

**2017 League of Southeast Credit Unions  
Regulator Roundtable**

**ACUA**

**Sarah H. Moore, Administrator**

**Lloyd H. Moore, Assistant Administrator**

**Carrie Ellis McCollum, General Counsel**



# Overview

- Proposed Legislation
- Proposed Regulatory Relief
- Alabama's Consumer Credit Task Force
- CFPB's Proposed Rulemaking on "Payday, Vehicle Title & Certain High-Cost Installment Loans"
- Risk Alerts



## Background of Proposed Legislation to Extend Exam Cycle

- Current Law requires State Chartered Credit Unions to be examined annually
- ACUA and NCUA have historically conducted joint examinations of all state chartered credit unions with assets of \$250 million and greater and joint examinations of smaller credit unions on a sample basis
- NCUA's Exam Flexibility Initiative extends the exam cycle for low-risk credit unions



# Background of Proposed Legislation to Extend Exam Cycle

- NCUA will conduct examinations of state chartered federally insured credit unions no less than once every 5 years except for credit unions that meet any one of the following criteria:
  - Greater than \$1 billion in assets;
  - Composite CAMEL code 4 or 5 with assets greater than \$50 million; or
  - Composite CAMEL code 3 with assets greater than \$250 million
- NCUA examinations of these three categories of federally insured state chartered credit unions will generally begin between 8 and 12 months from the completion of the prior exam



## Background of Proposed Legislation to Extend Exam Cycle

- Of Alabama's 62 state chartered credit unions, 60 are federally insured and 57 are less than \$1 billion in assets and would be subject to the extended exam cycle by NCUA if the other criteria were met.
- State chartered federally insured credit unions would not be on parity with federally chartered credit unions if Alabama's law was not changed; and
- ACUA would need to increase staffing significantly if the law is not changed.



## Current Status of Legislation

- Senate Bill 27 is sponsored by Senator Quinton Ross of Montgomery and proposes to extend the required examination cycle of state chartered credit unions from annually to at least every 18 months.
  - Passed Senate
- Matching or Companion bill House Bill 167 is sponsored by Representative Marcel Black of Tuscumbia
  - Passed House Financial Services Committee
  - Senate Bill 27 passed the House Financial Services Committee and will be substituted for HB 167
  - Expected to be passed and signed into law by the Governor with an effective date of no later than July 1, 2017.



# Proposed Regulatory Changes in 2017

- ACUA's regulations have not been updated in a number of years
- We conducted a detailed review of all regulations and identified many modernization opportunities in the regulations
- We prioritized changing regulations that would immediately provide regulatory relief to credit unions



# Proposed Regulations for Review and Comment

- **Allowance for Loan and Lease Losses**
  - Current Regulations require ALLL in accordance with GAAP although Call Report instructions only require GAAP for Credit Union's with assets greater than \$10 million
  - Proposed Regulations would require ALLL with \$10 million or less to reserve for expected losses rather than GAAP – conform to Call Report requirement
- **Limits on Loans and Investments in CUSO**
  - Current Regulations require an annual audit of any CUSO in accordance with GAAS
  - Proposed Regulation would eliminate the audit requirement for CUSOs consolidated into the audited financial statements of a credit union
  - Proposed Regulation would require an audit if the CUSO is not consolidated into the audited financial statements of the credit union and the investment plus loan to CUSO exceeds 2% of the assets of the credit union.





# Proposed Regulations for Review and Comment

- **Limits on Loans and Investments in CUSO**
  - Proposed Regulation adds to the list of preapproved activities of CUSO's the power to perform foreclosure and repossession services.
- **Filing of Group Return Form 990 with IRS**
  - Deletes the section in its entirety as it is outdated and no longer allowed
- **Credit Union Ownership of Fixed Assets**
  - Current Regulation limits a credit union's ownership of fixed assets to 5% of shares, deposits and retained earnings
  - Proposed Regulation deletes the 5% limit – conforms to NCUA rules and regulations



## Process for Comment

- Interested parties have until April 15, 2017 to submit comments to ACUA on the proposed regulations.
- ACUA will review and evaluate your comments to determine if changes are needed to the proposed regulations.
- If changes are not made to the proposed regulations, then the regulations will become effective on April 16, 2017.



## Areas for Future Proposed Changes

- Vendor Risk Management
- Appraisal section needs to be reworded for clarity-  
no substantive changes
- Information technology
- Corporate Governance, board member evaluations,  
training, etc.
- Mergers and Acquisitions including management  
payouts
- Let us hear from you- Other?



## Alabama's Consumer Credit Task Force

- The Alabama Consumer Credit Task Force was created by Governor Bentley's Executive Order No. 21, dated June 14, 2016
- ACUA appointed two members to the 34 member Task Force: Doug Key, Mutual Savings and Sarah Moore, Administrator of ACUA
- Mission of the Task Force was to “study and identify areas for potential revision of Alabama consumer credit laws.”
- The Task Force met routinely from September 21, 2016 to February 8, 2017.



# Alabama's Consumer Credit Task Force

- The Task Force did not recommend specific legislation.
- The Task Force discussed extensively the pros and cons of regulation, and especially limits on interest rates. Discussion Included:
  - Access To Credit
  - Consumer Protection Against High Rates
  - Ability to Repay
  - Cycle of Debt



## Alabama's Consumer Credit Task Force

- There was one area of complete agreement –  
Car and other vehicle title loans should be a separate law from the Pawn Shop Act.

Vehicle Title Loans are currently governed by the Alabama Pawnshop Act. Under the Act, a lender may make a one month, non-recourse pawn transaction secured by a vehicle title at the rate of 25% per month (or 300% APR).

There was not consensus on which law should cover vehicle pawn transactions. Suggestions included a new law or the existing Mini-Code.



## Alabama's Consumer Credit Task Force

There were other areas of “Common Ground”, in which there was not complete agreement, but a general consensus of the Task Force members.

- An “Off-Ramp” Loan Product should be available to borrowers who are unable to repay a small loan, such as a payday loan, during the loan term. Off-Ramps proposed would allow the loan to be repaid in an installment loan product that fully amortizes; and
- A “Cooling Off” period between loans where a borrower could not obtain a new loan or renew an existing loan for a set period of time after repayment.



## Alabama's Consumer Credit Task Force

- Task Force Members discussed Payday Lending and other Small Loans extensively, but reached no real agreement outside the “Cooling Off Period” and “Off-Ramp” discussed.
- The Alabama Deferred Presentment Services Act allows a short term, unsecured loan of no more than \$500 for a term of 10-31 days and a cap on the interest rate in the amount of 17.50% of the amount advanced.( NOT APY- RATE PER TRANSACTION- assuming 2 per month – up to 420% APY)
- This type of loan was also covered by a proposed rule issued by the CFPB in 2016.
- Credit Unions may make PAL Loans at an interest rate of 28%.





# Alabama's Consumer Credit Task Force

- Loans in the Amount of \$2,000 or more, no limit on rate
- Task Force noted the incentive to lenders to make loans of \$2,000 or more because there is no set maximum rate under Alabama law for these loans, which are governed only by the standards of unconscionability.



# Alabama's Consumer Credit Task Force

- Other Concepts Advanced or Discussed:
  - Balancing the Free Market with Consumer Protection
  - Cycle of Debt
  - Financial Education
  - Increased Use of Database Reporting
  - Internet Lending by Unlicensed Lenders
- Predatory lenders are taking their toll on Alabama consumers
  - 2.1 million loans to 246,000 borrowers in Alabama
  - 50% of those extended their loan over 6 times
  - \$116 million paid in fees



## CFPB's Proposed Rulemaking on "Payday, Vehicle Title, & Certain High-Cost Installment Loans"

- On July 22, 2016, the CFPB issued a proposed rule on Payday, Vehicle Title, and Certain High-Cost Installment Loans. The comment period deadline for the proposed rule expired on October 7, 2016. ACUA commented.
- The proposed rule would apply generally to loans:
  - 45 days or less
  - longer term loans with a cost of credit over 36%
  - loans with a vehicle security interest or leveraged payment mechanism.
- These are the same type of loans discussed by the Consumer Credit Task Force.



## Effects of the Rule

- Under the proposed rule, it would be *an abusive and unfair practice* for a lender to make a covered loan without reasonably determining the consumer will have the ability to repay the loan.
- Ability to repay is determined by a methodology in the rule to ensure the borrower can meet basic living expenses, and pay other existing debt obligations without needing to re-borrow during the loan term.



## ACUA's Comment Letter and Position on the Proposed Rule

- ACUA's comment letter supported NCUA's exclusion of credit unions from the scope of the rule as credit unions should be determining ability to repay for all loans
- ACUA urged the CFPB to remove the 72 hour loophole on auto title loans from this proposed rule as it could result in predatory lenders exploiting the loophole to avoid compliance
- Ability to repay would level the playing field to require auto title lenders, payday lenders and other predatory lenders to determine ability to repay on loans these lenders make.



## Risk Alerts

- Fraud has increased in small credit unions across the country
  - Typically, familiarity among the employees causes relaxation of internal controls
  - Internal controls are there to protect your credit unions – Supervisory committee should ensure that controls are operating as intended
- Auto Lending Programs- “Make more loans to high risk borrowers and make more money”



## Risk Alerts

- Merger opportunities
- Ensure that you continue to comply with the Military Lending Act regarding interest rates and collection activities
- Ensure that your credit union is underwriting auto loans for add-ons such as warranties, insurance products, etc.



## ACUA Focus

- Ensure a safe, sound, and healthy state credit union system.
- Further develop a regulatory environment that is transparent and effective.
- Cultivate an environment that fosters a diverse, well-trained staff.





## 2017 Examination Focus- What to Expect

- Increased emphasis on credit quality (loan underwriting and collection practices)
  - 19.39% increase Y/Y in FISCO Reportable Delinquency
  - 24.25% increase Y/Y in FISCO Net Charge Offs
- Focus on Corporate Governance
- IT Security and Cyber Security (Cat)



## 2017 Credit Quality –Deficiency Trends

- Underwriting deficiencies- lack of income verification or income is not adequate to service debt, etc.
- Lack of quality control reviews of new loan production
- Loan policies are often inadequate and do not limit new programs- expect to see limitations on new programs until the program is seasoned and enhanced collection practices
- Appraisals- seeing many FIRREA exceptions
- Allowance for loan losses
- Indirect Lending – Lack of monitoring loans by dealer, credit score.



## Credit Quality

- ACUA adopted the NCUA MBL rule
  - Expectations are that each credit union will have robust MBL policies and procedures in place and will have loan officers with the expertise to conduct MBL lending prior to granting MBL loans
  - Expect Boards to establish risk tolerance levels in policy; stay informed; and, monitor via monthly reporting at Board meeting.
  - Focus on increasing delinquency trends and adequacy of collection practices



# Corporate Governance Expectations

- Active Board (not just attendance)
- Active Supervisory Committee
- Updated Bylaws to comply with state law
- Training for officials and employees



# Cybersecurity

- Implement internal controls over vendor due diligence, password processes, patch management and network monitoring to prevent, detect and recover from cyber-attacks.
- New Cyber security assessment tool (CAT questionnaire) is being rolled out by NCUA. Already in use in corporates but will extend to large natural person credit unions soon.
  - The questionnaire is designed to assist credit unions in identifying cyber risks to the institution.
  - Internal risks are often overlooked but result in the largest losses to credit unions



## What is the Community Development Financial Institution certification?

- The Community Development Financial Institutions Fund, a department of the U.S. Treasury, designates organizations that provide financial services to low-income communities and to people who lack access to financing as Community Development Financial Institutions (CDFIs).



# Community Development Financial Institutions

- CDFIs are eligible to apply for technical assistance and financial assistance awards from the CDFI Fund and training provided through its Capacity Building Initiative. The Fund's awards can enable CDFIs to finance a wide range of activities, including:
  - Mortgage lending for first-time homebuyers,
  - Flexible underwriting for community facilities, and,
  - Commercial loans for businesses in low-income areas.



# How does an organization become CDFI-certified?

- ELIGIBILITY REQUIREMENTS:
- Be a legal entity;
- Have a primary mission of promoting community development;
- Provide both financial products;
- Serve one or more defined target markets;
- Maintain accountability to a defined market;
- Provide developmental services such financial literacy training; and
- Not be controlled by governmental organizations.





## News Just In....

- In an article published by the CU Times, President Trump's budget has slashed funding for the CDFI.
- Financial institutions are pushing back on this budget cut.... More to follow



## Alabama State Chartered Credit Unions Statistics as of 12/31/16

- 62 State Chartered Credit Unions
- Assets under supervision - > \$14.3B
  - Assets increased 3% over 2015; 5% ex. Corporate compared to National average of 7%
  - Loans grew 10.12%, compared to National average 10.43%
  - Shares and Deposits increased 3% over 2015; 6% ex. Corporate compared to National average of 7.5%
  - Asset size ranges from \$2.3 million to \$2.7 billion
- Average Net worth ex. Corporate 11.56% compared to National average of 10.89%



## Closing

- ACUA will work diligently with you to maintain a sound and healthy state chartered credit union system that can adapt to members' changing needs
- ACUA welcomes comments and feedback on examinations, laws and regulations
- Questions/ Comments?

