TMG FINANCIAL SERVICES

Newest NCUA Proposed CUSO Regulation Will Likely Stifle Innovation
By Jeff Russell

Innovation is my passion and has been during my two decades of work in the credit union industry. In reviewing the NCUA's proposed CUSO regulation, I am more than a little concerned about the impact that it will have on the ability to foster innovation in our industry. Ever since NCUA started dropping not so subtle hints about this change, I have wrestled with how these new rules would likely impact the ability to collaborate and create the necessary innovative member solutions credit unions need to remain relevant now and in the future.

At this time, I just can't see any upside to the proposed regulation.

My personal experience in working with NCUA has largely been positive. As we worked to launch TMG Financial Services in 2007, we interacted with thoughtful people at the agency who are clearly committed to the credit union industry and were helpful in working with us to change the CUSO rule to allow for credit card loan origination CUSOs. But the dynamics in a regulating innovation are problematic and often at cross-purposes – individual examiners, and the agency as a whole, are not praised when a new and innovative CUSO succeeds, but they are often taken to the woodshed when one encounters problems.

Perhaps this is because while most businesses work to *manage* risk, regulators often work to *eliminate* risk. And, there's the rub. At its core, innovation is about risk. And the key part about CUSOs is that they let the credit union industry take these risks collaboratively, minimizing the risk to any single institution. Let's be honest with ourselves – it will take a significant amount of innovation in the coming decade for credit unions to remain relevant to consumers. This is about transformational change, not incremental change. The days of posting marketing flyers in the break room and having HR supervisors sign up new credit unions members are long gone. Credit unions need to offer the types of products and services that resonate with younger consumers, consumers in emerging markets like the Latino market, and small businesses. These are different than the products we have offered in the past. If history is our guide, CUSOs are the most likely to bring these innovations to the credit union market in a wide scale manner.

But innovation doesn't happen overnight. Innovation can sometimes be a bit messy as you adapt to changing markets and work to define your long-term value proposition. Any new product, service or business needs time to become an established player. In reality, this often means losing money as a business starts up. In a world where NCUA is regulating CUSOs, you have to wonder how much time they'd allow to pass before they would feel compelled to close it down, even if a solid business plan was in place and the owners were supportive and well informed.

In my mind, it is not a huge leap to believe that while this proposed regulation is well intentioned to managing safety and soundness considerations, it could easily position NCUA to take over and run a CUSO.

That begs the question do they have the expertise? All CUSOs are not created equal. Just in our family of companies at Affiliates Management Company there is a card processing company, a compliance and public affairs company, a Hispanic-focused consulting company, a business lending CUSO and a credit card agent issuer. This doesn't even begin to cover new products like our partnership with alternative payments company Dwolla and many of the new CUSOs that are emerging across the country. It is unlikely that the NCUA could ever have the resources to adequately provide informed oversight over such a diverse group of businesses as are represented in CUSOs today.

Perhaps, more importantly, NCUA already has access to CUSO books and records. When a credit union loans, participates or invests in a CUSO, NCUA has the authority to provide oversight to the transaction. The argument for the proposed regulation is more transparency. The information is already at hand, so what more do they need?

I fundamentally believe that this proposal is born out of reaction to management issues and not regulatory issues. This is not to dismiss the severity of the problems that arose in various places in the country during the past few years, but there are few signs that this indicative of a larger problem. It certainly does not rise to the level of a systemic risk for the credit union industry.

In the coming weeks, I know there will be much more debate about this topic. But I believe that this new regulation will not protect the credit union industry from future threats, but instead stifle much needed partnerships and innovation that provide the competitive products and services that current (and future) credit union members deserve.

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