CUNA Credit Union National Association — Regulatory Advocacy

August 11, 2014

Fixed Assets

Executive Summary

- NCUA has proposed to amend its regulation governing federal credit union (FCU) ownership of fixed assets by removing the waiver requirement for FCUs to exceed the 5% aggregate limit on investment in fixed assets.
- An FCU that chooses to exceed the limit of 5% of shares and retained earnings on the ownership of fixed assets may do so if it implements a fixed assets management (FAM) program.
- An FCU's FAM program must demonstrate that it has analyzed an investment that would cause it to exceed the 5% limit prior to the purchase to ensure that the FCU can afford any impact on earnings and net worth levels.
- Also, the FAM program would be subject to NCUA supervisory scrutiny and must provide for close ongoing oversight of fixed assets levels and their effect on the financial performance of the FCU.
- The FAM would include a written FAM policy that establishes limits on the aggregate amount of the FCU's fixed assets. The FCU's board must approve this policy.
- The rule does not cover FCUs that have assets up to $1 M.
- It also does not cover state credit unions. However, state credit unions that have parity provisions may be able to receive comparable treatment and should check with their leagues and state regulators. State CUs as well as FCUs should comment on the proposal.
- Click here for the fixed asset proposal.
- NCUA is accepting comments on all aspects of the proposals until October 10; **please send comments to CUNA staff by October 1.**

Highlights of the Proposal

NCUA proposed this rule to increase an FCU's flexibility in the management and ownership of its fixed assets portfolios. FCUs are authorized by the Federal Credit Union Act (FCUA) to purchase, hold, and dispose of property necessary or incidental to credit union operations. NCUA has interpreted the FCUA to limit the fixed assets that an FCU can hold and to establish occupancy, planning, and disposal requirements for acquired and abandoned premises.

NCUA made technical revisions to its fixed assets regulation in 2013. At that time, CUNA urged the agency to eliminate the 5% ownership limitation and thus the necessity for waivers. In the alternative, we asked that the agency eliminate the 5% ownership limitation and create what NCUA is now calling the FAM program; which is what NCUA has proposed. After reviewing and discussing the proposal with NCUA, we believe that FCUs would gain flexibility because they no longer would have to justify the purchase of a fixed asset at the pre-acquisition phase but instead would receive ongoing approval through the FAM program, as long as the requirements of the rule are met.

Prior to the elimination of the Regulatory Flexibility Program (RegFlex) in 2012, FCUs that had a RegFlex designation could exceed the 5% aggregate limits on the ownership of fixed assets without prior NCUA approval. NCUA would still review the ownership of a RegFlex credit union's fixed assets to ensure safe and sound practices. After NCUA eliminated RegFlex, FCUs have been required to apply to NCUA for a waiver to exceed the 5% limits.

The proposal would eliminate the requirements for NCUA approval prior to the acquisition of fixed assets that cause an FCU to exceed the 5% fixed asset ownership threshold. FCUs that exceed the 5% fixed assets ownership would have to have a FAM program in place.

Although NCUA will apply similar standards to review a FAM program as it currently does for a waiver application, it would be more problematic for the agency and the credit union for NCUA to require divestiture than it would be to deny an initial waiver before a purchase took place.

FCUs could benefit from the proposal because they will not be required to obtain permission from the agency before acquiring fixed assets that cause an FCU to exceed the 5% ownership threshold. We think that these amendments could help restore credit unions to a similar place with fixed assets ownership as they were with RegFlex prior to the 2012 rule change. Even a RegFlex credit union would have been subject to examiner scrutiny if its ownership of fixed assets caused undo risk to the FCU. The proposal has a more formalized FAM program than would have applied to a RegFlex credit union, but it still allows credit unions to purchase fixed assets and *defend* their decision instead of trying to justify a need through a waiver process before the investment takes place.

Partial Occupancy of Premises

Under the current rule, if an FCU acquires premises for future expansion and does not fully occupy the premises within one year, the FCU must have a board resolution in place by the end of that year with definitive plans for full occupation. The current rule does not set a specific time period for full occupancy by an FCU of premises that were acquired for future expansion, but does have some other occupancy requirements. These are:

- An FCU must partially occupy the premises within a reasonable period, but no later than three years after the date of acquisition.
- If the premises are unimproved land or unimproved real property, the three-year partial occupation requirement is extended to six years.

The proposed rule would require partial occupancy within five years, and the occupancy must be sufficient to show that the FCU will fully occupy the premises within a reasonable time. The five year time period would also apply to unimproved land.

The proposed rule would retain the current waiver process for FCUs that require additional time to partially occupy premises acquired for future expansion. The current rule requires that an FCU apply for a waiver within 30 months. The proposal eliminates the 30-month requirement for partial occupancy waiver requests allowing waivers to be requested at any time.

This proposed rule does not amend the requirement for full occupancy of premises acquired for future expansion.

Grandfathering

If NCUA finalizes this proposal, FCUs with an existing waiver in place will be grandfathered at their approved limit of fixed assets ownership, and may continue to rely on the waiver until it expires. A credit union with an existing waiver will be required to implement a FAM program prior to making any future investment in fixed assets that exceeds the amount approved in the waiver. If an FCU's level of investment in fixed assets falls below the 5% limit, the waiver will cease and the FCU will be required to implement a FAM program prior to making any future investment in fixed assets.

NCUA's Supervisory Review of the FAM Program

A key aspect of this proposal is NCUA's supervision of a FAM program. NCUA indicates that the agency will review the FAM program of an FCU with fixed assets in excess of 5% of its shares and retained earnings during an FCU's examination. NCUA states that the analysis of a FAM program will be similar to the review conducted for waiver requests. This exam will include the following:

- NCUA evaluates the impact on earnings and net worth levels to determine if an FCU's FAM program is reasonable. According to NCUA, high levels of non-earning assets may lower income and increase operating expenses. Furthermore, FCU's will not be in compliance with the rule if they cannot demonstrate that operating at higher levels of fixed assets to expand an FCU's

service does not pose a material reduction in the FCU's ability to establish or maintain sound net worth levels.
- The FAM policy must be consistent with an FCU's strategic plan. An FCU must document sensitivity to material assumptions and must be supported by reasonable growth projections.
- NCUA will consider a credit union unsafe and unsound if a fixed asset investment has very limited marketability and will result in it operating at fixed assets levels above the 5% aggregate threshold.

An FCU can be ordered to reduce fixed assets levels or prohibited from making additional fixed assets acquisitions if it does not meet the requirements of the rule, fails to comply with its FAM program, or has an unsafe program or level of fixed assets.

As discussed in the summary CUNA believes that the FAM program will expand a credit unions' ability to acquire fixed assets. We do seek input from credit unions so that we can suggest changes to add more flexibility to the final rule.

State Chartered Credit Unions

This rule could have an impact on state chartered credit unions through a state's parity or "wild card" provision. These provisions could allow a state regulator to apply NCUA's requirements to state chartered credit unions.

Questions for Comment

Please provide feedback to CUNA by answering the following questions. Answers can be sent directly to CUNA by clicking here.

Do you support the process where credit unions are allowed to exceed the 5% fixed assets limit through a FAM program? Why?

Would you like to see the waiver option retained as an option for pre-approval of a fixed asset acquisition?

NCUA states that it will provide guidance at a later date. Guidance is very important and can make much difference in how the requirements in the proposal are applied. Do you think that NCUA should allow comments on proposed guidance?

Should NCUA include a formal appeals process in the regulation if NCUA contexts a fixed asset investment when the CU has a FAM?

The proposal does not amend NCUA's full occupancy requirements of premises that were acquired for future expansion. Should NCUA modify this rule? What changes to this requirement should the agency make?

Are there any other areas of the fixed assets rule that you would like to see updated?