



**National Association
of Federal Credit Unions**
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September 23, 2011

Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

RE: Proposed Rule on Credit Union Service Organizations

Dear Ms. Rupp:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents federal credit unions, I am writing to you regarding the National Credit Union Administration's (NCUA) proposed rule regarding Credit Union Services Organizations (CUSOs).

The proposed rule would represent a significant increase of NCUA's regulatory oversight of CUSOs. First, it would require CUSOs to submit financial reports to the NCUA and appropriate state supervisory authority at least annually. The report would be comprehensive, containing information such as a list of services a CUSO provides, a customer list, information about the CUSO's board and management, and balance sheet and income information. Second, the proposal would extend the application of Part 712 (CUSO rule) of NCUA's rules and regulations to CUSO subsidiaries, including the proposed requirement to submit financial reports to NCUA. Lastly, the NCUA proposal would extend a number of provisions in its CUSO rule that currently apply only to federal credit unions (FCUs) to federally-insured state chartered credit unions (FISCUs).

NAFCU strongly opposes the proposed rule and urges the agency to reconsider the proposal. NAFCU is greatly concerned about the effect of the proposed rule in the ability of credit unions to successfully utilize their CUSOs to meet the needs of their members. Further, as discussed below, NAFCU questions whether the NCUA is in keeping with both the letter and the spirit of the Federal Credit Union Act (FCU Act) by seeking to extend its regulatory reach over CUSOs.

General Comments

CUSOs have long been strong partners for credit unions to meet their members' needs. The range of services credit union members receive through CUSOs, from investments to marketing or insurance, and more, have added a welcomed value. In

addition, and very importantly, CUSOs have proved to be an important source of cost savings for credit unions. During these challenging economic times, credit unions need to be able to function effectively from a business standpoint, and not endure increased unnecessary regulations.

Over the past few years, NCUA has increased its focus on CUSOs through the agency's current regulations requiring credit unions to mandate, in their CUSO agreements, that their CUSOs provide the NCUA access to their books and records. Further, the NCUA has expressed concern over the attendant risk posed to credit unions and to the National Credit Union Share Insurance Fund (NCUSIF) by third parties with which credit unions do business.

Despite the concern expressed by the agency, credit unions, in a vast majority of cases, conduct their relationships with CUSOs and other third parties well within the agency's regulatory parameters and in accordance with all applicable laws and regulations. As the agency has indicated, there appear to be some cases where some credit unions have not appropriately managed their third-party relationships and, consequently, exposed themselves and the NCUSIF to increased risk. These are, however, rare cases and not representative of the conventional third-party relationship credit unions have with third parties, especially CUSOs.

To increase the regulatory burden on CUSOs based on a small number of cases is both unnecessary and unfair. If the NCUA adopts the proposed rule, the benefits that credit unions and their members receive through their partnership with CUSOs would inevitably decrease, even though the arrangements do not pose undue risk.

NAFCU does not agree with the NCUA that CUSOs pose a systemic industry-wide risk, not only because of the fact that a very small percentage of credit union assets have been invested in CUSOs but also because credit unions, under current laws and regulations are greatly limited in their ability to invest in CUSOs. According to the most recently available data, approximately 22 basis points of credit union assets have been invested in or loaned to CUSOs. This hardly constitutes an amount significant enough to be considered to pose a systemic risk. Additionally, credit unions may only invest a maximum of 1 percent of their assets in CUSOs. The fact that credit unions are investing in or lending to CUSOs less than one-quarter of the amount that they could, not only contradicts the agency's contention of system risk, but is also consistent with the risk averse and conservative business principle that credit unions have long followed.

As we have stated many times before, NAFCU strongly supports effective risk management by credit unions, whether it is reputation risk, balance sheet risk, third-party risk, or other risk management. Recently, for example, we wrote to the NCUA generally supporting its proposed rule on interest rate risk management. The heart of this CUSO rule, however, seeks to address manageable risk by means of regulatory over-reach and represents a significant departure from NCUA's traditional role of regulating and

overseeing only federally-insured credit unions. NAFCU cannot support a rule that creates additional regulatory burden without seeing a real need or benefit.

Authority of NCUA

As noted above, current regulations require credit unions to include, in their agreements with their CUSO, provisions to allow NCUA to access the CUSO's books and records. Reasoning that the information that the agency has compiled is incomplete and flawed, NCUA now seeks to require credit unions to include, in their agreements with CUSOs, provisions requiring the CUSO to submit financial reports to NCUA directly.

NAFCU does not believe that the NCUA has the legal authority to require CUSOs to submit their financial reports to the agency. As the NCUA clearly knows, it does not have the authority to examine third parties. In fact, Chairman Debbie Matz, in her testimony before the U.S. Senate Committee on Banking, Housing and Urban Affairs, noted the lack of such authority, stating "NCUA is the only regulator subject to the Financial Institutions Reform, Recovery and Enforcement Act of 1989 that does not have authority to perform examinations of vendors which provide services to insured institutions." *See* Testimony of Debbie Matz, "The State of the Credit Union Industry," December 9, 2010, p. 34.

NAFCU believes the proposed rule represents an attempt to usurp the limitations that Congress placed on the agency's regulatory authority over third-party vendors as the proposed rule enables the NCUA to directly examine CUSOs. In this regard, we note that the agency fails to cite or reference the statutory authority on which it relies in proposing the requirement on CUSOs to submit financial reports. The agency is simply over-reaching as it lacks statutory authority, and NAFCU does not believe the agency should resort to the proposed mechanism to effectively regulate and oversee CUSOs.

Effect on Credit Union Member Services

As stated above, CUSOs have proved to be important partners for credit unions in meeting the needs of their members. They have been innovative, including in terms of product and service development, and offer convenience that credit union members otherwise would not have.

The proposed rule unnecessarily increases regulatory burden on credit unions and their affiliated CUSOs, greatly increases regulatory compliance costs, and would undoubtedly decrease the benefits that credit union members receive from the efficiencies, economies of scale and other benefits and conveniences achieved through CUSOs. In situations where the CUSO is wholly-owned, for example, the CUSO's financials are often consolidated into the parent credit union's financial statements and the credit union incurs costs to obtain a single opinion by a Certified Public Accountant (CPA). The proposed rule's requirement for separate financial reporting and a separate

CPA opinion would not only result in double reporting, increasing the credit union's regulatory burden, but also significantly increase regulatory compliance costs because the credit union would effectively have to pay for the preparation of separate financial reports and for two CPA opinions, among other things.

In addition to the costs associated with compliance, the proposed disclosure requirements would decrease credit unions' ability to facilitate the provision of member services and products at low-cost. One of the agency's proposals, for example, seeks to require that CUSOs submit customer lists, and the agency does not provide any assurances that this information will remain confidential. A CUSO, thus, would have to compromise a valuable and well-guarded asset as a result of the proposal.

Conclusion

Simply put, NAFCU strongly believes that the NCUA should reconsider the proposed rule.

NAFCU appreciates the opportunity to provide comments on NCUA's proposed rule. Should you have any questions or would like to discuss these issues further, please contact me at (703) 842-2215 or by e-mail at fbecker@nafcu.org, or Tessema Tefferi, NAFCU's Regulatory Affairs Counsel, at (703) 842-2268 or by e-mail at ttefferi@nafcu.org.

Sincerely,



Fred R. Becker, Jr.
President and CEO