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National Association of Federally-Insured Credit Unions

May 18, 2021

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: Outstanding COVID-19 Regulatory Relief and Broader Reforms

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

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I would like to urge the National Credit Union Administration (NCUA), on behalf of the nation's credit unions, to quickly finalize all remaining COVID-19-related regulatory relief and to take additional steps to provide reform that will help credit unions better serve their communities. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 124 million consumers with personal and small business financial service products. As the COVID-19 pandemic stretches past the one-year mark, some of the crucial relief measures necessary to support the well-being of credit unions remain unfinished. Credit unions and their members continue to face the impacts of the pandemic and require regulatory relief, expanded flexibility, and even broader regulatory reforms to better assist their members. We hope that you will work with us to address these concerns.

Executive Summary

The NCUA should swiftly address the following items:

1. *Remaining COVID-Related Relief:* The NCUA should immediately finalize its proposed rule permitting credit unions to capitalize interest under Appendix B to Part 741 as well as its proposed rule eliminating the prescribed 45-day limit in its requirements for an overdraft policy in NCUA's lending rule.
2. *Capital Reform:* The NCUA should finalize its proposed three-year phase-in of the Current Expected Credit Loss (CECL) methodology and reconsider and simplify the NCUA's 2015 risk-based capital (RBC) rule.
3. *Field of Membership Reform:* The NCUA should modernize the definition of "service facility" in its Chartering and Field of Membership Manual to allow credit unions to leverage digital banking platforms to serve broader segments of their communities.
4. *Other Reforms:* The NCUA should modernize its regulations related to compensation in connection with lending to permit comprehensive incentive plans.

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Remaining COVID-Related Relief

Capitalization of Interest

Time is of the essence with respect to providing fair and efficient loan modification options to credit union members as they exit forbearance programs following a COVID-19-related hardship. The NCUA should no longer delay its finalization of the proposed rule, issued in November 2020, to undo its outdated and inappropriate prohibition on the capitalization of interest under Appendix B to Part 741. NAFCU first sought this relief in March 2020, and in a letter dated September 1, 2020, asked the NCUA to issue an interim final rule to remove the prohibition on capitalization of interest. Although the NCUA has issued this proposed rule, it has yet to be finalized and, unfortunately, it is too late for some credit unions who have had to pursue the other, inefficient, operationally burdensome, and confusing options to assist their members.

The NCUA's current interpretation of Appendix B to Part 741 poses challenges for both borrowers and credit unions and makes it harder for credit unions to work prudently with their members who may not be able to meet their loan payment obligations due to the effects of COVID-19. Permitting credit unions to capitalize interest in a loan modification allows them to work with borrowers in a safe and sound manner and provide an option that will mitigate adverse effects on the borrower. Additionally, permitting the capitalization of interest aligns with Generally Accepted Accounting Principles (GAAP), the practices of Fannie Mae and Freddie Mac, the government-sponsored enterprises (GSEs), as well as the rules issued by the other banking regulators.

Accordingly, the NCUA should immediately finalize the rule permitting capitalization of interest to alleviate operational challenges for credit unions and potential confusion and hardship for borrowers. This request is further bolstered by the fact that almost every comment submitted in response to the proposed rule clearly expressed support for the change. NAFCU certainly appreciates that the NCUA is currently dealing with many pressing issues, but the near-unanimous chorus of support for the proposed rule should make reviewing comments straight-forward and justifies a quick finalization.

Overdraft Policy

The NCUA should quickly finalize its proposed rule to eliminate the prescribed 45-day limit in its requirements for an overdraft policy in section 701.21(c)(3) of the NCUA's lending rule. NAFCU and its members have long advocated for the NCUA to eliminate this required timeframe as it creates operational burden, is inconsistent with GAAP and interagency guidance with the other banking regulators, and poses no benefit to credit union members. NAFCU supported the proposed rule's provision to replace this timeframe with a credit union-determined timeline that is reasonable and consistently applied as this will provide credit unions with appropriate flexibility to assist their members who may still be facing COVID-related hardships.

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The current requirements of section 701.21(c)(3) are unnecessarily burdensome for federal credit unions (FCUs), unnecessarily restrictive for members and should be eliminated. The rule, which requires an FCU to establish a written overdraft policy with a time limit not to exceed 45 days to either make the account current or approve a loan to cover the negative balance applies regardless of the size of the negative balance or the circumstances of the borrower. This timeframe ultimately harms members most by limiting FCUs' ability to work with the member. No consumer protection argument in support of a 45-day timeframe, as opposed to a 60-day or 90-day timeframe, has been raised and indeed there are no policy reasons for maintaining this shorter timeframe. Furthermore, there is no safety and soundness concern specifically alleviated by the 45-day timeframe as opposed to other reasonable lengths of time.

The replacement of the 45-day timeframe with one that is "reasonable and universally applicable," would be a vast improvement. This will allow FCUs to streamline processes related to reviewing these accounts, establish reasonable repayment periods and lending processes related to these negative balances, and, most importantly, offer members who are struggling financially with flexibility and understanding as they work with them. NAFCU urges the NCUA to immediately finalize its proposed rule regarding its overdraft policy.

Capital Reform

CECL Phase-In

NAFCU and its members appreciate the Board's willingness to offer credit unions important relief to mitigate CECL's impact on credit union capital and net worth. Given the adverse impacts that credit unions face as a result of the pandemic, this relief is more necessary and time-sensitive than ever. Thus, the NCUA should act fast to finalize this proposed CECL phase-in rule. In general, NAFCU supports the concept of phasing in CECL's negative hit to capital over a multi-year period but remains opposed to subjecting credit unions to CECL compliance. NAFCU reiterates its ask that the NCUA engage with the Financial Accounting Standards Board (FASB) and Congress to explore the benefits of an industry exemption. The NCUA should also consider additional actions that could help broaden the availability of an alternative accounting standard that functions as a CECL exemption.

NAFCU supports the NCUA's proposed phase-in, which will grant credit unions important CECL related relief, but has requested the NCUA provide an optional, longer phase-in option along with more flexible examination procedures. NAFCU maintains that credit unions should not be subject to the CECL standard given our industry's record of prudent fiscal management before and after the financial crisis, limited complexity, and structure as not-for-profit, member-owned cooperatives. The NCUA should recognize this difference and identify opportunities to work with the FASB and Congress to exclude credit unions from coverage under CECL.

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Simplification of Risk Based Capital Requirements

NAFCU appreciates the recent advance notice of proposed rulemaking (ANPR) to evaluate options to simplify the NCUA's 2015 RBC rule (final RBC rule), which lacks the type of important flexibility found in comparable bank capital regulations. NAFCU's members need capital relief as the challenges of the pandemic continue to linger and the nation moves into a mode of economic recovery. Despite healthy balance sheets, credit union asset growth due to stimulus money has created additional pressure on net worth ratios, and it remains uncertain how long these effects will last. Furthermore, the credit union industry has already weathered the recent period of financial stress without the final RBC rule, proving that existing supervisory mechanisms for assessing capital adequacy are sufficient. Accordingly, expeditious relief to simplify the final RBC rule will enable credit unions to focus more of their resources on helping their members overcome financial hardship, rebuild America's communities, and reduce administrative burdens that stand in the way of member service.

In general, NAFCU supports the development of an alternative to the agency's final RBC rule, such as an off-ramp which aims to reduce the complexity of risk-based capital compliance (i.e., Complex Credit Union Leverage Ratio (CCULR)), or a risk-based leverage ratio (RBLR) that is tailored to produce a less burdensome and less complex capital standard. NAFCU's members support the option that affords the greatest simplicity while also mitigating a "capital cliff" scenario, where a small increase in a certain type of asset results in a large increase in the risk-based capital requirement. NAFCU outlines in more detail its support for a simplified approach to the RBC rule in a recent letter, dated May 10, 2021.

NAFCU's members would also value a rulemaking trajectory that aims to provide risk-based capital relief before the final RBC rule takes effect next year and certainly before the CECL standard becomes effective. If the NCUA encounters barriers that would prevent it from developing a final rule before 2022, the agency should consider an approach where a preliminary off-ramp for the final RBC rule is proposed and finalized before January 1, 2022, or where the final RBC rule is delayed until a rulemaking can be completed. A fast-tracked, RBC off-ramp much like the CCULR could be proposed as an interim measure of relief with a narrower range of parameters for consideration, such as the calculation of just the leverage ratio and basic eligibility requirements. Meanwhile, the NCUA could continue pursuing a more complete rulemaking that compares the merits of the CCULR and RBLR. NAFCU encourages the NCUA to be transparent about its process and timeline for developing a proposal in response to the ANPR and thereafter publishing a final rule. Periodic updates would give credit unions confidence about the timing of expected relief.

Field of Membership Reform

NAFCU strongly supports NCUA's proposed rule which would define "service facility" in a manner that provides clarity, consistency, and the appropriate recognition of technological advances and the current operation of shared branching. NAFCU urges the NCUA Board to

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quickly finalize this rule, and to further modernize the Chartering and Field of Membership Manual by including online and mobile banking platforms in the definition of service facility in recognition of the role these channels play in modern consumer banking.

As the economic effects of the pandemic endure and the credit union industry continues to experience growing consolidation, credit unions need the tools and mechanism to reach new consumers who are not currently being served. The NCUA has identified modernization of the chartering process and field of membership requirements as an important piece of its own agenda through the Advancing Communities through Credit, Education, Stability and Support (ACCESS) Initiative. The current field of membership process is burdensome, difficult to navigate, and unnecessarily restrictive. Field of membership is an important part of what makes credit unions unique, but it should not be used as a stricture against healthy credit union growth and improving access to credit unions for underserved communities.

NAFCU has long maintained that the NCUA should either eliminate the service area requirement or alternatively revise the definition of service area to include "facilities that are accessible to groups within the FOM through online services." The NCUA should revise the definition of "service facility" to include an online internet channel or mobile application that otherwise meets the definitions of a service facility, meaning it is capable of accepting shares and loan applications, or disbursing loan proceeds. The use of online and mobile banking platforms also presents an opportunity for credit unions to provide their top-notch products and services to underserved communities.

NAFCU continues to advocate for legislative reform to the *Federal Credit Union Act* to permit all credit unions, including single common-bond and community charters, to add underserved areas to their fields of membership. Considering underserved communities have been especially hard-hit by the COVID-19 pandemic, such reform is urgent. NAFCU greatly appreciates the prior support of both Chairman Harper and Board Member Hood on adding underserved areas and asks for your continued support as Congress reviews this issue. Without such appropriate legislative relief, NAFCU and its members are concerned that credit unions will be unnecessarily and unjustifiably obstructed in their ability to invest in appropriate technology and perform in the consumer finance sector, which is increasingly competitive and innovative.

Other Reforms

Compensation in Connection with Loans to Members and Lines of Credit to Members

The NCUA should continue to strive for broader modernization of its regulations to adjust to industry practices and allow credit unions to remain competitive and grow. NAFCU requests that the NCUA proceed with a proposed rule following its 2019 ANPR on compensation in connection with loans to members and lines of credit to members. The NCUA should issue a proposed rule so that credit unions may create comprehensive incentive plans that include loan metrics without encouraging inappropriate risks, incentivizing bad loans, or creating conflicts of interest.

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Flexibility in compensation regulations is essential to credit unions' ability to attract and promote skilled employees and cultivate better organization-wide employee performance. Considering the current regulations do not allow credit unions operational flexibility, the NCUA should modernize its compensation rule by incorporating lending as part of a broad and balanced set of organizational goals and performance measures.

The Board has previously noted that the NCUA's regulations in this area are likely outdated, burdensome, and at odds with industry standards for senior executive compensation plans. In a letter dated, June 23, 2019, NAFCU supported the ANPR and advocated for specific changes to the NCUA's regulations, including: (1) updating the current structure of section 701.21(c)(8) to include loan metrics in setting compensation plans to ensure consistency and clarity across the industry; (2) restructuring section 701.21(c)(8) in a way that permits a credit union to develop a compensation plan based on its business model and the objectives its board has acknowledged as necessary for the credit union to grow; and (3) modernize regulations governing compensation associated with lending generally. NAFCU urges the NCUA to move forward with a proposed rule on this critical issue to better equip credit unions to attract and retain talent and serve their members.

Conclusion

NAFCU applauds the NCUA in its efforts to provide COVID-19 relief to credit unions, but it has been more than a year since the COVID-19 pandemic began, and some critical relief measures have yet to be finalized. NAFCU urges the NCUA to work quickly to address the issues outlined above, including (1) finalizing its proposed rule on capitalization of interest on loan modifications and the proposed rule on overdraft policies; (2) adopting broad capital reform, such as finalizing the three-year phase-in for CECL and simplifying the 2015 RBC rule; (3) modernizing the field of membership requirements to help credit unions reach more consumers using digital platforms; and (4) proposing a rule to modernize the agency's requirements regarding executive compensation in relation to lending. Thank you for your consideration and we look forward to working with you to address these outstanding regulatory relief measures. If we can answer any questions or provide you with additional information on any of these issues, please do not hesitate to contact me or Ann Kossachev, NAFCU's Director of Regulatory Affairs, at 703-842-2212 or akossachev@nafcu.org.

Sincerely,



B. Dan Berger
President and CEO