs that occupied 50 percent of their premises prior to the pandemic but have since seen a reduction in in-person workers would be able to lease unused portions of their premises and save precious credit union dollars. FCUs that wish to expand into new premises but are limited in their search to those buildings or spaces that are of a size which they can expect to occupy and use at least half would have greater flexibility in their search. And FCUs that wish to open premises in mixed-use developments in urban areas that require shared common areas and other shared fixtures and utilities would have increased ability to do so.

Although the Board considered many of these reasons for a reduction in 2016 and responded that the waiver provisions of Part 701.36 were sufficient to evaluate unique circumstances, it is precisely because the impact of COVID-19 is not unique that the waivers no longer suffice. As discussed previously, the COVID-19 pandemic impacted all organizations and all FCUs. Waivers were sufficient to address one-off zoning requirements or unique circumstances that required special consideration from the NCUA. As COVID-19 subsides from pandemic to endemic and it becomes clear that many of the effects of the virus are now permanent, credit unions need similarly permanent solutions that address this problem. Amending Part 701.36 and providing regulatory relief to credit unions is one such solution.

Conclusion

NAFCU would like to thank the NCUA for its continued focus on providing credit unions with much needed regulatory relief that will enhance safety and soundness and allow credit unions greater ability to expand into underserved areas. NAFCU urges the NCUA to provide credit unions permanent flexibility by reducing the occupancy and use requirement of Part 701.36. Thank you for your consideration and we look forward to working with you to attain this crucial flexibility. If we can answer any questions or provide you with additional information, please do not hesitate to contact me or James Akin, Regulatory Affairs Counsel at 703-615-5109 or jakin@nafcu.org.

Sincerely,

Ann C. Petros
Vice President of Regulatory Affairs