August 3, 2015

Regulatory Review 2015
Office of General Counsel
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

RE: Regulatory Review 2015

VIA ELECTRONIC MAIL: www.regulations.gov

To Whom It May Concern:

The Michigan Credit Union League (MCUL), the statewide trade association representing 98% of the credit unions located in Michigan and their 4.7 million members, appreciates the opportunity to comment on the National Credit Union Administration's (NCUA) annual review of one-third of its regulations. The MCUL appreciates the NCUA's continued effort to annually review one third of its regulations to "update, clarify and simplify existing regulations and eliminate redundant and unnecessary provisions." The MCUL believes this is necessary and efficient, especially in the current regulatory environment. The following suggestions are provided to the NCUA for consideration.

Part 701.1 and Appendix B: Federal Credit Union Field of Membership

When credit unions apply for a field of membership change for a new community area the NCUA requires credit unions to meet the burden of demonstrating that a proposed community area meets the necessary statutory requirements. Currently, § V.A.2 of Appendix B provides that a proposed community must be well-defined and a local community or rural district. "Well-defined" means,

> "The proposed area has specific geographic boundaries. Geographic boundaries may include a city, township, county (single, multiple, or portions of a county) or their political equivalent, school districts, or a clearly identifiable neighborhood. Although congressional districts and state boundaries are well-defined areas, they do not meet the requirement that the proposed area be a local community or rural district."

Under NCUA guidelines, the "well-defined" local community requirement is met if: (1) The defined area to be served is recognized as a single political district or (2) The area is designated as a Core Based Statistical Area (CBSA) or allowing part thereof, or in the

case of a CBSA with Metropolitan Divisions, the area is a Metropolitan Division or part thereof and the CBSA or Metropolitan Division must have a population of 2.5 million or less people.

The current cap of 2.5 million or less people is arbitrary and should be removed. Removing this cap would be consistent with NCUA's efforts as it continues to move forward with modernizing its Act as well as provide further regulatory relief to Federal credit unions.

Additionally, the current overall geographical requirements under the NCUA's field of membership are quite restrictive. As indicated by reference above, "well-defined" does not allow for the inclusion of congressional districts or state boundaries to be included as a local community or rural district, even though statute states that *"congressional district and state boundaries are well-defined areas…"* This limitation has not kept pace with various state credit union acts and their field of membership expansion. For example, under § 352(2) of the Michigan Credit Union Act, Michigan state chartered credit unions field of membership may consist of the following:

> (2) The credit union board of a domestic credit union shall establish the field of membership for a domestic credit union. The field of membership shall consist of 1 or more of the following:
> (a) One or more groups of any size that have a common bond of occupation, association, or religious affiliation.
> (b) One or more groups composed of persons whose common bond is residence, employment, or place of religious worship within a geographic area composed of 1 or more school districts, counties, cities, villages, or townships.
> (c) One or more groups whose common bond is common interests, activities, or objectives.

This expanded geographical area has allowed Michigan credit unions to expand their footprint. With the advancement of technology, rigid geographical limitations can hinder Federal credit unions ability to better serve a wider geographic area. Additionally, this limitation does not reflect the ever-growing digital age where online account opening and mobile banking are commonplace. The MCUL supports a strong dual chartering system and recommends that the NCUA revise its field of membership standards so that Federal credit unions can have parity with progressive state acts such as the Michigan Credit Union Act.

Federal Credit Union Bylaws 701.2

The NCUA should review the requirement that all Federal credit unions utilize a single set of bylaws, regardless of size and complexity.

The impetus behind §701.2 arises from Section 1758 (Section 108 of the FCU Act) which states in pertinent part:

> **"Bylaws.—**In order to simplify the organization of Federal credit unions the Board shall from time to time cause to be prepared a form of organization certificate and a form of bylaws consistent with this chapter, which shall be used by Federal credit union incorporators, and shall be supplied to them on request. At the time of presenting the organization certificate the incorporators shall also submit proposed bylaws to the Board for its approval."

While we agree this provision directs the NCUA to provide a form of bylaws for use at organization, it does not appear this section requires the NCUA to insist that a credit union continue to utilize the model form for its governance throughout the credit union's existence.

In our view, we believe this "one-size fits all" approach to credit union bylaws is archaic. The NCUA should provide flexibility to credit unions of varying size and complexity for purposes of their corporate governance. As such CUNA recommends the following:

- Issue suggested comprehensive bylaws that can be used by newly chartered Federally Chartered Credit Unions (FCU) to simplify their incorporation and by smaller FCUs to simplify their operations (but these bylaws would not be incorporated by reference into the NCUA regulations). This will satisfy the requirement of the FCU Act.
- Remove the requirement that every FCU board must follow every provision in the standard bylaws promulgated by the NCUA (or obtain approval for alternative language in specific bylaw provisions)
- Issue of list of items that must be in every FCU bylaws because of requirements in the FCU Act or for safety and soundness purposes. This list would be subject to notice-and-comment pursuant to the rulemaking process.

Implementation of these recommendations would allow NCUA to move from prescriptive type of requirements to broader principles for purposes of modern corporate governance. It further will allow flexibility in corporate governance for each credit union that can be tailored to their size and complexity.

As a general principle, and to echo CUNA's comments on this are the MCUL recognizes that NCUA has the legal authority to enforce federal credit union bylaws, but opposes NCUA's enforcement of bylaws that merely address administrative issues. NCUA should become involved in the enforcement of a federal bylaw only when a bylaw dispute cannot be resolved by the credit union first, using its own internal processes, before turning to the NCUA. If the NCUA must become involved, its actions should be reasonable and no harsher than actions taken by other regulators when addressing similar issues.

Part 702: Capital Adequacy - Prompt Corrective Action

The NCUA is seeking to reduce regulatory burdens for credit unions. One area such burden could be alleviated is within Prompt Corrective Action (PCA).

The MCUL understands the NCUA has yet to issue a final rule addressing the Risk Based Capital (RBC) 2 proposal and is conducting careful analysis based on comments received prior to issuance of a final rule. In previous comments to the NCUA regarding risk-based net worth standards under PCA, the MCUL expressed concern with the antiquated regulatory framework in the Federal Credit Union Act as well as the NCUA's proposal.

In the MCUL's previous communications to the NCUA it was expressed that the statutory net worth requirement for well-capitalized credit unions at 7% was not set by empirical studies but rather was the result of intense negotiation in the development of the Credit Union Membership Access Act. Bankers, who have a lower net worth requirement, wanted to set a higher net worth requirement for credit unions to slow the growth of credit unions. The credit union industry fought vigorously to avoid unnecessarily high net worth levels that would only act as a disadvantage for credit unions in the marketplace without providing any additional risk mitigation.

The NCUA has repeatedly indicated that the risk-based capital proposal was developed partly as a response to a Government Accountability Office (GAO) Study that was released in January of 2012. The study concludes that from January 1, 2008 to June 30, 2011, five corporate credit unions and 85 credit unions failed. The study further concludes the 85 failed credit unions were relatively small – accounting for less than 1% of total credit union assets. GAO also found that poor management was the primary reason for the failure of the 85 credit unions.[i] While the GAO's analysis of PCA and other NCUA enforcement actions highlights opportunities for improvement, ultimately these 85 credit unions did not fail solely due to inadequate capital.

The MCUL wants to reiterate the concern expressed in our previous comments to the NCUA. The MCUL believes there is a continued need for reform of credit union PCA as such, reevaluation of PCA is necessary. The current system is overly restrictive and the statute does not currently permit credit unions access to supplementary capital which could otherwise be used to augment retained earnings in order to meet capital requirements, nor does the RBC2 proposal provide access to supplementary capital.

Supplemental Capital

Credit unions are the only depository institutions in the United States without the ability to issue some form of capital instrument to augment retained earnings in order to build capital. A credit union's only source of capital is the retention of earnings. The requirement to maintain a higher capital ratio can only be accompanied by asset growth if there is sufficient net income. Increasing a net worth ratio requires even higher levels of net income or slower growth rates. This issue would not be of such concern if retained earnings could be enhanced to some degree, specifically by allowing credit unions access to alternate or supplemental capital.

Credit unions holding a Low-Income Designation from the NCUA can offer secondary capital accounts and can accept non-member deposits from any source. In many situations credit unions have experienced very strong balance sheet growth over the last few years. Due to the low interest rate environment, capital growth has not kept pace with asset growth. Loan growth has remained strong in many instances, yet with rates remaining low, loans do not generate sufficient interest income to maintain and increase capital. If interest rates continue to remain low over the long term, it will have a negative impact on the capital ratio of credit unions as assets continue to increase. Additionally, continued loan growth, while necessary, can cause a significant strain on liquidity and cash flow. All of these factors point to the necessity for credit unions to gain access to supplemental capital outside of obtaining a low income designation

Credit unions have maintained a conservative management style consistent with their cooperative structure. In order to maintain a "well" capitalized status credit unions must maintain a significant cushion above the required 7% level to avoid adverse action during a period of rapid growth. A typical target is to maintain a 200 basis point cushion above the required 7% standard. Current PCA requirements, which were intended to ensure that credit unions maintain a 6% capital ratio, have created powerful incentives to induce credit unions to hold net worth ratios roughly 50% higher than that level. In its present form the PCA regulation incents credit unions to operate at "overcapitalized" levels. Any changes to PCA, as dictated in RBC2, will dramatically impact the capital "buffer."

A potential resolution for the aforementioned issues would be to permit credit unions to issue some form of secondary capital in a way that provides both additional protection to the share insurance fund while not upsetting the unique cooperative ownership structure of credit unions. Secondary capital could come from members in the form of uninsured shares or from nonmembers in the form of subordinated debt. If this is allowed then the NCUA could consider limits on the extent to which a credit union could rely on secondary capital to meet net worth requirements.

The NCUA should consider two goals when considering PCA reform. First, it should preserve the requirement that regulators must take prompt and direct supervisory actions against credit unions that become seriously undercapitalized. This will maintain the very strong incentives for credit unions to avoid becoming seriously undercapitalized. Second, a reformed PCA should not induce well-capitalized credit unions to feel the need to establish such a large buffer over minimum net worth requirements that they feel required to become overcapitalized.

Part 707: Truth in Savings (TISA)

The NCUA issued a request for comment under its Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA) Regulatory Review. The purpose of this request was to identify outdated, unnecessary, or burdensome regulatory requirements imposed on federally insured credit unions. The NCUA chooses to participate in the EGRPRA even though it is not required by law to do so. The MCUL would like to take an

opportunity to echo these concerns during the NCUA's regulatory review process as well.

Many credit unions have provided comments to the NCUA regarding section 707.4 of the TISA. This section of TISA provides for the timing and delivery requirements of account disclosures.

> § 707.4 Account disclosures.
> (a) Delivery of account disclosures—(1) Account opening. (i) General. A credit union must provide account disclosures to a member or potential member before an account is opened or a service is provided, whichever is earlier. A credit union is deemed to have provided a service when a fee required to be disclosed is assessed. Except as provided in paragraph (a)(1)(ii) of this section, if a member or potential member is not present at the credit union when the account is opened or the service is provided and has not already received the disclosures, the credit union must mail or deliver the disclosures no later than 10 business days after the account is opened or the service is provided, whichever is earlier.
> (ii) Timing of electronic disclosures. If a member or potential member who is not present at the credit union uses electronic means, for example, an internet Web site, to open an account or request a service, the disclosures required under paragraph (a)(1) of this section must be provided before the account is opened or the service is provided.
> (2) Requests. (i) A credit union must provide account disclosures to a member or potential member upon request. If a member or potential member who is not present at the credit union makes a request, the credit union must mail or deliver the disclosures within a reasonable time after it receives the request and may provide the disclosures in paper form or electronically if the member or potential member agrees.

The cost associated with the production of the account opening disclosure booklet represents a significant regulatory burden on credit unions. This booklet, frequently covering more than 30 pages, encompasses TISA disclosures, as well as disclosure required by Regulation E, Regulation CC and Fee disclosures. Although each regulation allows for electronic delivery of disclosures, such disclosures are required to be provided to a member when applicable at either account opening or when a relationship is established.

The MCUL encourages the NCUA to amend the current requirements to provide the disclosures under TISA by allowing them to be provided no later than ten (10) days after an account is opened. The NCUA should also work with other regulatory agencies to ensure Regulation CC and Regulation E are updated as well. E-SIGN should also be amended to allow members to consent to receive electronic disclosures if consent is provided in writing.

Conclusion

The MCUL appreciates the NCUA's initiative to review their regulations and provide relevant updates on a consistent basis. In this regulatory environment, it is critical to build efficiencies and eliminate redundancy, while also providing regulatory relief wherever possible. The MCUL is pleased to provide recommendations to assist in this process.

Sincerely,

Ken Ross
Executive Vice President & Chief Operating Officer

[i] http://www.gao.gov/assets/590/587409.pdf