November 20, 2019

The Honorable Rodney E. Hood, Chairman
The Honorable Todd M. Harper, Board Member
The Honorable J. Mark McWatters, Board Member
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

BY EMAIL ONLY

RE: 2020-2021 Budgets and Budget Justification
BudgetComments@ncua.gov

Dear Chairman Hood and Board Members Harper and McWatters:

On behalf of the member credit unions of the Cooperative Credit Union Association, Inc. ("Association"), please accept this letter relative to the National Credit Union Administration's ("NCUA") proposed 2020-2021 budgets and budget justification. The Association is the state trade association representing credit unions located in the states of Delaware, Massachusetts, New Hampshire, New Jersey and Rhode Island, serving approximately 200 credit unions which further serve approximately 3.6 million consumer members.

Overview

The Association expresses its appreciation for the NCUA's efforts in soliciting comments on its proposed 2020-2021 budgets and budget justification. The congressional directive contained in the *Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018* that requires the agency to publish its budget, hold a public budget hearing and permit public comments on the draft budget has been strongly supported by our members. Furthermore, the Association finds the inclusion of the NCUA's rationale for its proposed budget decisions for the next two years found in its Federal Register notice dated November 1, 2019 insightful and helpful.

This comment letter contains a variety of comments for consideration and specific suggestions for further change. The Association emphasizes that it does not support micromanagement of the agency's strategic budget decisions. Similarly, we do not agree with agency micromanagement of credit unions when it occurs. Our objective in commenting on the proposed budget materials is to focus on ensuring that there is fair and reasonable transparency and accountability to credit unions which fund NCUA's regulatory and supervisory operations. This is a goal shared and promoted by our members, together with the NCUA Board.

A. NCUA Priorities to Manage Identified System Risks Reflected in the Proposed Budget

The agency's proposed budget justification provides a detailed description of how its proposed resource allocations support the NCUA's duties under the Federal Credit Union Act. The Association welcomed the inclusion of the economic outlook, which underlies the NCUA's needs for funding, and found it to be very useful. The Association also generally agrees with the major risk factors found within in the budget justification as those that the NCUA must be positioned to address: cybersecurity, financial technology, credit union membership, and industry consolidation.

Another factor identified by the NCUA, lending trends, is believed by the Association to be worthy of further consideration. Lending trends reflect the needs of credit union members for borrowings. While loan concentrations may raise risk issues, the Association asserts that proper management of such risks is inherent in the operations of well-managed credit unions. Accordingly, the Association urges the agency to refrain from imposing any undue supervisory constraints on lending programs that are needed by consumers and small businesses, are properly structured, and are planned for and monitored by credit unions to mitigate risks.

The agency's priorities also include technological changes within and outside the credit union system. The Association agrees that technological changes should be included but cautions against possible unintended consequences. Member reservation is centered, not so much on the capability of credit unions to participate in or respond to developments, but rather on well-intentioned supervisory interruption which could have the impact of curtailing the ability of credit unions to take advantage of technology to deliver expedient and quality service to members.

The Association requests the NCUA to work closely with the credit union system on this issue and proposes that the agency outreach by creating an agency-credit union advisory council to ensure that regulatory concerns are identified, while simultaneously ensuring that credit unions have the flexibility to utilize technology to fulfill members' financial expectations and needs. A council can be useful to the agency and credit unions in addressing further issues as they arise related to technological advances in the financial sector. The NCUA's Office of Business Innovation is set to receive $3.3 million in 2020 and $3.4 million in 2021 in the budget. The Association is not entirely clear on how the office fits into the NCUA's consideration of such issues and believes that further explanation of the office, its role, its funding needs and how the agency can help ensure that credit unions are able to take advantage of technology in their operations, would be useful.

Concerning membership trends, the agency's justification notes that all credit unions should ensure that their product mix is consistent with their members' needs. Without question, the Association agrees. However, the Association does not believe that there is a role for the agency in determining a list of services to be provided by a credit union to its members, absent demonstrable, material, safety and soundness issues identified.

B. Modern Examination and Risk Identification Tool (MERIT)

MERIT is the agency's new, long awaited, Modern Examination and Risk Identification Tool ("MERIT") and is designed to replace the AIRES examination system. The proposed budget includes funding for MERIT. The Association acknowledges that the NCUA used the services of an independent market research firm to estimate the cost of MERIT, which is initially projected to approach $37.9 million.

Many questions from member credit unions have surfaced about MERIT which are not addressed in the justification. There is a limited number of FAQs about MERIT on the agency's website, but the answers are very concise and not very useful. The Association urges the NCUA to provide a much more detailed explanation of the new system, including in the context of the agency's proposed budget.

The Association believes more information is needed to be provided to credit unions about MERIT and about how it will affect them, their examinations, the agency's supervisory priorities, and the NCUA budget. Examples of issues that members encourage the agency to address, at a minimum, include: which entity was selected to estimate the cost of MERIT implementation, how did it make the estimation, was an internal estimation created by the agency, how will MERIT affect the agency's budget going forward, and any other estimated budget implications of MERIT.

C. Agency Staffing (Full Time Equivalents, FTEs)

The NCUA notes that its proposed staffing level assumes there will be a 2.2% vacancy rate, which is estimated to be approximately 26 full time employees ("FTEs). The justification does not explain why the agency has not reduced the target FTE level to take this vacancy rate into account, since the vacancy rate aligns with the agency's recent attrition and workforce management efforts. The Association urges the NCUA to consider whether the FTE level, and therefore, the overall budget could be reduced by 2.2% to accommodate a vacancy rate that is more realistic.

The agency requests three additional staff in the proposed budget, bringing the agency's FTE level to 1,185 from 1,182 currently. Two of these staff members would be added for cybersecurity purposes and one would be added for outreach purposes for the Chairman and the Board. The Association does not oppose these additions, as the agency is in the best position to determine its own staffing needs and appreciates the level of detail in the proposed justification. However, the Association suggests that the NCUA should expand its proposed justification as to why it needs each of the 1,185 positions when the number of credit unions continues to decline, as well as why the three new positions would be funded in the aggregate at $0.9 million. Universal statements regarding the complexity of credit unions provide sufficient transparency and accountability to credit unions regarding the size of the agency's staff. The Association was unable to find an explanation of the projected $0.9 million funding level for the three added positions.

D. Contracted Services

The proposed budget would increase contracted services by 13.8%, with over $43 million for 2020 and $47 million for 2021. Member questions have arisen about the agency's funding level for contracted services, not satisfactorily addressed in the budget justification, including the details of the proposed $9 million increase over two years for contracted services.

The Association does not suggest that the use of contracted services is not within the agency's authority as such services can help mitigate agency costs, especially as services provided by contractors do not usually include expensive benefits, such as those associated with retirement and health. However, when NCUA relies on outside consultants for the maintenance and operation of key systems, such as MERIT, the Association urges the agency to provide much more information to credit unions about the process of how consultants were selected, the agency's oversight of consultants, the use of multi-year agreements, and the due diligence in selecting and maintaining consultants. Essential services are important, and our member credit unions urge the agency to be as transparent as possible about its use of consultants.

E. Operating Fees for Federal Credit Unions

Under the proposed budget, federal credit unions are set to provide 38% of the agency's 2020 operating costs through their operating fees. As proposed, a 1.2% increase to federal credit union annual operating fees is scheduled, with the exception for federal credit unions with assets under $1 million which are not assessed operating fees. The increase is due to the changes in the Overhead Transfer Rate ("OTR") and credit union asset growth. The Association urges the agency to revisit its budget to determine if this increase could be eliminated by reducing proposed costs throughout the budget that are not essential.

F. Overhead Transfer Rate (OTR)

NCUA proposes that for 2020, the federal credit union portion of the OTR would be 31.3% and the state-chartered credit union portion would be 30%. The Association has long struggled with understanding the levels of OTR and recognizes NCUA's efforts in rulemaking to add clarity on the OTR methodology in 2017. While the proposed levels appear balanced in terms of similar amounts, confusion continues as to how the agency allots expenses between supervision, which would apply to state and federally-chartered credit unions, and regulatory expenses, which are absorbed by federal credit unions. Issues regarding the fairness of the OTR will continue to surface as long as the expense allocation remains unclear. More specifically, relating OTR to particular, not general, safety and soundness issues would be more useful in providing increased transparency to the process.

G. Support for State Examination Strength

The Association strongly endorses cost-effective support for state examination strength, including training for state examiners. State regulators in our member states of Massachusetts, New Hampshire and Rhode Island rely on such training and often comment on its value and availability. Examiner education and career paths impact examiner retention which is always an issue for all. Training provided by NCUA helps position state regulators as competitive employers and helps to strength the credit union dual chartering system.

The proposed Share Insurance Fund Administrative Budget includes $1.67 million for state examiner training in 2020 but only allocates $899,508 for 2021, which is lower than the current amount of $992,000 for state examiner training this year. The NCUA is urged to ensure that sufficient funds are provided for state examiner training and to provide an explanation annually for funding for state examination support. Moreover, if and when the agency proposes to reduce state examination funding, credit unions should be provided a complete explanation for any decrease.

In the past, the Association has urged the agency to coordinate more thoroughly with state regulators on supervisory issues and is pleased that the budget justification discusses NCUA's efforts in this area. NCUA is encouraged to look for additional ways to minimize supervisory costs through greater reliance on and cooperation with state credit union authorities.

H. Planned Agency Engagement Summits for 2020

The Association supports the NCUA's efforts to reach out to credit unions on issues of significance. The budget justification indicates that topics at these summits may include cybersecurity, risk mitigation, financial inclusions, and others. Recently, the Association was pleased to participate in the agency's first Diversity, Equity and Inclusion event which proved to be both timely, informative and thought provoking. Looking ahead, another appropriate topic could be developed around the agency's forecast on the future of the credit union system as consolidations and new entrants into financial services continue to occur.

I. Fair Lending Examinations

At the October NCUA Board meeting, the issue of separate fair lending examinations for certain credit unions was discussed. The Association is not aware of problems that necessitate the establishment of exams that focus exclusively on fair lending or consumer compliance. The merits of this issue, which at its core is a policy issue, should be subject to sufficient notice and comment from stakeholders before any final agency decision is made regarding separate examinations. Similarly, the Association does not support including funding for such examinations in the 2020 or 2021 budgets, particularly without soliciting comments from the credit union system before proceeding. These issues are already reviewable as part of safety and soundness examinations conducted by NCUA and states, such as Massachusetts, already examine for such issues. Moving forward without further evaluation and industry considerations will run the risk of duplication and a higher regulatory burden.

Conclusion

Over time and as encouraged by Congress, credit unions, the Association and other stakeholders, NCUA has made important improvements in the amount and quality of information it provides to credit unions relative to its budget and budget decisions. Efforts today mark the fourth consecutive effort. Without question, the budget justification for the proposed 2020 and 2021 budgets provides significant details to help credit unions better understand the agency's budget process and decisions. Accordingly, on behalf of the Association's members, NCUA is commended for providing the information. As key issues raised in this letter deserve your attention, the Association urges the agency to provide additional explanations to enhance transparency and promote accountability to credit unions as funders of the agency's operations.

Thank you for the opportunity to express our members' views. The Association urges the Board to continue to do all it can to contain costs as it seeks to operate effectively and efficiently in fulfilling its statutory duties under the Federal Credit Union Act.

Sincerely,

Ronald McLean
President/CEO
Cooperative Credit Union Association, Inc.

cc: Mr. Rendell Jones, Chief Financial Officer
National Credit Union Administration

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