California CREDIT UNION LEAGUE NEVADA CREDIT UNION LEAGUE

VIA E-MAIL: regcomments@ncua.gov

May 25, 2010

Ms. Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

Dear Ms. Rupp:

RE: Comments on Proposed Rule 742, Regulatory Flexibility Program

On behalf of the California and Nevada Credit Union Leagues, I appreciate the opportunity to comment on NCUA's proposed changes to its Regulatory Flexibility (RegFlex) program. The proposal would rescind the following exemptions available to federal credit unions under the program:

- The limit on credit union investments in fixed assets, which is five percent of shares and retained earnings;
- The requirement to obtain the personal liability and guarantee of the borrower for a member business loan (MBL);
- The limit on delegating control over the purchase and sale of investments up to 100% of the credit union's net worth; and
- The requirement to stress test certain investments.

By way of background, the California and Nevada Credit Union Leagues (Leagues) are the largest state trade associations for credit unions in the United States, representing the interests of more than 400 credit unions and their 9 million members.

Summary of the Leagues' Position
The Leagues support the Agency's RegFlex program, which allows well-managed, well-capitalized federal credit unions to obtain relief from certain regulatory burdens, thereby providing them much-needed flexibility to effectively compete, grow, and serve their members. We also support NCUA's review of this program, so as to ensure that this initiative is continuing to meet its intended objective. However, it appears that the assumptions driving several of these changes are misguided and have led to what we believe is, overall, a flawed and unfair proposal. Therefore, the Leagues do not support the proposed changes in their current form, as we believe they would dramatically limit the usefulness of the RegFlex program and hamstring the majority of well-managed, well-capitalized federal credit unions that rely on and benefit from it.

Fixed Assets
NCUA purports to demonstrate that a rescission of the fixed asset exemption is needed by citing in the proposal four examples of credit unions experiencing financial problems—problems that NCUA believes are the result of excessive investment in fixed assets. The Leagues take issue with this approach and the Agency's resulting conclusion.

First, other than some financial information from the four credit unions, no statistical data is provided as to the trend in this area for all RegFlex credit unions, or the degree that this issue affects RegFlex credit unions—or all federally-insured credit unions—as a whole. Such an anecdotal approach is not only unusual for such a significant change, but is highly unconvincing. We ask that NCUA provide much more comprehensive, relevant data and analysis to support its conclusion.

Second, in our opinion, it is more reasonable to conclude from the examples given that it was limited analytical skills, lack of experience, and/or poor management that were the root cause of these credit unions' financial ills, rather than excessive investments in fixed assets. For example, Example 1 includes the statement: "The FCU expanded its operations without conducting a sufficient analysis of the impact of the expansion and developing a sound financial plan." Given statements like this, we believe the proposal falls far short in demonstrating that it was the flexibility to exceed the five percent limit in fixed assets that created the problems at these credit unions.

Third, the proposal does not acknowledge that many state-chartered/licensed credit unions are permitted by state law or regulation to exceed the federal limit of five percent, and most remain financially sound. In Nevada, for example, state-chartered credit unions are permitted, without regulator approval, to invest in fixed assets in an aggregate value of up to seven percent of assets. In California, state-licensed credit unions are permitted, without regulator approval, to invest in fixed assets and credit union service organizations in an amount of up to 10 percent of unimpaired capital and surplus. We are unaware of any regulatory efforts in either State to curtail these current limits. Given this additional, state-level view, NCUA's action appears to be an overreaction that penalizes the majority of well-managed credit unions at the expense of a few problem credit unions.

Finally, if NCUA proceeds with this change, the proposal is not clear as to how those RegFlex credit unions currently over five percent threshold will be treated. Will they be grandfathered? Or will they be urged—or required—to divest of these assets? The Leagues urge NCUA to clarify this aspect of the change. If the proposal is finalized in its current form, we recommend that the Agency grant a significant degree of time and flexibility regarding divesture of assets.

Member Business Loans
Like the change to the fixed assets limit, the proposal provides no data or analysis to support NCUA's assumption that the lack of a personal guarantee on an MBL adds more risk to the granting of a business loan. Instead, the proposal provides only general delinquency and charge-off MBL statistics for the industry, as well as a single credit union. There is no information provided that compares delinquency and charge-offs for MBLs with personal guarantees to those without personal guarantees. The Leagues find the lack of any empirical data to support the Agency's claim that this is a safety and soundness issue to be troubling. As with the fixed asset issue, this appears to be an overreaction by NCUA to the significant challenges faced by credit unions, banks—and many other businesses—throughout the nation during the recent recession.

While providing no data to support it, the proposal assumes that a loan relationship has added risk simply because it lacks a personal guarantee from the owners. Requiring or waiving a guarantee is more appropriately decided based on the financial strength and integrity of the borrower. Properly underwritten, only the strongest of borrowers are allowed the benefit of not having ownership contingently liable for the business obligations. Indeed, it is our understanding from the Regional CUSO Alliance (RCA) that, within the credit union portfolios serviced by RCA members, less than ½ of one percent of the loans have no personal guarantee. Most credit unions, whether they use in-house or outsourced underwriting, have very conventional risk appetites and credit policies.

While the proposed rule would preserve the ability of an FCU to request a case-by-case waiver, it is our understanding that it is not practical to use a waiver request on a regular basis. For example, once all origination documentation needed for final underwriting is obtained on a real estate MBL, a typical closing is held within 5 to 10 days. It is unlikely that a business owner will choose to wait an additional 10, 20, or more days while a waiver is being obtained. As a result, the Leagues believe that this change would be anti-competitive for credit unions, since it would deter the most qualified potential borrowers from applying to credit unions for MBLs, and push them toward non-credit union lenders where they don't have to provide their personal guarantee. This will, in turn, create a higher level of risk within credit union MBL portfolios, and will also drive away the most beneficial member business relationships.

Recommendations
The Leagues disagree with NCUA's approach that the problems of a few problem credit unions should be used as the justification to curtail the flexibility and benefits enjoyed by a majority of safe and sound federal credit unions participating in the RegFlex program. RegFlex has allowed many credit unions to control or reduce ongoing operational expenses, permitted them to remain competitive, and provided much-needed value and convenience to their members. Unfortunately, the proposed changes appear to be another example of NCUA attempting to eliminate risk at credit unions, instead of permitting credit unions to mitigate risk.

Rather than remove key exemptions for all federal credit unions, the Leagues urge the Agency to address case-by case problems through a more targeted approach. As NCUA is aware, the RegFlex regulations already allow the Agency to rescind RegFlex designations. We believe this approach would be much more equitable than the "broad brush" approach employed by the proposal. We believe it would be more appropriate to ensure examiners—and RegFlex credit unions—understand and appreciate that the RegFlex authority can be removed if a credit union no longer meets the criteria. NCUA may also want to consider moving more quickly to rescind RegFlex status if a credit union has problems. Or the Agency may want to decide to require additional capital when problems arise in order to maintain a credit union's RegFlex status.

Finally, we suggest that the NCUA consider gathering pertinent data from RegFlex credit unions that could assist the Agency in future assessments of the true effectiveness or detriments of various RegFlex exemptions. This would help to address the Agency's too-heavy reliance on anecdotal information and/or unfounded assumptions as found in this proposal.

The Leagues thank the NCUA for the opportunity to share our views on these proposed changes. We appreciate your consideration of our comments.

Sincerely,

Bill Cheney
President/CEO
California and Nevada Credit Union Leagues