

THE OFFICE OF GENERAL COUNSEL'S
2013 REGULATION REVIEW

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711 Management Official Interlocks

Part 711 implements the Depository Institution Management Interlocks Act, which generally prohibits financial institution management officials from serving simultaneously with two unaffiliated depository institutions. NCUA last amended this rule in June 2010 to add additional clarifying language to §711.2(e). We received no comments requesting changes to Part 711 and are unaware of any problems that would suggest Part 711 should be further revised at this time.

712 Credit Union Service Organizations

Part 712 sets out the permissible forms of organization and activities for credit union service organizations (CUSO). In July 2011, the NCUA Board issued a proposed rule to improve the quality of information regarding credit unions' use of CUSOs and to address certain safety and soundness concerns. Staff carefully considered all the comments NCUA received regarding the proposal. NCUA amended Part 712 in a final rule issued in November 2013. We do not recommend any further revisions at this time.

713 Fidelity Bond and Insurance Coverage for Federal Credit Unions

Part 713 articulates the requirements for fidelity bonds for federal credit union (FCU) employees and officials and for other insurance coverage for losses caused by persons outside the credit union. Five commenters supported making revisions to Part 713. Commenters requested that NCUA amend the rule to include a waiver process so FCUs that no longer qualify for the higher deductible have more than 30 days to obtain the required coverage. Commenters also suggested: (1) increasing the number of companies that are approved to write credit union bonds; (2) reworking the calculations for minimum limits and maximum deductibles; and (3) replacing the rule's formulas with dollar ranges. One commenter requested more flexibility with respect to required coverages based on risk. We are unaware of any problems that would suggest Part 713 should be revised at this time.

714 Leasing

Part 714 sets forth the requirements for FCUs to engage in direct and indirect leasing of personal property to members. This rule was last amended in November 2012 by updating the citation to Regulation M. Commenters have suggested the following changes to the leasing regulation: 1) not requiring a full assignment of the lease in an indirect leasing arrangement; 2) adopting a flexible approach on the 25% residual value limit; and 3) clarifying the types of leasing relationships covered by this regulation. Despite these comments, we do not recommend making any changes at this time.

715 Supervisory Committee Audits and Verifications

Part 715 prescribes the responsibilities of the supervisory committee to obtain an annual audit of the credit union according to its charter type and asset size and to conduct a verification of members' accounts. One commenter suggested that annual account verifications are outdated in today's marketplace because modern technology allows consumers to check and verify their accounts at any time. This commenter expressed concern that annual verifications only confuse members, and members view this correspondence negatively. This rule was last modified in 1999.

The Office of Examination and Insurance (E&I) is currently studying several potential substantive changes to Part 715. One option is to require each insured credit union with assets of \$50 million or more to have an annual independent audit of the financial statements of the credit union by an independent certified public accountant or public accountant licensed by the appropriate state. E&I expects to provide its findings to the Board in early 2014. We recommend the Board consider those findings at that time.

716 Privacy of Consumer Financial Information

Part 716 governed the treatment of nonpublic personal information of credit union consumers. NCUA recently amended Part 716 to reflect the Dodd-Frank Wall Street Reform and Consumer Protection Act's (Dodd-Frank's) transfer of authority for Part 716 to the Bureau of Consumer Financial Protection (CFPB). *See* 78 Fed. Reg. 32545 (May 31, 2013). The CFPB had previously published its consumer privacy regulation, applicable to credit unions and other entities, at 12 C.F.R. Part 1016 (Regulation P). *See* 76 Fed. Reg. 79025 (Dec. 21, 2011). Under Dodd-Frank, NCUA retains the enforcement authority for credit unions with assets of \$10 billion or less. NCUA will amend its former Paperwork Reduction Act OMB number 3133 0163 to reflect the new regulatory scheme under Part 1016.

Some commenters requested relief from certain statutorily mandated requirements. We do not recommend any further changes at this time.

717 Fair Credit Reporting

Part 717 establishes standards for FCUs concerning consumer report information. Under Dodd-Frank section 1025, NCUA retains regulatory authority for §§ 717.90 and 717.91, and Appendix J to Part 717. Appendix J contains red flag guidelines for FCUs to use in identifying patterns, practices, and specific forms of activity indicating possible identity theft. Section 717.90 requires each FCU to establish reasonable policies and procedures to address the risk of identity theft and incorporate the guidelines in Appendix J. Under Section 717.91, credit card and debit card issuers must implement reasonable policies and procedures to assess the validity of a request for a change of address under certain circumstances.

Consistent with comments we have received, we recommend that NCUA amend Part 717 to reflect Dodd-Frank Act's transfer of the rest of the sections of Part 717 to the CFPB. The CFPB has already published its Fair Credit Reporting regulation, reflecting this transfer of

authority over credit unions and other entities at 12 C.F.R. Part 1022 (Regulation V). *See* 76 Fed. Reg. 79308 (Dec. 21, 2011).

We recommend NCUA also request a new OMB Paperwork Reduction Act number to reflect NCUA's enforcement authority for credit unions under Part 1022.

721 Incidental Powers

Part 721 describes various activities that an FCU may engage in as a permissible exercise of its incidental powers. The rule was amended in May 2012 to codify an FCU's authority to make charitable contributions and donations. In December 2013, NCUA further amended the rule to clarify that, under certain circumstances, an FCU is authorized to fund a charitable donation account.

In addition, staff recommends the Board issue a proposed securitization rule to permit an FCU to securitize its own loans for sale on the secondary market, as a permissible exercise of its incidental powers authority, if certain conditions are met.

Commenters suggested several changes to the incidental powers rule to expand FCUs' authority to engage in incidental powers activities, including: (1) allowing FCUs to engage in incidental activities that are permitted for state-chartered credit unions; (2) supplementing the rule's three-part test for determining if an activity is a permissible incidental power; and (3) preapproving additional incidental powers activities, for example, pre-paid funeral home accounts, management of repossessed properties, and foreign currency investments. Because of the recent amendments to this rule, other amendments discussed above, and the nature of the additional powers requested by commenters, staff does not recommend making any additional changes at this time.

722 Appraisals

Part 722 sets forth the appraisal requirements for federally-related real estate transactions, which are substantially the same as the rules of the other financial regulators. Because of statutory changes in law governing appraisal requirements, appraisal independence, appraisal report portability, registration of appraisal management companies, and automated valuation model quality control standards, Part 722 must be revised to comply with Title XIV of the Dodd-Frank Act. Commenters requested greater parity with other FFIEC Agencies in the area of appraisal exemptions. Specifically, commenters noted that §722.3 allows for an exemption from certain appraisal requirements if, among other things, there is not advancement of new monies and there has been no obvious change in market conditions or physical aspects of the property. Commenters noted that interagency guidance allows credit unions to select between the two conditions. 2010 Interagency Appraisal and Evaluation Guidance. As NCUA subscribes to this guidance, we recommend making a technical change to the regulation to change the word "and" to the word "or."

Additional rules on appraisals are being developed through an interagency working group process. Further, as part of the continuing interagency review on appraisal-related issues, we

recommend the Board eliminate any redundant NCUA requirements on credit unions to provide copies of appraisals upon request.

723 Member Business Loans

Part 723 defines member business loans (MBLs), establishes minimum standards for making MBLs, and implements various statutory restrictions. Public comments included general requests for more flexibility in the rule. Specific requests for relief focused on provisions pertaining to the loan-to-value ratio requirement and construction and development lending. Other comments pertained to vehicle lending and requests to streamline the waiver process. Other commenters very broadly asked NCUA to eliminate from the regulation any restrictions that are not required by the Act, revisit exemptions for credit unions “primarily making MBLs,” and eliminate the personal guarantee requirements. Of the comments submitted by the public, we believe some of the most pressing issues they raised pertain to the personal guarantee requirement and the MBL waiver process, including the use of blanket waivers.

While we do not believe all of the commenters’ suggestions should be adopted in a rulemaking, some are worth considering. We believe the MBL rule should be revisited and updated to reflect the current business climate and to address certain other pressing issues facing credit unions including: 1) whether “soft costs” should be included in calculating the market value of a construction and development project; 2) clarifying the meaning of “associated borrower;” 3) collateral valuation; and 4) determining appropriate financial analysis practices as part of the underwriting process.

To modernize the MBL rule and provide reasonable regulatory relief, we recommend exempting well capitalized credit unions with sufficiently high CAMEL ratings over a stated period of time from the MBL rule’s personal guarantee requirement. To that same end, we recommend replacing the MBL rule’s 2-year direct experience requirement with a more flexible, user friendly method of ensuring a credit union is utilizing qualified individuals in its business lending program. Additionally, we believe the MBL rule needs to be updated to clarify the legal relationship between NCUA and state supervisors in those states that administer their own state MBL rules.

The Office of Examination and Insurance recently established a committee to review the MBL rule and make further recommendations for amendment. The committee is slated to propose amendments in early 2014. We recommend the Board consider amending the MBL rule after the committee submits its results.

724 Trustees and Custodians of Certain Tax-Advantaged Savings Plans

Part 724 authorizes and sets forth the rules governing FCUs acting as trustees or custodians of pension and health care plans. Part 724 was last amended in July 2004 to authorize FCUs to act as trustees for health savings accounts. We are unaware of any problems regarding Part 724 and received no comments on this Part. We do not recommend any changes at this time.

Part 725 sets out rules concerning CLF operations. The rule was adopted in 1979 and underwent its last substantive amendment in 1997. Technical amendments making minor changes were adopted in 2004 and 2011. Of the five public comments we received that made reference to CLF, none identified specific suggestions for changes to Part 725. Instead, each focused more on NCUA's recent rulemakings concerning emergency back-up liquidity requirements. In general, these commenters urged NCUA to update and modernize the CLF before implementing a final rule on emergency liquidity. Two commenters expressly questioned whether, in its current form and subject to its current regulatory and statutory constraints, CLF can continue as a viable source of liquidity for credit unions.

Following structural changes in the credit union industry caused by the recent financial crisis and recession, the need for change to the CLF is apparent. NCUA intends to prepare and submit to Congress a whitepaper outlining certain recommendations for statutory changes that will enable CLF to move forward as a meaningful resource for the industry. Accordingly, we believe that wholesale change to Part 725 should await the outcome of this legislative initiative.

Nevertheless, we suggest that certain amendments of a clarifying or technical nature should be considered at this time. These include:

- Changing references to “central credit union,” which appear throughout, to “corporate credit union,” which is current terminology.
- Deleting the reference in the last line of §725.2(h)(2) to “the Federal Savings and Loan Insurance Corporation,” which has been defunct for almost 25 years.
- Deleting footnotes one and three, which contain transitional references to actions that would had to have been accomplished by October 1979.
- In the last sentence of §725.4(f), the word “or” needs to be inserted between the words “chartered” and “within.”

Part 740 sets out the requirements governing the NCUA official sign and how it should be displayed, the official advertising statement and the manner in which it should be used, and the accuracy of any advertising used by a federally insured credit union. In May 2011, this rule was amended to require insured credit unions to include the official advertising statement in a greater number of radio and television advertisements, annual reports, and statements of condition.

Two commenters made specific recommendations regarding changes to the text, font, and size of the official sign and official advertising statement. One commenter stated that the rule should be revised to prohibit including the official advertising statement on credit union web pages advertising non-deposit investment products. Another commenter urged NCUA to provide approved translations of the official advertising statement in other languages, so that credit unions and Regional Directors do not have to go through the approval process provided

for in §740.5(d). Six commenters suggested that requirements regarding the official sign and official advertising statement be revised to accommodate the rise of social media and mobile banking.

We believe the commenters have raised some practical concerns about the current rule. We recommend the Board consider amending the rule to modernize it in light of the growing use of quickly advancing technology and to meet consumer needs.

741 Requirements for Insurance

Part 741, in addition to establishing requirements for insurance, places various substantive requirements applicable to FCUs on federally insured, state-chartered credit unions (FISCUs). The rule has been amended numerous times in recent years, paralleling changes to substantive FCU requirements. Four commenters object generally to what they perceive as the increasing practice of applying FCU rules to FISCUs. They argue that the practice threatens the viability of the dual chartering system. One commenter recommends clarifying that a more restrictive state law would preempt Part 741's application of an FCU rule to a FISCU. This commenter also asks NCUA to create an index to the regulations indicating which ones apply to FISCUs. One commenter requests more exemptions for FISCUs located in states with regulations that are substantially similar to NCUA's. This commenter also notes six sections of Part 741 that it believes improperly intrude on state authority. Finally, this commenter asks NCUA to create a consolidated reference in Part 741 to all of NCUA's rules that apply to credit union boards and to consolidate and publish those rules applicable to FISCUs separately to reduce the burden on FISCUs. We do not recommend making any amendments to Part 741 at this time. We also do not recommend NCUA produce separate indexes, references, or publications for FISCUs. However, nothing precludes a trade group or a state league from creating such a separate guide if it wishes to do so.

745 Share Insurance and Appendix

Part 745 contains the rules governing share insurance coverage for various types of member share accounts. This regulation has been amended several times in recent years to comply with statutory amendments to the FCU Act. Six commenters provided comments on various aspects of Part 745 including requesting NCUA to provide broader coverage for Interest On Lawyers Trust Accounts (IOLTA). We support broader IOLTA coverage to the extent that statutory amendments are enacted to permit that. Otherwise, we are unaware of any problems suggesting that we should further amend Part 745 at this time.

747 Administrative Actions, Adjudicative Hearings, Rules of Practice and Procedure, and Investigations

Part 747 sets forth the various formal and informal adjudicative and non-adjudicative proceedings available to the NCUA Board. Three commenters suggested NCUA update the appeals process and make other modifications to Part 747 to ensure fairness. We believe the

actions taken under Part 747 and the procedures used are fair and work well. We are unaware of any reason why Part 747 should be revised at this time.