CUNA
Credit Union National Association

CUNA Regulatory Advocacy Report
Delivering the regulatory news important to credit unions.

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NCUA Extends Effective Date for New Loan Participation Rule

NCUA announced last week that it is extending the effective date of the loan participation rule to Sep. 23, 2013. The effective date was originally July 25, which was 30 days after the rule was published in the Federal Register. CUNA advocated for this change to ensure that credit unions had enough time to comply with the provisions of the new rule.

Housing Finance Reform Progresses as CUNA Advocacy Continues

In the last two weeks, there has been a significant amount of legislative and regulatory movement on how to meaningfully reform Fannie Mae and Freddie Mac. Congress is expected to, for the first time, actively consider the topic after the July Fourth recess.

CUNA's Chief Economist, Bill Hampel, at far left.

Senate: Borrowing significantly from the Bipartisan Policy Center's Housing Policy Commission report, Senators Mark Warner (D-VA) and Bob Corker (R-TN), joined by six bipartisan colleagues from the Senate Banking Committee—Sens. Mike Johanns (R-NE), Jon Tester (D-MT), Dean Heller (R-NV), Heidi Heitkamp (D-ND), Jerry Moran (R-KS), and Kay Hagan (D-NC)—have introduced a bill that would wind down Fannie Mae and Freddie Mac over five years, replacing them with a single housing finance system. At the heart of the new system would be the Federal Mortgage Insurance Corporation (FMIC), a government corporation that would oversee mortgage lending activities; establish and monitor compliance with mortgage requirements; and guarantee and insure a conforming mortgage segment. In addition, the FMIC would fulfill a role in the mortgage finance industry similar to that of the NCUA for credit unions, overseeing an insurance fund that would further protect the taxpayer in the event of losses. Capitalization of the mortgage insurance fund would be through a small fee rolled into the mortgage interest. Corker and Warner

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argue this system would better protect taxpayers from potential loss, rely more heavily on diverse private capital, and continue to keep the mortgage market competitive and liquid. The bill preserves a government guarantee, which Corker and Warner say is necessary to encourage investment in housing finance.

The proposal outlines certain limitations and restrictions for mortgages insured by the FMIC. Eligible mortgages would be required to be Qualified Mortgages under the CFPB's rule, and have borrower equity of no less than 20 percent at closing. Borrowers with less than 20 percent equity would need to purchase mortgage insurance. The idea behind the minimum equity requirement is for borrowers to absorb some of the credit risk in the event of default. After that, the lender and the FMIC insurance fund share risk, with the private capital taking the first part of any losses. The lender, or mortgage-backed security issuer, would take the first 10 percent of the loss, with the FMIC fund absorbing the risk. Should the FMIC fund ever be insufficient to cover losses, the full faith and credit of the U.S. government are guaranteed as to the remainder.

Of particular importance, the bill calls for participation from a wide range of lenders, specifically including credit unions. The bill calls for equal access and equal pricing to any secondary market. Needless to say, CUNA strongly urges Congress to include similar provisions in any housing finance bill.

The proposal calls for Fannie Mae and Freddie Mac to be phased out of business over a five-year timeframe and their portfolios reduced from a balance of $552.5 billion on Dec. 21, 2013 by at least 15 percent each year. After the fifth year, the remaining portfolio balance of mortgages held and guaranteed would transfer to a receiver and the two firms would no longer exist.

Although CUNA has concerns about certain aspects of the legislation, upon introduction, CUNA thanked Senators Warner and Corker for fully considering credit union concerns as the bill took shape. Warner-Corker "is an important first step to creating a secondary mortgage market that focuses on ensuring access to all financial institutions in need of a functioning mortgage market, including credit unions," CUNA President/CEO Bill Cheney said. "We recognize that the legislative process of housing finance reform will be a considerable effort, and credit unions are ready to work with lawmakers to enact changes that will ensure that smaller institutions continue to have fair and affordable access to a vibrant, well-regulated and affordable housing market," he added.

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House: There are increasing signs that the House will begin to consider a very different housing finance reform package after the July 4 recess. Republicans on the House Financial Services Committee are preparing to introduce a bill that would expressly eliminate the government guarantee and replace Fannie and Freddie with a fully private, or mostly private, market. It would also scale back the role of FHA. It has been reported in the press that the committee is also mulling whether to add additional changes to help smaller lenders and credit unions finance home loans more easily by providing some relief from the CFPB's mortgage rules.

Meanwhile, House Democrats are developing their own proposals. On Friday, June 28, Financial Services Committee Ranking Member Rep. Maxine Waters (D-CA) hosted a panel of industry experts, including CUNA's Chief Economist Bill Hampel, regarding how to reform the housing finance system. Credit union access to the secondary mortgage market is important, Hampel said, because credit unions are increasingly selling mortgages to mitigate interest rate risk. Credit unions originated $120 billion in mortgage loans last year, but since the financial crisis, have sold about half of those mortgages. During the first quarter of 2013, Hampel said, credit unions

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sold 60% of all mortgages to the secondary market.

Before the crisis, when rates were higher, credit unions only sold one-third of their mortgages. "That practice of selling loans means a robust secondary market is important to credit unions," Hampel said. Hampel argued that the price to access the secondary market should not be based upon volume of mortgages sold into it, noting that the default rate for credit union mortgages is extraordinarily low, and much lower than that of banks.

Regulatory: The Federal Housing Finance Agency (FHFA), which regulates Fannie and Freddie, is also developing new mortgage-backed securities (MBS) structures to increase private capital in the mortgage market even without legislation. Freddie Mac last week began marketing a new product, Freddie Mac Structured Agency Credit Risk (STACR) securities, designed to offload the first-loss piece of certain government-guaranteed MBS into the private capital markets. The structure of the securities, dubbed "novel and complex" by some traders, was jointly developed by Credit Suisse. Fannie Mae is expected to begin marketing its own similar security shortly.

Regulators Approve Basel III for Banks

The Federal Reserve Board approved a Basel III rule for banks last week. The rule implementing Basel III was jointly written by the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Federal Reserve Board. It represents a significant overhaul of regulatory capital requirements for U.S. institutions. The rule requires thousands of banks to hold higher, more loss-absorbing capital in order to help prevent a repeat of the financial crisis.

The final rule was similar to an initial draft proposal released last June, leaving most of the capital requirements unchanged, including two proposed leverage ratios. There were, however, some exceptions for community banks. Regulators made changes to risk-weights for residential mortgages and gave them a one-time opportunity to "opt-out" of a requirement to include unrealized gains and losses in their capital calculation. The rule also effectively grandfathers certain existing trust-preferred securities. Additionally, smaller institutions are provided a longer transition period, with implementation starting on Jan. 1, 2015, while larger banks must begin compliance on Jan. 1, 2014.

CFPB Issues Procedural Rule on Supervising Nonbanks that Pose Risks to Consumers

The CFPB has recently issued a final procedural rule on supervising nonbanks when the agency has reasonable cause to believe such entities pose risks to consumers. Nonbanks covered by the rule are companies that offer or provide consumer financial products or services; nonbanks do not include banks, thrifts, or credit unions. The agency is authorized to require reports from and conduct examinations of nonbanks subject to its supervision. CUNA strongly agrees that non-depository institutions engaging or that have engaged in conduct that poses risks to consumers on financial products or services should be subject to the most rigorous consumer protection supervision, regulation, and enforcement, as contemplated by the Dodd-Frank Act.

CFPB Publishes Final List of Rural & Underserved Counties for use in 2014

Last week, the CFPB published its final list of rural and underserved counties for use in 2014. The agency previously issued a list of rural and underserved counties for use during 2013. Several of the mortgage rules issued by the CFPB have provisions related to mortgage loans made by creditors that during the preceding year operated predominantly in "rural" or "underserved" counties or mortgage loans made in "rural" counties. The use of the published lists from the CFPB will serve as a safe harbor to determine whether a county is "rural" or "underserved" for a given calendar year.

The CFPB is re-examining the definitions of "rural" and "underserved" and will be studying both of these terms over the next two years. Additionally, some counties' status as rural or non-rural has changed between the 2013 and 2014 lists due to updated information from the 2010 Census, which could result on some creditors losing eligibility for some of the exemptions contained within the escrows final rule, the ability-to-repay final rule, the high-cost mortgage and HOEPA final rule, and the appraisals for higher-priced mortgage loans final rule. To alleviate these concerns and provide additional flexibility for affected small creditors, the CFPB has taken the following steps in recent rulemakings and proposed rulemakings:

- The recently finalized ability-to-repay rule extends the ability to originate balloon qualified mortgages (QM) to certain small creditors that do not operate predominantly in rural or underserved areas during the period from Jan. 10, 2014, to Jan. 10, 2016, to facilitate transitioning from balloons to adjustable rate mortgages. Small creditors that do not operate predominantly in counties on the Bureau's list can still take advantage of the balloon QM provision if they meet the rule's other criteria.
- The CFPB has proposed to extend the same treatment to small creditors for purposes of the high-cost mortgage balloon exemption. If adopted, this proposed change also would allow small creditors not operating predominantly in rural or underserved counties to take advantage of the exemption from the high-cost mortgage balloon restrictions.
- The CFPB has also proposed to extend eligibility for the rural or underserved exemption from the escrows requirement to creditors that operated predominantly in rural or underserved counties in any of the previous three years. Under this proposed change, creditors that operated predominantly in rural or underserved counties in 2012 (and also meet the other criteria and thus are eligible for the exemption during 2013) would not lose eligibility during 2014 as a result of any differences between the 2013 list and the 2014 list that we are posting today (or in 2015 if a county's status changes next year).

For more information on the rural and underserved lists and the requirements under each of the mortgage rules involving these lists, click here.

CFPB Fines U.S. Bank $6.5 million for Violations related to Auto Loans made to Servicemembers

The CFPB recently ordered U.S. Bank and its nonbank partner, Dealers' Financial Services (DFS), to return about $6.5 million to servicemembers for failing to properly disclose an allotment fee charged to participants in the Military Installment Loans and Educational Services (MILES) auto loan program.

In addition to the $6.5 million refund, the companies have agreed to:

- Stop deceptive practices – U.S. Bank and DFS are required to end deceptive marketing and lending practices and will be prohibited from making misleading claims or omissions when marketing add-on products through MILES or similar programs in the future.

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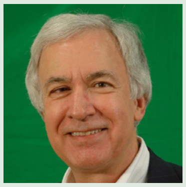
- Provide refunds or credits without any further action by consumers – Servicemembers are not required to take any action to receive their reimbursement.
- Improve disclosures – The companies will take steps to improve their disclosures to servicemembers regarding the cost and other material terms of add-on products.
- Required reporting – Under the orders, both companies will be required to submit a redress plan that we must approve. They must also provide reports to the CFPB to demonstrate their compliance with the orders.

CUNA Regulatory Advocacy Resource Chart

Current CUNA Comment Calls
NCUA Requests Comments on its 2013 Regulatory Review *(submit comments to NCUA by August 5)*
NCUA Proposes a Rule on Derivatives Investment Authority *(submit comments to CUNA by July 22)*
CFPB Seeks OMB Approval to Conduct a Survey on Credit Card Arbitration Provisions *(submit comments to CUNA by July 23)*
Regulatory Advocacy Resource Charts
CFPB Rulemakings - This is a regularly updated chart of proposed & final rules from the CFPB
Rules Applicable to Credit Unions - This is a current chart that shows at least 157 finalized federal regulatory changes that apply to credit unions since 2008

CUNA's **Regulatory Advocacy Team**



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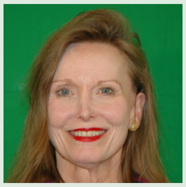

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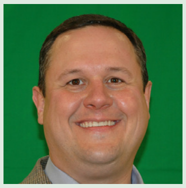

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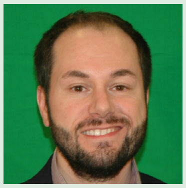

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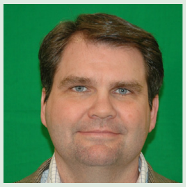

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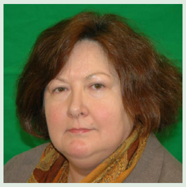

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