January 22, 2019

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

RE: Comments on Proposed Rulemaking - Fidelity Bonds

Dear Mr. Gerald Poliquin,

I am writing on behalf of the California and Nevada Credit Union Leagues (Leagues), one of the largest state trade associations for credit unions in the United States, representing the interests of more than 260 credit unions and their approximately 10.7 million members.

The Leagues support the NCUA Board's (Board) efforts to protect the National Credit Union Share Insurance Fund (NCUSIF). However, we believe the proposed rule creates undue burden on federally insured credit unions (FICUs) and their volunteer board and supervisory committee members. We respectfully offer the following comments on the proposed rulemaking for Fidelity Bonds.

Scope – Part 713.1

Part 713 is made applicable to all federally insured, state-chartered credit unions (FISCUs) through Part 741.201 of the NCUA's regulations. The proposed rule would: add the words "federally insured" before the words "credit union;" cross reference the requirement in Part 741; and refer to FICUs throughout the rule instead of federal credit unions. The Leagues support the proposed amendments as they will enhance clarity and more accurately describe which credit unions are subject to the Fidelity Bonds rules.

Board of Directors Responsibilities – Part 713.2

The Leagues agree with and support the current rule's requirement that a FICU's board annually review its fidelity bond and other insurance coverage to ensure it is adequate. We also agree that a FICU's board should be informed and provided with any information necessary to fulfill this role.

We do not support the proposal that would require a FICU's board, and, if applicable, a FICU's supervisory committee, to review all applications for purchase or renewal of bond coverage and to pass a board resolution approving the purchase or renewal.

The bond purchase process is a highly technical, involved, and operational process. As such, in depth involvement by the board is not appropriate. Involving the board or supervisory committee in operational processes distracts from the board's oversight role in establishing controls and monitoring enterprise risk as well as the supervisory committee's role of ensuring safety and soundness.

FICU boards should have a strong understanding of enterprise risk management, of which the fidelity bond coverage is just one component. Instead of looking at the root cause of fraud losses, the proposed rule creates additional administrative work and regulatory burden.

The proposed rule would also require a FICU's board to delegate one board member, who is not an employee of the FICU, to sign the attestation for bond purchase or renewal and also prohibit the same board member from signing consecutive purchase or renewal agreements for the same fidelity bond coverage policy. The Board's reasoning for this is that if the signatory to an application for purchase or renewal is knowledgeable of fraudulent activity, the bond issuer may void the policy and not make a payout when losses are discovered.

The Leagues do not support this proposed amendment. We believe the Board's analysis is flawed and seems to intentionally circumvent "knowledge." Any person who signs the attestation should be in a position to know.

Further, if a FICU is transparent with their board, they will disclose potential problems; thus, board members should have knowledge. The proposed rule could have the unintended consequence of FICUs not fully disclosing potential issues to their boards.

The proposed board and supervisory committee requirements also exacerbate they already difficult task of attracting unpaid, volunteer board members. Increased complexity and liability can result in making individuals even more hesitant to volunteer on boards.

Required Bond Coverage – Part 713.3

The Leagues do not support the proposed requirement that FICUs have fidelity bond coverage that includes an option for the liquidating agent, in an *involuntary* liquidation, to purchase coverage that extends the discovery period for at least two years after liquidation.

The Leagues believe the proposed change will result in increased costs for all FICUs. Due to the increased risk to insurance companies, it is likely the fidelity bond policy costs will also increase.

We are also concerned with the availability of such bond policies. We believe it is likely that CUNA Mutual Group (CMG) would, if it were an NCUA requirement, implement the extended discovery period option in their fidelity bond policies. This is due to their closely defined credit union customer base. However, it is possible that other insurance companies would not implement such an option and that would reduce competition and an FICU's ability to shop other insurance companies.

Further, we believe a 24-month discovery period seems excessive. Typically, if a person is given a deadline, then it is easy to put off action until that deadline is imminent. A shorter time frame would require that claims are submitted in a more expeditious manner. If the Board decides to move forward with an extended discovery period option, we recommend the Board first consult with the insurance industry, including CMG, to determine industry standards.

For *voluntary* liquidations, the proposed rule would require that a FICU's fidelity bond coverage remain in effect, or provide that the discovery period is extended, for at least four months after the final distribution of assets. This is currently required for federal credit unions in Part 710, the NCUA's voluntary liquidation regulations. For clarity purposes, the Leagues support placing this current requirement for FCUs in the fidelity bonds rule. However, we do not support adding this requirement for FISCUs, as the NCUA is not the liquidating agent for FISCUs. Voluntary liquidation is accomplished in accordance with state law or procedures established by the state regulatory authority.

The Leagues do support the NCUA codifying a 2017 NCUA Office of General Counsel legal opinion that permits a natural person credit union's fidelity bond to include coverage for certain credit union service organizations (CUSOs). This is permissible if the FICU owns greater than 50 percent of a CUSO it wishes to cover, or a covered CUSO is organized by the FICU for the purpose of handling certain of its business transactions and composed exclusively of its employees. We agree that incorporating the 2017 legal opinion into Part 713 will improve clarity and ease of reference.

Bond Forms – Part 713.4

The current rule provides that the NCUA will maintain a current list of bond forms approved by the Board for use by FICUs. The rule also states that a FICU must obtain the approval of the Board before it can use any other basic bond form or any rider or endorsement that limits coverage of an approved bond form.

The Board is proposing to sunset its approval on all bond forms ten years after the form is approved. With respect to bond forms that the Board has approved before 2019, the Board is proposing to allow its approval on these forms to continue until January 1, 2029.

The Leagues have concerns with the proposed 10-year sunset for approved forms from a process standpoint. It is our understanding that before a form is submitted to the NCUA, insurance providers submit the forms for approval to all 50 states. In the event the NCUA rejects a form, an insurer must amend their form and resubmit it to all 50 states for approval once again. Adding NCUA's review adds another layer of complexity and creates a huge burden and process delays.

Additionally, if NCUA's approval sunsets on all current forms on the same date, January 1, 2029, does the

NCUA have the resources and processes to review this volume, provide insurance providers sufficient notice to make amendments and seek approval from all 50 states, and ensure new, approved forms are available before the sunset date? Are there processes in place to ensure there is no window of time in which approved forms would not be available? At a minimum, we recommend the NCUA include a qualifier to the sunset deadline, such as a form's approval will sunset on that date "unless otherwise determined by the NCUA". This will prevent approvals from expiring simply because the NCUA has not yet made their determination or allowed sufficient time for insurance providers to complete their requirements.

Conclusion

The Leagues thank the Board for its continued efforts to protect the NCUSIF. However, we believe the proposed rule creates unnecessary regulatory burden for FICUs.

We thank you for the opportunity to comment on the proposed rule and for considering our views and recommendations. If you have any questions regarding our comments, please contact me.

Sincerely,

Diana Dykstra
President and CEO
California and Nevada Credit Union Leagues

cc: CCUL