Cooperative
Credit Union Association

Creating Cooperative Power

December 16, 2019

Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

RE: Cooperative Credit Union Association Inc.'s Comments on Interagency Policy Statement on Allowances for Credit Losses, ACL; RIN 3133–AF05

BY EMAIL ONLY: regcomments@ncua.gov

Dear Secretary Poliquin:

On behalf of the member credit unions of the Cooperative Credit Union Association, Inc. ("Association"), please accept this letter relative to the National Credit Union Administration Board's ("NCUA") request for comments in response to the proposed interagency policy statement on allowance for credit losses ("Statement"). The proposed interagency statement was developed in light of the changes in the accounting treatment of credit losses contained in the Financial Accounting Standards Board's ("FASB") Accounting Standards Update 2016-13, Financial Instruments-Credit Losses, known as Topic 326 (Current Expected Credit Losses or "CECL"). The Association is the state trade association representing credit unions located in the states of Delaware, Massachusetts, New Hampshire, New Jersey and Rhode Island, serving approximately 200 credit unions which further serve over 3.6 million consumer members.

In preparation for the development of this comment letter, the Association recently solicited the views of its members and received valuable perspectives from a variety of both state and federally-chartered credit unions. This letter incorporates feedback received through a member survey relative to the proposed interagency policy statement, which addresses operational issues associated with the implementation of CECL, published in the Federal Register on October 17, 2019. The Association recognizes the difficulties in trying to provide guidance on CECL implementation as many key issues are not addressed in Topic 326. Based on input from members, the Association also recommends several revisions designed to minimize confusion and to improve the utility of the guidance.

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A. Initial Comments and Request for Further Change as NCUA Has Legal Authority to Improve Credit Loss Assessments for Credit Unions and Their Members

The position of the Association and its members has not changed. CECL under Topic 326 should not apply to credit unions and it remains our belief that it is not too late for NCUA to address this major issue.

Before addressing the specifics of the Statement, members continue to have very serious concerns about the application of CECL to credit unions. The Association notes that even though its application will be delayed, credit unions urge NCUA to reconsider its role in implementing the CECL accounting standard now. The overarching concerns about CECL continue to include its potential impact on capital, allowance for credit losses, lending, implementation complexities and costs, and ongoing compliance. Despite the protracted development of CECL, its impact on credit unions has not been fully considered because no one can know with certainty today how its implementation in January 2023 will affect credit union operations.

It is clear that FASB has concerns about the implementation of CECL or it would not have delayed again the effective date for credit unions and smaller banks. Moreover, on a bipartisan basis, Members of Congress in both chambers have supported a delay as well as a stop and a study of CECL's effects on financial institutions. Within our delegations in response to member concerns, six (6) lawmakers[1] have taken a public stand and are in support of the need for change.

Under the Federal Credit Union Act ("FCU Act"), the NCUA possesses the authority to allow credit unions to follow an agency-developed accounting standard that differs from one created by FASB.

> "If the Board determines that the application of any generally accepted accounting principle to any insured credit union is not appropriate, the Board may prescribe an accounting principle for application to the credit union that is no less stringent than generally accepted accounting principles." 12 U.S.C. 1782(a)(6)(C)(ii)

The Association urges NCUA to revisit its legal authority and reconsider the "appropriateness" of CECL for credit unions. NCUA has the power to prevent CECL from creating serious problems for credit unions by developing an approach tailored for credit unions or fine tuning the current methodology to help credit unions assess credit losses. At a minimum, NCUA should work with the bank regulators to determine whether the agencies could adopt an interagency accounting standard for credit unions and smaller banks that would position institutions to

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[1] H.R.3182, *CECL Consumer Impact and Study Bill of 2019*, co-sponsored by New Hampshire Congresswoman Ann Kuster and Congressman Chris Pappas and New Jersey Congressman Josh Gottheimer. Direct letter of support for study and change submitted to the Federal Accounting Standards Board, Federal Deposit Insurance Corporation, Federal Reserve Board of Governors and the Securities and Exchange Commission by Delaware Senator Chris Coons, New Hampshire Senators Jeanne Shaheen and Maggie Hassan.

manage expected credit losses without subjecting them to a public accounting standard that is potentially harmful.[2]

If the agency determines it cannot help credit unions as outlined above, then the NCUA is requested to address the following concerns set forth in this comment letter.

B. Specific Questions for Response

The Statement includes three questions for comment which are addressed in this letter.

(1) Does the proposed interagency policy statement clearly describe the measurement of expected credit losses under CECL in accordance with FASB ASC Topic 326? Why or why not? If not, what additional information is needed? What information should be omitted from the policy statement?

The document should begin with a clear, summarized description of CECL which it currently lacks. The objective of the proposed guidance does not appear to provide "the" measurement of expected credit losses, but rather, discusses parameters for institutions to remain within in choosing and applying measurements for assessing credit losses and ACLs.

(2) Does the proposed interagency policy statement clearly describe the measurement of credit losses on impaired AFS debt securities in accordance with FASB ASC Topic 326? Why or why not? If not, what additional information is needed? What information should be omitted from the policy statement?

Members did not provide comments or raise concerns on this issue.

(3) Does the proposed interagency policy statement clearly communicate supervisory expectations for designing, documenting, and validating expected credit loss estimation processes, internal controls over ACLs, and maintaining appropriate ACLs?

While the Statement would afford flexibility to credit unions in making those choices, real concerns remain that examiners will second guess a credit union's approach, despite language in the document that examiners should not substitute their views for reasonable, well-developed methods selected by a credit union. The document acknowledges that a credit union's decisions regarding credit loss estimations and its ACL should be made based in part on size and resources, yet the standards presented in the document are of general application and could be applied by any examiner to any credit union.

(4) Has the proposed interagency policy statement appropriately included concepts and practices detailed in the existing ALLL policy statements that also are relevant under FASB ASC Topic 326? If not, what additional information should also be included?

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[2] Respondents noted that "CECL is unnecessary for credit unions in general."

Some issues are set forth in this comment letter, but no other topics are suggested.

C. Additional Comments

1. Loans Held for Sale

Loans held for sale are not assessed for credit losses using the CECL methodology and is an approach supported by the Association. Credit unions may change asset classifications as needed, and the policy statement should address how institutions should transition from an assessment for loans held for sale to those held for investment, which would be covered under CECL.

2. Measurement of ACLs

The proposed Statement relative to allowance for credit losses ("ACL") provides:

> "Estimating appropriate ACLs involves a high degree of management judgment and is inherently imprecise. An institution's process for determining appropriate ACLs may result in a range of estimates for expected credit losses. An institution should support and record its best estimate within the range of expected credit losses." 84 Fed Reg 55510, 55514

It is unclear, given the range of information an examiner may request, whether a credit union would need to maintain data on processes or estimates it did not choose to use as a basis for maintaining the ACL. Only data to support estimates and valuations selected by a credit union should be sufficient.

3. Evaluation of Expected Losses

Several statements in the proposed Statement, when read together, appear to be contradictory, even though the Association acknowledges that it is intended to be helpful to both credit unions and examiners.

For example, provisions for Estimation Methods for Expected Credit Losses provides:

> "FASB ASC Topic 326 does not require the use of a specific loss estimation method for purposes of determining ACLs. Various methods may be used to estimate the expected collectability of financial assets, with those methods generally applied consistently over time. The same loss estimation method does not need to be applied to all financial assets. Management is not precluded from selecting a different method when it determines the method will result in a better estimate of ACLs." 84 Fed Reg 55515

Yet, the Statement further provides that examiners may:

> "Evaluate the institution's ACL policies and procedures and assess the loss estimation method(s) used to arrive at overall estimates of ACLs, including the documentation supporting the reasonableness of management's assumptions, valuations, and judgments." 84 Fed Reg 55521

As a result, even though a particular method may not be required by policy, examiners by practice would be authorized to impose their choice of evaluation methods.

Under "Reasonable and Supportable Forecasts[3]" the Statement provides:

> "Management is not required to search for all possible information nor incur undue cost and effort to collect data for its forecasts. However, reasonably available and relevant information should not be ignored in assessing the collectability of cash flows. Management should evaluate the appropriateness of the reasonable and supportable forecast period(s) each reporting period, consistent with other inputs used in the estimation of expected credit losses." 84 Fed Reg 55515

While under "Qualitative Factor Adjustments" the Statement directs:

> "The estimation of ACLs should reflect consideration of all significant factors relevant to the expected collectability of the institution's financial assets as of the reporting date." 84 Fed Reg 55516

These examples raise the specter of confusing credit unions regarding expectations and the extent to which more factors than those identified in the policy or are necessary to reach reasonable decisions should be considered. Members specifically noted that factors such as regulatory, legal and technological environments; competition; events; and actual and expected changes in economic and business conditions, are somewhat vague and subject to interpretation. The Association urges NCUA to view these provisions together with an eye toward clarification.

4. Troubled Debt Restructurings

The proposed Statement is proscriptive regarding Troubled Debt Restructurings ("TDRs") and estimating the ACL using the fair value of collateral in connection with TDRs. The Association understands that the policy must reflect Generally Accepted Accounting Principles but remains concerned whether credit unions will have sufficient flexibility to provide TDRs to members in need of them without being unduly encumbered by accounting technicalities. The Association encourages the NCUA to provide as much flexibility as possible in the Statement under GAAP in addressing TDRs.

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[3] Respondents noted that this area will cause the greatest amount of disparity and confusion in forecasting future losses as it provides a great deal of subjectivity which may lead to issues with examiners located in another part of the country or simply difference in interpretations.

5. Financial Assets with Zero Credit Loss Expectations

This area of the Statement should be better tailored for credit unions to reflect their historically low default and delinquency rates. Credit unions should have wide latitude to determine that particular loans to members, with a proven record of timely repayment, have zero credit loss expectations.

In addition, loans that are fully secured, guaranteed or have a portion guaranteed by federal agencies as well as held to maturity debt securities backed by the U.S. government should, without question, be handled as zero credit loss expectation assets or portion of an asset. The proposed document describes these assets as "likely" to have zero losses, raising the possibility that an examiner could require such loans or investments be given more thorough assessments under CECL as if they did not have zero credit loss expectations. Furthermore, the Association suggests that not much credit loss assessment on a credit union's part, if any, should be required for loans or securities backed by the federal government.

6. Documentation Standards

The Association agrees that credit unions should maintain and make available for review by boards of directors and examiners sufficient documentation to explain CECL and ACL estimation decisions. The documentation "standards" appear to be requirements and appear to be excessive. The proposed Statement lists a range of documents and "may" include others not listed, opening the door for examiner requests for documentation that is not listed in the policy. Also, it is not clear at what point an institution with, for example, assets under $10 billion and a non-complex asset structure, would have to produce all the documents listed. NCUA is urged to revisit this section of the proposed Statement and revise it to provide clear expectations based on a credit union's size, complexity, and resources.

7. Comparisons with Peers

This issue is another area of the proposed Statement that raises the possibility of confusion and should be clarified. For example, the Statement provides:

> "Comparing the institution's ACLs to those of peer institutions may provide management with limited insight into management's own ACL estimates. Management should apply caution when performing peer comparisons as there may be significant differences among peer institutions in the mix of financial asset portfolios, reasonable and supportable forecast period assumptions, reversion techniques, the data used for historical loss information, and other factors....When an appropriate expected credit loss framework has been used to estimate expected credit losses, it is inappropriate for the board of directors or management to make further adjustments to ACLs for the sole purpose of reporting ACLs that correspond to a peer group median, a target ratio, or a budgeted amount." 84 Fed Reg 55520

If authority exists to prevent the use of peer analyses, then they should be prohibited in the context of CECL valuations. Such action does not appear to be the case. Therefore, peer analysis should clearly be permitted if a credit union chooses to utilize such analyses as part of the estimation process. Given the range of standards in the Statement, adjusting estimates based on the "sole" purpose of corresponding to peer analyses would not even be possible.

8. Responsibilities of the Board of Directors and Management

There is no question that CECL will impose heavy burdens on volunteer credit union boards of directors as well as management. These responsibilities, given all the other requirements credit union boards and management face, could be overwhelming. Many credit unions will likely utilize third party products and services to help them implement and maintain compliance. The Association requests that federal regulatory resources be aggregated and made available as much more may be provided in the way of **free**, accessible, on-demand, on-line and in-person training to boards of directors and management.

Finally, members suggest that the responsibilities of boards of directors are too open-ended as the Statement provides that:

"(T)hese activities should include, but are not limited to…"

A similar characterization is proposed for management. The policy should be clear as to the full extent of board and management responsibilities and not raise or leave unstated other duties they are expected to fulfill without knowing about them. This is particularly important given that the actions or inactions of boards and management under the Statement are subject to examiner review.

9. Examiner Review of ACLs

Examiner review of the adequacy of the ACL is expected, but it is the position of the Association that the scope of examiner authority under the Statement is simply overstated. Not only would it allow the examiner to assert herself or himself into assumptions and calculations, but the examiner is directed to evaluate "supporting activities" that are not completely identified in the policy. Similarly, the review of the activities of the board of directors and management may extend beyond factors identified in the Statement.[4]

NCUA should develop a specific checklist of what examiners will seek and provide it to credit unions well in advance of CECL implementation. Also, the list should vary based on the size, complexity, and resources of each credit union.

Furthermore, the Statement provides:

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[4] Respondents commented that credit union CPA firms already review current ALLL methodology and compliance with GAAP standards. Examiner oversight in this area is burdensome, redundant and costly for most credit unions.

> "Examiners generally should accept an institution's ACL estimates and not seek adjustments to the ACLs, when management has provided adequate support for the loss estimation process employed, and the ACL balances and the assumptions used in the ACL estimates are in accordance with GAAP and regulatory reporting requirements." 84 Fed Reg 55522

Yet, under the proposed policy, examiners would be able to dismiss a credit union's decisions if it is determined that they are based on support that is deemed to be inadequate. The Association believes that this standard is too thin to support examiner authority that is too broad.

Finally, members expressed continuous concern that there is no consideration of or consultation with certified public accountants ("CPAs") hired by a credit union in the Statement.

10. Sanctions

The proposed Statement provides:

> "Additional supervisory action may be taken based on the magnitude of the shortcomings in ACLs..." Ibid.

The Statement should detail any additional sanctions. Examiners should also be required in the Statement to take into account the credit union's current exam ratings, past record of compliance with NCUA requirements, and efforts to meet accounting standards before imposing sanctions.

11. Legal Status of the Statement

The nature of the Statement and its implementation is unclear and should be included in the final version. Public comment is sought on the Statement in the nature of rulemaking, but the clear legal authority, other than general powers to supervise institutions, is not provided in consideration of the heavy range of burdens credit unions face. The authority of prudential regulators to impose supervisory standards is not questioned by the Association, but the extent to which the policy is rulemaking, as opposed to guidance, is not clear.

12. Phasing in CECL

There is some confusion about the implementation of this policy and the NCUA's statements that CECL will be phased in. The Statement states that it will take effect when CECL takes effect, but it is unclear how that aligns with efforts to implement CECL in a phased-in manner. NCUA is encouraged to clarify how these objectives will be met and consider any phase-in or transition period from when the policy takes effect to minimize supervisory issues as credit unions work to implement CECL.

C. Conclusion

The Association urges NCUA to revisit CECL and reconsider its authority under the FCU Act to improve the outcome for credit unions as envisioned by Congress. In the interim, the Association appreciates efforts to clarify CECL implementation. In the event that CECL cannot be improved for credit unions, then the NCUA is urged to improve the Statement by addressing the issues raised in this letter.

Thank you for the opportunity to share the views of members on this very significant issue for credit unions and their members and for your consideration of the Association's comments. If you have any questions about the recommendations set forth in this comment letter or require further information, then please do not hesitate to contact me.

Sincerely,

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

RM/mac/kb