

Exam Appeals: Credit Unions Deserve A Better Process

If 2015 is a “year of regulatory relief” for NCUA, credit union officials are not feeling any less burdened. In fact, credit union officials tell me they are increasingly anxious as examiners receive even more discretion, such as through the final risk-based capital rule, the final fixed asset rule, and the proposed member business lending rule. All the while a credit union’s ability to appeal an exam directive remains as futile, ineffectual, costly, and fraught with risk as ever.¹

The agency’s exam appeals process is discussed in the “Review Of NCUA’s Examination And Complaint Processes For Small Credit Unions,” Report #OIG-12-10, August 31, 2012, which was produced by the NCUA Office of Inspector General (OIG) in response to a request from the Senate Banking Committee. The report found serious flaws in the agency’s record keeping as it relates to appeals but was able to ascertain that from 2007 through 2011, a yearly average of only six credit union “complaints” to their regions regarding exams were filed. Only two such appeals made their way to NCUA headquarters during that period. In 2011, NCUA supervised over 7,000 credit unions. What accounts for such a low number of exam appeals, particularly during the financial crisis? Is it the result of examiner performance or were other factors present? A murky process? Fear of retaliation?

What is Wrong with NCUA’s Process

What our process is and what it should be are just not the same.

The 2012 NCUA OIG report described NCUA’s Appeals Process:

...NCUA has an appeals process where credit unions can question examination results through informal and formal channels. Specifically, NCUA has in place a two-tiered appeal process which encourages that disputes over examiner determinations get resolved at the regional office level and at the central office level through the SRC² (Supervisory Review Committee, parenthesis added).

Such a process might indeed produce an objective procedure in which credit union officials feel free to disagree with and challenge exam results without reproach and without sensing that the deck is stacked against their claim, yet credit union officials say this is not the reality. Credit union officials who speak to me feel they can't even present reasonable alternatives or dispute exam conclusions, much less actually seek a review.

¹ For additional insights and information, see: Hill, Julie Anderson, When Bank Examiners Get it Wrong: Financial Institution Appeals of Material Supervisory Determinations, Washington University Law Review, Vol. 92, 2015.

² NCUA’s SRC is a three-person review panel that should be available to review CAMEL ratings of 3, 4, and 5 and their component ratings; the adequacy of ALLL provisions; loan classifications on significant loans and denials of technical assistance grants. Other regulators permit more types of issues to be reviewed by their SRC. Also, unlike other regulators, NCUA does not address the standard of review regarding its appeals process.

These directors and officers also express their uncertainty about how the appeals process actually works in practice.

The OIG report recommended that the agency develop a better system of reporting determinations at the regional level and an electronic system to document any SRC decisions. It is unclear how even these modest recommendations have been fully addressed by the agency.

The NCUA Must Address CUs' Rights Appeal Now

I support appropriate supervision and the full measure of enforcement for bad actors, but every credit union that reasonably concludes an exam directive is inappropriate should be entitled to challenge that directive in a cost effective manner and without fear of retaliation. NCUA must have an open and fair process that allows for such challenges and provides each credit union an appropriate level of due process, consistent with our Constitution, the Federal Credit Union Act, and other applicable law.

Two bills are pending in Congress to improve supervisory appeals for credit unions and banks, S. 774 and H.R. 1974, both of which NCUA and other regulators oppose. A key provision in those bills is an independent process under which a credit union or bank could challenge a supervisory material determination from an examiner and receive a timely review from a third party at the Federal Financial Institutions Examination Council, outside of the reach of retaliation from its prudential regulator. These bills would amend the Riegle Community Development and Regulatory Improvement Act of 1994, which already requires NCUA to maintain the SRC (and an ombudsman, which NCUA describes as the "public's voice to NCUA leadership").

I support these bills, which would not even be on the table if we were faithful to what I believe Congress intended. Yet, NCUA does not have to wait for a new law to make its appeals process better.

Recommendations for NCUA Action

NCUA on its own authority, right now, could develop a much more open and user-friendly appeals process by taking some simple steps:

- Seek general comments from credit unions and other stakeholders through an Advance Notice of Proposed Rulemaking on the flaws in and improvements to our appeals process; NCUA Interpretive Ruling and Policy Statement 11-1, as amended, could serve as a starting point.
- Use those comments to develop a new proposal on exam appeals that articulates the kinds of issues that may be reviewed and the procedures for the review.
- Allow credit unions and other stakeholders to comment and respond to the comments by modifying the final rule as needed; revisit the final rule as part of NCUA's rolling regulatory review.

Among other issues, the final rule should address:

- All of the rights of a credit union in challenging examiner findings and directives, including the use of counsel and other advisors.
- The right of all credit unions to representation by counsel and other advisors in all appeals proceedings, including those before the NCUA Board.
- The right of all credit unions to receive a timely written determination of all appeals proceedings, including those before the NCUA Board.
- A requirement that the NCUA examiner must provide a list to the credit union, along with the written exam report, of all the authorities relied upon to support directives, and respond to credit unions' questions regarding those authorities. As practical, NCUA examiners should also provide other information relied upon as well as data sources.
- A requirement that NCUA staff provide regular reports to the NCUA Board in a public meeting and to the credit union community and public on the use of the appeals process, including the number of appeals, issues appealed, length of time each appeal took, and how the issues were resolved. The reports should also include appeals to regional directors as well as to the SRC.
- That the NCUA Board should appoint all members of the SRC and the ombudsman.
- That the SRC and the ombudsman should report to the NCUA Board quarterly, and
- That the NCUA ombudsman should not serve on the SRC.

NCUA Should Have an Exam Outreach Officer

In addition, the NCUA Board should designate a senior executive as an outreach officer who will contact credit unions that have just completed an examination to obtain retaliation-free feedback from them regarding their experience. The outreach officer should report directly to and provide the NCUA Board with quarterly reports on his or her findings and analysis. NCUA should utilize the information from that outreach and undertake periodic short surveys to credit unions on examinations to develop recommendations that are incorporated into future exam appeals proposals to continually improve our process.

NCUA Should Revisit Examiner Training and Provide A New Appeals Process Resource Webpage

More must be done within NCUA's examiner training programs to promote a culture of tolerance and respect for credit unions throughout their exam and any appeal. In addition, NCUA should make all information regarding appeals – including the reports of the outreach officer made to the NCUA Board – accessible in a fully transparent manner on a separate NCUA web page.

The credit union community, rightly so in my view, has grown exceedingly weary with the agency's failure to address the glaring inadequacies in its appeals process. That the appeals process offered by other regulators of financial institutions also remains deficient should not offer NCUA a justification for inaction. The NCUA Board's job is not merely to follow the script set by other financial regulators, but to lead and set the standard of transparency and accountability for all such regulators.

NCUA Really Should Have an Advisory Council

As I have often stated, one of the most important steps NCUA could take to address regulatory relief and examination issues would be to establish a credit union advisory council. In fact, NCUA is the only federal financial institution regulator that does not utilize the talents and expertise of such a council, as the Federal Deposit Insurance Corporation has an Advisory Committee on Community Banking, the Federal Reserve Board has the Community Depository Institutions Advisory Council (and the Federal Reserve Banks have their own councils), the Consumer Financial Protection Bureau has the Community Bank Advisory Council, and the Office of the Comptroller of the Currency has the Mutual Savings Association Advisory Committee and Minority Depository Institutions Advisory Committee. I continue to urge the agency to follow suit and not remain a regulatory outlier.

Meanwhile, it is not beyond NCUA to provide a fully functional exam appeals process that does not dictate outcomes or block challenges, but affords robust transparency and due process rights, without the use of ex parte hearings where neither credit unions nor their counsel participate. By law, credit unions should be able to present their concerns in a timely manner before an impartial forum and in my view, accompanied by counsel, with the expectation that right-sized solutions will result, and without retaliation or the appearance of impropriety. Credit unions may not always prove to be right in their appeal, but our process must not preordain that they are always wrong, either.

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