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National Association of Federally-Insured Credit Unions

May 31, 2019

Michael J. McKenna
General Counsel
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314

RE: 2019 Regulatory Review

Dear Mr. McKenna:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing to you regarding the National Credit Union Administration's (NCUA) 2019 Regulatory Review of one-third of its regulations. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 116 million consumers with personal and small business financial service products. NAFCU looks forward to an open dialogue with the agency regarding ways to modernize its existing regulations and find new opportunities to provide more flexibility to credit unions so they are able to grow and better serve their communities. NAFCU and its member credit unions greatly appreciate the NCUA Board's openness to closely examining the current and potential effects of the agency's regulations. In recent testimony before Congress, NCUA Chairman Rodney Hood expressed that the agency is reviewing its approach to guidance and is working to reduce regulatory burden on credit unions so that the industry may continue to grow. NAFCU appreciates Chairman Hood's thoughtful comments and strongly supports his position on regulatory reform. NAFCU eagerly awaits future opportunities to work with the NCUA to achieve these objectives.

With respect to the regulations under consideration this year, certain aspects may require Congressional action to achieve full modernization with industry standards and practices today. In such instances, NAFCU urges the NCUA to coordinate with members of Congress and support legislation to update the *Federal Credit Union Act* (FCU Act). As for areas of the regulations in which the agency has ample authority to modify or delete provisions, NAFCU asks that the NCUA carefully consider the recommendations outlined below and continue to provide an opportunity for comment on regulations that are in need of reform.

General Comments

In this letter, NAFCU details its member-recommended changes to the list of regulations under review this year. In addition, in this section, NAFCU requests that the agency evaluate the following items as equally critical in its regulatory review process.[1] Although these items fall

[1] Additionally, as a reference, attached please find NAFCU's 2019 priorities for the credit union industry. This document has been distributed to all current NCUA Board members.

outside the scope of the regulations identified for review in 2019, NAFCU and its member credit unions have highlighted these issues as priorities for the NCUA Board as it strives to modernize rules to provide increased flexibility for credit unions.

Fairness in the Examination Process

The NCUA has made significant strides in its exam modernization initiative and NAFCU encourages the NCUA to continue to find areas for improvement to streamline the examination process and reduce burdens on credit unions. NAFCU is particularly supportive of efforts to incorporate new and emerging technologies, while balancing cybersecurity and data security concerns, to make examinations more efficient and transparent. However, with respect to the NCUA's continuous supervision program, NAFCU asks for increased transparency as to the elements of the program. There is concern that technology could be used as a method to second guess credit union management decisions, which would reduce autonomy.

NAFCU has also heard from its member credit unions that certain aspects of the examination process continue to cause frustration. We continue to hear that informal guidance is sometimes treated as de-facto policy and has resulted in examination findings even though there is no basis in law for faulting the credit union. NAFCU is optimistic that with the recent regional restructuring and supervisory examiner review of examination reports prior to delivery, examinations will continue to improve.

Current Expected Credit Loss (CECL)

The NCUA's 2019 Supervisory Priorities, include examination of credit unions' CECL preparedness efforts as the implementation date approaches. The NCUA recently updated its AIRES questionnaire with a section on CECL preparedness, containing nine questions that examiners will use this year. NAFCU appreciates the agency updating credit unions on what to expect during the examination process regarding CECL preparations. Nonetheless, NAFCU maintains that credit unions should never have been included within the scope of CECL. As such, NAFCU encourages the NCUA to continue to have discussions with the Financial Accounting Standards Board (FASB) to find ways to reduce CECL's burden on credit unions, particularly smaller credit unions with limited resources. NAFCU thanks the NCUA for its continued efforts to educate the industry about CECL and hopes to continue to coordinate with the agency to provide credit unions with access to the information and materials they need to prepare for CECL implementation. Please find a more detailed description of capital issues as well as potential concerns regarding mergers relative to the CECL standard in the Capital Adequacy and Mergers of Federally-Insured Credit Unions sections below.

Regulatory and Supervisory Expectations Regarding Cybersecurity

Cybersecurity continues to be a top concern for NAFCU's member credit unions, especially as technologies advance and cyber criminals become more sophisticated in their approaches to hacking institutions' systems. As the NCUA continues to test and deploy its Automated Cybersecurity Examination Tool (ACET) and begin integrating it with the Cyber Security

Evaluation Tool (CSET), NAFCU urges the NCUA to allow credit unions to adopt the cybersecurity protocols that are most appropriate based on their complexity and risk profile. NAFCU supports the supervision of credit unions' cybersecurity measures to ensure the safety and soundness of the industry, but encourages the agency to refrain from requiring the use of these tools to meet supervisory and regulatory expectations.

Relatedly, NAFCU would also like to reiterate its concerns regarding supervision and examination authority for third-party vendors. Although NAFCU appreciates the NCUA's commitment to enhancing oversight of vendors with respect to cybersecurity examinations, our members continue to have concerns about increased regulatory burden, a lack of examiner training regarding vendor relationships and the potential for such authority to impair the credit union's partnerships, as well as the extent of the NCUA budgetary and staff resources that will be required to establish and manage the supervision of third-party vendors. NAFCU supports the agency's increased focus on cybersecurity but cautions it to critically evaluate whether obtaining third-party vendor authority will be a net positive for an industry that is already subject to strict vendor due diligence requirements. Short of seeking expanded authorities and a larger budget to conduct an entirely new form of examination, the NCUA should consider whether there are alternative mechanisms for overseeing the most interconnected service providers through the FFIEC's joint-examination program.

Finally, NAFCU encourages the NCUA to coordinate with other federal regulators to better identify emerging cybersecurity threats and how to address them. This coordination should include an evaluation of existing approaches to monitoring, sharing, and responding to cybersecurity threats and vulnerabilities and how to improve those processes across the financial services industry.

Below are NAFCU's comments and recommendations regarding the OGC's 2019 review of Regulations Part 700-710.

701.1 Federal Credit Union Chartering, Field of Membership Modifications, and Conversions

Strengthening the credit union dual chartering system is imperative to the future strength and well-being of the credit union industry. The dual chartering system functions best when the state and federal credit union charters keep pace with one another. But in recent years, several states have been much more progressive in modernizing their field of membership (FOM) rules. As a result, the industry has seen multiple credit unions convert to state charters because of the inability to grow under a federal charter. NAFCU supports broader FOM relief including: 1) elimination of, or increasing, the population limits applicable to community charter credit unions (Chapter 2, Section V.A.2 of Appendix B); 2) establishing a formal notification process for credit union making FOM-related applications (Chapter 1, Section VII of Appendix B); and 3) considering new ways to efficiently address mergers (Chapter 2, Sections II.D; IV.D; and V.D of Appendix B).

The NCUA has made substantial efforts to expand credit unions' ability to grow and serve their communities through modernized FOM rules and NAFCU applauds these efforts. Moving

forward, NAFCU encourages the NCUA to ensure that the federal charter keeps pace with changes in state laws, technology, and the financial services industry. Although legislation is necessary to amend portions of the FCU Act's limitations on chartering, the credit union industry as a whole will benefit from the continued modernization of NCUA's chartering and FOM procedures, as well as removing all non-statutory constraints on FOM chartering and expansion.

Greater outreach to underserved areas is of particular importance. More flexibility under the FOM rules would help federal credit unions reach potential members who want and need affordable financial services as well as provide much needed regulatory relief by streamlining the FOM process for community, multiple common bond, and TIP charters alike. NAFCU encourages the NCUA to find additional opportunities for relief under the FOM rules to ensure the future welfare of the credit union industry and the communities they serve.

701.2 Federal Credit Union Bylaws

NAFCU continues to advocate for greater flexibility for credit unions to develop bylaws that cater to their unique fields of membership and dynamic member needs. The NCUA should revisit the bylaws on a more consistent basis to identify and reduce confusing bylaw provisions, and to incorporate technological advances. NAFCU appreciates the NCUA's commitment to updating, clarifying, and simplifying the bylaws. The agency's swift rulemaking process over the past year has allowed credit unions to provide important feedback about how the bylaws are affecting their daily operations and ways in which the bylaws can be improved to provide more opportunities for customization based on the needs of the credit union, its employees and members.

To illustrate, NAFCU recommends the re-establishment of standard and non-standard bylaw amendment categories, each with a distinguishable timeline for approval. An expedited and simple process for bylaw amendments should be adopted, which could include the expansion of the options for "fill-in-the-blank" provisions that have been vetted by the NCUA's Office of General Counsel, and are low risk amendments. In addition, the NCUA should implement a process to notify applicant credit unions of their approval process status. Next, the limitation of services provision should set forth factors to measure physical and verbal abuse so that credit unions can make risk-based decisions on whether to limit services.

The bylaws should continue to allow a quorum at member meetings to include board members, directors, and employees. Members should be permitted to attend meetings and participate utilizing technology, such as video conferencing or web-based conference tools, so long as comprehensive cybersecurity measures are in place. These virtual or hybrid meetings would encourage greater member participation at member meetings. Election options should allow for more combinations utilizing technology. Lastly, the NCUA should expand the definition of "non-participation" to include those members who do not utilize credit union services in a legitimate or legal manner. Credit unions need an expedited process for expelling those members who are a threat to the safety of the credit union, its employees and members. While NCUA's proposed bylaws changes were an improvement in this areas, we believe that incorporating such amendments into the federal credit unions bylaws would provide additional flexibility for the industry.

701.21 Loans to Members and Lines of Credit to Members

Maturity Limits

NAFCU members generally support longer maturity limits in sections 701.21(c)(4)(i)-(ii). NAFCU recognizes the statutory limitations on modifying the 15-year general maturity limit for loans to members in section 701.21(c)(4)(i) but encourages the NCUA to support legislation amending the FCU Act to provide the agency with the discretion to set extended maturity limits for various loan products as appropriate. Flexibility in maturity limits would provide credit unions with a level playing field with other lenders by offering competitive loan products. The existing disparity between the maturity limits and the needs of credit union members leads to increased costs to members, and ultimately hurts credit union growth when members choose to procure a loan from a different lender in order to have an extended loan term.

Specifically, NAFCU urges the NCUA to reevaluate the definition of "principal residence" in section 701.21(g)(2) regarding long-term mortgage loans to include non-owner occupied residences in certain scenarios. In addition, the NCUA should amend section 701.21(f) to extend the maturity limits for those loans for mobile homes, second mortgages, and improvements to residences. Extended maturity limits will provide flexibility and parity for credit unions. Lastly, NAFCU recommends that the NCUA expand the advanced commitment exception in section 701.21(c)(4)(i)(A) to include government-sponsored enterprises (GSEs). The GSEs purchase a sizeable quantity of credit union mortgage loans, demonstrating their willingness to assume the risks of credit union loans and offer longer maturity terms; therefore, there is no reason why the NCUA should restrict maturity limits beyond what the GSEs are willing to allow in the secondary market.

Definition of "Overall Financial Performance" Relative to Compensation

Section 701.21(c)(8) prohibits most credit union employees and officials from receiving compensation made "in connection with any loan" a credit union makes. There are some exceptions to this prohibition, namely that an employee, including senior management, may receive an incentive or bonus based on the credit union's "overall financial performance." *See* section 701.21(c)(8)(iii). Despite these general exceptions, NAFCU member credit unions continue to report issues with NCUA examiner findings that compensation programs that appear to comply with the requirements of NCUA's antiquated rule do not actually fit within its parameters.

In an effort to remedy this issue, the NCUA appropriately issued an advance notice of proposed rulemaking (ANPR) in April 2019. NAFCU appreciates the recommendations of the agency's Regulatory Reform Task Force and the Board's initiative to modernize this outdated and confusing regulation. NAFCU looks forward to engaging with the agency through the rulemaking process to clarify and interpret the term "overall financial performance" to better align with industry practices. Consistent with our previous position, NAFCU again encourages the NCUA to define "overall financial performance" as:

> "A quantifiable metric, set by the board of directors of the credit union, used for the purposes of measuring a credit union's achievement of targeted performance goals. This metric may include, but not be limited to, total asset growth, overall loan growth, return on assets, net-worth ratio, loan-to-value ratio, and delinquency ratios."

Absent further explanation from the NCUA on what "overall financial performance" means and modernization to account for industry practices, NAFCU's member credit unions are concerned that NCUA examiners will continue to apply subjective interpretations of the rule to penalize otherwise compliant compensation programs. NAFCU appreciates the NCUA's response to this issue, and looks forward to NCUA's clarification that the regulation should allow for loan growth to be included as a part of the "overall financial performance" calculation.

701.22 Loan Participations

Loan participations enable credit unions to diversify their loan portfolios, improve earnings, generate loan growth, and manage their balance sheet. In addition, loan participations allow credit unions to generate liquidity. The current rule places a concentration limit on loan participation purchases involving one borrower or a group of associated borrowers to 15 percent of the credit union's net worth, unless waived by the credit union's regional director. Although the rule allows for a waiver, the concentration limit is arbitrary and the NCUA should reevaluate whether this limit is still appropriate. Given the recent regional restructuring, NAFCU would also like to ensure that those credit unions seeking a waiver are still able to do so in a timely and efficient manner.

In addition, NAFCU recommends that the NCUA contemplate an impact study on the benefits and delinquency rates of loan participations over the last few years to ensure that current concentration limits are still appropriate. Potential risks to the National Credit Union Share Insurance Fund (NCUSIF) should be contemplated by this impact study. Loan participations are beneficial for credit unions, and the NCUA should evaluate this rule to ensure access is not impaired.

701.30 Services for Nonmembers within the Field of Membership

The NCUA's regulations regarding the types of services that may be offered to nonmembers are largely limited to certain "money transfer instruments," such as travelers checks, money orders, electronic funds transfers, and remittance transfers. This does not reflect modernizations in payment methods because many consumers utilize prepaid cards and non-reloadable gift cards on a regular basis. The NCUA has explicitly said that the sale of such products to nonmembers is impermissible; however several Legal Opinion Letters have explained instances where such a sale may be permissible if it occurs indirectly while assisting a member.

For example, in a 2003 legal opinion regarding payroll card services for members and whether a member could disburse funds from her share draft account to her employees, the NCUA said: "While the proposed activity may result in nonmembers obtaining store value cards branded by the FCU, the activity is permissible because the FCU is providing a financial service through electronic means to its sponsor, a member of the FCU, by offering an alternative to share drafts."

In a 2008 legal opinion regarding gift cards and whether a member could sell the credit union's gift cards on her website, the NCUA said the activity was permissible as providing an electronic financial service to the member because the credit union would be receiving and transferring funds on behalf of the member.

NAFCU encourages the NCUA to reevaluate this portion of its regulations to determine whether it is appropriate for credit unions to offer prepaid cards or non-reloadable gift cards to nonmembers outside of the context of providing electronic services to members. The NCUA's incidental powers rule permits federal credit unions to engage in preapproved certain activities incidental to its business, including marketing activities that are geared toward attracting or retaining members or encouraging use of the federal credit union's products and services. *See* 12 C.F.R. §721.3(h). Utilizing a prepaid card or non-reloadable gift card as a marketing tool to attract non-members in the hope that they become a member is an activity that fits squarely within this incidental power and should be preapproved.

The NCUA should also consider the effect other agency regulations have had on the availability of certain money transfer instruments, including the Consumer Financial Protection Bureau's (CFPB) rule on remittance transfers. The compliance burden associated with this rule has reduced the number of credit unions that offer remittance transfers, which may mean that consumers are relying on other, more readily available means of transferring money to or from nonmembers. Accordingly, NAFCU requests the NCUA evaluate ways to expand section 701.30 to include providing instruments such as prepaid cards and non-reloadable gift cards as services available to nonmembers within the activities preapproved as an incidental power of federal credit unions.

701.32 Payment on Shares by Public Units and Nonmembers

In general, NAFCU supports the NCUA's May 2019 proposal to increase the limit on public unit and nonmember shares to 50 percent of paid-in and unimpaired capital surplus. The decision to measure the limit as a percent of paid-in and unimpaired capital and surplus less public unit and nonmember shares is a reasonable approach that will help avoid circular increases. It is also a better alternative than the current measure of total shares since it would include undivided earnings. These improvements will help all credit unions attract deposits and facilitate growth, but the greatest benefits will likely accrue to low-income credit unions.

NAFCU asks that the NCUA consider eliminating the language in Section 701.32 which limits the amount of public unit and nonmember shares to either a fixed percentage of the credit union's total shares, or $3 million, whichever is greater. In order to maximize the benefits of nonmember deposit funding, the NCUA should either use a fixed percentage limit as a standalone measure or increase the dollar amount limit based on an assessment of the credit union's overall risk profile.

The NCUA should not foreclose a more flexible approach to waivers of the 50 percent limit. While NAFCU understands the NCUA's safety and soundness concerns related to waivers of the proposed limit on public unit and nonmember shares, the justification for eliminating the waiver relies on historical losses that occurred in a different regulatory environment. Specifically, the proposal draws attention to credit union failures that occurred prior to 1999, when the NCUA's

supervisory tools were far less sophisticated. Supervision of credit unions has advanced considerably since that time and the NCUA's exam modernization efforts should be able to accommodate a waiver process if utilized on a case-by-case basis and within conservative limits.

701.34 Designation of Low-income Status; Acceptance of Secondary Capital Accounts by Low-income Designated Credit Unions

Since the financial crisis tipped our country into recession, credit unions have served as a vital source of capital and market liquidity in local communities. A regulatory capital framework that authorizes subordinated debt (previously referred to as supplemental capital) would grant credit unions an additional option to guard against risk, achieve growth, and ensure that our industry remains a bedrock of stability for the 116 million Americans who currently look to credit unions as a vital source of affordable financial services.

In general, the ability to issue subordinated debt would help credit unions adjust to changing economic conditions more effectively. When a credit union's economic outlook fluctuates, either as a result of asset growth or declines in capital resulting from losses on loans or other assets, it must rely on retained earnings to satisfy regulatory capital requirements. Because retained earnings accumulate slowly, the present cost of ensuring future financial stability may necessitate less than desirable tradeoffs. For example, a credit union may need to offer less attractive rates in order to build retained earnings that will support future growth and guard against unexpected downturns. The ability to issue subordinated debt would make this process of capital planning and adaptation more cost-effective and predictable.

The NCUA should adhere to the following principles as it develops a subordinated debt option for credit unions:

1. Preserve the not-for-profit, mutual, member-owned and cooperative structure of credit unions and ensure that ownership interest (including influence) remains with the members.
2. Ensure that the capital structure of credit unions is not fundamentally changed and that the safety and soundness of the credit union community as a whole is preserved.
3. Provide a degree of permanence such that a sudden outflow of capital will not occur.
4. Allow for a feasible means to augment subordinated debt as the credit union grows.
5. Provide a solution with market viability.

NAFCU understands that statutory amendments may be necessary to provide meaningful capital options for all credit unions; however, a regulatory capital framework would still offer increased flexibility to credit unions that must meet the NCUA's risk-based net worth requirement.

NAFCU urges the NCUA to pursue a subordinated debt framework that does not impose burdensome registration requirements on credit unions that are disproportionate to the complexity and risk of the instrument. In connection with a subordinated debt offering, the NCUA should not require credit unions to register a prospectus with either the SEC or NCUA, and instead seek parity with the current model that LICUs use when issuing secondary capital. NAFCU believes that

streamlining investor disclosures while reasonably balancing the need for transparency is essential to ensuring future market viability of subordinated debt.

702 Capital Adequacy

As the effective date for the FASB's CECL standard draws near, NAFCU is concerned that it could result in a significant decline in capital across the credit union industry. Recent disclosures from SEC filers indicate that increases in loan loss reserves of 25 percent or more will be common. JPMorgan Chase & Co., for example, expects a 35 percent increase in loss reserves, and Citigroup's most recent SEC disclosures estimate an increase in the range of 20 to 30 percent. Although the impact will vary among institutions, a same-sized increase in loss reserves for credit unions would result in a capital outage of roughly $2.5 billion for the industry.

NAFCU still maintains that credit unions should never have been included within the scope of CECL because they did not engage in the poor lending practices that precipitated the financial crisis. Nevertheless, many of the institutions that did have been granted a measure of relief from the standard. In December 2018 the federal banking regulators allowed an optional three-year phase-in of the capital impact related to CECL. NAFCU recognizes that NCUA has limited discretion to provide a similar type of capital relief to credit unions due to the unique statutory definitions of capital in the *Federal Credit Union Act*. Nevertheless, NCUA should look for every opportunity to minimize the impact to credit unions in order to, at a minimum, provide a level playing field for credit unions.

A related area of concern is the upcoming effective date for NCUA's risk-based capital (RBC) rule. On May 15, 2019, NCUA Chairman Hood delivered prepared testimony to the Senate Banking Committee, which stated that credit union capital requirements should be tailored to risk profiles. Although no concrete plan to review RBC has materialized, NAFCU has advised the NCUA that the close proximity of the RBC and CECL effective dates could create challenges for credit unions. In a May 2019 survey of NAFCU members, nearly three-quarters indicated that they were somewhat or very concerned over their impact on capital. More than two-thirds of respondents indicated that the RBC would not serve a useful purpose once CECL becomes effective, and only 6 percent of respondents said that RBC would offer a meaningful increase in the level of protection for the Share Insurance Fund. NAFCU urges NCUA to carefully consider the anticipated impact of the CECL standard on credit union capital, and to review the appropriateness of RBC within that context.

Additionally, with respect to the RBC rule, NAFCU encourages the NCUA to reevaluate the treatment of "goodwill" under the rule. As a result of the expiration of the goodwill grandfathering provision, some of NAFCU's credit union members will face significant disruptions to their growth strategies and ability to offer products and services to their members. NAFCU requests that the NCUA permanently grandfather all goodwill to exclude it from the RBC rule so that credit unions may continue to grow and serve their members as effectively as possible.

704 Corporate Credit Unions

NAFCU supports corporate credit unions and the invaluable role they play as providers of liquidity. To ensure that corporate credit unions are adequately equipped to serve the needs of the credit union industry, the NCUA should consider improvements to *both* Part 704 and Part 725 of its regulations, with special attention given to rules governing liquidity management provisions, corporate access to the central liquidity facility (CLF), and investments in corporate credit union service organizations (CUSOs). NAFCU requests the NCUA make some amendments to its rules to allow more flexibility without impacting the safety and soundness of the corporate system.

Investments in Corporate CUSOs

Corporate CUSOs are uniquely equipped to deliver products and services that are tailored for credit unions, and in turn, support industry-wide growth and modernization. Unfortunately, the regulatory limitations placed on corporate CUSOs have sometimes discouraged innovative companies from accepting investments from corporate credit unions, which has placed the credit union industry at a disadvantage at a time of rapid technological change. As documented in the NCUA's most recent Regulatory Reform Task Force Report, there is concern that companies shun corporate credit union investment dollars due to the regulatory constraints of having to primarily serve credit unions and to follow the various restrictions in section 704.11.

Corporate credit unions that cannot invest in technology partners, even at a de minimis level, lack the ability to direct development of credit union specific products or features, and therefore reinforce a prevailing attitude among financial technology firms that credit unions are a secondary or tertiary market. Accordingly, NAFCU recommends that the NCUA consider changes to section 704 that would permit corporate credit unions to make non-controlling, strategic investments in companies without triggering corporate CUSO rules. Doing so will help ensure that corporate credit unions are able to direct product development early on and secure competitive pricing and features for their credit union members, who might otherwise turn to less accessible or more expensive bank-developed technologies.

Enhancements to Corporate Credit Union Liquidity and Access to CLF

NAFCU urges the NCUA to modernize the investment and liquidity provisions contained in Part 704 in concert with a review of the central liquidity facility regulations in Part 725. NAFCU has always supported low-cost means of meeting credit unions' liquidity needs, and as such, NAFCU remains convinced that a viable and dependable resource such as the CLF should continue to evolve to reflect modern approaches to liquidity management.

Current regulations governing corporate access to the CLF are hindering corporate credit unions' ability to efficiently meet their members' liquidity needs. Historically, the CLF has served an important role in times of financial stress, yet the lack of flexible access at a time when corporate credit unions hold a much stronger capital position creates costs for all credit unions and degrades an important source of contingent liquidity. Although certain improvements will require legislative

amendments to the FCU Act, others are within the NCUA's power to effectuate through its regulatory review process.

As an initial step, the NCUA should seek to modernize CLF collateral requirements which have fallen out of sync with current market conditions. The general requirement in section 725.19 that pledged collateral equal 110 percent of CLF advances does not compare favorably with the margin guidelines established by the Federal Reserve Banks and Federal Home Loan Banks. To correct this discrepancy, the NCUA should require CLF advances to be secured by collateral of the credit union with a net book value equivalent to those collateral instruments readily accepted by the Federal Reserve Banks and the Federal Home Loan Banks.

For corporate credit unions to remain an effective source of liquidity, the NCUA should also modernize its rules related to secured borrowings, limits on credit union member investments, and weighted average life (WAL) for corporates assets. Greater flexibility in each of these three areas would reflect industry adoption of stronger contingent liquidity plans, the improved capital strength of corporate credit unions, and a general reduction in systemic risk affecting the corporate network.

In addition, certain legislative amendments to the FCU Act would also improve the current CLF framework. Provided there is necessary Congressional support, the CLF should be modernized to meet liquidity needs by: (1) adjusting the subscription requirement for membership, and (2) expanding the CLF borrowing cap so that it may meet current industry needs. To realize the first of these goals, the NCUA should explore options for corporate credit unions to purchase of capital stock on behalf of a select group of member credit unions (specifically those who wish to become members of the CLF), which would facilitate more cost-effective access to the CLF during periods of tight liquidity.

Corporate Credit Union Governance

The NCUA's current rules regarding corporate credit union board representation require that a majority of the board of directors of a corporate credit union must consist of individuals with the following title or role: CEO, CFO, COO or treasurer/manager. The NCUA has stated in previous rulemakings that the need for such a specific board requirement bears little relation to the goal of ensuring corporate credit union stability during periods of economic stress. In 2010, the NCUA's final rule adopting this requirement contained the following observation: "[w]hether or not these new provisions might have affected the size or scope of the losses is not determinable." The NCUA should reconsider corporate board requirements to improve board diversity and experience, and should permit an individual who holds a senior management position at a member credit union to be eligible for board election.

Corporate Credit Union Fidelity Bond Coverage

The NCUA should maintain its current rule requiring board of directors (BOD) approval only for fidelity bond coverage instead of requiring a corresponding review from the corporate credit union's supervisory committee. In general, NAFCU supports a flexible process for reviewing the

purchase of fidelity bond coverage, but does not agree with the NCUA's proposed approach in its November 2018 notice of proposed rulemaking. The 2018 fidelity bond proposal requires bond contracts to include a provision allowing the liquidating agent to purchase an extended discovery period to find any claims that may be brought to the bond insurer. The proposed change could lead to limited competition as bond insurers may no longer offer as many fidelity bonds to credit unions due to the requirement and additional risks posed. If this occurs, corporate credit unions, as well as natural person FCUs, would be left with little bargaining power.

708b Mergers of Federally-Insured Credit Unions

NAFCU contends that the impacts of the CECL standard will be wide ranging. Numerous commenters have rated it the most impactful accounting change to credit unions and banks in decades, if not ever. One area of concern for NAFCU is the likelihood that CECL will complicate and delay credit union mergers, and in some cases may prevent otherwise viable mergers from taking place. Although NAFCU is dismayed by the rise in regulatory burden during the past decade which often makes mergers inevitable, in some cases mergers do provide benefits of economies of scale to members, along with added protection to the Share Insurance Fund.

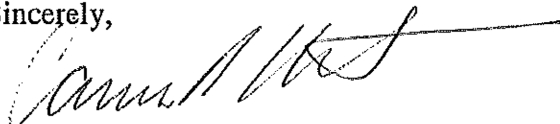
Due to the fact that the CECL standard is principles-based, it is likely that credit unions will take a range of approaches depending on the complexity of the institution, the availability of historical data, the unique composition of the credit union's balance sheet, and other factors. Following CECL implementation, it is inevitable that challenges will arise in trying to marry the reserving methods of the acquiring credit union with those of the acquiree. Data used by the acquirer may not have been collected by the acquiree, leaving the acquirer to either alter its methodology or run parallel loss methodologies for the purchased assets, which may involve collection of additional data points.

Given these added complexities, NAFCU believes that NCUA should make every effort to reduce the burdens on merging credit unions. One way to provide additional certainty to merging credit unions would be to consolidate existing sources of guidance regarding merger accounting in a single location with special attention given to CECL-related issues.

Conclusion

NAFCU appreciates the opportunity to provide comments on the regulations under consideration in this year's annual regulatory review. If you have any questions or require additional information, please do not hesitate to contact me or Ann Kossachev, NAFCU's Director of Regulatory Affairs, at akossachev@nafcu.org or (703) 842-2212.

Sincerely,



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B. Dan Berger
President & Chief Executive Officer

National Association of Federally-Insured Credit Unions

January 9, 2019

The Honorable J. Mark McWatters, Chairman
The Honorable Rick Metsger, Board Member
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

RE: Priorities of our Nation's Credit Unions

Dear Chairman McWatters and Board Member Metsger:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I would like to share with you the top priorities of our nation's credit unions. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 115 million consumers with personal and small business financial service products. Each year, the NAFCU Board, made up of credit union CEOs from across the nation, identifies the top issues in the upcoming year that impact credit unions.

Below, NAFCU outlines these general priorities, which touch upon both legislative and regulatory concerns, followed by a more detailed discussion of the priorities that specifically concern the National Credit Union Administration (NCUA). We hope that you will work with us to address these top legislative and regulatory issues for credit unions.

1. **Growth.** Support legislation and regulation that helps credit unions grow and better serve their membership.

2. **Strong NCUA.** Advocate for the NCUA to be the sole credit union regulator, including exempting credit unions from the Bureau of Consumer Financial Protection's (Bureau) authority.

3. **Regulatory Relief.** Fight for clear, streamlined regulations that allow credit unions to put more resources toward serving their members.

4. **Fair and Innovative Market.** Promote innovation, create national data security standards, and push back against big banks' baseless attacks on credit union growth.

5. **Promote Transparency.** Encourage government accountability, including reducing the NCUA's overall operating budget, establishing a commission at the Bureau and pushing for additional National Credit Union Share Insurance Fund (NCUSIF) distributions for credit unions.

6. **Tax Exemption.** Preserve the credit union tax exemption to save U.S. consumers $16 billion annually, protect nearly 1 million jobs and keep the focus on credit union members, not shareholders and profits.

NCUA-Specific Priorities

Field of Membership

Strengthening the federal charter and pursuing regulatory relief for federal credit unions is at the core of NAFCU's advocacy efforts. NAFCU fundamentally believes the industry's dual chartering system works best when the state and federal charters keep pace with each other. Several states, however, have been much more progressive in modernizing their field of membership (FOM) rules to recognize today's dynamic and ubiquitous marketplace. Additionally, NAFCU supports broader FOM relief, including: 1) eliminating or increasing the population limits applicable to community charter credit unions; 2) establishing a formal notification process for credit unions making FOM-related applications; and 3) considering new ways to efficiently address mergers. NAFCU is committed to supporting the NCUA as it works to modernize the FOM rules in order to help credit unions grow and better serve their communities.

Such support includes standing by the NCUA as the banking trade groups continue to challenge the legality of the agency's 2016 FOM rule and partially invalidated provisions aimed at granting community charters relief. NAFCU maintains that the NCUA's FOM reforms fall well within the bounds of its legal authority. NAFCU is committed to ensuring the swift and smooth implementation of the FOM rules and defending the interests of credit unions.

NAFCU is also committed to working with the NCUA and members of Congress to push for legislative improvements to sections of the *Federal Credit Union Act* (FCU Act) that restrict the ability of credit unions to serve their desired fields of membership, including allowing all credit unions to add underserved areas. NAFCU appreciates Chairman McWatters's support of such a legislative reform and is optimistic that Congress will make changes to help the credit union industry serve those Americans in need of access to financial services.

Capital/Risk-Based Capital Reform

NAFCU remains concerned about the impact the risk-based capital (RBC) rulemaking will have on the credit union industry, including regulatory burden and increased costs. Considering the changes to bank capital in the *Economic Growth, Regulatory Relief, and Consumer Protection Act* (S. 2155), from a parity perspective, the appropriate level of credit union capital requires further study. NAFCU appreciates the NCUA's recently finalized one-year delay of the implementation date and its fresh approach to the definition of "complex" credit union that would exclude more credit unions from the RBC rule; however, the NCUA should make further changes to its RBC rule. NAFCU opposes an approach to complexity that arbitrarily divides the industry based on an asset threshold in favor of a case-by-case determination of complexity and exemptions for those credit unions whose net worth ratios provide adequate protection from material risks, regardless

of their asset size. Therefore, NAFCU will continue to advocate for the NCUA to revise or withdraw the agency's RBC rule or for Congress to step in and delay the rule's effective date until 2021.

NAFCU will also continue to advocate for improved access to subordinated debt (formerly known as alternative capital), including both secondary capital and supplemental capital. NAFCU supports changes to the secondary capital plan approval process and a streamlined application to help low-income designated credit unions access capital faster. NAFCU also supports changes to the FCU Act that would permit credit unions to count certain forms of supplemental capital towards the net worth ratio calculation to alleviate current constraints on building net worth.

Current Expected Credit Losses (CECL)

In the NCUA's recently released 2019 Supervisory Priorities, credit unions are informed that examiners will inquire about efforts taken to prepare for the implementation of CECL. NAFCU still maintains that credit unions should never have been included within the scope of CECL because they did not engage in the poor lending practices that precipitated the financial crisis. Nevertheless, NAFCU greatly appreciates the NCUA's efforts to educate the industry about CECL. As the implementation date draws nearer, it has become apparent that more needs to be done. NAFCU remains focused on coordinating its efforts with those of the NCUA to provide credit unions with access to the resources they need to prepare for this comprehensive change to estimating allowances for credit losses. NAFCU will work with the NCUA to find ways to ensure that credit unions are not overly-burdened by CECL's impact on regulatory capital. NAFCU will also look for additional opportunities to partner with the NCUA to educate the industry about future implementation challenges.

Exam Fairness

NAFCU has consistently urged the NCUA to reduce examination burden by expanding eligibility for extended exam cycles to more credit unions and by conducting more efficient, virtual examinations. Although NAFCU is encouraged by the positive developments documented in the NCUA's 2019-2020 Budget Justification, recent outreach to our membership suggests that smaller credit unions are not seeing a meaningful reduction in exam duration. NAFCU generally supports the NCUA's long term exam modernization plans, which seek to leverage new technology, analytics, and monitoring capabilities to reduce examination burden. More specifically, NAFCU supports reforms to the examination process to improve consistency, speed, and cost savings for both credit unions and the NCUA. NAFCU encourages the NCUA to fervently continue to pursue its exam modernization efforts in a transparent fashion that allows credit unions to provide feedback. Additionally, NAFCU will work with the NCUA as it advances its continuous supervision program to ensure that the enhanced monitoring techniques do not threaten the autonomy of credit unions and interfere with their day-to-day operations.

Cybersecurity

NAFCU supports the NCUA's focus on protecting the security, confidentiality, and integrity of credit union member information. In 2018, the agency started formally testing its Automated Cybersecurity Examination Tool (ACET), which is largely based on the Federal Financial Institutions Examination Council (FFIEC) Cybersecurity Assessment Tool. The NCUA recently announced it would integrate the ACET with the standardized Cyber Security Evaluation Tool (CSET), used by the Department of Homeland Security, and continue to expand deployment of the tool at credit unions of different asset sizes. NAFCU will work with the NCUA to ensure that it employs a risk-based approach to cybersecurity that provides the necessary flexibility for a credit union to adopt controls based on their complexity as an institution and objective risk management principles. NAFCU fully expects the NCUA to continue to examine its own cybersecurity procedures to produce a safer and stronger credit union system.

Loan Maturities

NAFCU has long advocated for the NCUA to grant credit unions additional flexibility with respect to loan maturity limits. In August 2018, the NCUA issued a proposal inviting comment on extending maturity limits for certain types of loans. NAFCU recognizes that extending the general 15-year maturity limit requires legislative action and continues to urge the NCUA to support any legislative efforts that would amend the general maturity limit. The current 15-year limit is not on par with that of other lenders in the marketplace, and credit unions are at a competitive disadvantage. NAFCU encourages the NCUA to re-evaluate its definition of "principal residence" to conform with recent amendments to the FCU Act.

Interest Rate Ceiling

The fixed 18 percent interest rate ceiling has been in place since 1987. NAFCU has long advocated for a variable interest rate, specifically a 15 percent spread over Prime. Growth opportunities are stifled by credit unions' inability to take reasonable amounts of risk to lend to those members not suitable for an 18 percent rate. A variable interest rate will eliminate the need for credit union members to pursue higher rate alternatives, such as high-cost, traditional payday loans, or high interest credit cards. In addition, credit unions will be able to utilize tailored risk-based pricing, which reduces risks to the NCUSIF. NAFCU will continue to provide the NCUA with detailed feedback from its members regarding the potential benefits of a variable interest rate and collaborate with the NCUA to find other areas of opportunity to help credit unions grow and help their members access the credit they need.

Refunds of Stabilization Assessment Monies

Although NAFCU appreciates the NCUA's commitment to reevaluating the normal operating level (NOL) on an annual basis and the recently announced decrease to 1.38 percent, NAFCU continues to question the NCUA Board's original decision in to raise the NOL to 1.39 percent. The 2018 rebate to credit unions was a good first step, but NAFCU will continue to urge the agency to

focus on ways to provide additional refunds to credit unions and return the NOL to its customary level of 1.30 percent as soon as possible. Returning additional funds will allow credit unions to put those dollars to work helping their members.

Conclusion

NAFCU would like to thank the NCUA for its dedication to helping credit unions grow and improving the regulatory structure while ensuring a safe and sound system. NAFCU is also pleased to see the NCUA continually expanding the breadth of its credit union resources so that credit unions stay alert and informed. Thank you for your consideration and attention to the above-referenced matters. We look forward to working with you to address these priorities. If we can answer any questions or provide you with additional information on any of these issues, please do not hesitate to contact me.

Sincerely,

B. Dan Berger
President and CEO