CUNA MUTUAL GROUP

CUMIS Insurance Society, Inc.

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

Via email: regcomments@ncua.gov

Re: Notice of Proposed Rulemaking (Fidelity Bonds)

Dear Mr. Poliquin:

On behalf of CUMIS Insurance Society, Inc. (CUMIS), this letter responds to the National Credit Union Administration Board's Notice of Proposed Rulemaking issued in November 2018 seeking comments on issues regarding requirements for the filing, administration and content of fidelity bonds purchased by both corporate and natural person credit unions.

By way of background, CUMIS is part of CUNA Mutual Group, the nation's leading provider of financial products and services to credit unions. CUMIS issues fidelity bonds that protect the majority of federal and state-chartered credit unions. CUMIS insures corporate credit unions and credit union service organizations (CUSOs), as well. CUMIS brings nearly 60 years of experience with this line of insurance and the role it plays in maintaining the financial health of the credit union movement.

Summary of CUMIS' Views

- CUMIS supports the NCUA Regulatory Reform Task Force's stated goals of implementing the Federal Credit Union Act (FCU Act) in a cost-efficient manner. CUMIS supports allowing a credit union to make a business decision based on its own circumstances and reducing the NCUA's involvement in a credit union's operational decisions consistent with the FCU Act. (p. 6)
- CUMIS generally supports the four objectives outlined in the NCUA's summary seeking comment on the proposed rule. (pp. 1-2) In this spirit, we offer information on possible unintended and practical outcomes related to the proposed changes and include suggestions to further the NCUA's stated intent.

Discussion

The proposed regulations focus on four objectives. We will address the proposed revisions themselves, as well as the NCUA's analysis, in order of priority to CUMIS. From the outset, CUMIS wishes to emphasize that we support the NCUA's overarching objectives and appreciate its willingness to take a fresh look at current credit union regulations.

Strengthening boards of directors' oversight of credit unions' fidelity bond coverage.

CUMIS supports actions to reduce incidences of fraud in credit unions by strengthening oversight requirements. NCUA rules already require a credit union board of directors to annually review the credit union's fidelity bond coverage. Parts 704 and 713 of NCUA rules require such a review to ensure the credit union's coverage is adequate in relation to the potential risks facing the credit union and minimum requirements set by the NCUA Board.

The NCUA's proposal includes a new paragraph in both parts, Section 704.18(b)(2) and Section 713.18(b)(2), containing new, mandated actions by boards of directors for both corporate and natural person credit unions that increases a board of directors' existing oversight responsibility.

CUMIS agrees that the proposed new requirements should "help ensure the board is addressing the adequacy of the coverage at all stages," rather than retrospectively. (p. 13) CUMIS fully endorses more active involvement by credit unions' boards of directors in overseeing credit union operations as a key factor in reducing the risk of loss. We believe these changes add an important layer of review over a credit union's operational risks in order to promote earlier discovery and reduce the overall incidence of employee dishonesty and fraud.

Board member oversight in the bond application or renewal process can reduce the risks of dishonesty and fraud so long as credit union directors engage in robust due diligence prior to application sign-off. At signing, a board member attests that to the best of his or her knowledge, the information provided is accurate. Directors insulated from credit union operations and who do not verify the accuracy of application answers are not positioned to provide information critical for insurance underwriting. Further, directors that do not engage in due diligence may miss opportunities to discover and timely report credit union employee dishonesty and fraud.

For the protection of the credit unions for whom CUMIS provides fidelity bond coverage, CUMIS depends on accurate attestations in the fidelity bond application process. To that end, CUMIS encourages the NCUA to enhance the proposal by including a requirement that credit unions have a roll-up certification process in place to assure board member due diligence prior to signing a fidelity bond application. CUMIS acknowledges that for some credit unions this type of process may present a significant administrative burden. As an alternative, an authorized senior executive employee could co-sign the application.

CUMIS supports the NCUA's goal to strengthen boards of directors' oversight of credit union fidelity bond coverage. While we remain concerned that a lack of board member due diligence could undercut the stated goal, we appreciate any additional steps taken to reduce the likelihood of employee dishonesty and fraud. Further, CUMIS is willing to work with the NCUA following this comment period to explore additional measures to strengthen the oversight of credit union's fidelity bond coverage.

Bond document filing clarification and requirement that all bond forms receive Board approval every ten years.

While CUMIS recognizes the reason for the NCUA's request to review previously approved bond forms at a set interval, practical challenges could arise to frustrate their objective. Under the terms of the proposal, it is possible that hundreds of bond forms will all sunset and be due for Board approval at the same time. Even under the best conditions, an onslaught of form reviews will challenge NCUA resources and could cause significant delays.

Further, as the proposal is written, if there is a delay in the NCUA's fidelity bond form approval, existing bond forms will be invalid and credit unions will be forced to seek other coverage if no approved form exists at the time of fidelity bond renewal. For credit unions, this could result in confusion, a lapse in coverage, or a loss of coverage if the replacement carrier does not provide similar product features. In addition, carriers could experience a significant loss of business if the NCUA is delayed in their review of bond forms.

To preserve some flexibility and prevent delays, CUMIS recommends the NCUA include language such as, "unless otherwise determined by the NCUA Board" to the proposed changes to §713.4(d). The addition would give the NCUA authority to deviate from the new ten-year approval mandate if exigent circumstances would cause bond form approval delays or other unforeseen hardships for the NCUA and credit unions. Such a provision would be particularly beneficial in the event of an extended government shutdown, for example, which could create timing issues that disrupt the scheduled bond form approval process.

Compared to current fidelity bond form approval requirements, the proposed rules provide very little flexibility for the NCUA. Practical realities may one day demand the NCUA have the authority to reevaluate form approval timing. Through the addition of the provision above, we believe such needed flexibility can be achieved while preserving the NCUA's goal to regularly approve fidelity bond forms.

Ensuring that there is an adequate period to discover and file fidelity bond claims following a credit union's liquidation.

CUMIS supports aims to ensure there is an adequate period to discover and file fidelity bond claims following a credit union's liquidation. More in line with industry standards, however, CUMIS supports a 12-month discovery period rather than the proposed two years.

CUMIS believes a 12-month discovery period would achieve the NCUA's goal of providing a liquidator with adequate time to discover and report losses. In addition, a 12-month discovery period may also incentivize liquidator action to prioritize the identification of claims during the liquidation process. As the investigation of claims of dishonesty and fraud can become more difficult with each day that passes, a shorter timeline would encourage timely action.

CUMIS notes that a mandatory reporting period is outside the norm for the fidelity bond industry and creates uncertainty from an underwriting perspective that would put upward pressure on costs. While the benefit of this requirement would go to only a small number of insureds, the cost would be borne by all.

Expressly permitting a natural person credit union's fidelity bond to include coverage for certain credit union service organizations (CUSOs).

CUMIS supports the NCUA's proposal to permit a natural person credit union's fidelity bond to include coverage for certain CUSOs. In addition, CUMIS appreciates the clarifications provided by NCUA's Office of General Counsel over the years regarding joint coverage under fidelity bonds.

Conclusion

NCUA's proposed rules reflect a focus on solving challenges NCUA has experienced over the past several years. CUMIS supports NCUA's efforts to identify effective solutions that do not unduly burden credit unions or unnecessarily drive up their insurance costs. We believe that orienting the proposals around addressing risk is the most effective way to forward NCUA's goals.

Thank you for the opportunity to comment on these very important issues. CUMIS looks forward to many more years of helping credit unions manage their risks so that they can thrive.

Sincerely,

Michael F. Anderson
Senior Vice President and Chief Legal Officer