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A CONVERSATION WITH NATIONAL CREDIT UNION ADMINISTRATION CHAIRMAN TODD M. HARPER

February 6, 2024

Washington, D.C.

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KEYNOTE REMARKS:

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Aaron Klein And on behalf of Brookings Economic Studies in the Center on Regulation and Markets. It's my pleasure to welcome everyone here in person and online. As we listen for the path of credit union regulation coming forward, and I can think of, a topic that really is important. There are more credit unions today in America than there are banks. Over 130 million Americans are members of a credit union. I'm proudly a member of two. In fact, for over a decade, I didn't have a bank account. And to this day, a credit union remains my primary financial institution and that of millions of other Americans. Credit unions were founded, almost 100 years ago on a principle that cooperative finance of a common bond of people can produce a better outcome for society than for profit banking. And wherever people come down on that intellectual question, the explosive growth and success of the credit union movement in America and globally has shown the power of that idea. Part of my portfolio for this upcoming year is going to be trying to rethink of a new concept in financial services that can better meet the needs of working people, and I'm often inspired by the folks a century ago that came up with the credit union movement. Given this explosive growth in credit unions in America and their increasingly important role in today. It is vitally important that these institutions are properly regulated. And I rest assured, as a credit union member, knowing that Todd Harper is on the case.

Chair Harper, was appointed, to the three member National Credit Union administration, in 2000 and 17, 19, 2019 under President Trump and then appointed as chair under President Biden and has recently been reappointed for another five year term. When chair Harper, was originally appointed, he came from the staff of the organization being the first person to make that transition. I first got to know Chair Harper when he worked on Capitol Hill as an institution for Congressman Kanjorski, helping work through legislation spanning from Gramm-Leach-Bliley through Dodd-Frank. If there is a major piece of financial services legislation during that window, you came through, Todd Harper and, Congressman Kanjorski, and you left knowing that there was a person who was in it for the right reasons, who was trying to make policy better and navigating a complex environment with a skill and deftness, and with that background and steeped in the organization of which he now heads. It is my distinct honor and privilege to join him, to welcome him to the Brookings Institution and to hear him lay out his agenda for credit union regulation coming forward. Todd.

Todd Harper So good morning, everyone, and Aaron, thank you so much for that warm introduction. It's always good to see you. Although it's a little different environment than Capitol Hill. And thank you to the Brookings Institution for inviting me to join you today. Although I may have grown up a Chicago Cubs fan, I have long appreciated the wisdom of New York Yankees baseball legend Yogi Berra, who famously once said, the future ain't what it used to be. His astute, if slightly mind bending observation rings true for today's credit union system. The future viability and success of the evolving credit union system requires not only planning, but flexibility and agility, as new developments call for changes or course corrections.

Before delving into what will be needed in the future, let me first speak briefly about the foundation laid in the past and the challenges of the present for the credit union system. Credit unions actually date back in the United States to 1909, when Saint Mary's Co-operative Credit Association opened its doors in Manchester, New Hampshire. The number of state chartered credit unions and their members grew at a healthy rate then for 25 years. But when the Great Depression set our economy spiraling, it became clear that we also had to look differently at the way we organized financial institutions at the federal level. So in 1934, President Franklin Delano Roosevelt signed the Federal Credit Union Act to expand access to the credit union system in our country. In those early years sfter that bill became law, my grandfather helped to start a credit union at a soap factory in Indiana, and about 30 years later, my father would go on to do the same by starting a teacher's credit union in Illinois. And about 20 years after that, I would join my first credit union before starting to work on credit union policy issues shortly thereafter. So my family has firsthand experience with the benefits of cooperative credit, including lower interest rates on loans and higher interest rates on shared deposits that have allowed us to build intergenerational wealth.

This year marks the 90th anniversary of this landmark legislation that established the federal credit union system. That law also set up a federal agency to oversee credit unions at the national level. The then newly created Federal Credit Union Division was initially placed in the Farm Credit Administration, but over time moved to other agencies until the National Credit Union Administration was created in 1970. The NCUA has evolved considerably since then, as has the credit union system into what it is today. That evolution includes creating the National Credit Union Share Insurance Fund in 1970, to protect the share insured deposits of now nearly 139 million Americans.

Until 1970, it's hard to believe credit unions had operated without federal deposit insurance. That evolution of the law has also included the establishment of a board to oversee the NCUA operations in 1979, and that evolution included the enactment of legislation in 1998 to allow for the organization of multiple common bond federal credit unions, with many smaller groups within a federal credit unions field of membership, and to establish, comparable to banks, minimum capital ratios that a federally insured institution must maintain and triggers that limit the activities of that institution should it drop below those levels.

The passage of the Federal Credit Union Act was a watershed moment in our nation's history. But just as that law was forward thinking when enacted nearly a century ago, it has continued to evolve to reflect current realities with an eye to the future. As of today, the credit union system remains largely stable in its performance and relatively resilient against economic disruptions. For the $2.2 trillion federally insured credit union system total loans increased 9.1%, total assets rose 3.7%, and total insured shares and deposits grew 1.4% over the year ending in the third quarter of 2023. Together, these metrics demonstrate signs of strength for the system.

However, in recent quarters, the NCUA has also seen growing signs of financial strain on credit union balance sheets and household budgets, along with growing consumer financial stress. For instance, during the third quarter of 2023, the overall delinquency rate for federally insured credit unions was 72 basis points, up 19 basis points from one year earlier. Credit card and automobile delinquencies are elevated at 190 and 78 basis points, respectively. In fact, the dramatic year over year rise of 60 basis points in credit card delinquencies is well above historic averages, and aggregate credit card balances are rising, while share deposit ups per member are following. The NCUA therefore continues to watch credit union performance closely and urges credit unions to remain diligent in managing the potential risks on their balance sheets and when monitoring economic conditions and the interest rate environment. These aggregate statistics result from economic warning signs that have been flashing for some time, including inflationary pressures, geopolitical turbulence, changes in supply chains and growing interest rate, liquidity and credit risks within the credit union system. The numbers also show that today's economic environment requires active, not passive, management by credit union boards and senior leadership. We all need to be paying attention.

The NSA's recent Share Insurance Fund quarterly update in November additionally illuminated that action is needed to ensure that the credit union system's continued health and members financial security. As part of the examination process, the NCUA uses its CAMELS rating system, which, like the system used by other federal banking safety and soundness regulators, is based on an evaluation of six critical elements of a credit unions operations, namely capital adequacy, asset quality, management, earnings and, liquidity and sensitivity to market risk.

A credit union with a CAMELS one rating generally exhibits sound performance and risk management practices, whereas a credit union with a CAMELS five rating exhibits extremely unsafe and unsound practices and conditions. According to the latest data, the number of CAMELS code threes, fours and five credit ratings is increasing. More concerning is that assets in composite CAMELS code three institutions increased sizable during the last quarter. In fact, the number of large complex credit unions with a composite CAMELS code rating of three increased by nine credit unions to a total of 51 credit unions in the third quarter. Assets in the CAMELS Code three group for credit unions of all sizes also increased to 131.7 billion, nearly a 45% jump from the previous quarters results. We expect those trends to continue, and we have seen more credit unions fall into the composite CAMELS Code three offers and five ratings during the second and third quarters. This means a large and growing share of the credit union systems assets reside in institutions with potential safety and soundness concerns that require immediate. Let me stress that immediate remediation.

Given the current economic conditions and the stress in the credit union system from growing liquidity, interest rate and credit risks, the NCUA board decided to build up the liquidity position of the Share Insurance Fund, which is used to protect the deposits of the members , in case of credit union, is liquidated, to $4 billion and we reached that target last September. By years end the overnight reserves had increased to 5.2 billion. Protecting the Share Insurance Fund against losses is job number one of the NCUA board. And going forward, the board will continue to closely monitor credit union and performance and the Share Insurance Fund performance in the quarters ahead.

Rest assured, the NCUA is committed to protecting credit union members and the safety and soundness of the credit union system no one has. Ever lost a single penny of insured shared deposits at a federally insured credit union. The NCUA board's decision to increase the Share Insurance Fund's liquidity position was made to prepare for potential losses. That same forward thinking is needed by credit unions. Credit unions can and must identify and mitigate risks that endanger their operations, their institutions and their members. We speak about the importance of innovation to maintain longevity, but credit unions must also be careful, meticulous, scrupulous and attentive. In today's economic environment, it's not a single catastrophic event that wipes out financial institutions. Human errors, cutting corners and passivity are also key ingredients that lead to a crisis. What's more, risks in the credit system often lurk in the regulatory shadows beyond the NCUA's reach, namely within credit union service organizations and third party service providers. Because the NCUA does not have supervisory authority over these third party vendors, unlike its federal banking agency counterparts.

This lack of authority is an Achilles heel for the credit union system. Increasingly, activities that are fundamental to a credit unions mission such as loan origination, loan servicing, Bank Secrecy Act, and anti-money laundering compliance, financial management are being outsourced to third party vendors, and credit unions use third party vendors to provide technological services, including information security and mobile and online banking. Member data is also stored on vendors servers, including, as we've been told by concerned credit unions on servers not utilizing industry standard cybersecurity practices. The pandemic, which accelerated the credit unions industry movement into digital services, has only increased credit union reliance on third party vendors. Yet, the NCUA's lack of visibility into these critical industry participants is a major problem that poses a systemic risk to the financial services system and our national security. And it costs the agency and the industry money. Consider these statistics. The NCUA Office of Inspector General stated that between 2008 and 2015, nine credit union service organizations contributed to material losses to the Share Insurance Fund, costing credit unions more to maintain it. That same report noted that one of the credit union service organizations caused losses in 24 credit unions, a number of which failed, and according to staff calculations, at least 73 credit unions incurred losses between 2007 and 2020, as losses of credit union service organizations rolled on to credit union ledgers and led to some credit union liquidations. More recently, the implementation of the NCUA Cyber Incident Notification Rule last year yielded new insights into the scale of third party vendors vulnerability to cyber attacks. Within just the first 30 days of implementation of that rule, on September 1st, the NCUA received 146 incident reports, roughly 60% of which involved third party service providers. Moreover, there's an associated concentration risk as five core banking processors handle more than 90% of the credit union system's assets. A failure of any one of these third parties could cause hundreds of credit unions, and potentially tens of millions of members to lose access to their funds simultaneously. In fact, we encountered that very scenario last November when the NCUA received cyber incident reports from multiple small credit unions stating their core service provider had been experiencing intermittent system outages. Dozens of credit unions across 40 states, with aggregate assets of nearly $1 billion and nearly 100,000 members, experienced outages or disruptions of services in some form.

The fallout of this incident demonstrates how a single vendor's problem can quickly metastasize into crisis for credit unions, members, and the overall system. The lack of vendor authority impeded the NCUA's ability to quickly respond to the situation, and the lack of vendor authority will become an even larger issue, as credit union service organizations and third party service providers are poised to capitalize on financial institutions growing use of artificial intelligence and real time payment services.

To be clear, restoring the NCUA's vendor authority is not just about what credit unions stand to lose. It's also about what they stand to gain. The benefits include credit union access to NCUA examination information when conducting due diligence with vendors. Which would enhance the credit union industry's competitiveness, vis-a-vis the banks, which have access already to such reports when they conduct due diligence. Other benefits for credit unions include fewer requests from the NCUA to credit unions to intervene with vendors experiencing problems, and fewer losses to the Share Insurance Fund. Again, both are a savings of time and money. Consistent with board approved policy the NCUA will continue to ask Congress for this authority, as we have in multiple testimonies.

The NCUA is not alone in recognizing this problem as well. Other government officials support this request, including the Government Accountability Office, the Financial Stability Oversight Council, the NCUA s Office of Inspector General, and the Federal Reserve Bank of Atlanta, which cited the Treasury Department's Office of Financial Research 2023 annual report that underscored how smaller banks and credit unions are especially vulnerable to ransomware attacks due to a greater reliance on third party service providers. Until Congress restores vendor authority, the onus remains on credit unions to ask the right questions of their vendors. Those questions include what are they doing to safeguard their members hard earned savings, as the economic environment continues to experience turbulence and the financial services industry endures regular cyber attacks, and what practices are credit unions engaging and to remain competitive amidst an evolving technological landscape and an increasingly demanding consumer expectations? When the NCUA is given this authority by Congress to complete its job, it will implement a risk based examination program for third party vendors focusing on services that relate to safety and soundness, cybersecurity, Bank Secrecy Act, and anti-money laundering compliance, consumer financial protection and areas posing significant risk for the Share Insurance Fund, including national security. In short, the time has come to close this growing regulatory blindspot.

Liquidity management also remains a focus of the NCUA in this current economic environment of heightened interest rates and liquidity risk for credit unions, including several with more than $1 billion in assets, the role of the NCUA Central Liquidity Facility as a liquidity backstop has taken on greater importance. Created by Congress in 1979, the Central Liquidity Facility functions as an emergency liquidity backstop for the credit union industry, similar to the Federal Reserve's discount window. The saying there's strength in numbers is applicable to the Central Liquidity Facility, because the more members it has, the more effective it is is a liquidity shock absorber. Unfortunately, statutory enhancements that allowed for greater flexibility in accessing the facility expired at the start of 2023. This statutory lapse requires membership in the facility to decline and consequently, its effectiveness diminish. Between the end of 2022 and September 30th, 2023, central liquidity membership declined from 3990 members to 399 credit unions. That's a contraction of 90% and 3322 credit unions, with less than $250 million in assets lost access to the facility. This means that $211 billion in credit union members assets are no longer protected by access to the Central Liquidity Facility, and its borrowing capacity has contracted by almost $10 billion, impacting its current members. This development comes at a time when the need for the central liquidity facility's role as a liquidity backstop has grown. For example, out of the 443 credit unions that were potentially affected by last November's cybersecurity incident, only 4 less than 1% currently have access to an emergency liquidity backstop like the facility. Access to the Central Equitity Credit Facility and the Federal Reserve's discount window should be a part of participating credit unions broader liquidity risk management plans for a variety of contingencies, and not just used during times of crisis.

For that reason, the NCUA board has repeatedly asked Congress to allow corporate credit unions to purchase capital stock in the Central Liquidity Facility to help smaller credit unions access that liquidity and to provide other regulatory flexibilities to increase the facility's accessibility. We are hopeful that Congress will make these changes.

The safety and soundness concerns for the credit union system that I have so far described tell only part of the story. Protecting consumers interests and their hard earned savings is equally important. Some critics have drawn a false dichotomy between the NCUA's two missions. But the truth is, you can neither separate them nor have one without the other. The NCUA's vision statement, unanimously approved by the NCUA board in 2022, is part of the strategic plan, is a clear confirmation of that relationship, and let me quote it here. Our vision is to strengthen communities and protect consumers by ensuring equitable financial inclusion through a robust, sound and evolving credit union system. And the investment in consumer financial protection isn't only a good principle, it's a good business practice. The NCUA supervisory efforts over the last few years are aimed at creating a more equitable and legally compliant financial system. That commitment is reflected in the agency's 2024 and 2025 budgets, approved in December and in this year's supervisory priorities, which the agency issued just last month. Overdraft and non sufficient fund fees are a critical component of the NCUvAs review this year, and two ways examiners this year are continuing to an expanded review of credit union overdraft programs, including website advertising, balance calculation methods and settlement processes. Problematic overdraft programs and non sufficient fund funds alerts include fees that are aren't reasonable and proportional, reliance systems that authorize positive and settle negative or impose multiple represent and fees, often on the same day. The NCUA's Fair Lending examinations will also increase the number and focus on ensuring that policies and practices are fair and not discriminatory, and examiners will continue to evaluate credit union policies and procedures governing compliance with flood insurance rules. Other areas of focus for the agency in 2024 include Bank Secrecy Act compliance and support for small credit unions and minority depository institutions.

So as we approach the 90th anniversary of the Federal Credit Union Act in late June, it's appropriate to consider where we've been, where we are now and where we are going. What began with paper ledgers, volunteers meeting on factory floors, including that soap factory where my grandpa worked, limited hours of service and simple appliance loans, has evolved into a $2.2 trillion system serving tens of millions of members and employing in excess of 350,000 full and part time professionals. That monitoring system also includes 24/7 mobile and online services, automated underwriting, a complex system of third party vendors, and a full array of financial products and services. The NCUA's regulatory and examination framework must likely keep pace, evolve, and adapt to this changing system. The phrase regulatory parity has taken on a negative connotation as a euphemism for overreach, or worse, a one size fits all approach. But credit unions face the same challenging economic environment, growing interest rate and liquidity and credit risks, a shifting technological landscape and evolving consumer expectations that banks do. And with the creation of the Federal Financial Institutions Examination Council in 1979, Congress called on the federal banking agencies and the NCUA to promote uniformity in the supervision of financial institutions. As such, the NCAA legislative requests and initiatives are aimed at safeguarding credit union members choice of financial institution and ensuring their savings are equally protected. Similarly, the agency's initiatives to support small credit unions and minority depository institutions, streamline the chartering process, amend field of membership rules will enhance consumer access to safe, fair and affordable financial services, especially in under-resourced communities across the country. Together, these efforts can ensure the credit union system thrives in an increasingly competitive marketplace while remaining faithful to the statutory mission of meeting the credit and savings needs of their members, especially those of modest means.

In closing, let me return to the wisdom of Yogi Berra, who said, you've got to be very careful if you don't know where you are going, because you might not get there. The statutory mission of the credit union system is clear, but the path to accomplishing that mission in today's evolving marketplace must be charted with an appreciation for the achievements of yesterday, an understanding of the conditions today, and ability to anticipate and meet the challenges of tomorrow. Those changes and developments require a more level playing field when it comes to regulations, examination and supervision, especially of the largest credit unions. Thank you again, Aaron, for the invitation. I look forward to our conversation.

Aaron Klein I feel like I have to jump up on the stage. I'm so excited. Somebody took my prop. So, Todd, you laid out a robust vision of a lot in that speech, and, I'll say it because I know institutions are, like, yours are nonpartisan at a certain level, but there's a partisan requirement in the statute of the board. And just this year, around Christmas time, Democratic appointees, became the majority of the board. It's a three member board. And even though President Biden is up for reelection later this year, it was not until functionally this year that, you had a majority of votes. So you've laid out an aggressive agenda. But I'm very fond, as as those of us who spent a lot of time on Capitol Hill are of your first boss. And mine was the great Senator Sarbanes, who was very fond of his Greek heritage. And one of the words he used to talk about a lot was telos, which is the ancient Greek concept of a true North star. One organization, one principle. And it drives home the idea that you have to have one number, one priority. If you have five number one priorities, you have none right? So what is your number one priority?

Todd Harper So I as I said in my remarks, our job number one is protecting the Share Insurance Fund. That's job number one. And from that priority flows everything that we do. That includes our increased emphasis on liquidity management. It includes consumer financial protection. If you're not protecting your consumers. And there is this myth within the credit union system that because credit unions are owned by their members, they're always going to do right by their members. Generally, that can be true. I do think that most credit unions seek to do that, but there's this little issue in between. It's called the principal agent problem. I learned about it in college, and it's that the people who manage the credit union, their interest doesn't always align with that of the members, and it's our job to make sure that there's an alignment there. When a credit union, acquires a bank. And we've seen that happen, recently, there are about 64 in the last decade or so. Why is it that on the bank side of the ledger, there is a separate consumer compliance exam with a separate consumer compliance score that is done every three years, and that's not done on the credit union side. We're working to fix that problem and to change that problem. So, you know, everything we do flows from job number one, protecting the Share Insurance Fund. If you're not protecting your members, you're going to be at reputation risk. You're going to have any types of compliance risk and legal risks. And those are going to actually lead to higher costs for you up front. So let us come in. Let us do our jobs. Let us check around, kick the tires, to see how you're doing. And if I were somebody having a third party evaluation of how I'm doing, it's actually a good thing.

Aaron Klein Well, let me build on that, because I appreciate the number one priority. I appreciate how you link that number one priority of the Share Insurance Fund to consumers and protections. And one area which I've been very focused on is overdraft. And you mentioned it in your remarks and you talk about having people look at a system. Right? I'm a researcher. I have access to data. I can manipulate that data. I can process that data, analyze that data, publish that data. I've done that a lot on overdrafts. Yes. And I've discovered a handful of banks that I would say are engaged in unsafe and unsound operating practice. I have been structurally hampered because that same information that banks over $1 billion put in their call reports on a quarterly basis on overdraft is nowhere to be found federally on overdraft. The state of California acted produced the first overdraft data from credit unions that I'm aware of, and it was startling. 30 California credit unions derive more than half their net revenue in overdraft, eight more than 100%. Some egregiously so, CFPBdata, to the extent they've shared data, shows problems in settlement practices on overdrafts that you've described. Or you mentioned briefly in terms of reordering transactions, credit unions being more likely in the CFPB data than banks. Why don't we have access to this type of data on overdraft for credit unions?

Todd Harper So the world is changing, Aaron. On the banks side of the ledger, the banks have long had a requirement that for billion dollar plus institutions, they have to report an aggregate number of their overdraft and not sufficient fund fees collected. We are in the process of going through the Paperwork Reduction Act steps that we've got to go through to amend our call reports. We will require for those credit unions above $1 billion in assets they make up. They're about 427 of those credit unions overall, they make up roughly 90% of the industry's assets. We will require, this is going to be different from banks, we're going to require separately reporting of overdraft fees and non sufficient fund fees. So you'll have greater granularity in order to track. If I could though you talked about 100% of their earnings coming from it. I'd encourage you to take a look at revenue, because there are many revenue streams, and it's just one piece of the, you know, the revenue streams that are coming in that contribute to earnings. So there's not a, a to b connection necessarily. It's just one pot of money that happens to be that amount.

Aaron Klein Yeah, no, first of all, that's fantastic. I would commend you, and commend the NCUA for requiring that level of disclosure, because that's the same transparency that other financial institutions of that size have. And we can debate whether it's good or bad. But the facts are the facts, and the facts shouldn't be hidden from the public. You talk about CAMELS -

Todd Harper And the members. The members deserve to know what's happening because there's an equity issue here. Overdraft fees are falling disproportionately on people of color, and on lower income families overall. So a credit union, which was created and as I quoted, the statutory mission of credit unions is to meet the credit and savings needs of their members, especially those of modest means, if they're falling disproportionately on it. Credit unions really need to be asking a hard look what were we created for? Why were we created, and who are we serving?

Aaron Klein So, so on that line, right? The only person that's ever paid an overdraft is a person who ran out of money in their account. You cannot pay an overdraft if you haven't run out. 8% of Americans are responsible for 80% of the overdrafts. This is a highly concentrated situation where a group of people are paying disproportionately amount, sometimes as a result of of back office settlement processes that you described in terms of reordering your transactions during the day from your debit card, from highest to lowest right that maximizes the number of overdrafts. There's no requirement that the bank or credit union process it in order of transaction, when you had the money there. But there was another pending transaction, the authorized positive settle negative. There are a bunch of these points. You and we discussed it in a consumer protection, angle. And I'm totally with you. And the credit union members ought to know and be able to vote and and question their board and say, what is this become? There's also a safety and soundness aspect when you're unduly, dependent on that. You talk about asset management and earnings. Right. If you're.

Todd Harper Running concentration risk.

Aaron Klein I'm getting the concentration risk if in the banking sector, if you said commercial real estate was the entire source of your net profit for the last eight years, the regulators would have a five alarm fire. You substitute that for overdraft and the comptroller of the office seems to go good job, which disgusts me as a as a safety and soundness person. I think there's a safety and soundness issue, particularly in these folks that are depending. I don't know how long it's been going because the data hasn't been out there. It is for the banking. But when you see this as a, as a system of earnings, the other aspect that you raise is what's it going for, right? Golden One Credit Union, got $28 million last year in non sufficient funds fees and overdraft revenue. And they spent $6 million on stadium naming rights. I had a prop here that, I got in the mail yesterday. It seemed to have gotten taken away, which was, from SECU Credit Union in Maryland, which, was offering $250 to the current resident of my address to open a brand new account with them because any Marylander is eligible. They bought the stadium naming rights to Pier Six Pavilion, up in Baltimore, where I've seen many great shows. And, you know, I'm asking myself, what are these? I mean, is this a nonprofit or is this a, you know, for profit, growing institution operating as a as a nonprofit? What do you make of this field of membership where anyone can join? If you fly out of Dulles Airport, you walk through a hallway of a credit union advertising great rates for anyone. Is there a difference? I'm a member of two credit unions, one employer based, where I work in the United States Senate. Tight field of membership. Their big step forward was allowing the Government Accountability Office and arm of Congress to join. Another I joined with three clicks of a mouse by stating that foster children need love too. And through that, and the credit union paid $5 to be a friend of foster children. Now, anybody is eligible. Should these two institutions, should a credit union that anyone can join functionally be treated differently than a credit union that has a real tight field of membership?

Todd Harper So first of all. You raised complaints about marketing practices of credit unions. And certainly we have seen in recent years enhanced credit union presence, on the airwaves, on the internet, and certainly, as you've pointed out about, Arena State, arena is being named after it. I think it's an important issue that the credit union has to decide what it wants to be, and who it is overall on that way. Certainly if I were on a credit union board, I would be advocating that rather than spending that money necessarily on naming rights, I'd be pointing in the direction of what can we do to lower the prices of our loans and increase the service to our members? Second, you talked about liberalized fields of membership. My understanding is that there are just two credit unions with nationwide fields of membership. So when you say you when you say everyone, there's usually an asterisk after that, everyone and there are qualifiers along the way. Related to that point, though, is that states, especially out in the West, have been at the forefront of liberalizing their field of membership rules overall. And if you take a look at the 100 largest potential fields of membership in the country, so credit unions with the largest, there are those two nationwide that are happy to have federal charters. And then behind it, the next out of that next 98, 90 plus, I think it's like 94 are state chartered credit unions. So, there are still some controls on the federal side, and there are also some states that are even more, conservative, if you will, when it comes to their rules with regulation, and of field of membership. The third point I want to make, though here is that as credit unions grow in size, they do change. And it's important that the NCUA scale its regulation based on the size, scale and scope of the institution's offerings, who its serving, how it's serving and advance that uniformity that I spoke with, which is the mission of the Federal Financial Institutions Council. We are working to advance that uniformity in a couple of ways at the NCUA. For example, we have stress testing for our $10 billion plus institutions. We have capital planning for our $10 billion plus institutions, and we are working, as I was mentioning earlier, for credit unions with more than $1 billion in assets to have that consumer financial protection, we're initially going to focus at $5 billion with what the board approved in the budget. So we'll start there and start doing a try. You know, try annual has that where exams every three years. Just to be clear, we will be doing that. So we are modifying our regulations so that as a credit union expands, as it becomes more permissive, we really need to change our regulation and oversight with it.

Aaron Klein Yeah. I mean, the theory behind the exemption for credit unions from the Community Reinvestment Act was predicated on the idea that they can only serve their members, and so they don't need a broader community requirement. But when anybody is a member functionally, then the the rationale for the exemption for the Community Reinvestment Act to me, goes away. I've written that the Community Reinvestment Act should apply to credit unions that are functionally eligible for anyone.

Todd Harper So, first of all, that's a issue for Congress to decide. Congress decides the CRA. But what is instructive here is what we've seen happening in the States. And you've recently seen. Well, first of all, there have been a number of states that have had Community Reinvestment Act like requirements for state chartered institutions for some time. And in recent years, you've seen a number of other states join them. Illinois comes to mind. If Congress were to act to provide that, apply that element to, a credit union, it's important to have flexibility. And I say that because credit unions have a number of different ways that they are chartered. And you have to think about it. One is the community charter. What if that credit union is chartered to only serve a wealthy zip code community, where is necessarily the ability for them to reach in, and find that investment overall, they may need to move and go elsewhere. What do you do with a credit union that is focused, as you pointed out earlier, on employer, and maybe it's the police department or a teacher's credit union like the one my dad started or the one that my mom belongs to. And it's a fairly narrow bandwidth when it comes to salaries, and you have to have some flexibility in your application there. And then the more interesting, animal is the Multiple Common Bond Credit Union, which Congress again allowed for and created in 1998 to overturn a Supreme Court decision, and allow credit unions rather than just being very small, to lumped together a number of smallish groups. The garage down the street that may have 30 employees overall. The accounting business on Main Street that may have another 20, a small business provider and a light manufacturing, facility that may have 500 employees. Lumping them because none of them could create a credit union on their own, but they can enjoy. There would have to be some flexibility in how we would apply it for that.

Aaron Klein So look at SECU Credit Union, which I'll pick on because they sent something to my mail, and I wonder if they sent that same mailer to lower income zip codes. Has 2091 ways to join. I looked up on their website, and that's in addition to anybody who's a resident of the state of Maryland, America's best state, in my opinion. And so, you know, I think that there's a way intellectually.

Todd Harper This Hoosier would disagree with you.

Aaron Klein I think there is a way, intellectually to bifurcate whether that's based on size, whether that's based on field of membership, between the tight employee base, credit unions. Right? And the ones like, you know, NASA credit union that's open to any person who joins Friend of Space. So as long as you're not an enemy of space, you're eligible to to join. I know that there's there's some great people in the audience I want to turn to them for, for for questions first.

Todd Harper Yeah. If I could just. Yeah, respond there for a second. I'm not going to comment on any one individual credit unions. I'm the regulator. It's not, my job to do, but it is my job to improve our fair lending program to make sure that people are, you know, who are getting loans, who are applying for credit, are being protected, as that is happening under the Equal Credit Opportunity Act and under fair lending laws. Since I've joined the board, we've tripled the staff that are committed to fair lending. We are continuing to build out our fair lending program. Uvntil about 8 or 9 years ago, we had never referred a case to the Justice Department. Never, never. We do do that now. And in fact, we are regularly referring. For me, it's a problematic practice if there is a particular group that is being denied credit, then we've got an obligation to go in and look and dig a little deeper to see what are the reasons for it. Some of the reasons may be that they've got a great outreach program, and they're doing a lot of, you know, lending in a community, to say in African-American community overall. But they're also having turn downs as a result of that outreach. So you do have to dig deeper into the numbers, but we're increasing our fair lending in response to this. And in some ways, that's, you know, I know you don't have CRA here, but fair lending also provides an important check, on credit unions overall.

Aaron Klein No, it's great wisdom there. I remember when I served on the Tarp Investment Review Committee looking at small, small banks that were applying for Tarp funds, the heterogeneity within organizations, particularly smaller organizations who are dedicated to serving. I'm always remember this one institution that had too much commercial real estate exposure, until I learned that those were all loans to churches, and that loans to churches are considered commercial because they're not residential. And I thought to me, well, you know, you may want to treat a church differently than you would consider an office building. And it's just that there's huge heterogeneity. Are there lessons that you've seen in the banking community, places that serve particularly communities that you've seen of smaller scale since most credit unions are are of smaller scale, that you think that you think are illustrative for answers here.

Todd Harper So I listen, case in point is minority depository institutions. Last year we added a new column on our quarterly data summary sheet where we not only broke down, credit unions by different asset size buckets and their performance, federal and state chartered credit unions. But we added a new column on MDI, minority depository institutions. And that column was eye opening for me, and it was eye opening in this way. Minority depository institutions, hyper focused, as you said, on serving their members in their communities. There are countless churches on the South side of Chicago, that have a credit union that is attached to them. And those credit unions are two, three, five, $10 million. So they're really, really small. The number that popped out at me was the earnings, the return on average assets. We don't talk about profits in the credit union system. We talk about the return on average assets because they're not for profit institutions. The return on average assets for MDIs, which average $133 million overall, was just as strong as billion dollar plus institutions. What's more, those credit unions, if you looked a little bit deeper while they had higher delinquency rates and you should expect them to, they're doing relationship banking or what was relationship banking. They're helping out that member of the congregation who got into trouble, who, you know, happened to lose their roof in a storm, who happened to have their car break down and need a way to get you? They're helping those people. They may have higher delinquencies along the way, but they have lower charge offs than institutions above billion dollars. So what that says to me is a credit union that has a great focus, good leadership, is able to be just as competitive and in this current environment, achieve the same earnings as $1 billion plus institution. To me, that's a story that's not told often enough and should be told more.

Aaron Klein Yeah, that's that's a powerful story and reminds me, Martin Meeks founded Self-Help Credit Union who talks a lot about that people want to pay back their loan. This idea that there are defaulters out there. And the more you have that relationship, or the fact that they have higher delinquencies but lower charge offs, that common bond when it's real, works in both directions and can work to the benefit of the institution and allow these fantastic results. Let me pause for for questions from from the audience here. I got one up front man over there. Please introduce yourself and please ask a question.

Audience member Hi, my name is [unintelligable]. And my question is with the rise in high interest rate environment and constrained liquidity, what steps is the National Credit Union taking to assist members with, you know, mitigating the credit default risks arising from a lot of small and medium sized enterprises that have taken out huge loans during the pandemic, post pandemic, in the low interest rate environment that are now at risk of defaulting on these loans.

Todd Harper So, in 2022, we saw the largest increase in lending than we had seen in more than 30 years. Year over year loans grew very dramatically. In 2023, we started to see the credit risk developed because many of those loans were given and there was an inflated, if you will, credit score, because the pandemic relief programs had supported people and they had money and they were paying their bills on time. And starting in 2023. Especially as we saw price pressure out there, we started to see some credit quality issues. We're going in to credit unions. We've reminded credit unions that the best thing that they can do is when there is an initial delinquency, it's to work with that member early, start working with them, because those early changes early on can actually prevent that loan that's delinquent from eventually going into default. We've emphasized that in guidance, to credit unions, but also to our examiners that say, if you are taking and looking and working with your members consistent with your policies and practices, we're not going to discourage you and we're not going to look negatively on that in the process. And the place where you really see that happening is the MDI credit unions.

Audience member Good morning, Robert Flock. Thank you for being here, Mr. Chairman. So obviously yesterday we had seven members of the Financial Services Committee send a letter to Chairman McHenry requesting a hearing on the country's largest credit unions lending practices and some reports, the last few months, you know, you talked about some very significant issues today that the industry is facing as it, you know, continues its march into the 21st century with over 130 million members now. It's been about 20 years since Congress has convened an oversight hearing on this growing industry. A lot's changed in that time. Would it behoove Congress to devote some time and energy to some of the issues you discussed here today?

Todd Harper So certainly I am no stranger to the witness table at congressional hearings. I've testified generally twice a year, and, in both the House and Senate, actually, is that four times a year when you consider it, all told, before the House and Senate, I have been available and take questions. I'll continue to make myself available to make questions. It's up to Congress to decide how it wants to, whether it wants, you know, generally what they do is they bring up the NCUA, the Federal Reserve, head of supervision, the FDIC and the OCC. So it's the four of us at the table, together. If Congress wants to organize a hearing that is different than that, I'm certainly happy to participate in it, but that's for Congress to decide.

Aaron Klein I don't know if you've ever thought this way, but I've wondered about Benjamin buttoning my career. You know, we're on the hill when we were younger, working in Congress. And I remember writing all these letters to agencies, and you write the letter to the agency, and then you get something back and it would be a little bit, shall we say, less than fully informative. And it wasn't till I went into the Treasury Department where I realized often what happened was the question was asked, it was answered. And then large parts of the answer were deleted in the official response. But the act of asking the question motivated a whole set of activities behind the scenes that I, as a young staffer, didn't fully appreciate. And then, in point of fact, often would even have greater power because the principal in the agency would say, wait a second, we are going to have to change something. Because if I get asked this question live, I'm not in love with the answer I'm giving in the soft power of letters like that and hearings.

Todd Harper So absolutely. And sometimes it's just a phone call. You know, early on in the creation of the Emergency Capital Investment Program, which was a nine some billion dollar program, that was created to provide investments in minority depository institution and community development financial institutions. The there was a decision made to move what the extension of the period was, and this is was money that was going to be laid out through the institutions at 2% or less interest, or initially for 15 years. And then there and then Treasury made a decision after talking to Senator Warner and others who were sponsors of that legislation to make it 30 years. And our rules didn't allow, we allowed for 15, for subordinated debt, but we didn't allow for 30. And staff said, well, we're only going to be able to allow for 15. And I said that and I talked to staff. I said, well, at the statutory mission, the credit and savings needs some members, especially those of modest means, and this is going to MDIs and to community development institutions. We're going to find a way to get to yes, and it took us some time. But you're right, there is that power of knowing that if you're going to go up, I'm less than satisfied with the answer or not. I didn't want to go to Capitol Hill, certainly, and say, I'm sorry, we're not going to we're only going to allow this money to be used for 15 years into the banking side. It can be used for 30. It made no sense to me. So we do. And you're absolutely right. That does influence how we think, and what we do.

Aaron Klein Yeah. We got time for another question, sir.

Audience member John Collins, nice to see you, Mr. Chairman. Question on the Central Security facility. The central liquidity facility, the 10% who remain, are they the larger institutions? And second, for all those in the that have been in a liquidity facility. Where would they find liquidity resources? You've mentioned the discount window. Many credit unions are now members of the Federal Home Loan Bank system.

Todd Harper So there are many sources of liquidity for a credit union overall. I was focused on the federal liquidity backstop. When all heck happens. Who are you going to turn to to make sure that you can get that money when you need it? And, and it's important to establish your liquidity lines before the pipes freeze, because once the pipes freeze, it takes an incredibly long time to unfreeze them. Short of a federal liquidity backstop, there are a number of other institutions that provided in the credit union space. A corporate credit union can help to provide that liquidity. Also, to Federal Home Loan Bank, there are 1400, 1500 , if I remember correctly numbers. Credit unions belong to federal home loan banks. With respect to the central liquidity facilities members, generally they are larger credit unions, more than $250 million in assets. In fact, we've got a rule that says if you have more than $250 million in assets, you have to have access to at least one federal liquidity facility. Many credit unions have chosen the central liquidity facility. Some have chosen, the Federal Reserve's discount window. Some have actually chosen both, and to make sure that they're set up in both camps. Should they need it overall. We have seen, while we have seen a contraction initially because of that change in the law, that took away the ability of credit unions below $250 million to have access through their corporate credit union. We've seen that number gradually rise over the last year. I think we added, 60 credit unions in all, or so over the last year. We anticipate adding another 80 or so credit unions this year. And that's increasing, what is available. We now have 20.1 or $2 billion, in liquidity that the system can provide. And we recently provided, a liquidity loan to a credit union, that was having some seasonal issues. I anticipate seeing more credit unions applying and using it in the future. Federal home loan banks. I know you've got an interest. There are a way to do that, but they're not that liquidity backstop at the end of the day. When all heck happens.

Aaron Klein Well, a year ago, almost to the day in this very room, Brookings held an event, with Boston University on the federal home loan bank system. I see, former FHFA director Mark Calabria, who spoke at that, at that event. And it was fortuitous because, a month after that event, SVB failed, Silicon Valley Bank and then First Republic, they were the first and second largest borrower, respectively, from the San Francisco Federal Home Loan Bank. And my own research on home loan banks found several credit unions among the five largest borrowers that, various home loan banks have to disclose. We're just about a time, there's one question that came in from the audience online that I'm going to mention. I'm going to mention another question. I'm going to let you pick out what you want to do with with your last word. Online there was a question about how you see artificial intelligence impacting credit unions and impacting credit union regulation. I know that's a topic of, FSOC, has mentioned in their annual report it's something I think the Center on Regulation of Markets is doing a lot of work on. And I anticipate more there. You mentioned credit service organizations in your speech. You also made a comment about focusing on wealthy zip codes. I can't let go that I don't. I walk around and I see this thing called Penn Fed Realty sponsored with Berkshire Hathaway. And I tend to think Berkshire Hathaway is not really focused on low income, real estate communities. And that interaction between the third party organizations and the mission that you mentioned. And the third question I'm going to let you pick from is you mentioned, whenever we we do one of these priority speeches, I'm reminded of the seminal event in my career, when I worked for for Senator Sarbanes, who was the ranking member, and it started in the minority. And then there was a change of control in the Senate in May of 2001. And the senator had a ten page agenda, which he laid out at a press conference and the staff spent time and time working on this. And I view that agenda fascinatingly, because it was put out in May of 2001, and nowhere on that will you find the word accounting. Which perhaps Sarbanes is most associated with and was probably the biggest piece of legislation we pass during the next 18 months, the Sarbanes Oxley Act. Nowhere in those ten pages will you find comments about terrorism. Which was not exactly front and center in May 2001 yet we passed a section of the Patriot Act in response to 9/11 in the Terrorism Risk Insurance Act, which I know we both remember fondly. These were all major pieces of legislation which went through that committee under the next 18 months of his chairmanship. How do you think about the unexpected? Because the only thing I know for sure is between now and when your term expires in 2027, there's going to be something that no one saw coming. And you're going to it is going to become the number one priority. I'm going to tell you the number one priority in America. September 12th, 2001 was not the number one priority september 10th. So how do those three choices take your pick and take us away?

Todd Harper So first of all, I'll start with the last and then, jump to some of the other points. How do I think about the unexpected? It's important for a regulator to have an underlying philosophy. And mine happens to be an acronym. It's FIRE, and good regulators need to be fair and forward looking. They need to be innovative, inclusive and independent. They need to be risk focused and ready to act expeditiously as needed at the institution they regulate, and oftentimes we don't see them acting ready to act expeditiously. Sometimes they they wait. And then we need to be engaged, appropriate with stakeholders to develop effective regulation and efficient supervision. That's FIRE. If you pull out all of those words, that's what underlies how I think about issues. And whenever I get into something unexpected, it's what I fall back on. We knew you started off with talking about the liquidity crisis that we saw one year ago. We knew liquidity issues were happening. We saw that there were fractures happening within the system. And in fact, at the NCUA, I had been directing staff, you know, well ahead of when we saw what happened at SVB and the other institutions. To that, we need a dashboard. We need to have better metrics. We need to have a better understanding of where we are on our liquidity. One thing that I didn't highlight in my remarks today is how the credit union system is the converse of what happened at SVB and Silicon Valley Bank and others. And that converse is reflected in insured deposits. 91% plus of the deposits in the credit union system are insured versus 90 plus percent were uninsured. So when people became uncertain that, oh my God, my money might not be there. That's when the flight occurred. You didn't see that happen on the credit union side. And in fact, you saw greater stability overall. Again, it was that FIRE philosophy that was helping us to plan in advance and think about what we're doing, and we're taking some lessons that we learned from that. We need to have better metrics. For example, at the NCUA. And we're working to, we'll be working to refine our call report systems on liquidity here in the year ahead.

You talked a little bit about AI. And the question that came in, from the online audience. Artificial intelligence has both the promise and the peril as I like to see it. It has the promise that it could make us do our jobs more efficiently. It could help us in making decisions. It could assist us in answering consumer calls. Although I'm going to say this, I personally always press zero, or asterisk or ask for a representative, depending on what system I'm going, because I really can't stand those systems. But I has some real broad promise. But the peril is, is the credit unions need to be handling that risk. It's an issue for banks as well. We're looking at, what should be guidance in this area about managing these risks appropriately. And eventually you will see us come out with something on this area. Overall, we also need to make sure that if you're a lending institution and you're building a model. That that model is not creating a black box for what the credit decision happens, because you're going to then violate the Equal Credit Opportunity Act. If you can't give the reason for why the loan was turned down. So you really need to think about it. You need to think about. We're currently kind of addressing this in some ways with automated valuation models. It was a rule that I actually it was a law and required by the Dodd-Frank act that I worked on that specific provision. And here we are, 14 years later, still working to implement the rule that was required by the Dodd-Frank act. But we know more than about these systems and how they are and how they're evaluating. So that's in some ways actually helpful to us. We've got to balance both the promise and the peril, the risks to the system. The risks to the credit union, the risks to the institution. And we're working to do that. And the last thing you talked about, credit union involvement in real estate. When I was also on the Hill, I led the efforts, to, prohibit banks from engaging in real estate brokerage. It was a huge fight between bankers and the realtors system. Overall, I do believe firmly in the separation of banking and commerce. To me, when you get involved in real estate brokerage, you're starting to step on and make decisions. You've got a vested interest in the loan closing. And that may be counter to what the safety and soundness concerns are. So it's something you need to think about carefully and watch. It's allowed on the credit union side of the coin. Certainly now. But, it doesn't mean that it's always right.

Aaron Klein Yeah. Great. Well, join me in thanking Chair Harper for sharing his wisdom, and we look forward to watching this agenda be implemented. Absolutely. Thank you. Thank you very much.