DAKOTA CREDIT UNION ASSOCIATION

August 16, 2022

Regulatory Review (2022)
Office of General Counsel
National Credit Union Administration
1775 Duke Street, Alexandria
Virginia 22314-3428

Submitted electronically to
OGCMAIL@NCUA.GOV

RE: Regulatory Review 2022

Dear Office of General Counsel,

The Dakota Credit Union Association (DakCU), which represents state and federally chartered credit unions in the states of North Dakota and South Dakota, appreciates the opportunity to provide comment to the National Credit Union Administration (NCUA) regarding its 2022 regulatory review which encompasses 12 CFR 700 to 12 CFR 710.

DakCU fully supports the NCUA's stated goal in this review to ensure that its regulations remain "clearly articulated and easily understood." We further applaud the NCUA's proactive process to continually review its regulations to identify any that may need updating. We also appreciate the NCUA in allowing for public feedback and input during this annual regulatory review process of one-third of the NCUA regulations impacting credit unions.

§ 701.2 Federal credit union bylaws/Appendix A to Part 701 Federal Credit Union Bylaws

DakCU urges the NCUA to expedite implementation of the Credit Union Governance Modernization Act of 2022 (Act of 2022), which became law March 15, 2022.

Prior to the Act of 2022, the Federal Credit Union Act (FCU Act) Section 1764 limited expulsion of member to either a two-thirds vote - a member may be expelled by a two-thirds vote of the members of a Federal credit union present at a special meeting called for the purpose, but only after opportunity has been given him to be heard; or expulsion based on nonparticipation - in which the board of directors of a Federal credit union adopt and enforce a policy with respect to expulsion from membership based on nonparticipation by a member in the affairs of the credit union.

The Act of 2022 amended the FCU Act to provide that a member may be expelled "for cause" by a two-thirds vote of a quorum of the directors of the Federal credit union, however, this avenue is not available until the NCUA adopts its regulations to implement these new provisions. *12 U.S.C. § 1764(c)(1).*

The amended Section 12 U.S.C. 1764(c)(2) of the FCU Act requires a FCU may not expel a member under this new provision unless the FCU has provided, in written or electronic form, a copy of the policy adopted by the NCUA Board to each member of the FCU.

New section 12 U.S.C. 1764(c)(5) of the FCU Act, for purposes of expulsion, defines "cause" as "(A) a substantial or repeated violation of the membership agreement of the Federal credit union; (B) a substantial or repeated disruption, including dangerous or abusive behavior (as defined by the National Credit Union Administration Board pursuant to a rulemaking), to the operations of a Federal credit union; or (C) fraud, attempted fraud, or other illegal conduct that a member has been convicted of in relation to the Federal credit union, including the Federal credit union's employees conducting business on behalf of the Federal credit union."

As noted previously, the FCU Act provides that a member may be expelled for cause by a two-thirds vote of a quorum of the FCU's board of directors. *12 U.S.C. § 1764(c)(1*). Following such vote, the member has 60 days to request a hearing. If requested, the board of directors "shall provide the member with a hearing." *12 U.S.C. § 1764(c)(3)(C)(i)*. DakCU fully supports and recognizes the right of the member to be heard. However, there may be potential risk in having a member who is challenging expulsion to be in close physical proximity to the individuals that voted for such expulsion, particularly in instances where the expulsion resulted from "a substantial or repeated disruption, including dangerous or abusive behavior," as included as a "for cause" reason in the FCU Act. *12 U.S.C. § 1764(c)(5)(B)*. DakCU urges the NCUA to consider this concern as it promulgates a member expulsion regulation and FCU Bylaw provision. A possible solution is to allow the credit union board to require the requesting member to attend the hearing virtually and/or telephonically.

§ 701.4 General authorities and duties of Federal credit union directors.

With regard to 12 CFR 701.4, DakCU reiterates our concerns to the proposed amendments to this section relating to NCUA's February 2, 2022, proposed rulemaking concerning succession planning. As we previously stated, DakCU agrees with the NCUA that succession planning is very important for the credit union industry. Furthermore, DakCU is likewise concerned with the decline in the number of credit unions. This decline follows the long-running trend of consolidation across all depository institutions. As noted in the proposed rule, "One of the reasons for the consolidation is the lack of succession planning. An NCUA analysis found that poor management succession planning was either a primary or secondary reason for almost a third (32 percent) of credit union consolidations." *87 FR 6079, February 3, 2022*. However, DakCU continues to believe that creating more rules and regulations is not the best solution or approach to resolve this issue.

As previously discussed in our March 29, 2022, comment letter, DakCU believes a better approach to encouraging meaningful succession planning is through guidance, tools, educational material, and financial support for credit unions to identify and develop leadership talent. If the credit union does not have the resources or opportunity to learn the importance and value of succession planning, even with a regulatory requirement, they may just “check the box” to get the task done instead of putting meaningful effort into the process.

§ 701.6 Fees paid by Federal credit unions.

Section 12 CFR 701.6 addresses fees paid by Federal credit unions and our comments relate to the operating fee. As illustrated in the recent NCUA Operating Fee Schedule for 2022, attached to Letter to Federal Credit Unions 22-FCU-01, the NCUA does not assess an operating fee to FCUs with less than $1 million in assets. DakCU believes the current threshold of less than $1 million in assets, which has not been adjusted for inflation and is not in line with system-wide growth, is insufficient. While the amount of the operating fee collected by credit unions between $1 million and $10 million is relatively small in the aggregate, it accounts for real dollars that are diverted from serving the members of the nation’s smallest FCUs.

DakCU urges the NCUA to increase the threshold from less than $1 million in assets to less than $10 million in assets. The FCU Act establishes that FCUs with less than $10 million in assets do not have to apply GAAP. *12 U.S.C. § 1782(a)(6)(C)(iii).* This is also the level below which a credit union could still be considered “new” under the FCU Act’s prompt corrective action provisions. *12 U.S.C. § 1790d(o)(4)(B)*. Thus, we believe $10 million is an appropriate threshold in regard to paying the operating fee.

§ 701.21 Loans to members and lines of credit to members.

Section 12 CFR 701.21(c)(3) relates to credit applications and overdrafts. In relevant part this section provides that credit union’s overdraft policy must…”establish a time limit not to exceed forty-five calendar days for a member either to deposit funds or obtain an approved loan from the credit union to cover each overdraft.” In January 2021, the NCUA proposed to revise the 45 day time limit that the FCU overdraft policy mandates. As noted in the proposed rule, “the Board believes that this change would help ensure that FCUs have the additional flexibility necessary to provide relief to their members in a manner consistent with the NCUA’s responsibility to maintain the safety and soundness of the credit union system.” 86 FR 3877 (January 15, 2021). As discussed in our February 16, 2021, comment letter, DakCU believes FCUs can still operate an overdraft program without a prescriptive regulatorily mandated time limit while adhering to safety and soundness principles.

DakCU continues to support the proposed revisions to 12 CFR 701.21(c)(3) regarding overdraft policy requirements. Allowing a FCU to "establish a specific time limit that is reasonable and universally applicable for a member either to deposit funds or obtain an approved loan from the credit union to cover each overdraft" will provide FCUs the needed flexibility in meeting their members' needs. We urge the NCUA to proceed with finalizing this proposed rule.

Section 701.21(c)(4) addresses maturity limits for loans to member. Specifically, section 701.21(c)(4)(ii)(A) provides, "Notwithstanding the general 15-year maturity limit on loans to members, a federal credit union may make loans with maturities: (A) As specified in the law, regulations or program under which a loan is secured, in full or in part, by the insurance or guarantee of, or with an advance commitment to purchase the loan, in full or in part, by the Federal Government, a State government or any agency of either, as provided in paragraph (e) of this section." Section 701.21(e) provides, "Insured, guaranteed, and advance commitment loans. Notwithstanding the general 15-year maturity limit on loans to members in paragraph (c)(4) of this section, a loan secured, in full or in part, by the insurance or guarantee of, or with an advance commitment to purchase the loan, in full or in part, by the Federal Government, a State government or any agency of either, may be made for the maturity and under the terms and conditions, including rate of interest, specified in the law, regulations or program under which the insurance, guarantee or commitment is provided."

DakCU urges the NCUA to reconsider its position on Fannie Mae and Freddie Mac which are under the conservatorship of the Federal Housing Finance Agency (FHFA). In its Legal Opinion Letter 05-0514, the NCUA took the position that government-sponsored enterprises (GSEs) are not government agencies. The GSEs have been under conservatorship of the federal government for a decade with no specific anticipated end-date. Therefore, we ask the NCUA to reverse its determination and conclude that the GSEs are "government agencies" for the purposes of these rules.

Section 701.23(c)(2) provides that "if a Federal credit union makes a commercial loan through a program in which a federal or state agency (or its political subdivision) insures repayment, guarantees repayment, or provides an advance commitment to purchase the loan in full, and that program has requirements that are less restrictive than those required by this rule, then the Federal credit union may follow the loan requirements of the relevant guaranteed loan program."

By allowing GSEs to be recognized as "government agencies" under NCUA regulations would then allow business loans with an advance commitment from Freddie Mac or Fannie Mae to be exempt from the

MBL definition; it should also exclude mortgages guaranteed, insured, or purchased by the GSEs from the maturity limits in section 701.21(e).

With regard to 12 CFR 701.21(c)(7), the regulation provides the general rule that “Except when the Board establishes a higher maximum rate, federal credit unions may not extend credit to members at rates exceeding 15 percent per year on the unpaid balance inclusive of all finance charges. Federal credit unions may use variable rates of interest but only if the effective rate over the term of a loan or line of credit does not exceed the maximum permissible rate.” The regulation goes on to provide that “At least every 18 months, the Board will determine if federal credit unions may extend credit to members at an interest rate exceeding 15 percent. After consultation with appropriate congressional committees, the Department of Treasury, and other federal financial institution regulatory agencies, the Board may establish a rate exceeding the 15 percent per year rate, if it determines money market interest rates have risen over the preceding six-month period and prevailing interest rate levels threaten the safety and soundness of individual federal credit unions as evidenced by adverse trends in liquidity, capital, earnings, and growth.” *12 CFR 701.21(c)(7)(ii)(A)*.

On June 24, 2021, NCUA extended the 18 percent ceiling through March 10, 2023. Letter to Federal Credit Unions 21-FCU-04. Given the current rising interest rate environment, we believe it is appropriate for the NCUA to review this section with an eye toward avoiding elevated risk not only to the safety and soundness of individual FCUs but to the collective credit union industry at large. DakCU believes it is necessary to at least maintain the current cap of 18%, however, we ask the NCUA to examine the potential benefits associated with a floating interest rate cap, such as the enhanced ability of FCUs to manage interest rate risk.

§ 701.22 Loan participations.

Section 12 CFR 701.22 addresses loan participations and includes several prescriptive thresholds. Specifically, sections 701.22(b)(5)(ii) and (iv) provides, “A federally insured credit union may purchase a participation interest in a loan from an eligible organization only if the loan is one the purchasing credit union is empowered to grant and the following additional conditions are satisfied: the purchase complies with the purchasing federally insured credit union's internal written loan participation policy, which, at a minimum, must: (ii) Establish a limit on the aggregate amount of loan participations that may be purchased from any one originating lender, not to exceed the greater of $5,000,000 or 100 percent of the federally insured credit union's net worth, unless this amount is waived by the appropriate regional director, and, in the case of a federally insured state-chartered credit union, with prior written concurrence of the appropriate state supervisory authority; …(iv) Establish a limit on the aggregate amount of loan participations that may be purchased with respect to a single borrower, or group of associated borrowers, not to exceed 15 percent of the federally insured credit union's net worth, unless waived by the appropriate regional director, and, in the case of a federally insured state-chartered credit union, with prior written concurrence of the appropriate state supervisory authority."

DakCU believes returning flexibility to the individual credit union to set its own established limit within its risk appetite and consistent with the established policies of the credit union's board of directors is appropriate given the inadequacy of a one-size-fits all standard in this regard. We believe the individual credit union and its board of directors is in the best position to make these decisions.

§ 701.33 Reimbursement, insurance, and indemnification of officials and employees.

Section 12 CFR 701.33(b)(1) provides that "only one board officer, if any, may be compensated as an officer of the board. The bylaws must specify the officer to be compensated, if any, as well as the specific duties of each of the board officers. No other official may receive compensation for performing the duties or responsibilities of the board or committee position to which the person has been elected or appointed." The regulation goes on to explain what is excluded from the term "compensation."

In its 1995 Legal Opinion Letter 95-1218, the NCUA noted that "You may be interested to know that in 1988, the NCUA Board proposed to amend Section 701.33 by expanding it to permit FCUs to reimburse officials for pay or leave lost while attending board or committee meetings. Of the 86 commenters, 62 opposed the expansion. The primary reason given for opposing the proposal was that reimbursement would be contrary to the credit union philosophy of volunteerism. In light of the comments received, the Board decided not to go forward with the proposal."

DakCU urges the NCUA to revisit this proposal as credit unions struggle to find volunteers to fill vacancies on the board and committees. Allowing a FCU to reimburse officials for pay or leave lost may open opportunities for younger professionals to consider being nominated for positions on the credit unions board of directors. Young employees, just starting in their career, may find themselves financially unable to leave work to volunteer – due to student loan debt among other financial obligations – and therefore, giving FCUs the ability to reimburse some of the expenses would allow the credit union to seek potential volunteers that may better reflect their overall membership.

§ 701.34 Designation of low income status.

We urge the NCUA to explore additional avenues in which a credit union may be able to qualify for the low-income designation under 12 CFR 701.34. We acknowledge that NCUA has made significant efforts to help identify credit unions that qualify for low-income designation and provided education to credit unions on the benefits of this designation.

As the NCUA is already aware of, the low-income designation provides credit unions additional opportunities to serve their communities. We urge the NCUA to explore other approaches for credit unions to qualify as low-income, such as a potentially narrative approach where credit unions could describe why they should be given a low-income designation without statistical analysis. This would allow more credit unions to better serve their communities through the additional tools made available to low-income designated credit unions.

Part 702 – Capital Adequacy

DakCU appreciates the recent regulatory relief relating to prompt corrective action (PCA) the NCUA has granted credit unions through interim final rules, the most recent being that approved February 28, 2022. *87 FR 10,944 (Feb. 28, 2022)*. DakCU urges the NCUA to consider opportunities for additional PCA relief by temporarily excluding certain assets from the net worth ratio. Credit unions continue to invest funds—which have significantly increased due to an influx of consumer deposits—in zero- and low-risk assets, such as shorter-term Treasury securities. These deposits and resulting investments, however, have caused a decrease in the net worth ratio for many credit unions. Therefore, we ask the NCUA to follow the lead of other federal banking regulators and exclude such investments, as well as 10% of deposits held at the Federal Reserve, from the net worth ratio calculation.

DakCU also requests the NCUA consider amendments to the definition of "total assets" to exclude certain zero- and low-risk assets, as this would provide credit unions with additional flexibility regarding credit union capital. Thus, we ask the NCUA to explore ways to reduce the denominator of the net worth ratio—including by excluding certain assets from the calculation—given that savings growth is a result of the current environment as opposed to something credit unions are actively encouraging. Credit unions do not want to turn away members or their deposits, however, this is a reality that could happen more frequently in an environment of declining net worth ratios.

Part 708b – Mergers of Insured Credit Unions into Other Credit Unions; Voluntary Termination or Conversion of Insured Status.

Subpart A to Part 708b addresses mergers between credit unions where at least one of the credit unions is federally insured. The NCUA finalized a rule in 2018 that made significate amendments to this section including extending these requirements to state chartered credit unions. Several Dakota credit unions have since merged while this rule was in effect and offer the following suggestions for improvements.

In a recent merger between two federal credit unions, the merging credit union was very well capitalized. The board of directors of the two credit unions agreed that an extraordinary, or "bonus", dividend would go to the merging credit union's members based on the average deposit balance such that the two credit unions would be left with similar capital levels. The CEO and board members of the merging credit union were obviously members of the merging credit union with funds in their accounts and therefore received part of this distribution, along with every other member of record in an equal percentage of their deposits. However, the CEO and board member were required to disclose this distribution to the membership as part of the member notice concerning the merger.

Section 7088.103(a)(7) requires, among other things, that “Upon the approval of a proposition for merger by the boards of directors of the credit unions, the two credit unions must prepare a plan for the proposed merger that includes: …Description of any merger-related financial arrangement, as defined in § 708b.2.” Furthermore, section 708b.104(b)(4)(v) details the contents of the member notices, which includes – “A summary of the merger plan, including but not necessarily limited to:… A detailed description of all merger-related financial arrangements. This description must include the recipient's name and title as well as, at a minimum, the amount or value of the merger-related financial arrangement expressed, where possible, as a dollar figure.”

12 CFR 708b.2, defines “Merger-related financial arrangement” to mean “a material increase in compensation or benefits because of, or in anticipation of, a merger that any covered person of a merging credit union has received during the 24 months before the date the boards of directors of both credit unions approve the merger plan. It also means a material increase in compensation or benefits that any covered person of a merging credit union will receive in the future because of the merger. This includes the sum of all increases in direct and indirect compensation, such as salary, bonuses, leave, deferred compensation, early payout of retirement benefits, or any other financial rewards, other than benefits available to all employees of the continuing credit union on identical terms and conditions. A material increase is an increase in value that exceeds the greater of 15 percent of existing compensation or benefits or $10,000.” “Covered person” is defined as “the chief executive officer or manager (or a person acting in a similar capacity); each of the four most highly compensated employees other than the chief executive officer or manager; and any member of the board of directors or the supervisory committee.” *12 CFR 708b.2*

DakCU recommends the NCUA revisit the definition of “merger-related financial arrangement” and provide an exclusion when the increase is directly related to a bonus dividend that is paid to all members of record.

With regard to the North Dakota state chartered federally insured credit union mergers, this regulation has created another layer of rules and regulations over an area that already had procedures prescribed under North Dakota state administrative rules. The NCUA extended Part 708b to federally insured state chartered credit unions in 2018. DakCU acknowledges that voluntary mergers must be in the members’ best interest and any potential conflicts of interest need to be vetted out. DakCU continues to believe that

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rulemaking regarding mergers of federally insured state chartered credit unions is best accomplished by the State Credit Union Board. The State Credit Union Board is best suited to tailor merger rules for stated chartered credit unions as they are sometimes more in tune with local issues and concerns, and draft regulations to address these local issues more aptly.

Conclusion

As the NCUA is aware, regulatory burden remains a constant concern for our credit unions, especially the small credit unions with limited staff and resources. Therefore, we urge the NCUA to promulgate new or expand existing rules only if such rules are clearly warranted based on a compelling need. Similarly, we ask the NCUA to strongly consider the current regulatory burden on credit unions as it proceeds with this and future regulatory reviews.

Thank you for this opportunity to share our comments and concerns.

Respectfully,

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CEO/President

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Chief Compliance Officer