Testimony of

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“International and Domestic Implications of De-Risking"

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Introduction

Good afternoon Chairman Luetkemeyer, Ranking Member Clay and Members of the Subcommittee. Thank you for the invitation to appear before you today. My name is John Lewis and I am testifying today on behalf of the National Association of Federally-Insured Credit Unions (NAFCU). I am the Senior Vice President of Corporate Affairs and General Counsel of United Nations Federal Credit Union (UNFCU), headquartered in Long Island City, New York.

UNFCU was established in 1947 by 13 United Nations staff members. Some 70 years later, we have over 127,000 members and $5.2 billion in assets, Still, UNFCU remains committed to its mission of "serving the people who serve the world."

As you are aware, NAFCU is the only national organization exclusively representing the interests of the nation’s federally-insured credit unions. NAFCU's member credit unions collectively account for approximately 70 percent of the assets of all federal credit unions. It is my privilege to submit the following testimony on behalf of NAFCU, our credit unions, and the 113 million credit union members that have been impacted by the compounding regulatory burdens placed on the industry. We appreciate the opportunity to speak about how "de-risking" affects credit unions and their members.

NAFCU's Principles of a Healthy Regulatory Environment for Credit Unions

NAFCU has established a set of tenets that we believe are important aspects of a healthy regulatory environment for credit unions. Some key elements of these tenets can also be applied when looking at the issue of "de-risking."

- **NAFCU supports a regulatory environment that allows credit unions to grow.** NAFCU believes that there must be a regulatory environment that neither stifles innovation nor discourages credit unions from providing consumers and small businesses with access to credit. It is important that concerns about regulators cracking down on risk do not stifle innovation, nor overburden credit unions to the point that they cannot serve members.

- **NAFCU supports appropriate, tailored regulation for credit unions and relief from growing regulatory burdens**. Credit unions are swamped by an ever-increasing regulatory burden from the Bureau of Consumer Financial Protection and other regulatory entities, often on rules that are targeting bad actors and not community institutions. NAFCU supports cost-benefit analysis in regulation, and wants to ensure that we have an effective regulatory environment where positive regulations may be easily implemented and negative ones may be quickly eliminated. NAFCU also believes that enforcement orders from regulators should not take the place of regulation or agency guidance to provide clear rules of the road. This includes seeking regulatory relief and reform that allows credit unions to better serve their members, including in the Bank Secrecy Act and Anti-Money Laundering arena.

- **NAFCU supports a fair playing field.** NAFCU believes that credit unions should have as many opportunities as banks and non-regulated entities to provide provident credit to our nations' consumers. NAFCU wants to ensure that all similarly situated depositories follow the same rules of the road and unregulated entities, such as predatory payday lenders, do not escape oversight. We also believe that there should be a federal regulatory structure for non-bank financial services market players that do not have a prudential regulator, including emerging Fintech companies.

- **NAFCU supports government transparency and accountability.** NAFCU believes regulators need to be transparent in their actions, with the opportunity for public input, and should respect possible different viewpoints. When credit unions provide important information to regulators, the regulator should be transparent in why it was requested and how it is to be used.

- **NAFCU supports a strong, independent NCUA as the primary regulator for credit unions.** NAFCU believes that the National Credit Union Administration is best situated with the knowledge and expertise to regulate credit unions due to their unique nature.

The current structure of NCUA, including a 3-person board, has a track record of success. NCUA should be the sole regulator for credit unions and work with other regulators on joint rulemaking when appropriate. Congress should make sure that NCUA has the tools and powers that it needs to effectively regulate the industry, including in areas that deal with riskier members.

De-Risking and Credit Union Challenges

NAFCU and its member credit unions have consistently recognized the importance of the *Bank Secrecy Act* (BSA) and Anti-Money Laundering (AML) requirements, as further outlined by the Federal Financial Institutions Examination Council (FFIEC), in assisting in the prevention of tax evasion, money laundering, terrorism financing, and other illicit activity. Credit unions are fierce supporters of efforts to combat criminal activity utilizing our financial systems. Our members work closely with examiners to ensure consistent application of BSA risk assessments and regularly inform us that the publication of periodic BSA/AML guidance is very helpful. Still, the implementation of BSA requirements remains a burden for many of our smaller members, especially in the post-financial crisis regulatory environment.

Given credit unions' field of membership limitations, it is important for credit unions to have the potential to serve everyone in their field of membership, including legitimate businesses. Some businesses may come with heightened risks due to the nature of their business. These higher risk businesses increase compliance burdens, costs, and pressures on credit unions. With our unique field of membership at UNFCU, we have been fortunate to have good relationships with our examiners who have worked with us in riskier areas. However, NAFCU has been informed by some of its member credit unions that, while National Credit Union Administration (NCUA) examiners generally will not direct credit unions to stop providing services to higher risk

individuals or businesses, these credit unions can feel pressured by examiners to limit services in order to avoid future examination issues.

It is important to note that when a credit union is serving a higher risk individual or business, they are very thorough in their evaluation and record-keeping; however, when examiners evaluate that relationship, they can be very demanding of the credit union. NAFCU has heard reports that sometimes examiners go beyond what is required by guidance and take action if these heavier demands are not met, even if no issues are found. In some instances the examiner finds no problems on site, but comes back with new requirements after a supervisor's review. NAFCU has even heard of examples of credit unions being downgraded in their CAMEL rating solely for serving certain types of businesses, despite no problems being found in their AML program. This additional pressure and scrutiny from examiners can lead institutions to "de-risk" by limiting services for certain types of members.

UNFCU as well as many other credit unions enjoy good working relationships with their examiners and recognize the importance of working with NCUA, and other regulators, as they examine higher risk members. Sometimes the pressure to "de-risk" comes not from the regulators, but from law enforcement. Although credit unions that deal with higher risk members recognize the importance of sharing critical information with law enforcement, including through subpoenas, some report that they have received unreasonably broad subpoenas asking for all information and correspondence related to any members in a certain type of business. The threat of overbroad investigatory demands makes credit unions hesitant to provide services to legitimate businesses that are targeted as higher risk.

Credit unions can also be impacted by others making the decision to "de-risk." At UNFCU, some of our members have international ties and some are located abroad. As a result, we are presented with a unique set of risks for which we have learned to adapt. We have found that some of UNFCU's traditional partners and vendors have re-evaluated their relationship with UNFCU with more scrutiny, or even "de-risked" by ending our long-standing relationship due to the fact that we serve higher-risk members, despite having no previous problems. This loss of partners and vendors has led to a significant disruption of services and increased costs to us and our members, forcing us to bring on additional staff in order to maintain established service levels. Our unique membership coupled with our vendor relationships gives UNFCU a strong understanding of the challenges from both sides of the de-risking issue.

Ideas to Address De-Risking

In a U.S. Government Accountability Office (GAO) report released in February concerning the impact of "de-risking" by financial institutions in the Southwest, the GAO made the recommendation that FinCEN and the federal banking regulators undertake a retrospective review of the BSA regulations with a focus on how regulatory concerns may be influencing financial institutions' willingness to provide banking services. According to the report, regulators have not fully assessed de-risking trends in previously conducted reviews of BSA/AML regulations.

Credit unions continue to work with FinCEN and other regulators to develop ways to provide services to legitimate higher risk businesses without incurring compliance burdens and costs that are so onerous that "de-risking" becomes the only option. Some ideas for improvement include:

- Creating a "safe-harbor" for the financial institution providing services to high risk accounts if they have met certain requirements in the scrutiny of those accounts.

- Ensuring that risk-based review requirements for financial institutions are understood by examiners. Credit unions report that examiners sometimes request the same maximum review of all entities in higher risk fields, despite varying levels of actual risk.

- Not making the financial institution the "de facto" regulator of a business. It is not uncommon for the financial institution to be pushed to scrutinize legitimate businesses that are already regulated by another entity (often the state). While it may make sense for a financial institution to verify registration and licensing, they should not be forced to verify levels of compliance by the business.

Legislative Proposals to Help

NAFCU supports legislative proposals to address some of the issues raised above and to improve and streamline the BSA/AML process to provide meaningful relief to credit unions in areas where they may be forced to "de-risk."

H.R. 6068, the *Counter Terrorism and Illicit Finance Act*

H.R. 6068 takes important steps to update and modernize the BSA/AML regime. In particular, we support the legislation's proposed increases to the dollar-amount thresholds for Suspicious Activity Reports (SARs) and Currency Transaction Reports (CTRs). The current thresholds were set in 1996 and are now outdated, and because the thresholds have failed to keep pace with inflation, they have led to increased filings that provide questionable benefits. We are also pleased to see that the legislation would require the Secretary of the Treasury to work to streamline and improve the current reporting requirements.

We also appreciate H.R. 6068's focus on encouraging more coordination between law enforcement priorities and financial institution examiners. Although not in UNFCU's experience, many of NAFCU's members have indicated that their examiners are too heavily focused on auditing absolute numbers of SAR filings and identifying procedural issues that do not materially affect risk. As an example, some credit unions have experienced situations where an examiner makes a finding on a CTR based on a pure technicality, such as a strict timing deadline, which does not truly affect the usefulness of the CTR as they are often not as time-sensitive. Clarifying priorities for the nation's BSA/AML policy will help in this regard.

H.R. 6068 also contains important provisions that help ensure financial institutions can innovate in the BSA/AML space, including requiring FinCEN to establish a no-action letter process, and would improve the ability of financial institutions to share suspicious activity.

The bill contains a provision providing an 18-month safe harbor for good faith compliance with the new FinCEN Customer Due Diligence (CDD) Rule as well as the studies regarding the collection of beneficial ownership information as part of the CDD Rule. NAFCU would also support, and encourages the Committee to consider, expanding these provisions to help ensure credit unions have access to beneficial ownership information from the state in which the corporations or limited liability companies were formed.

H.R. 4545, the *Financial Institutions Examination Fairness and Reform Act*

NAFCU is pleased that the House has already passed this important legislation introduced by Representatives Scott Tipton (R-CO) and Carolyn Maloney (D-NY) to help create and ensure an independent process to appeal examiner findings. Enacting this legislation would be an important step to provide relief for financial institutions experiencing perceived pressures from examiners leading them to "de-risk" certain entities.

H.R. 2706, the *Financial Institution Customer Protection Act of 2017*

NAFCU is pleased to see that the House has also already passed this important legislation that would ensure "Operation Choke Point" policies will not be used by regulators to prevent the provision of financial services to a member without a valid reason for doing so that is not based solely on reputation risk. We thank Chairman Luetkemeyer for his leadership on this issue.

International Remittances

Credit unions have the power to provide remittances to individuals in their field of membership; however, the remittance rule issued by the Bureau of Consumer Financial Protection after the

Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), has led many credit unions to "de-risk" and stop that service. Credit unions do not have the ability to control the end-to-end process of an international remittance in the same way that a large international financial institution does. The inability of credit unions to comply with the new disclosure requirements has created additional risks for those credit unions who offer remittance services. Now many credit unions must partner with third-party providers to provide remittance services, often incurring additional costs, which are then passed along to their members.

Some credit unions have determined that originating remittances was not worth the additional cost and risk, and no longer offer the service. The remittance rule is an example of an area where the Bureau could have used its authority under Section 1022 of the Dodd-Frank Act to exempt credit unions, but chose not to do so. As a result, the "de-risking" of remittance services has sent some individuals to underground and online channels to transfer funds, often avoiding the scrutiny such international transactions could have faced by doing it via a regulated financial institution. NAFCU is pleased to see that the Bureau's Acting Director Mick Mulvaney is reviewing this rule.

Marijuana Banking

Although not the subject of this hearing, the banking of individuals and businesses in the marijuana industry is an area of higher risk and scrutiny. The growing number of states that have legalized marijuana in some form has led to uncertainty for credit unions and other financial institutions on how to provide financial services to businesses engaged in these state-approved industries. The large amounts of cash generated by these businesses, creates risk as well as these

businesses are not able to use financial institutions. Not all credit unions have such businesses in their fields of membership, nor have an interest in providing these services. However, others that may be interested have "de-risked" and declined to provide services, due to the legal uncertainty surrounding these businesses. NAFCU encourages Congress to enact legislation that would address the legal ambiguities and uncertainties in the provision of financial services to state-approved marijuana businesses.

Conclusion

NAFCU and its member credit unions recognize the importance of the BSA/AML regime as well as the importance of regulator and law enforcement scrutiny of riskier businesses. Given UNFCU's field of membership, we serve as an example that it can be done. Nonetheless, heavy compliance costs, burdens, and pressures from regulators and law enforcement when dealing with higher risk members and business, can lead many to "de-risk" and stop providing services to them. In addition to advancing the proposals and legislation outlined in my testimony, Congress can help by working with financial regulators and law enforcement to alleviate these burdens and pressures. NAFCU stands ready to work with you in this regard. Thank you for the opportunity to appear before you today. I welcome any questions you may have.