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National Credit Union Administration

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Congressional Testimony

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Hearing on Oversight of Financial Regulators

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Congressional Testimony

Chairman Crapo, Ranking Member Brown, and Members of the Committee, as Chairman of the National Credit Union Administration (NCUA) Board, I appreciate the invitation to testify today about the state of the credit union industry and provide background on the efforts, activities, objectives, and plans that the NCUA has undertaken and will undertake to fulfill its mission.

The NCUA's mission is to "provide, through regulation and supervision, a safe and sound credit union system, which promotes confidence in the national system of cooperative credit."[1] This system is vital to the American economy, touching more than one-third of all U.S. households.[2] In turn, the NCUA is charged with, and focused on, ensuring the safety and soundness of the National Credit Union Share Insurance Fund (Share Insurance Fund). The agency takes seriously its paramount responsibilities to regulate and supervise approximately 5,375 federally insured credit unions with more than 116 million member-owners and more than $1.45 trillion in assets across all states and U.S. territories.[3] As an adjunct to that mission, the agency has developed initiatives to make it easier for credit unions to serve their members more effectively, including members of modest means and those in underserved areas.[4]

The first part of my testimony today focuses on the strong state of the credit union industry and the Share Insurance Fund. Next, I will discuss the efforts and initiatives the NCUA has undertaken to meet the goals the agency set out in its *2018–2022 Strategic Plan*: (1) ensuring a safe and sound credit union system; (2) providing a regulatory framework that is transparent, efficient, and improves consumer access; and (3) maximizing organizational performance to enable mission success.[5] In describing how the NCUA is meeting these goals, I will focus on the NCUA Board's ongoing efforts to improve the agency's efficiency and effectiveness in light of the ever-changing financial services marketplace. The NCUA is striving to reduce the regulatory, reporting, and examination burdens facing credit unions without sacrificing the safety and soundness of the credit union system and, in turn, the Share Insurance

[1] See NCUA Mission and Vision, https://www.ncua.gov/about-ncua/mission-values.
[2] NCUA calculations using the Federal Reserve's *Survey of Consumer Finances, 2016*.
[3] Based on December 31, 2018 Call Report Data.
[4] *Serving the Underserved*, National Credit Union Administration, https://www.ncua.gov/support-services/credit-union-resources-expansion/field-membership-expansion/serving-underserved. The Federal Credit Union Act, the statute governing this agency and federally insured credit unions, specifies that this national system is intended to meet "the credit and savings needs of consumers, especially persons of modest means." Credit Union Membership Access Act, Pub. L. No. 105-219, § 2(4), 112 Stat. 913, 914 (1998).
[5] See *NCUA Strategic Plan 2018–2022*, https://www.ncua.gov/files/agenda-items/AG20180125Item3b.pdf.

Fund. I will also address some of the ways the NCUA is promoting financial inclusion and making it easier for credit unions to more effectively serve their members, including the underserved, those of modest means, people with disabilities, and those in vulnerable communities. Finally, I will detail several areas where Congressional action could enhance how the NCUA carries out its safety and soundness mission and allow credit unions to serve their members and communities better, including those of modest means and the underserved.

I. State of the Credit Union Industry and the Share Insurance Fund

Federally insured credit unions continued to perform well in 2018. By year's end, credit union membership grew by more than five million to more than 116 million members. Assets in the credit union system increased to $1.45 trillion, and the system's aggregate net worth ratio stood at 11.30 percent, well above the seven percent statutory level to be considered a well-capitalized credit union.

The NCUA continues to be a responsible steward of agency funds and remains dedicated to sound financial management practices. Through various actions taken by the NCUA Board from 2017 through the present, the agency has increased the strength of the Share Insurance Fund, paid record distributions back to credit unions, and covered the costs of the recent failure of two large credit unions.

Through prudent management, in 2017, the NCUA was able to close the Corporate Credit Union Stabilization Fund (Stabilization Fund) four years ahead of schedule and transfer its assets and obligations to the Share Insurance Fund. This transfer increased the Share Insurance Fund's equity ratio from 1.25 percent to a strong 1.39 percent as of December 31, 2018 — even after reserving for more than $750 million in losses associated with the failure of two relatively large credit unions heavily concentrated in taxi medallion secured lending. This higher equity ratio level positions the Share Insurance Fund to cover expected losses and withstand the impact of a moderate recession without needing to assess credit unions a premium to restore the Share Insurance Fund to its statutory minimum level of 1.20 percent.[6] Because the Stabilization Fund closed early, the NCUA was able to avoid assessing credit unions as much as $1.3 billion in share insurance premiums, while also providing an historic Share Insurance Fund dividend to be paid to credit unions. In July 2018, the NCUA paid a Share Insurance Fund dividend to credit unions of almost $736 million — the largest in its history. Another dividend of $160.1 million will be paid to credit unions in 2019.

At various times throughout 2018, the NCUA was the conservator of six credit unions. As of December 31, 2018, however, no credit unions remained under the NCUA's

[6] 12 U.S.C. § 1782(c)(2)(C).

conservatorship. For 2018, there were eight credit union failures, compared to 10 failures in 2017. The cost to the Share Insurance Fund for insurance losses was $785.0 million in 2018, an increase from $24.4 million in 2017. As discussed above, this increased cost was largely because of actions needed to address the failure of two large credit unions, each of which was highly concentrated in taxi medallion loans. The NCUA continues to evaluate all courses of action that will maximize potential recoveries from the assets of liquidated credit unions and minimize losses to the Share Insurance Fund. Despite these losses, the Share Insurance Fund remains financially strong and has sufficient equity and reserves to cover anticipated losses.

Despite the strong state of the credit union industry and the Share Insurance Fund, we appreciate the NCUA's duty, as a prudential regulator and insurer, to remain cognizant of the various risks and opportunities posed by the rapidly evolving financial services landscape. Below is a more thorough examination of some of the risks facing the broader economy, including the credit union industry.

Market Risks

As noted above, the credit union system is generally quite strong. There are broader market risks on the horizon, however, that could threaten financial stability generally, including the safety and soundness of the credit union system. For example, rising debt levels may pose some risks to the economy. Corporate debt has increased steadily since 2012,[7] and non-financial debt as a share of the economy is currently at very high levels.[8] A number of factors has driven or facilitated this run-up in borrowing, including share buybacks, low interest rates, and high profits. Since 2012, there has been a particularly sharp increase in the pool of higher-risk debt. The volume of BBB-rated debt, the riskiest tier of investment grade debt, has increased significantly over the last several years.[9] An economic downturn or credit quality downgrades for these lower quality bonds could push them into the speculative grade or "junk" category, which might produce a sell-off in these bonds because some investors are restricted to holding investment-grade debt. A sell-off could limit capital investment and diminish financial stability.

Another market risk is continued uncertainty about the post-Brexit future of the European Union and the United Kingdom.[10] This uncertainty could lead to increased financial market volatility and greater risk aversion, stressing the banking system, causing financial conditions to tighten, and possibly leading to slower economic growth

[7] See https://fred.stlouisfed.org/series/NCBDBIQ027S.
[8] See https://www.dallasfed.org/research/economics/2019/0305.aspx; https://www.marketwatch.com/story/these-5-charts-warn-that-the-us-corporate-debt-party-is-getting-out-of-hand-2018-11-29.
[9] See https://www.dallasfed.org/research/economics/2019/0305.aspx.
[10] See https://www.reuters.com/article/britain-rating-moody-s-idINKCN1RN165.

in Europe. Foreign economic activity has already showed signs of slowing and is expected to moderate further over the next year. While experts are not predicting a global recession, a significant deterioration in global economic conditions would have ramifications in international financial markets and the U.S. economy.

Cybersecurity and Technology

Cybersecurity threats and other technology-related issues continue to be of key interest and concern to the NCUA. Cyberattacks pose an acute threat to credit unions, financial regulators, and the broader financial system. Cyber threats such as phishing scams, ransomware, and malware have proliferated in recent years, and financial institutions like credit unions are prime targets. That is why the NCUA again made cybersecurity assessment one of its primary areas of supervisory focus in 2018, and why I will continue to prioritize it as the NCUA's new Chairman.[11] I will make certain that we employ all available resources to ensure data protection for consumers and combat cybersecurity threats.

Last year, the NCUA began implementing a new Automated Cybersecurity Examination Tool, or ACET, to improve and standardize supervision related to cybersecurity.[12] The new examination tool currently is being applied to larger credit unions with over $250 million in assets, but the NCUA continues to test and refine the tool so that we can properly scale it down to apply to smaller, less complex institutions. We believe this will help focus and prioritize cybersecurity for credit unions and make it an integral part of their risk-management strategies.

We also have placed a very strong emphasis on protecting the NCUA from cybersecurity threats and data breaches. The NCUA's Office of the Chief Information Officer is continually taking steps to enhance the agency's information security posture and ensure the NCUA's systems and information are protected from compromise.

Additionally, while technological advances provide credit unions with tremendous opportunities, they also bring new risks. Consumer demand for more modern services and realities about economies of scale have forced many credit unions, particularly smaller ones, to either merge or rely heavily on third-party vendors to enable them to provide those services. As discussed throughout my testimony, the NCUA is working to keep pace with the changes brought by emerging technology and the related threats they pose. In July 2018, the NCUA created Blockchain and Fintech Working Groups to perform an in-depth analysis of financial technology developments, including cryptocurrencies, and their implications for the credit union system. The working

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[11] "Supervisory Priorities for 2018," NCUA Letter to Credit Unions, Number 17-CU-09, Dec. 2017, available at https://www.ncua.gov/files/letters-credit-unions/17-CU-09-supervisory-priorities-2018.pdf.
[12] *Id.*

groups have been evaluating both the opportunities and risks associated with these new technologies.

Fintech and credit union reliance on third-party vendors increases systemic cybersecurity risks across the financial services landscape. The credit union system is particularly at risk because the NCUA does not have sufficient legal authority to directly identify and address systemic cybersecurity risk and the potential contagion risk that key fintech service providers can pose.

Currently, the NCUA may only examine credit union service organizations (CUSOs) and third-party vendors with their permission. We cannot enforce any necessary corrective actions or share the results of a voluntary review with customer credit unions of the third-party vendor. In recent years, nearly all of the core technology service providers that exclusively serve credit unions declined a voluntary review by the NCUA. Even though CUSOs are required to give the NCUA access to their books and records, without the NCUA's enforcement authority, the CUSOs are free to reject the NCUA's recommendations to implement the appropriate corrective actions that would mitigate identified risks. This lack of vendor authority stands in contrast to the powers of the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and most state regulators, a situation identified as a concern by both the Government Accountability Office and the Financial Stability Oversight Council (FSOC).[13]

As Chairman, I am committed to working with the NCUA's partners on the FSOC to ensure that various threats to financial markets are properly monitored and mitigated. In March 2019, the FSOC proposed new interpretive guidance on how it would consider designation of nonbank financial companies for enhanced supervision by the Federal Reserve.[14] The guidance calls for the FSOC to focus on an activities-based, or product-based, approach for identifying risks to U.S. financial stability. It would increase the analytical rigor of company determination analyses and ensure that the anticipated benefits of a designation are expected to justify the expected costs. This guidance will increase the FSOC's transparency and will provide the market with much needed clarity on its deliberations. It also ensures that the FSOC is looking at the widest range of potentially problematic financial activities that could threaten market stability.

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[13] GAO, Electronic Banking: Enhancing Oversight of Internet Banking Activities, GAO/GGD-99-91 (Washington, D.C.: July 6, 1999). Also, see GAO-04-91 and See U.S. Gov't. Accountability Office, GAO-15-509, Cybersecurity: Bank and Other Depository Regulators Need Better Data and Analytics and Depository Institutions Want More Usable Threat Information 32 (2015), available at https://www.gao.gov/assets/680/671105.pdf.
[14] U.S. Treasury Department, "Financial Stability Oversight Council Proposes Changes to Nonbank Designation Guidance," Mar. 6, 2019, available at https://home.treasury.gov/news/press-releases/sm621.

II. The NCUA's Recent Efforts and Activities

The NCUA's primary mission is to protect the safety and soundness of the credit union system and the Share Insurance Fund. As an adjunct to that mission, the agency has developed initiatives to facilitate credit unions more effectively serving their members and communities, including the underserved and those of modest means. As mentioned, as part of the agency's *2018–2022 Strategic Plan*, the NCUA established three goals: (1) ensuring a safe and sound credit union system; (2) providing a regulatory framework that is transparent, efficient and improves consumer access; and (3) maximizing organizational performance to enable mission success.[15] Below I will detail the steps the agency is taking to fulfill these missions and achieve these goals.

In meeting the established goals, it is essential that the NCUA Board develops a regulatory environment that meets our safety and soundness mission, but does not unnecessarily inhibit flexibility and innovation within the credit union system and allows credit unions to continue to serve all of their members. As the financial services landscape evolves, the NCUA must evolve with it to promote continued financial stability within the credit union system. In so doing, it is imperative that the agency continues to fulfill its mission in a fully transparent, accountable, and efficient manner. I believe that the NCUA Board is obligated to consider the compliance burdens and the costs our institutions shoulder on a day-to-day basis. As a result, we must reduce, streamline, or eliminate outdated or overly burdensome regulations where possible, so credit unions can simultaneously stay competitive in the changing environment and continue to provide financial services to their members and communities.

Since 2017, the NCUA has been undergoing a reform and modernization effort. This effort has seen the NCUA reduce the agency's regional structure from five to three regional offices and reorganize several central office functions to reduce costs and increase efficiencies. As part of the agency's broader reform plan, we also undertook a number of actions and initiatives designed to: (1) increase the agency's effectiveness in maintaining the safety and soundness of the credit union system and the Share Insurance Fund; (2) increase the efficiency in our examination, data collection, and reporting efforts; (3) decrease regulatory burdens; (4) increase diversity within the NCUA and the broader credit union industry; and (5) empower credit unions to better serve those of modest means and the underserved.

a. Initiatives Aimed at Increasing Agency Effectiveness in Maintaining Safety and Soundness of the Credit Union System and the Share Insurance Fund

[15] See *NCUA Strategic Plan 2018–2022*, available at https://www.ncua.gov/files/agenda-items/AG20180125Item3b.pdf.

The NCUA has undertaken a variety of initiatives to improve the agency's effectiveness in fulfilling our core mission: protecting the safety and soundness of the credit union system and the Share Insurance Fund. More specifically, in ensuring the success of this mission, the NCUA has: (1) continued to modernize and improve how it conducts examinations of federally insured credit unions; (2) worked to become more proactive in ensuring accountability through enforcement actions against credit union employees and officials engaging in unsafe and unsound practices or fraud; (3) committed to keeping pace with financial technology developments and the opportunities and risks they pose to credit unions; (4) continued efforts to ensure compliance with consumer protection laws and regulations, the Bank Secrecy Act (BSA), and other applicable laws and regulations; and (5) enhanced transparency surrounding voluntary mergers for the benefit of members. These initiatives complement the NCUA Board's efforts to reduce regulatory, examination, and reporting burdens for federally insured credit unions discussed later.

i. Modernized Examination Considerations

The NCUA has several ongoing initiatives to improve and modernize how the agency conducts its examination and supervision of credit unions. The goals of these initiatives are to streamline processes, adopt enhanced examination techniques, and leverage new technology and data.

<u>Improved Risk Identification Techniques</u>

The NCUA is developing new and advanced risk identification and monitoring capabilities and techniques. These new data and analytical techniques will facilitate more data-driven supervision and enable the agency to better identify and address risk outliers. Additionally, the NCUA incorporated advances in identifying credit unions with an elevated risk of fraud. This further supports the objective to spend less time onsite at low-risk credit unions and leverage technology to maximize efficiency.

<u>Increased Use of Specialists</u>

With the increasing complexity of the financial services landscape, the NCUA has expanded its use of specialists within its examination ranks. We added additional disciplines and subject matter experts to our examination teams to address a broader range of financial products, services, and risks effectively.

<u>Expanded Examiner Training and Guidance</u>

The NCUA recognizes the importance of identifying undue risk exposures timely and relies on both specialized staff and techniques to do so. The agency updated its subject matter examiner training to ensure specialists maintain current knowledge sets and are consistent in the analysis of risk and determination of safety and soundness concerns.

The NCUA has also conducted a comprehensive update to its core examiner training. Additionally, the NCUA's *Examiner's Guide* is undergoing an extensive update to expand and clarify risk management expectations for the growing range of financial services credit unions engage in.

Enhanced Examination Quality Control

The NCUA is improving its quality control program to strengthen the examination and supervision process. These improvements will increase our consistency when assessing risk. It will also enable the agency to better identify and address safety and soundness issues.

ii. More Proactive Enforcement

Over the last several years, the NCUA has made a concerted effort to take a more proactive approach to policing the actions of credit union employees and officials through Administrative Orders. As background, Administrative Orders are formal enforcement orders issued by the NCUA pursuant to Section 206 of the Federal Credit Union Act (FCU Act).[16] Generally, the NCUA issues Administrative Orders when it finds that a person affiliated with a credit union has engaged in an unsafe or unsound practice, committed a breach of fiduciary duty, or violated a law, rule, or regulation. The most common orders issued by the NCUA include:

- An **Order to Cease and Desist**, which requires a party to take action (or refrain from taking action), including making restitution; and
- An **Order of Prohibition**, which prohibits a party from ever working for a federally insured financial institution.

The NCUA has increased enforcement staff within the Office of General Counsel and has made efforts to proactively impose administrative sanctions, including Orders of Prohibition, against individuals whose conduct constitutes an unsafe or unsound practice, breach of fiduciary duty, or violation of law, rule, or regulation, but has not yet resulted in criminal charges or a conviction. For a variety of reasons, federal, state, and local law enforcement may opt not to pursue charges against an individual despite their improper conduct. This more proactive approach has allowed the NCUA to remove bad actors from the industry and ensure they do not pose further risk to another federally insured financial institution. In several instances, the NCUA's enhanced investigative and enforcement actions have led law enforcement authorities to file charges and obtain convictions.

[16] 12 U.S.C. § 1786.

The NCUA takes seriously its paramount responsibility to protect the safety and soundness of the credit union industry and the Share Insurance Fund. The agency is committed to supervising the industry to prevent illicit or unsafe or unsound conduct.

iii. NCUA Action Related to Financial Technology and the Credit Union Industry

Financial technology, or fintech, generally refers to the use of technology to provide financial services in an innovative way. Such services can involve directly serving consumers as well as back office support functions. Some examples of technologies that are upending the delivery of traditional financial services include:

- Peer-to-peer payment systems;
- Artificial intelligence and machine learning that can be used to develop lending models or identify fraud; and
- Blockchain and distributed ledger technologies that can be used for various credit union operations, including payment systems and identity management.

Fintech companies are rapidly changing, and in some cases disrupting, the design and delivery of financial services. Many consumers, businesses, and financial institutions are eager to engage in financial transactions with added convenience and efficiency. Fintech can be developed and offered by financial institutions, third-party vendors, or new entrants into the financial services market. Some fintech companies compete directly with traditional financial institutions, including credit unions, by providing products and services that were once predominantly only available through depository institutions. While financial innovation holds promise, it is crucial that credit unions, consumers, and other stakeholders understand and mitigate associated risks. The NCUA's goal is to balance maintaining the safety and soundness of credit unions without stifling their use of innovative technology and related vendors. Credit unions need to embrace fintech as their banking counterparts do, while simultaneously clearly understanding and managing any risks they incur. To that end, the NCUA has undertaken several initiatives to address the changing financial services landscape, including:

- In 2018, the NCUA convened two working groups to study these issues: the Fintech Working Group and the Blockchain Working Group.
    - The NCUA's Fintech Working Group is working to identify ways federally insured credit unions can adopt and embrace fintech so they can effectively compete in the changing financial services industry.
    - The NCUA's Blockchain Working Group was established to understand the impact of cryptocurrencies and their underlying distributed ledger technology on the credit union system. The Blockchain Working Group

briefed the NCUA Board at the December 2018 open Board meeting and is currently conducting industry outreach efforts.

- Ongoing Monitoring
    - The NCUA is continuing to research and monitor financial technology including online lenders, machine learning, artificial intelligence, and payment systems to identify how they may impact credit unions. The NCUA is interested not only from a competitive standpoint, but also in how credit unions are partnering with market place lenders and other fintech companies.

Fintech is revolutionizing financial services and the delivery of those services, and consumers are benefiting from increased access to efficient and affordable financial services. It also is requiring traditional financial service providers to adapt and embrace methods, technological innovations, and new technology partners in order to remain competitive in the marketplace. The adoption of many modern technologies requires contractual relationships with third-party vendors. Many fintech companies, however, operate outside of the existing regulatory regime that governs financial institutions, even though most of the key infrastructure vendors (including data processing, payment systems, information technology, lending, and shared branching) have a definite information security and/or anti-money laundering (AML) dimension. Further, fintech increases potential systemic cybersecurity risks across the financial services landscape. The credit union system is particularly vulnerable to this risk because the NCUA does not have sufficient legal authority to directly identify and address systemic cybersecurity risk and the potential contagion risk that key fintech service providers can pose.

Overall, the reduced scrutiny of fintech companies has the potential to present an uneven playing field between them and traditional financial institutions. In addition, without clear-cut oversight from federal regulators, the NCUA has concerns about the risks fintechs could pose to credit union members, the Share Insurance Fund, and the stability of the broader financial system. To help address concerns about regulatory arbitrage, the NCUA is also actively coordinating its supervisory efforts with the Board of Governors of the Federal Reserve, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation.

Additionally, the NCUA is participating in the following interagency initiatives:

- <u>Interagency Fintech Discussion Forum</u>—This forum, convened by the Board of Governors of the Federal Reserve, provides an opportunity for senior-level representatives to discuss each agency's actions related to fintech and identify opportunities for collaboration, specifically related to consumer protections.
- <u>Mobile Payments Industry Working (MPIW) Group</u>—The NCUA participates in the MPIW Group, which meets regularly to consider potential resolutions for

shared issues and the elimination of barriers to adoption of retail mobile or digital payments.

- Federal Financial Institutions Examination Council (FFIEC) Task Force on Supervision (TFOS)—The TFOS coordinates and oversees matters relating to safety-and-soundness supervision and examination of depository institutions. It provides a forum for Council members to promote quality, consistency, and effectiveness in examination and other supervisory practices. While significant issues and recommendations are referred to the Council for consideration and action, the Council has delegated to the TFOS the authority to make certain decisions and recommendations, provided that no TFOS member dissents or requests review by the Council. Meetings are held monthly to address and resolve common supervisory issues. The TFOS also maintains supervisory communication protocols to be used in emergencies. These protocols, established by the TFOS, are periodically tested through exercises with TFOS members and key supervisory personnel.
- FFIEC Task Force on Consumer Compliance—The Task Force on Consumer Compliance (TFCC) promotes policy coordination, a common supervisory approach, and uniform enforcement of consumer protection laws and regulations. The TFCC identifies and analyzes emerging consumer compliance issues and develops proposed policies and procedures to foster consistency among the agencies. Additionally, the TFCC reviews legislation, regulations, and policies at the state and federal level that may have a bearing on the consumer compliance supervision responsibilities of the member agencies.

iv. Ensuring Compliance with Consumer Protection Laws and Regulations, the Bank Secrecy Act, and other Applicable Laws and Regulations

Ensuring Compliance with Consumer Protection Laws and Regulations

The NCUA performs annual targeted reviews for compliance with various consumer financial protection regulations during the agency's safety and soundness examinations of federal credit unions. Additionally, in 2018, the NCUA's Office of Consumer Financial Protection spent over 4,700 hours examining credit unions for compliance with fair lending laws and regulations. In addition, agency staff spent approximately 1,000 hours performing offsite supervision contacts to review credit unions' loan policies and, if necessary, provide recommendations to bring them into compliance with fair lending laws. The Consumer Assistance Center is another critical part of the NCUA's enforcement of consumer financial protection laws and regulations. It receives and handles consumer complaints and does its own investigation to determine compliance with applicable federal consumer financial protection laws and regulations. During the year, the Consumer Assistance Center assisted 53,337 consumers, up from

52,635 in 2017, and recorded more than $822,000 in monetary benefits for complainants.[17]

Additionally, the NCUA participates on the FFIEC's Task Force on Consumer Compliance, which promotes policy coordination, a common supervisory approach, and uniform enforcement of consumer protection laws and regulations.

Ensuring Compliance with the Bank Secrecy Act

The NCUA takes seriously its obligations to supervise federal credit unions for compliance with the various BSA and AML laws and regulations. As technology has become embedded in financial systems, even small financial institutions like credit unions can be vulnerable to illicit finance activity. The NCUA examines federal credit union compliance with BSA during every examination that we conduct. Additionally, the NCUA assists state regulators by conducting BSA examinations in federally insured, state-chartered credit unions where state resources are limited. In 2018, the NCUA conducted 3,308 BSA examinations in federal credit unions.

The NCUA's BSA reviews are risk-focused and include a set of core procedures that cover an institution's compliance with the pillars of the BSA. These core procedures are based on the FFIEC examination procedures we issue jointly with the other federal financial regulatory agencies. In addition to the core procedures, examiners are trained and directed to tailor examinations based on the unique risk characteristics of each federal credit union. Federal credit unions that have diverse platforms with higher risk activities will receive an expanded review tailored to the unique risk characteristics they present. Conversely, examinations of smaller, low-risk credit unions are appropriately scaled to minimal necessary procedures consistent with their risk characteristics and our obligations under the FCU Act.

The NCUA coordinates regularly with our counterparts as the other federal financial regulatory agencies, as well as the Financial Crimes Enforcement Network (FinCEN). The NCUA actively participates in the Bank Secrecy Act Advisory Group (BSAAG) and the FFIEC BSA Working Group. Additionally, the NCUA is part of a recently established interagency working group to improve effectiveness and streamline, where possible, our regulations and supervisory processes. The working group recently issued a Joint Statement on Innovative Efforts to Combat Money Laundering and Terrorist

[17] This figure includes restitution by the credit union, relief from an alleged monetary obligation imposed by the credit union, and access to disputed credit or financial services products otherwise not available to the member by the credit union.

Financing,[18] as well as an Interagency Statement on Shared BSA Resources.[19] Both joint statements provide appropriate information for institutions to leverage resources and new technologies to improve and streamline their BSA compliance obligations. The NCUA intends to continue to foster collaborative working relationships with our regulatory counterparts, including FinCEN. I believe that this is especially important in addressing substantial concerns related to the proliferation of cash-based businesses, which further necessitates reforming and modernizing the BSA regime.

Finally, the NCUA also communicates with the credit union industry through numerous channels, including: BSAAG participation and outreach; assistance and participation in national events applicable to the BSA attended by credit union industry professionals and leaders; and through periodic and ongoing training via webinars. The NCUA continues to maintain transparency in its policy positions. To that end, the agency publishes our examination and policy manuals, as well as nearly all guidance and directives provided to examiners related to the supervisory process or examinations.[20]

v. Enhancing Transparency Surrounding Voluntary Mergers

The NCUA Board recently adopted changes to the agency's voluntary mergers regulation designed to increase transparency and member engagement.[21] As background, the FCU Act requires the NCUA Board's "prior written approval" for any merger or consolidation between insured credit unions.[22] In granting or withholding this approval, the FCU Act requires the Board to consider six factors, which are:

1. The history, financial condition, and management policies of the credit union;
2. The adequacy of the credit union's reserves;
3. The economic advisability of the transaction;
4. The general character and fitness of the credit union's management;
5. The convenience and needs of the members to be served by the credit union; and
6. Whether the credit union is a cooperative association organized for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes.[23]

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[18] The statement can be found at https://www.ncua.gov/files/press-releases-news/joint-statement-bsa-innovation.pdf.
[19] The statement can be found at https://www.ncua.gov/newsroom/press-release/2018/agencies-issue-joint-statement-encourage-innovative-approaches-bsaaml-compliance.
[20] Some examiner guidance is kept confidential, such as fraud detection techniques, in order to maintain their integrity and effectiveness.
[21] 83 Fed. Reg. 30301 (June 28, 2018).
[22] 12 U.S.C. § 1785(b)(3).
[23] *Id.* § 1785(c).

These factors are broader than safety and soundness and require the NCUA to consider the effect of the proposed merger on credit union members. The NCUA's merger regulation ensures that consideration of member interests by requiring a member vote on the proposed merger in addition to the NCUA's oversight.

Under the revised merger rule, members of a credit union whose board has voted to merge must receive notice at least 45 days before the vote, and have an opportunity to submit comments about the proposed merger for posting on a section of the NCUA's website where other members can view the comments. The revised regulation also more clearly articulates the required content and format of the member notice to ensure that credit union members have all relevant information about the proposed merger, including merger-related financial incentives for staff or officials. The revised rule applies to all insured credit unions, whether state or federally chartered. The NCUA's Regional Offices review merger application packages and member notices to ensure compliance with the regulation before the members vote.

The FCU Act also requires the NCUA Board's prior approval for most transactions between insured credit unions and other institutions,[24] and directs the NCUA to oversee the methods and procedures of the member vote when an insured credit union proposes to convert to a mutual savings bank.[25] The NCUA has adopted regulations addressing credit union conversions to banks, mergers into banks, and mergers with privately insured credit unions, all of which provide for member votes.[26] The NCUA is also aware that the number of transactions where an insured credit union has acquired a bank or portions of a bank have been increasing. Currently, the NCUA addresses these types of transactions on a case-by-case basis. The NCUA's oversight of these transactions focuses on ensuring that insured credit unions retain only permissible assets and that former bank customers receive all the rights and privileges of credit union membership when such transactions close.

b. Initiatives Aimed at Increasing Agency Efficiency and Reducing Examination and Reporting Burdens

The NCUA continues to improve the regulatory environment for credit unions without sacrificing our safety and soundness mission. Pursuant to its reform and modernization efforts, the agency has reduced its regional structure from five to three regional offices and reorganized several central office functions to reduce costs and increase efficiencies.

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[24] 12 U.S.C. § 1785(b)(1).
[25] *Id.* § 1785(b)(2)(G)(ii).
[26] 12 CFR §§ 708a, 708b.

As part of the agency's reform efforts, the NCUA has also undertaken a number of initiatives to increase the efficiency in our examination, data collection, and reporting efforts. Specifically, I call your attention to the following three programs:

Exam Flexibility Initiative[27]

This initiative provides greater examination efficiency and flexibility for credit unions and the agency, and improves coordination with state supervisors. Because of this initiative, the NCUA adjusted the frequency of examinations based on a credit union's size, complexity, operating condition, and, in the case of state-chartered credit unions, the frequency of state examinations. This initiative resulted in meaningful regulatory relief for the vast majority of credit unions, led to greater coordination between federal and state regulators, and allowed the NCUA to focus more efforts on troubled credit unions, with the anticipated benefit of addressing some problems earlier when they are easier and less costly to resolve.

The Enterprise Solution Modernization Program[28]

This multi-year program modernizes the NCUA's technology infrastructure to create an integrated examination and data environment, and further enhances the agency's cybersecurity posture. It incorporates emerging technology solutions that support the NCUA's examination, data collection, and reporting efforts to improve key, integrated business processes and meet applicable security protocols. The program will improve the examination process and ease burdens on credit unions and staff by reducing the amount of examination and supervision time spent onsite in credit unions. The NCUA expects an improved user experience and increased efficiencies when the new systems are in place.

The Call Report Modernization Project[29]

This project complements the Enterprise Solution Modernization Program and involves a comprehensive review of Call Report and Credit Union Profile data content.[30] The NCUA developed a prototype Call Report and Profile that eliminated outdated fields and simplified the reporting process without sacrificing important information

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[27] See NCUA Exam Flexibility Initiative, https://www.ncua.gov/About/Pages/open-government/exam-flexibility-initiative.aspx.

[28] See NCUA Enterprise Solution Modernization (ESM) Program, https://www.ncua.gov/About/Pages/open-government/enterprise-solution-modernization-program.aspx.

[29] See NCUA Call Report Modernization, https://www.ncua.gov/About/Pages/open-government/call-report-modernization.aspx.

[30] The NCUA uses the Call Report and Profile to collect financial and nonfinancial information from federally insured credit unions. The resulting data are integral to risk supervision at institution and industry levels, which is central to safeguarding the integrity of the Share Insurance Fund.

necessary for proper supervision and data analyses. In order to ensure a transparent and collaborative process, the agency solicited public comment on the prototype. The NCUA estimates the proposed changes will reduce the number of account codes collected from credit unions. If the proposal is adopted, the agency will revise and improve its Call Report schedules and instructions to make it easier for credit unions to complete this critical regulatory filing.

c. Initiatives Aimed at Decreasing Regulatory Burdens

My longstanding regulatory philosophy is that regulation needs to be effective, but not excessive. Consistent with the spirit of President Trump's regulatory reform agenda and Executive Order 13777, the NCUA established a Regulatory Reform Task Force to oversee the implementation of the agency's own regulatory reform agenda. Although the NCUA, as an independent regulatory agency, is not required to comply with Executive Order 13777, the agency chose to comply with its spirit by undertaking a comprehensive review of all of the NCUA's regulations. Beginning in 2017, the Regulatory Reform Task Force began reviewing the agency's rules with an eye towards creating a transparent and fully accountable regulatory framework that acknowledges the need for flexibility, creates new avenues for growth, and strengthens the system's resiliency, while simultaneously reducing the regulatory burden where prudent and appropriate.

The Regulatory Reform Task Force published the NCUA's first report for public comment in August 2017.[31] This reform agenda proposed a four-year, three-tiered regulatory relief plan with approximately 40 regulatory relief recommendations. After reviewing and considering the comments received, the Task Force issued its second and final report in December 2018.[32] This second report provided an updated blueprint for the agency's regulatory reform agenda and a formal means of measuring the agency's regulatory relief efforts moving forward.[33]

To date, the NCUA has completed twelve of the reports' regulatory relief recommendations and proposed rules or commenced action on seven others. Specifically, the NCUA issued final regulations or took other final actions designed to:

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[31] 82 FR 39702 (Aug. 22, 2017), available at https://www.ncua.gov/About/Pages/board-actions/comments/Documents/regulatory-review-notice-2017.pdf.
[32] 83 FR 65926 (Dec. 21, 2018), available at https://www.govinfo.gov/content/pkg/FR-2018-12-21/pdf/2018-27473.pdf. A consolidated version of the final report is available at https://www.ncua.gov/files/agenda-items/AG20181213Item1b.pdf.
[33] See Implementation of the NCUA's Regulatory Reform Agenda, available at https://www.ncua.gov/regulation-supervision/rules-regulations/regulatory-reform-agenda/implementation-ncuas-regulatory-reform-agenda.

- Provide additional flexibility to corporate credit unions' capital standards;[34]
- Improve the NCUA's emergency merger process;[35]
- Recognize that federal credit unions may securitize the loans they make;[36]
- Improve the NCUA's appeals process for examination determinations to ensure due process and fairness;[37]
- Improve and centralize the NCUA's appeals procedures in one section of the NCUA's regulations;[38]
- Provide greater transparency regarding the calculation of each eligible financial institution's pro rata share of a declared equity distribution from the Share Insurance Fund;[39]
- Decrease the burden and improve the efficiency of the NCUA's capital planning and stress testing rules;[40]
- Decrease burden and add flexibility to the NCUA's advertising requirements;[41]
- Add flexibility to the NCUA's field-of-membership processes;[42]
- Make clarifying and technical changes to improve the user-friendliness of the NCUA's loan maturities requirements;[43]
- Clarify the NCUA's limits on loans to a single borrower or group of associated borrowers;[44] and
- Delay the effective date of the NCUA's risk-based capital rule and decrease the number of credit unions covered by the rule.[45]

Additionally, the NCUA proposed or sought advanced comment on amendments that would provide regulatory relief by:

- Permitting federal credit unions the ability to provide an additional market-based alternative to payday loans;[46]
- Improving the NCUA's regulations governing federal credit union bylaws;[47]

[34] 82 FR 55497 (Nov. 22, 2017).
[35] 82 FR 60283 (Dec. 20, 2017).
[36] Asset Securitization Authority, NCUA OGC Op. Ltr. 17-0670 (June 21, 2017), available at https://www.ncua.gov/regulation-supervision/Pages/rules/legal-opinions/2017/asset-securitization-authority.pdf; and 82 FR 29699 (June 30, 2017).
[37] 82 FR 50270 (Oct. 30, 2017).
[38] 82 FR 50288 (Oct. 30, 2017).
[39] 83 FR 7954 (Feb. 23, 2018).
[40] 83 FR 17901 (Apr. 25, 2018).
[41] 83 FR 17910 (Apr. 25, 2018).
[42] 83 FR 30289 (June 28, 2018).
[43] 84 FR 10971 (Mar. 25, 2019).
[44] *Id.*
[45] 83 FR 55467 (Nov. 6, 2018).
[46] 83 FR 25583 (June 4, 2018).
[47] 83 FR 56640 (Nov. 13, 2018).

- Improving the NCUA's appraisals regulation to reduce burden and make compliance easier.[48]
- Improving the NCUA's regulations governing fidelity bond for credit unions;[49]
- Simplifying and clarifying the audit process required by the NCUA's regulations by replacing the current highly prescriptive standard to comply with the Supervisory Committee Guide with minimum procedures to be included in an audit;[50]
- Providing flexibility on the NCUA's regulations regarding the timing of a compensated auditor delivering the written annual audit report to the credit union;[51] and
- Seeking advanced comment on how to enhance the clarity of, and potentially provide greater flexibility to, the NCUA's requirements governing compensation for credit union employees and officials in connection with loans to members.[52] These requirements are separate from the interagency action undertaken by the NCUA and various other regulators related to the incentive compensation requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act).[53] The agencies continue to work on these incentive compensation requirements in order to resolve outstanding issues and move forward with further action.

With the Regulatory Reform Task Force's review of the NCUA's regulations complete and its recommendations in the process of being implemented, the NCUA has reinstituted its annual regulatory review to provide stakeholders with an ongoing means of providing feedback on the NCUA's regulations. As part of this process, the agency reviews and solicits public comment on one-third of the agency's regulations each year. Agency staff then provides the NCUA Board with regulatory recommendations, based in part on the comments received. The NCUA opened the comment period for the first one-third of its regulations in January 2019.[54]

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[48] 83 FR 49857 (Oct. 3, 2018).
[49] 83 FR 59318 (Nov. 23, 2018).
[50] 84 FR 5957 (Feb. 25, 2019).
[51] *Id.*
[52] 84 FR 16796 (Apr. 23, 2019).
[53] In 2011, the NCUA joined with six other federal financial regulators to issue a proposed rule implementing Section 956 of the Dodd-Frank Act. The agencies issued a revised proposed rule in 2016. The 2016 proposed rule would require federally insured credit unions with assets of $1 billion or more to provide the NCUA with information about the structure of future incentive-based executive compensation programs. The joint agency rulemaking would prohibit incentive-based compensation payment arrangements in financial institutions with $1 billion or more in assets that the agencies determine would encourage inappropriate risks by providing excessive compensation or that could lead to material financial loss.
[54] See Regulatory Review, https://www.ncua.gov/regulation-supervision/rules-regulations/regulatory-review.

Separately, I would also like to emphasize that, as the NCUA's new Chairman, it is a priority of mine to ensure that the NCUA's regulations governing risk and capital are appropriately harmonized. Risk and capital are the underpinnings of a safe and sound credit union system and need to work in concert. Capital requirements must be properly tailored to ensure that credit unions are holding levels of capital that are appropriate for and commensurate with their individual risk profiles. I will do my level best to ensure that the NCUA's requirements properly balance risk and capital to ensure a credit union system that is both safe and sound and allows for maximum efficiency.

d. Diversity and Inclusion at the NCUA and in the Credit Union Industry

The NCUA has worked hard to encourage diversity and inclusion both within the agency and the broader credit union industry. Below is a summary of the NCUA's diversity and inclusion activities and efforts related to implementation of Section 342 of the Dodd-Frank Act and compliance with Section 308 of Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), as amended by the Dodd-Frank Act, as it relates to minority depository institutions (MDIs).

i. The NCUA's Implementation of Section 342 of the Dodd-Frank Act

<u>Assessing the Diversity Policies and Practices of Entities Regulated by the Agency</u>

Pursuant to Section 342(b)(2)(C) of the Dodd-Frank Act, credit unions and other financial institutions, especially those with more than 100 employees, are encouraged to conduct annual self-assessments of diversity and inclusion practices and policies related to workforce and contracting activities. To facilitate the self-assessment process, the federal financial regulatory agencies collectively established the diversity standards set forth in the 2015 Interagency Policy Statement Establishing Joint Standards for Assessing the Diversity Policies and Practices.[55] The joint standards are grouped into these five areas, or sets of standards:

1. Organizational commitment to diversity and inclusion;
2. Workforce profile and employment practices;
3. Procurement and business practices (supplier diversity);
4. Practices to promote transparency; and
5. Entities' self-assessment.

The standards provide a framework for a financial institution to create or strengthen its diversity policies and practices. Using these joint standards, the NCUA created the

[55] 80 FR 33016 (June 10, 2015).

Annual Voluntary Credit Union Diversity Self-Assessment tool, tailored for credit unions, that provides guidance for advancing diversity and inclusion.[56] It also highlights best practices for demonstrating a commitment to diversity and inclusion. Credit unions began conducting and submitting self-assessments voluntarily to the NCUA's Office of Minority and Women Inclusion (OMWI) in 2016. The NCUA uses the aggregated self-assessment data to monitor progress and trends in credit union diversity-related activities. OMWI only shares the results anonymously, primarily in the NCUA's annual *OMWI Report to Congress* and in an annual report of the self-assessment results. The first of these reports is the *2017 Credit Union Diversity Self-Assessment Results Report* issued in 2018.

The self-assessment data also informs the NCUA of areas where additional guidance could be useful. When appropriate, the NCUA issues such guidance to assist credit unions with their diversity efforts. In 2018, the NCUA issued a *Credit Union Guide to Supplier Diversity* after identifying that many credit unions reported low levels of engagement in this area. The NCUA's OMWI also participates in credit union industry and league conferences promoting the benefits of conducting the self-assessment and the value of diversity and inclusion for credit unions.

Inclusion in all Levels of Business Activities

Section 342(c) of the Dodd-Frank Act directs each OMWI Director to "develop and implement standards and procedures to ensure, to the maximum extent possible, the fair inclusion and utilization of minorities, women, and minority-owned and women-owned businesses in all business and activities of the agency at all levels, including in procurement, insurance, and all types of contracts." When the NCUA first began tracking the participation of minority- and women-owned businesses in the agency's contracting opportunities in 2011, minority- and women-owned businesses represented 6 percent of the agency's vendors. Since implementing procurement guidance that promoted the inclusion of one-third minority- and women-owned businesses of all invited vendors, the agency has made consistent progress year after year. The agency achieved 45 percent minority- and women-owned business participation in its 2018 contracts.

Diversity in the Agency's Workforce

Section 342(f) of the Dodd-Frank Act directs each agency to "take affirmative steps to seek diversity in the workforce of the agency at all levels of the agency in a manner consistent with applicable law."

[56] Annual Voluntary Credit Union Diversity Self-Assessment, available at https://cudiversity.ncua.gov/.

The NCUA has made progress toward greater diversity in its workforce. Over the last four years, the minority representation has improved each year, increasing from 26.32 percent to 29.74 percent over that period. The percentage of women and minorities at the executive level also has improved each year. Female representation in the executive ranks grew from 41.2 percent to 45.3 percent, while minority representation increased from 11.8 percent to 18.9 percent.

The NCUA has also implemented the following as part of our organizational diversity and inclusion efforts:

- Included diversity and inclusion as a strategic objective in agency strategic plan;
- Developed a five-year diversity and inclusion plan;
- Established a diversity advisory council;
- Provided annual diversity and inclusion training;
- Established a mentoring program;
- Maintained a student intern program;
- Participated in targeted diverse recruitment;
- Established a policy to use diverse interview panels when possible;
- Used structured interviews in examiner and senior staff interviews;
- Conducted annual adverse impact analysis on principal examiner testing;
- Provided unconscious bias training for all staff and additional training for managers;
- Included a diversity and inclusion element in all supervisor performance plans;
- Provided special emphasis programs for the following groups;
    - African American
    - Women
    - Asian
    - LGBTQ
    - Hispanic
    - Disability
    - Veterans
    - Native American
- Held monthly diversity discussions;
- Issued monthly diversity newsletters;
- Resurveyed the workforce to update disability status;
- Established employee resource groups; and
- Released annual policy statements from the NCUA Chairman reinforcing commitment to equal opportunity employment and diversity and inclusion in the agency's workforce, workplaces, and business practices.

ii. The NCUA's Compliance with Section 308 of FIRREA as it Relates to MDIs

Minority depository institutions, or MDIs, play a crucial role in providing affordable financial services in areas that have been largely unserved or underserved by the traditional banking system. MDIs often are the only federally insured financial institutions in these areas.

<u>MDIs-at-a-Glance</u>[57]

- 529 federally insured credit unions are designated as MDIs.
- MDIs are located throughout 37 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. Texas, California, New York, Hawaii, Illinois, and Louisiana have the highest number of MDIs.
- Collectively, MDIs serve 3.9 million members and manage $38.5 billion in assets. Texas, by far, has the highest number of members with more than 1.5 million followed by Hawaii, California, Maryland, and New Mexico. Hawaii, California, Maryland, New Mexico, the District of Columbia, and North Carolina, each have more-than $1 billion in aggregate MDI assets.

<u>The NCUA's MDI Preservation Program</u>

A federally insured credit union may self-designate as an MDI through the NCUA's Credit Union Online Profile. The credit union must affirm that more than 50 percent of its current members, eligible potential members, and board of directors are from one of the four minority categories specified under the law. The NCUA relies on the definition of "minority" in Section 308 of FIRREA, which identifies an eligible minority exclusively as any Asian American, Black American, Hispanic American, or Native American.

The NCUA's most recent actions to preserve and promote MDIs include:

1. *Preserving the present number of MDIs*

The NCUA's MDI Preservation Program is designed to provide needed support to credit unions that serve communities and individuals who may lack access to mainstream financial products and services. The NCUA's examination staff work directly with credit unions on this program and the NCUA's Office of Credit Union

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[57] Based on the Call Reports and Credit Union Online Profiles as of Dec. 31, 2018.

Resources and Expansion (CURE) provides several support services.[58]

- **Field of Membership Expansion:** During 2018, the NCUA approved the chartering and field of membership expansions for 28 MDIs These approvals allowed the credit unions to add, in aggregate, more than 650 groups or expanded geographic areas to their memberships.[59]
- **Increasing the Number of MDIs:** During 2018, the NCUA launched a social media campaign to identify new MDIs. The campaign coincided with Minority Enterprise Development Week.[60]
- **Direct Feedback from MDIs:** The NCUA surveyed MDIs about the challenges of serving their members. Chief executive officers, managers, board members, and staff of MDIs responded to the survey, which was designed to ensure the agency's services are responsive to the needs of the credit unions consistent with Section 308 of FIRREA.[61]

2. ***Preserving their minority character in cases of merger or acquisition of a MDI***

During 2018, 21 MDIs merged into other credit unions. Five of the continuing credit unions, 24 percent, were MDIs. MDI mergers represented 12 percent of all mergers of federally insured credit unions during 2018.[62] In most cases, the NCUA's examination staff work directly with a credit union providing guidance to the board and management throughout a merger.

3. ***Providing technical assistance to undercapitalized credit unions***

When a credit union becomes undercapitalized, it is required to develop a net worth restoration plan, subject to the NCUA's approval. The NCUA assists MDIs that are undercapitalized and subject to prompt correction action in developing these net worth

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[58] CURE assumed responsibility for administering the NCUA's MDI Preservation Program in January 2018, as part of an agency-wide restructure. Prior to that, the program was administered by the NCUA's OMWI. CURE fosters credit union development by offering support services to all credit unions. The resources particularly appeal to small and low-income designated credit unions and MDIs, and include: chartering and field of membership activities; grant and loan programs; the MDI Preservation Program; and training services.
[59] A credit union's field of membership represents the legal definition of who is eligible to join. A federally chartered credit union must receive approval from the NCUA prior to changing its field of membership. Excerpt from "Field-of-Membership Expansion," Support Services section of the NCUA website, April 1, 2019.
[60] Minority Enterprise Development Week is a commemoration sponsored, in part, by the Minority Business Development Agency of the U.S. Department of Commerce.
[61] The results of this survey were qualitative in nature and are not generalizable to the population of the study.
[62] There were 34 fewer MDI credit unions at December 31, 2018 than at the end of the prior year. Mergers accounted for 62 percent of the decrease in the number of MDIs.

restoration plans. Both CURE and examination staff work with credit unions in this area with the goal of restoring the credit union to an acceptable level of capital.

4. ***Promoting and encouraging the creation of new MDIs***

CURE now administers the chartering of new credit unions. This was a key component of the recent agency-wide realignment. The realignment now makes it easier to coordinate the agency's work to encourage new credit unions, including MDIs. As detailed later in my testimony, one of my top priorities as the NCUA's new Chairman is enhancing and modernizing the federal credit union chartering process. It is my belief that enhancing and modernizing the federal credit union chartering process will encourage the creation of MDIs and promote greater financial inclusion.

5. ***Providing funding, technical assistance, training and educational programs***

- **Funding:** Through its Community Development Revolving Loan Fund, the NCUA awarded 31 grants totaling $284,200 to MDIs during 2018. This fund is unique among federal depository regulators and provides loans and grants to low-income credit unions as designated by the NCUA. These grants will assist the credit unions in their ability to provide financial products and services to approximately 133,850 members in aggregate, the majority of whom are minorities. Nine of the credit unions, almost 30 percent, were first-time recipients of the grant; 87 percent were small credit unions with assets below $100 million.

- **Technical Assistance:** The NCUA qualified six MDIs through the NCUA-CDFI Certification Initiative during 2018. The Initiative began in 2016 between the NCUA and the U.S. Department of the Treasury's Community Development Financial Institutions (CDFI) Fund.[63] The initiative streamlines the qualification and application processes for low-income credit unions that qualify to be certified as a CDFI. The NCUA leverages existing data and processes the agency has as the primary regulator of federally insured credit unions. Once the NCUA determines a credit union qualifies for the streamlined application, it provides the credit union with information necessary to complete and submit a certification application to the CDFI Fund. The application requires less data and independent analysis than the traditional process. The CDFI Fund has the sole authority to determine an applicant's certification status.[64]

[63] Joint Initiative Press Release: https://www.ncua.gov/newsroom/Pages/news-2016-jan-community-development-financial-institutions.aspx.
[64] CDFI certification is the U.S. Department of the Treasury's recognition of specialized financial institutions serving low-income and economically disadvantaged communities. CDFI Certification

Having the CDFI certification affords such organizations access to a variety of funding programs through the CDFI Fund. Such funding can enable a credit union to finance a range of activities, such as mortgage lending for first-time homebuyers and commercial loans.

- **Training and Educational Programs:** Training for credit union management, board members and staff can significantly influence the success of an MDI. This year, the NCUA will offer training targeted to MDIs on financial analysis/statement analysis and board of director responsibilities. During 2018, the agency updated its Learning Management Service, which provides online access to a variety of training topics such as credit union governance, operations, and products and services. The service offers on-demand learning opportunities and is available free of charge to all credit unions.

  In March, the NCUA launched an educational series of semi-annual conference calls featuring topics of interest to MDIs. The first call entitled, "An Introduction to CURE," provided an overview of the office and the services it offers to MDIs. The next call will occur during the third quarter of 2019.

e. Initiatives Aimed at Empowering Credit Unions to Better Serve the Underserved

America's credit unions are on the frontline of providing affordable access and opportunity to the financial system. Credit unions play a critical role in helping families achieve the American dream of homeownership, assisting entrepreneurs in creating small businesses, and providing the trusted affordable and essential financial services so families can save for the future.

Promoting financial inclusion and shared prosperity in underserved communities is a priority of mine. I still fondly remember the joy and excitement I saw when a young woman who attended one of my bank's homebuyer education classes learned that homeownership was not just a dream for her and her family. She was able to attend a series of homebuyer classes, build a credit profile and obtain down-payment assistance to purchase her first home. She showed her appreciation by inviting me to tour her new home and share a meal with her family.

As described below, the NCUA has developed initiatives to help create opportunities to promote financial education and financial inclusion, and foster an environment where the low-to-moderate income, people with disabilities, and the otherwise underserved have access to affordable financial services.

Eligibility Requirements: https://www.cdfifund.gov/programs-training/certification/cdfi/Pages/default.aspx.

Payday Alternative Loans

There continues to be persistent demand for short-term, small dollar loans. To provide credit union members with a safe and less expensive alternative to high-cost, traditional payday loans, the NCUA's regulations permit federal credit unions to offer small-dollar loans called payday alternative loans (PALs).[65] As of the end of 2018, 502 federal credit unions reported that they made PALs loans during the year. These credit unions reported making 211,574 loans amounting to $145.2 million in PALs during the year. In comparison, in 2012, 476 federal credit unions reported that they made 115,809 loans amounting to $72.6 million of lending during the year.[66]

Credit unions can present consumers with a viable alternative to predatory lenders. In June 2018, the NCUA Board proposed amendments to the NCUA's PALs regulation to provide federal credit unions with an additional payday alternative loan option.[67] The new proposed payday alternative loan option (PALs II) would not replace the current payday alternative loan program (PALs I), but would serve as an additional market-based alternative. The proposed PALs II option has features to enable federal credit unions to meet the needs of certain borrowers not met by the current program and encourage additional federal credit unions to offer PALs.

The NCUA Board also sought public comment on a possible third option (PALs III), asking, in particular, for feedback on interest rates, maximum loan amounts, loan terms, and application fees.

Expanding Access to Affordable Financial Services

Small credit unions, low-income designated credit unions, and MDIs play a critical role in providing affordable financial services to millions of Americans. Often, these credit unions are the only federally insured financial institutions in underserved and rural communities. Yet, they face the challenges of increased competition, stagnant membership, and lagging earnings.

A critical component of NCUA's efforts to support these credit unions is the low-income designation. To qualify as a low-income designated credit union, a majority of a credit union's membership must meet certain low-income thresholds based on data available from the American Community Survey taken by the U.S. Census Bureau.

[65] 12 CFR 701.21(c)(7)(iii).
[66] 83 FR 25583 (June 4, 2018).
[67] *Id.*

There are several benefits for credit unions that carry a low-income designation, including:

- An exemption from the statutory cap on member business lending, which expands access to capital for small businesses and helps credit unions diversify their portfolios;
- Eligibility for grants and low-interest loans from the Community Development Revolving Loan Fund;
- Ability to accept deposits from non-members; and
- An authorization to obtain secondary capital.

In 2018, the NCUA approved 18 community-charter conversions, the expansion of 53 existing community charters, and 16 expansions into underserved areas. The agency also approved the addition of 9,732 groups to the fields of membership of multiple common-bond credit unions.
The NCUA also issued one new federal credit union charter in 2018 to Everest Federal Credit Union in Jackson Heights, New York.

While I appreciate the agency's hard work in this area, one of my top priorities as the NCUA's new Chairman is enhancing and modernizing the federal credit union chartering process. The current processes for the de novo chartering, conversion, and expansion of federal credit unions is burdensome and time-consuming. I have directed staff to find meaningful ways to reduce the amount of time and the hurdles to chartering a new credit union. It is my belief that enhancing and modernizing the federal credit union chartering process to help individuals better understand the value of the federal credit union charter will encourage and enable the credit union system to better serve vulnerable communities, promote greater financial inclusion, and bring more people into the economic mainstream.

In this vein, next week, I will have the honor of presenting a new federal credit union charter that will serve a Native American community. This low-income credit union will provide much needed financial services to individuals and businesses in one of our nation's most underserved areas. This is just one example of credit unions doing what they can to help residents of rural areas and tribal lands, many of whom are unbanked or underbanked. Through their mission to serve the underserved, credit unions, such as the newly chartered one that I will visit next week, can help to ensure that those in rural areas and on tribal lands receive adequate financing for home loans and new housing construction in these areas. I am excited to continue working with my fellow Board Members and agency staff to explore all avenues within the NCUA's authority to increase access for unbanked and underbanked individuals to credit union products and services, including building upon the NCUA's already impressive financial literacy efforts.

Empowering Consumers with Information to Make Independent and Informed Financial Decisions

While credit unions serve the needs of their members and promote financial capability within the communities they serve, the NCUA reinforces credit union efforts, and raises consumer awareness about the importance of saving and having a strong understanding of the concepts of financial literacy and personal finance.

The NCUA participated in 41 events, meetings, and conferences in 2018 reaching educators, financial literacy professionals, credit union officials, non-profit leaders, and other stakeholders. The NCUA also participated in national financial literacy initiatives, including the Financial Literacy and Education Commission, an interagency group created by Congress to improve the nation's financial literacy and education.

In December 2018, the NCUA launched an updated version of its consumer website, MyCreditUnion.gov, featuring a mobile responsive design, enhanced search functions, and improved navigation for easy access to consumer financial protection and financial literacy topics. By the end of the year, the English and Spanish-language versions of MyCreditUnion.gov had 865,195 visits, up 14.8 percent from 753,588 visits in 2017.

As discussed in greater detail below, there are a number of areas where Congressional action can help credit unions better serve the underserved and those of modest means.

III. Potential Areas for Beneficial Congressional Action

While the NCUA Board does its best to provide federally insured credit unions with meaningful regulatory relief to enhance credit union operations and encourage better service of those of modest means and the underserved, Congressional action can provide additional flexibility in some areas. Today, I would like to highlight three areas where Congressional action can provide new avenues for credit union growth and enhanced service, without sacrificing the safety and soundness of the credit union system. These include modifying the FCU Act's provisions related to field of membership, providing the NCUA Board the authority to set maximum loan maturities by regulation that exceed the Act's general 15-year limit, and taking action to provide greater flexibility related to the statutory cap on member business lending.

a. Field of Membership

The FCU Act currently permits only federal credit unions with multiple common-bond charters to add underserved areas to their fields of membership.[68] Modification to the FCU Act to permit all types of federally chartered credit unions to add underserved

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[68] 12 U.S.C. 1759(c)(2)

areas to their fields of membership would allow such institutions to offer financial services to those with no or limited access to federally insured financial institutions.

Specifically, federally chartered credit unions would greatly benefit from Congressional action to allow all federal charter types, not just multiple common-bond charters, to add a local community, neighborhood, or rural district that is an investment area and underserved, as determined by the NCUA Board, if the credit union establishes and maintains an office or facility within an underserved area. Allowing federal credit unions with a community or single common-bond charter the opportunity to add underserved areas would open up access for many more unbanked and underbanked households to credit union membership. This change also could enable more credit unions to participate in programs offered through the congressionally established CDFI Fund, thus increasing the availability of affordable financial services in distressed areas.

Additionally, several other statutory reforms to the FCU Act's field-of-membership provisions would enhance credit union operations, promote financial inclusion, and encourage better service of those of modest means and the underserved. These include:

- Allowing federal credit unions to serve underserved areas without also requiring those areas to be local communities;
- Simplifying or removing the "facilities" test for determining if an area is underserved;[69]
- Eliminating the FCU Act's requirement that a multiple common-bond credit union be within "reasonable proximity" of the location of a group to provide services to members of that group;[70]
- Granting explicit authority for web-based communities as a basis for a credit union charter, thus better recognizing the ways in which people share common bonds today; and
- Providing greater flexibility for low-income individuals to join federal credit unions, including by revising the FCU Act to allow the NCUA to permit federal credit unions to add anyone residing in a census tract where current estimates indicate he or she qualifies as low-income.

b. Loan Maturities

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[69] The Federal Credit Union Act presently requires an area to be underserved by other depository institutions, based on data collected by the NCUA or federal banking agencies. 12 U.S.C. 1759(c)(2)(A)(ii). The NCUA has implemented this provision by requiring a facilities test to determine the relative availability of insured depository institutions within a certain area. Congress could instead allow the NCUA to use alternative methods to evaluate whether an area is underserved to show that although a financial institution may have a presence in a community, it is not qualitatively meeting the needs of an economically distressed population.
[70] See 12 USC 1759(f)(1).

The FCU Act currently places a blanket 15-year maximum maturity on federal credit union loans.[71] The Act provides several exceptions to this blanket maturity by permitting longer limits and providing the NCUA Board the authority to set alternate limits.[72] However, these exceptions are limited. Notably, a residential real estate loan on a one-to-four-family dwelling that is *not* the primary residence of the borrower has a maximum maturity of 15 years. The same is true of member business loans and student loans. This greatly disadvantages federal credit unions and their members, including those who are already underbanked and underserved. Congressional action to provide the NCUA Board the discretion to set alternate maturity limits, such as would be granted by HR 1661, would provide a great deal of flexibility to the industry and allow them to better serve their members' needs, including those who are of modest means or underserved.

c. Member Business Lending

The FCU Act limits federally insured credit unions' member business loans to the lesser of 12.25 percent of assets or 1.75 times net worth, unless the credit union qualifies for a statutory exemption.[73] For smaller credit unions with the membership demand and the desire to serve the business segments of their fields of membership, the restriction makes it very difficult or impossible to successfully build a sound member business lending program. As a result, many credit unions are unable to deliver commercial lending services cost effectively, which denies small businesses in their communities access to an affordable source of credit and working capital.

These credit unions miss an opportunity to support the small business community and to provide a service alternative to the small business borrower. Small businesses are an important contributor to the local economy as providers of employment and as users and producers of goods and services. The NCUA believes credit union members that are small business owners should have full access to financial resources in the community, including credit unions, but this is often inhibited by the statutory cap on member business loans.

The NCUA has done its best to provide federally insured credit unions with flexibility within the statutory limits. In 2016, the NCUA modernized its member business lending rule with that aim.[74] Additionally, just a few weeks ago, the NCUA entered into a memorandum of understanding with the U.S. Small Business Administration (SBA) to enhance cooperation in increasing credit unions' awareness and knowledge of

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[71] 12 U.S.C. § 1757(5).
[72] *Id.* § 1757(5)(A)(i)-(iii).
[73] *Id.* § 1757a.
[74] 81 FR 13530 (Mar. 14, 2016).

programs offered by SBA.[75] The partnership with SBA provides credit unions more opportunities to meet the credit needs of their small business members. The memorandum of understanding seeks to expand credit unions' understanding of, and participation in, SBA lending programs, including programs for certain SBA-guaranteed loans, which are statutorily exempted from the FCU Act's member business lending cap.[76] Both the NCUA and the SBA believe that credit unions are particularly well suited for expanding small business access to credit.

The NCUA is committed to doing everything it can to help credit unions leverage existing government loan programs so that they can provide additional capital to their small business members. Additionally, any Congressional action to provide additional flexibility under the member business lending cap would also be tremendously beneficial to the credit union industry and their small business members.

Should Congress choose to address any of these issues, I would welcome the opportunity to work with you. Thank you for the opportunity to provide an update on the strong state of the credit union industry and to detail the NCUA's recent and current initiatives and actions.

[75] See "NCUA/SBA Partnership Will Help Credit Unions Support Small Businesses," available at https://www.ncua.gov/newsroom/press-release/2019/ncuasba-partnership-will-help-credit-unions-support-small-businesses.
[76] 12 U.S.C. § 1757a(c)(1)(B)(iv).