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National Association of Federally-Insured Credit Unions

April 1, 2022

Melane Conyers-Ausbrooks
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

RE: Succession Planning (RIN: 3133-AF42)

Dear Ms. Conyers-Ausbrooks:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing in response to the National Credit Union Administration's (NCUA) proposed rule that would require federal credit union (FCU) boards of directors to establish and adhere to processes for succession planning. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve 130 million consumers with personal and small business financial service products. NAFCU does not support this proposed rule, as it is burdensome and unnecessary to ensure the safety and soundness of the credit union system. Instead of a rulemaking, NAFCU recommends that the NCUA consider issuing guidance, conduct a new market analysis on the correlation between poor management succession planning and consolidation, and adding more resources that will assist credit unions in succession planning.

General Comments

Succession planning is the process through which an organization identifies, develops, and retains key personnel to ensure its viability and continued effective performance. It allows an organization to prepare for the unexpected and is a valuable part of a credit union's overall strategic plan. The relevance of succession planning has increased due to the decline in the number of credit unions, mainly resulting from the long-running trend of consolidation across all depository institutions for the last three decades. Another reason for a focus on succession planning is the ongoing retirement of the "Baby Boomer" generation, which has accelerated during the COVID-19 pandemic. Succession planning is critical to the continued operation of those credit unions with board members and executives who are part of this retirement wave.

Despite the benefits of succession planning, this proposed rule may have negative impacts on some credit unions through the imposition of an additional regulatory burden. There are a number of credit unions that already have succession plans in place, with many updating them recently as a consequence of the COVID-19 pandemic. The NCUA imposing this mandatory process on credit unions serves as another regulatory administrative process that is unlikely to improve governance or have the desired outcome of substantially reducing the consolidation trend. Rather than focusing

on a rule on succession planning, the NCUA should be focusing on promoting the strength of the National Credit Union Share Insurance Fund, which will lead to a stronger credit union industry that is able to focus on the needs of their communities.

Regulation Should be Effective and Not Excessive

NAFCU agrees with Board Member Hood’s sentiment that “regulation should be effective and not excessive.”¹ NAFCU understands the importance of regulation through rulemaking and supports a safe and sound credit union system. In the case of succession planning, mandatory compliance with this rule has the potential to impose a significant burden on credit unions. Board Member Hood, in his statement on the proposed rule, said that it is not the NCUA’s responsibility to micromanage credit unions. NAFCU agrees. The credit union system is diverse and made up of different sized credit unions that all serve different communities, making a one-size-fits-all rule that affects the strategic plans of all FCUs excessive and unnecessary.

The NCUA has expressed that by implementing this rule the issue of increasing consolidation will be resolved and smaller credit unions will be preserved. However, a rulemaking that increases the regulatory burden and compliance costs for smaller institutions could actually lead to further consolidation. Credit unions are best suited to make their own management decisions and will do so without regulation from the NCUA. The NCUA should not substitute its own judgment for that of credit union management, as only an individual credit union can determine the appropriate timing and extent of succession planning needed to preserve the health of the credit union and its members.

The proposed rule further states that an NCUA analysis found that poor management succession planning was either a primary or secondary reason for 32 percent of credit union consolidations, meaning it was not a primary or secondary factor in roughly two-thirds of mergers, and there was no insight into how relevant a “secondary reason” was in the decision. This suggests that increased succession planning may not address the issue the NCUA is seeking to resolve. Moreover, the analysis was conducted on data collected from 2003-2013. This analysis concluded nearly a decade before the publication of this proposed rule, and includes the years immediately following the financial crisis and passage of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, which was undoubtedly a compounding factor in credit union consolidation. NAFCU suggests that the NCUA conduct further market analysis on current data before pursuing a rulemaking.

Much of the proposed rule discusses purported benefits to smaller credit unions. The proposed rule explicitly states that the NCUA considers smaller credit unions to be those with under \$100 million in assets and that those with less than \$10 million in assets will be the primary beneficiaries of this proposed rule. However, mandatory requirements through a rulemaking may not achieve the goal of helping smaller credit unions. The development of mandatory plans does not guarantee the plans will be effective or even relevant when a succession event occurs, nor does it guarantee that these

¹ NCUA Board Member Rodney E. Hood Statement on Proposed Rule, Part 701, Succession Planning (January 2022). <https://www.ncua.gov/newsroom/speech/2022/ncua-board-member-rodney-e-hood-statement-proposed-rule-part-701-succession-planning>.

will influence decisions regarding consolidations. If anything, the NCUA should be revising its definition of smaller credit unions based on current economic conditions. The COVID-19 pandemic and resultant government stimulus have dramatically increased inflation rates. Therefore, NAFCU recommends that the NCUA revise its definition of small credit union to those with less than \$250 million in assets to adjust for inflation and the changing economic environment.

Compliance with rulemakings can often be burdensome for smaller credit unions; if this proposed rule becomes final, credit unions will have to create a succession plan that fits the final rule's requirements by a mandatory effective date. Smaller credit unions will likely have to find outside resources to assist them in compliance with the proposed rule. Smaller credit unions may only have a few employees in total, and the time it takes to draft succession plans could be better spent serving their communities.

NAFCU's members have expressed that creating a succession plan will require a lot of work from their employees and, in some cases, they may be required to bring in a third party to help them comply. The agency's estimate that compliance with the rule can be achieved, in most instances, in 30 minutes or less, is aspirational at best. The process for credit unions to closely evaluate their pool of management to identify key individuals, then develop comprehensive succession plans will generally take days, if not weeks or longer, to finalize. The contention that a smaller credit union would have a simple succession plan ignores the complexity and sensitivity involved in developing a succession plan. In fact, a smaller credit union would be more susceptible to having to execute an emergency succession from a smaller pool of potential candidates. The goal should be to develop an environment where credit unions can thrive by eliminating costly rule requirements, minimizing and streamlining examination processes, and supporting business judgment. Such efforts would do more to achieve successful succession planning than a rule requiring a written document to be evaluated by examiners.

The proposal also requires credit union boards of directors to conduct an annual review of the succession plan, which likely will not have significant year-to-year changes. This part of the proposal is also burdensome, excessive, and a waste of examiners' time. Even if this proposal were to become a final rule, requiring the succession plan to be reviewed yearly is not helpful to any party involved. Succession plans are not a dynamic and ever-evolving document and, therefore, should only be reviewed as needed; credit unions have shown themselves to be trustworthy and able to make that decision on their own.

Parity with Bank Succession Planning Requirements and the Existing Regulatory Framework

Bank regulators have issued guidance instead of a rule on succession planning, and this guidance provides greater certainty to institutions based on their size and complexity than the NCUA's proposed rule. This guidance on corporate governance from the Office of the Comptroller of the

Currency² (OCC) and the Federal Deposit Insurance Corporation³ (FDIC) suggests that succession planning should be a regular topic of discussion among the financial institution's board of directors. The OCC describes the benefits of succession planning as "stability in tumultuous financial times" and a way to "lessen the influence of dominant personalities and behaviors." The OCC suggests different ways of succession planning for smaller and larger institutions. It suggests that smaller banks consider increasing the formality of management training programs, development, and talent identification; while suggesting that larger institutions develop a talent pool of employees who have the necessary qualifications, skills, experience, and exposure to the board and senior management. Some of NAFCU's members have expressed that rather than a succession plan, their credit unions have adopted a talent review process that serves to highlight and develop team members so that they are creating more real value over time.

In its guidance, the FDIC explains that a succession plan is "a valuable tool to build bench strength and maintain continuity" in the key management positions, as well as a means of "identifying potential successors from outside the organization, when necessary." The OCC and FDIC each provide banks with suggestions that may benefit them, but do not specify any mandatory requirements. NAFCU suggests that the NCUA follow the lead of the FDIC and OCC and issue similar guidance that will assist credit unions, if needed, but leave the decision of creating a succession plan to the credit unions themselves.

Additionally, examiners should already be doing a high-level evaluation of a credit union's succession planning as it is a part of the management component of the CAMELS rating system, which makes this rulemaking redundant. Similarly, the OCC and FDIC also require their examiners to do a high-level assessment of banks' succession planning in their rating of the capability and performance of management, as well as the risk management component of their rating system. According to Appendix A of the NCUA's CAMELS Rating System, when assessing the management of a credit union, examiners should consider the succession planning for "key management positions."⁴ That the existence of succession planning is already being evaluated in a credit union's CAMELS rating further obviates the need for this proposed rule.

Impact on Examinations

This proposed rule explains that examinations would simply confirm the existence of a succession plan and defer to a credit union's self-assessment of its succession planning needs. If this is the case, then this burdensome rulemaking would have little practical effect since examiners would be told to defer to a credit union's self-assessment regardless of the quality or thought. However, based on historical examination trends, NAFCU predicts that examiners will vary with how much

² *Corporate and Risk Governance, Comptrollers Handbook* (July 2019). <https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-handbook/files/corporate-risk-governance/pub-ch-corporate-risk.pdf>.

³ *Supervisory Insights: Special Governance Edition* (April 2016, Revised October 2018). <https://www.fdic.gov/regulations/examinations/supervisory/insights/sise16/si-se2016.pdf>.

⁴ *Appendix A – NCUA's CAMELS Rating System (CAMELS)*. <https://www.ncua.gov/files/letters-credit-unions/camels-rating-system-appendix-a.pdf>.

time, evaluation, and weight they give to reviewing a credit union's succession plan, especially because examiners are not the same from year to year as well as different across regions.

Consistency in exams has long been an issue for NAFCU's members. According to NAFCU's October 2021 *Economic & CU Monitor*, over 85 percent of respondents showed some level of concern about exam consistency. In NAFCU's November 2020 *Economic & CU Monitor*, NAFCU's members suggested that examinations are sometimes inconsistent due to inconsistencies amongst the approaches taken by individual examiners; credit unions have found that examination findings often differ based on examiners.

Alternatives to a Rulemaking and Additional Clarifications

While NAFCU does not doubt that succession planning is helpful for credit unions, a rulemaking is not. Instead, NAFCU suggests that the NCUA add resources that will assist smaller credit unions in developing succession planning. Like the two-part video series available on the NCUA's YouTube channel titled "Board of Directors Video Series 4: Succession Planning," the NCUA can create more videos and webinars aimed at assisting credit unions in their succession planning efforts. The NCUA should also offer succession planning webinars with outside experts, as well as guidance letters to credit unions.

The NCUA could also determine the existence of succession planning at credit unions by asking the question on the Call Report form. The Call Report is a way for credit unions to report to the NCUA a big picture of what is going on at their credit union and to document any potential risk areas. Call Reports must be submitted quarterly, so the NCUA will always have up-to-date information on a credit union's succession planning. Examples of questions that may be asked on the Call Report are "Does your credit union conduct succession planning? The NCUA's suggested timeframe for compliance with this rule, and the self-assessment, lead to a check-the-box analysis of compliance rather than a full rulemaking that would require examiners to delve deeper into its compliance. Therefore, credit unions checking the box on a Call Report would suffice.

Should the NCUA proceed with this rule on succession planning, NAFCU requests clarification on several critical issues. First, although NAFCU recognizes that deferring to credit unions to decide the management positions that must be accounted for in a succession plan provides necessary flexibility, NAFCU's members are concerned about the lack of specificity and clarity in the proposed rule and what this may mean in terms of examiner review of their succession plan. Accordingly, NAFCU recommends that the NCUA provide clarity around this definition. Credit unions do not want to have to guess what the NCUA means, risking being incorrect and being penalized in examinations for not identifying the appropriate management positions that need to be included in a succession plan. Guessing what positions the NCUA deems to be "key management" positions can be burdensome for larger credit unions. For example, one of NAFCU's members reported that this would mean developing a succession plan for 19 of its positions, which would be very time-consuming, expensive, and more importantly excessive.

The proposed rule is also vague about the idea of requiring a credit union's board of directors to have a "working familiarity" with the credit union's succession plan. The proposed rule further explains that training is not mandated to meet this requirement, which causes this requirement to be vague and subjective. Vagueness and subjectivity in a requirement of the rule can lead to inconsistencies in the examination process, leaving the door open for credit unions to have a different understanding than the examiners and examiners to have differing understandings from each other. The proposed rule is also unclear about the potential impact on a credit union if an examiner determines a credit union's succession plan to be inadequate. NAFCU urges the NCUA to be clear about what it expects of credit unions in terms of meeting requirements so that all examinations are consistent. Additionally, NAFCU emphasizes that it is unrealistic to expect potential board members to attend twelve meetings a year, perform functions such as reviewing and approving every policy and procedure issued by the credit union, and maintain the increasing level of education required by this portion of the proposed rule when these are volunteer positions and only one board member is allowed to be compensated for their time and effort.

NAFCU also recommends that the NCUA provide clarity on the next steps a credit union should take if it is not able to adhere to its succession plan, which could happen under a number of circumstances. As the past couple of years have taught us, unprecedented times cause unexpected events to occur. Plans may not always be able to be adhered to and new challenges or changing circumstances may arise before a plan can be made or before a credit union can adjust its formal plan to meet these changes. Credit unions should not have to guess what the NCUA expects of them when an unexpected situation arises. If the NCUA is to finalize a rule on succession planning, that rule must be very clear about what to do in unexpected situations.

Conclusion

NAFCU does not support this proposed rule as it is excessive and unnecessary to ensure the safety and soundness of the credit union system. Instead of a rulemaking, NAFCU recommends that the NCUA further study the relationship between succession planning and consolidation, issue guidance on succession planning, and adding more resources that will assist credit unions in succession planning. If you have any questions or concerns, please do not hesitate to contact me at (703) 842-2268 or amoore@nafcu.org.

Sincerely,



Aminah M. Moore
Regulatory Affairs Counsel