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

Submitted electronically via regcomments@ncua.gov

RE: Comments on Advance Notice of Proposed Rulemaking – RIN 3133-AE97 (Compensation in Connection With Loans to Members and Lines of Credit to Members)

Dear Mr. Poliquin:

On behalf of the United Nations Federal Credit Union (UNFCU) I would like to thank the National Credit Union Administration Board (NCUA or Board) for allowing comments on the change to the regulations regarding compensation in connection with loans and lines of credit to members proposed in the Federal Register on 23 April, 2019 (the Proposed Rule). UNFCU's members are located in over 200 countries and territories throughout the world; our mission is to "serve the people who serve the world."

As a general matter, UNFCU supports the Board's evaluation of the existing regulations and its efforts to modernize them. These efforts should help to level the playing field for credit unions, allowing us to better compete in the marketplace of financial products and thereby to better serve our members. UNFCU's specific comments pertaining to several of the interrelated questions raised in the Proposed Rule's section II follow.

The Board's inquiry into "industry" standards should extend beyond the credit union industry to the broader financial industry.

As a threshold matter, the Board's inquiry into current industry standards would benefit from clarifying the scope of the "industry" to which it refers. An inquiry into practices across the credit union industry, for example, is likely to yield pronouncedly different results from an inquiry into practices across the broader financial industry. The employees whose expertise lies in developing, originating, and servicing loan products may develop knowledge of practices particular to credit unions, but such knowledge does not then prevent them from taking their lending expertise to the banking sector. The competitive market for talented lending professionals spans the entire financial industry.

Moreover, consumers do not think of their options in the marketplace for financial products as extending only to credit union providers. Acting in their own best interests, consumers regularly look to banks, brokerages, or other non-credit union financial service companies to consider all their options. Credit unions' competitiveness depends on being in a position to offer the best service at the best rate even in this crowded field. The Board should therefore extend its inquiry into industry-wide standards and practices across that more expansive scope.

The Board should modernize § 701.21(c)(8) to reflect current practices necessary for credit unions to remain competitive.

Across the financial industry, the prevailing practice is for financial institutions to pay mortgage lenders commissions. To remain competitive in hiring professionals within this industry, credit unions must be permitted to compensate loan officers and executives on a commission basis.

The current regulation allows for some exceptions to the blanket prohibition on credit union employees receiving compensation in connection with loans a credit union makes. Notably, credit unions may pay employees, including senior management, an incentive based on the credit union's "overall financial performance." Also, employees other than senior management can receive an incentive in connection with loans provided that such compensation is subject to a written policy. These exceptions—codified respectively at 12 CFR § 701.21(c)(8)(iii)(B) and (C)—are necessary but insufficient steps toward giving credit unions the opportunity to remain competitive.

One key improvement the Board could make to § 701.21(c)(8) would be to clarify that loan metrics are a valid and permissible factor in assessing a credit union's overall financial performance. UNFCU supports the National Association of Federally-Insured Credit Unions (NAFCU)'s proposed definition of "overall financial performance" as it relates to § 701.21(c)(8). NAFCU proposes defining overall financial performance as:

> A quantifiable metric, set by the board of directors of the credit union, used for the purposes of measuring a credit union's achievement of targeted performance goals. This metric may include, but not be limited to, total asset growth, overall loan growth, return on assets, efficiency ratio, net-worth ratio, loan-to-value ratio, and delinquency ratios.

See NAFCU's Comments on RIN Number: 3133-AE97.

Such a definition would provide credit unions flexibility in establishing the incentive structures appropriate for their particular circumstances, while still reining in the imprudent, high-risk practices that the regulation seeks to prevent. As NAFCU correctly notes, clarifying the definition of overall financial performance would also help ensure that examiners and credit unions have a mutual understanding of what kinds of compensation plans are permissible.

To truly bring credit union regulations in line with industry practice, however, the Board should strongly consider eliminating its broad prohibition of compensation made "in connection with" loans. To ensure the safety and soundness of credit unions, the Board could substitute a rule that no individual involved in the actual credit decisions—*i.e.*, the underwriting of particular loans—may be compensated by commission. Such a rule, in concert with the other preventative limitations discussed in more detail below, would not only reflect the prevailing standards across the financial industry. It would unshackle credit unions, affording them the opportunity to compete on the same terms as the rest of the industry and thereby, ultimately, provide better service and lower rates to their members.

Sufficient limitations exist to prevent individuals from being incentivized to take inappropriate risks.

The Board's blanket prohibition on compensation for credit union lenders is unnecessary in the regulatory climate presently in place across the financial industry. Several interrelated factors serve to limit a credit union's incentives to take on inappropriate risks.

Existing regulations currently act as a check on the risks that the prohibition on compensation for lenders seeks to mitigate. For example, the Bureau of Consumer Financial Protection (CFPB) has codified a loan originator compensation rule (LOCR) at 12 CFR § 1026.36. The LOCR prohibits terms-based compensation to loan originators, including compensation derived from mortgage-related profits. It also prohibits originators receiving "dual compensation"—*i.e.* from both the consumer and the creditor. In addition, the LOCR contains anti-steering provisions that prohibit originators from directing consumers to a particular type of transaction because the originator will be better compensated.

Credit unions' governance provisions provide another effective preventative measure to limit inappropriate risk-taking by lenders. Any credit union that seeks to lend to its members must, through its board, establish a written lending policy in keeping with 12 CFR 701.21(c). A credit union's internal audit department then exercises regular oversight over its adherence to that policy. Enterprise Risk Management and quality control standards both act as safeguards to prevent a credit union from exposure to an undesirable level of risk by reporting such risks to senior management and the credit union's board. Therefore, even if lending officials derive some part of their compensation from commissions, a well written and enforced lending policy stands to prevent any potential abuse of the commission-based compensation plan.

Furthermore, any pressures created by establishing lending targets—such as loan volume—are tempered by other pressures, such as targets for delinquencies and charge-offs. The inverse relationship between these targets helps to offset risk. For example, if a credit union chooses to meet a loan volume target by taking on more risky loans, its increased risk exposure is likely to lead to a corresponding increase in delinquencies and charge-offs. The credit union would therefore meet one target at the expense of the other. A soundly structured compensation plan that balances these countervailing factors thereby reins in an individual's incentive to take inappropriate risks without the need for additional regulation or a blanket prohibition on volume-based incentives.

Standard compensation plans in the industry achieve such a balance by granting commissions to loan officers, but rescinding, or "clawing back," those commissions in certain instances. For example, claw-back provisions often apply in the case of loans with short-term payoffs or loans that enter delinquency within the first four months. A credit union may also claw back a loan officer's commission if, for example, she makes a rate lock error or fails to meet minimum performance standards on member satisfaction surveys. Such provisions incentivize loan officers not just to increase loan volume, but to maintain loan quality.

Another critical factor in maintaining the safety and soundness of lending institutions that grant commissions is that no individuals involved in making an actual credit-granting decision—*i.e.* underwriters—are compensated by commission. This distinction prevents abusive practices in at least two ways. First, it inoculates underwriters against any pressure to hit lending targets that might otherwise exist. Second, it adds another incentive to the loan officer to bring the underwriter not just a high volume of loans, but loans of high enough quality that they are likely to be approved under the institution's standards.

Finally, the Nationwide Multistate Licensing System (NMLS) helps provide accountability for lenders that might seek to abuse a commission-based compensation plan. The NMLS maintains a registry of mortgage loan originators as required by the CFPB's rules and the Secure and Fair Enforcement for Mortgage Licensing (SAFE) Act. Federal registration of originators holds those originators accountable in multiple ways. A consumer who wishes to register a complaint against a particular originator, for example, can find that originator even if she has relocated to another institution since originating the loan—even if that institution is in another city or state. Also, it puts financial institutions on notice during the hiring process of any outstanding or past complaints against an originator. Knowing that they are likely to face career-long repercussions, originators are far less likely to act against the interests of consumers. These CFPB and SAFE Act provisions therefore act as an additional, final bulwark against the practices that the existing prohibition seeks to prevent.

Overall, UNFCU supports the NCUA's efforts to update the regulations relating to compensation for lenders. Such updates will greatly benefit both credit unions and their members. Thank you for the opportunity to comment and for your consideration of UNFCU's position.

Very Truly Yours,

Eric Darmanin
Chief Lending Officer

cc: William Predmore, President/CEO, UNFCU