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National Association of Federally-Insured Credit Unions

March 26, 2020

The Honorable Rodney E. Hood, Chairman
The Honorable Todd M. Harper, Board Member
The Honorable J. Mark McWatters, Board Member
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

RE: Additional Examination and Regulatory Relief Due to COVID-19

Dear Chairman Hood and Board Members Harper and McWatters:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I write to request assistance from the National Credit Union Administration (NCUA) in regulatory flexibility to credit unions grappling with the COVID-19 pandemic. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve nearly 120 million consumers with personal and small business financial service products. Lawmakers are working tirelessly to provide relief to American consumers and industries amid this public health and economic crisis. The NCUA should take steps to cease all examination activity unless critical to the safety and soundness of the institution and adopt other regulatory adjustment to alleviate some of the strict compliance requirements for various products and services. Such measures are necessary to preserve the health of the credit union industry as many institutions are struggling to provide their members much needed assistance during this time of uncertainty and hardship.

Cease Examination Activities

The NCUA should revise its approach to supervision and examination of the credit union industry during this unprecedented time. On March 24, 2020, the Board of Governors of the Federal Reserve System (Federal Reserve) announced that it would change its focus on examinations and inspections during the COVID-19 outbreak to help minimize disruption and burden on financial institutions.¹ The Federal Reserve aims to conduct all examination activities off-site until further notice and cease all regular examination activity for those institutions under \$100 billion in assets, unless doing so would pose a safety and soundness concern or an urgent matter requires attention.

NAFCU requests the NCUA issue a statement adopting a similar approach for the credit union industry. NAFCU does not support an arbitrary asset threshold as the deciding factor for which institutions receive an off-site examination versus no examination at all, but instead urges a risk-based analysis and approach to deciding whether safety and soundness concerns or another urgent need demands an examination now instead of deferring to later in the year. Although the NCUA's

¹ Federal Reserve Statement on Supervisory Activities (Mar. 24, 2020), <https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20200324a1.pdf>.

recent Letter to Credit Unions 2-CU-02 and updated FAQs indicate that the NCUA will be focused on off-site examinations through its secure information exchange portal, it is not only information requests, but rather the entire examination process that may pose substantial burdens for credit unions.

Credit unions have had to shift their strategies to accommodate this public health crisis by adopting flexible telework policies, closing branches, and enhancing online banking platforms. In the midst of the COVID-19 pandemic, those credit unions scheduled for an examination may be facing a multitude of challenges, including technological issues that can make the process more time-consuming and burdensome. For example, a credit union in a rural area may face the challenge of having several of its staff members who are responsible for submitting examination documentation working with limited internet access. Staff may be using a hotspot on their mobile phone for faster internet connection in these rural areas, but this hotspot connection is still slower compared to the internet service within the credit union branch. Thus, as many credit union staff members are working remotely and taking care of children home from school, the examination process will prove to be more burdensome.

Considering all credit unions across the country are affected, to some extent, by COVID-19, this extraordinary situation warrants a pause on examination activity until the fall of 2020 to allow credit unions an opportunity to focus on working with and meeting the needs of their members. Absent substantial safety and soundness concerns or other urgent circumstances, the NCUA should cease examination activity to align with the Federal Reserve's recent guidance.

Additional Regulatory Relief

The NCUA should also provide several relief measures aimed at simplifying the regulatory hurdles associated with loan modifications, appraisal requirements for mortgages, and limitations on carrying and charging off negative balances. These changes would help hard working Americans who may be furloughed or laid-off now as a result of the COVID-19 pandemic.

Troubled Debt Restructurings (TDRs)

NAFCU appreciates the clarification in the recent interagency guidance on loan modifications and TDRs. Moreover, the *Coronavirus Aid, Relief, and Economic Security Act* (CARES Act) provides the NCUA with broad authority to suspend Generally Accepted Accounting Principles requirements with respect to loan modifications related to COVID-19 that would otherwise be categorized as TDRs. Despite this additional flexibility, credit unions still anticipate a substantial uptick in TDRs because some businesses and consumers will likely not be able to recover sufficiently to resume normal payments within the next six months. To further ease compliance requirements for loan modifications, the NCUA should reinterpret the capitalized interest section of Part 741 Appendix B to be consistent with the requirements of Fannie Mae and Freddie Mac, the government-sponsored enterprises (GSEs) and the other banking regulators.

Currently, in order to make a TDR modification work for the member, the credit union must pursue one of the following options: (1) collect interest current at the time of modification, which causes

additional hardship for the member, especially as many Americans have now lost their jobs; (2) forgive the interest, which harms the credit union, making it more difficult to loan to other members and creates potential tax ramifications for the members; (3) defer the interest until the end of the loan term, which creates a balloon payment for the member and could cause additional hardship; or (4) adjust the amortization on the loan and bifurcate it to create a modified rate component and a zero-interest component, which is confusing for the member and poses operational challenges for the credit union as many systems are not designed to easily incorporate such an adjustment.

Many of NAFCU's members' loan systems are generally modeled to work based on GSE practices, which means they assume a re-amortization with capitalized interest. Re-amortizing a loan without capitalizing the interest is not currently possible and would require the establishment of two different loans for the borrower: one to repay the outstanding principal balance, and one at a zero percent interest rate to repay the interest owed. Taking these steps as many examiners have required of credit unions during the latest examination cycle, creates additional documentation burdens and confusion for the borrower. This complicated bifurcation also creates servicing and monitoring challenges for the credit union in addition to complicating the net present value process used to create the required loan loss reserve at the time of modification and in future periods.

In the current environment, all four options listed above would have detrimental effects on American consumers during a time of significant uncertainty while the nation faces a pandemic and economic crisis. The time is now for the NCUA to take drastic measures to alleviate as many operational challenges for credit unions and potential confusion and hardship for borrowers. The focus should be on the overall safety and soundness of the industry while ensuring that credit unions have as many tools available to them as possible to quickly help their members. Accordingly, the NCUA should reinterpret the capitalized interest section of Part 741 Appendix B to permit credit unions to modify loans to help borrowers in need.

Residential Real Estate Appraisals

As COVID-19 continues to spread, many states across the country have issued "shelter in place" orders and closed non-essential businesses. This has had an impact on credit unions seeking to comply with the NCUA's appraisal standards in Part 722.4, particularly with respect to residential real estate appraisals of the interior of homes. Many appraisers are not comfortable entering a borrower's home right now given the risk of contracting COVID-19. The Federal Housing Finance Agency recently directed the GSEs to adopt flexible appraisal requirements through at least May 17, 2020 to accommodate this challenge. Alternative appraisal options include a "drive-by appraisal," whereby an appraiser may drive by a property to evaluate the neighborhood and surrounding homes to determine the value; a "desktop appraisal" where appraisers use public and private data about the home to determine an appraised value; or permitting appraisers to obtain pictures of the interior of the property from the borrower to use to conduct the appraisal.

Moreover, the Appraisal Standards Board of The Appraisal Foundation (tasked with developing, interpreting, and amending the Uniform Standards of Professional Appraisal Practice (USPAP)) issued 2020-21 USPAP Q&A on March 17, 2020, encouraging lenders, regulators, and

government agencies to “consider suspending or relaxing requirements for interior inspections during a national health emergency.”² The NCUA’s regulatory requirements for appraisals cite the USPAP.

NAFCU’s members who sell mortgage loans to the GSEs are struggling to meet the NCUA’s appraisal requirements during the COVID-19 pandemic. Some may not have the sale of more loans to the GSEs in their business plans, which means they must portfolio the loan and attempt to meet the NCUA’s requirements, with more and more appraisers refusing to conduct on-site appraisals. NAFCU urges the NCUA to heed the USPAP’s guidance and temporarily align its appraisal requirements with that of the GSEs’ recently announced changes through December 31, 2020 to allow credit unions relief and in completing these loans already underway.

The NCUA should also fast-track the finalization of its recently proposed rule amending Part 722 regarding appraisals for residential real estate loans, which raises the current threshold of \$250,000 to \$400,000 and establishes parity with bank appraisal requirements. This rule should be finalized as soon as practicable to provide credit unions and borrowers with further relief and an opportunity to more quickly purchase or refinance a home to lower payments during this uncertain and unstable time. This is particularly critical for credit unions right now, as the low rate environment has substantially increased demand from members for mortgage loans.

Negative Balances

The NCUA should also grant credit unions flexibility regarding carrying and charging off negative balances. As members experience significant hardship as a result of no longer having a job and a steady stream of income and struggle to make ends meet, it is likely that negative balances will become more common. Credit unions will have to cope with an increase in volume in such accounts and the need to convert these negative balances to loans and repayment plans. Given reduced staff, the unknown length of time consumers may need to wait for monetary assistance, and difficulties surrounding establishing loans and repayment agreements during social distancing, the current 45-day limit on carrying negative balances in Section 701.21(c)(3) should be extended.

The NCUA should permit credit unions to determine on a case-by-case basis whether an extension of this 45-day limit is warranted depending on the member’s circumstance. Additionally, the 60-day determination period for charge-offs in the interagency guidance attached to Letter to Credit Unions 05-CU-03 should be extended to allow credit union members more flexibility if they are facing extreme hardship due to the COVID-19 pandemic. NAFCU urges the NCUA to issue a clarification on these two items regarding negative balances to allow enhanced flexibility for Americans who have been hard-hit by the pandemic.

² The Appraisal Foundation, USPAP Q&A (Mar. 17, 2020), <https://appraisalfoundation.sharefile.com/share/view/s607dbda9e9b41cb9>.

Conclusion

NAFCU and its member credit unions urge you to act swiftly to address these issues as consumer hardships and economic realities have already started to impact credit union operations. Upcoming congressional action will also have a profound impact on the credit union industry, so any and all regulatory flexibility right now will prove to substantially ease the burdens that credit unions and their members will face in the coming months. Thank you for your attention to these important issues during this unprecedented time. If you have any questions or concerns, please do not hesitate to reach out to me directly, or Ann Kossachev, NAFCU's Director of Regulatory Affairs, at (703) 842-2212 or akossachev@nafcu.org.

Sincerely,

A handwritten signature in black ink, appearing to read "B. Dan Berger". The signature is stylized with a large initial "B" and a long horizontal stroke extending to the right.

B. Dan Berger
President and CEO