



4309 North Front Street
Harrisburg, PA 17110-1618
800-932-0661 • 717-234-3156 • Fax 717-234-2695

August 1, 2016

Keith Morton, Regional Director
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

Re: Examination Flexibility

Dear Director Morton:

The Pennsylvania Credit Union Association appreciates this opportunity to offer ideas for improving the examination process. PCUA is a state-wide trade association that represents a significant majority of the credit unions located in the Commonwealth of Pennsylvania.

PCUA and its member credit unions support and appreciate NCUA's Exam Flexibility Initiative. This initiative presents an opportunity to alleviate regulatory burdens while maintaining the safety and soundness of the credit union system. We applaud the NCUA Board for making examination flexibility a priority. We look forward to reviewing the work product of the NCUA's internal working group.

During the July NCUA Board meeting the agency adopted its 2017-2021 Strategic Plan. Within the plan, NCUA retired the requirement for examinations of all federally insured credit unions with assets greater than \$250 million and all federal credit unions in each calendar year. This represents a positive step toward modernizing the exam process and alleviating the work associated with undergoing an examination. We offer the following suggestions, using NCUA's list of questions to organize the comments.

As a regulator, how can NCUA conduct future credit union examinations in ways that minimize disruptive operational impacts during your credit union examination?

Adequate notice would minimize disruption. In addition, our members have provided anecdotal evidence suggesting that examination teams arrive and spend some time at a credit union. Then, the examination team may go offsite or to other credit unions and return. So, sticking to a schedule to the greatest extent possible would minimize disruption.

What concerns do you have with respect to the agency's current examination and supervision program?

Our members routinely cite examination findings as a chief concern about the current examination and supervision program. Specifically, managing the grey area between a recommendation and a mandate is difficult. If an examination team wants a certain action or a specific practice stopped, it would be best if that finding is grounded in a regulation or readily recognizable best practice.

Here is a common example offered by PCUA members. The examination team states that liquidity, investment or asset-liability management policies are satisfactory. However, the agency still recommends adjusting net economic value to X. If the exam team states that the underlying policies are satisfactory, isn't that evidence that the credit union is managing risk in an appropriate manner? We appreciate that an exam team has to make a judgment call. All parties concerned would benefit if there was some outside limit on an examiner's discretion to require adjustments where a given regulation is factor oriented versus a bright line.

We also suggest that the creation of an independent appeals process would alleviate the situation described above and enable the parties to resolve disagreements over findings. We view a robust appeals process as beneficial to both NCUA and the credit union. An appeals process creates a venue for independent review. The review should be conducted with some formality. Both parties should have an opportunity to be heard and present evidence or data that supports their position. As such, the appeals process that we advocate is not a forum for trivia. Rather, it is a reasonable means to adjudicate material disagreements over examination finding or the conduct of an examination. The hearing officer should prepare a written decision supported by findings of fact and conclusions of law.

What actions should the NCUA consider to improve the efficiency of its examination program, while ensuring it remains effective?

Our suggestions for question 1 apply here as well. In addition, greater use of technology and conducting as much review off-site would assist examiner and credit union alike.

How can NCUA better use technology?

More modern technology platforms could enhance both the examination process and call reporting process. What lessons could be learned from FinTech? For example, we are aware of loan underwriting platforms that can dramatically reduce the amount of time and expense associated with analyzing a member business loan. Can decision-making or analysis oriented technology be deployed in examinations? Updates to AIRES would generate benefits to NCUA and credit unions. Technology could minimize on-site time, enabling NCUA to focus on specific risks versus what we know as a traditional examination.

What metrics should the agency consider in determining a credit union's eligibility for a longer examination cycle?

Reasonable metrics to consider in extending the examination cycle might include: key ratios; a strong CAMEL rating in management; and evidence of thorough risk management and internal controls.

Keith Morton
Regional Director

-3-

August 1, 2016

Call report reform

We understand that NCUA is likely to undertake revisions to the Report of Financial Condition or Call Report as a separate matter. PCUA would like to offer suggestions at this time; however, because we view the labor related to preparing the Call Report and preparing for an examination as integrally related. A significant difficulty with the Call Report arises when NCUA changes a regulation which requires adjustments to the large volume of fields contained in a Call Report. For example, while the changes to Part 723 that take effect in January of 2017 are welcome, we anticipate changes to the Call Report regarding member business loans.

The Call Report should focus on areas of significant risk. Much of a Call Report includes routine financial statements. Credit unions would benefit from not having to reproduce, if you will, their quarterly financial statements, in the format of the Call Report. Accordingly, the data gathering could focus on risk areas within a portfolio, enabling the NCUA to spend more time concentrating on risk versus more routine data. Technology could increase efficiency in terms of completing the report. We encourage NCUA to explore technology that would gather the necessary data while reducing the labor required to format and submit the current version of the Call Report.

Conclusion

The effort put forward by the NCUA Board and Examination Flexibility Working Group creates an opportunity for NCUA and credit unions to reduce the time and labor devoted to examination and call reporting. We view this undertaking as a significant regulatory reform and look forward to continuing a dialogue with the NCUA to improve the examination process. A critical analysis of risk combined with adopting new technology will lead to a better process.

We would be happy to discuss our comments or address any questions you might have at your convenience.

Sincerely,

PENNSYLVANIA CREDIT UNION ASSOCIATION



Richard T. Wargo, Jr., Esq.
Executive Vice President/General Counsel

cc: P. Conway
Association Board
Regulatory Review Committee
State Credit Union Advisory Committee

