



4309 North Front Street Harrisburg, PA 17110 Phone: 800-932-0661 Fax: 717-234-2695

September 23, 2011

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

Re: Notice of Proposed Rulemaking, CUSOs

Dear Ms. Rupp:

The Pennsylvania Credit Union Association (PCUA) is a state-wide advocacy organization that represents a majority of the 537 credit unions located within the Commonwealth of Pennsylvania. PCUA appreciates this opportunity to comment on the National Credit Union Administration's (NCUA) Notice of Proposed Rulemaking that addresses Credit Union Service Organizations (CUSOs), 12 C.F.R. Parts 712 and 741.

PCUA enlisted the assistance of its Regulatory Review Committee and State Credit Union Advisory Committee (the Committees) to review the Notice of Proposed Rulemaking. The Committee members are the chief executive officers of credit unions representing all peer groups based on asset size. The comments contained in this letter reflect the input of the Committees and PCUA staff.

Overview

As a general proposition, PCUA supports CUSOs and the ability of credit unions to utilize CUSO structures in an effort to enhance the products and services offered to their members. With the stresses impacting credit unions, any regulatory initiative undertaken by NCUA should produce a more robust environment for credit unions, including CUSO investments or the activities in which CUSOs engage. PCUA remains mindful of the importance of safety and soundness. During our deliberations over the proposed rule, the Committees stressed their support for greater transparency in terms of corporate governance in connection with CUSOs. We maintain that NCUA can strike an appropriate balance between fostering the CUSO environment and safety and soundness considerations by adopting a final rule consistent with the comments offered below.

712.2, CUSO Investment

Proposed section 712.2(d)(3) restates the requirement for a federal credit union that is less than adequately capitalized to seek prior approval to invest in a CUSO if the total cash outlay is more than 1% of the credit union's paid in and unimpaired capital and surplus. The proposal extends this requirement to

federally insured state-chartered credit unions with the investment limit being consistent with state law. The prior approval requirement advances safety and soundness interests. The final rule should ensure, however, that a federally insured credit union has a legitimate opportunity to make a CUSO investment or loan. It is foreseeable that the CUSO activity could enhance the services and earning power of a less-than adequately capitalized credit union. Accordingly, the final rule should outline a procedure for a credit union to submit a request to NCUA or the state regulator. The regulation should establish a time certain for NCUA to either approve or deny the request. (The Pennsylvania Credit Union Code sets a timeline for responses to notices submitted to the Department of Banking.) The rule should articulate the criteria that NCUA will employ when reviewing a request for a CUSO investment. An approval or denial should be reduced to writing and explain the rationale for NCUA's decision. A credit union should have the right to appeal a denial to the NCUA Board.

712.3, NCUA Access to CUSO Information

Section 712.3 poses a troubling dichotomy between competing interests. On the one hand, we understand NCUA's desire to evaluate any risks that a CUSO might present to a federally insured credit union. Conversely, the proposed scheme, which mandates specific contractual terms between a federally insured credit union and a CUSO, treads on an area where NCUA might not have the statutory authority to compel such terms. The proposed rule also threatens traditional notions of freedom of contract.

The requirements of section 712.3(d)(1)-(4) detail a rational set of due diligence standards for almost any commercial transaction. PCUA would support the rule if it were drafted in a manner that recast the section as a set of due diligence standards for federally insured credit unions to follow when making an investment, loan, or transactional decision in connection with a CUSO. This would afford greater transparency to the credit union yielding a more informed business decision. The rule would also place CUSO entities on notice that credit unions investing or obtaining services from the CUSO will expect transparency and adequate access to information. NCUA or state regulators could obtain information regarding the CUSO during the course of an examination.

Our concern over the present language of the rule is that it may exceed NCUA's authority to supervise CUSOs pursuant to the Federal Credit Union Act. In anticipation of Y2K, Congress permitted NCUA and other regulators with examination authority over third parties. NCUA's authority for direct examination of CUSOs sunset in 2001. Section 1757 of the Federal Credit Union Act provides authority for federal credit union to invest in or lend to CUSOs; however, whether NCUA has direct power to procure financial information directly from a CUSO is an open question.

PCUA submits that a rational result would be a reworking of section 712.3. The final language should establish that provisions such as GAAP accounting, provision of financial statements and the requirements for newly formed CUSOs are required due diligence for a federally insured credit union that is contemplating an investment in or loan to a CUSO. The federally insured credit union should obtain that same information on a periodic basis. The due diligence information must be available for the NCUA or the state regulator for inspection. Where a CUSO fails to deliver the due diligence information, it may be prudent for the federally insured credit union to plan an exit strategy. However, a federally insured credit union should not be at risk to lose NCUSIF coverage in such an instance.

712.4, Separate Corporate Identity

Section 712.4, maintenance of separate corporate identities between a CUSO and credit unions, is a prudent rule. This offers significant protection for federally insured credit unions and PCUA supports the

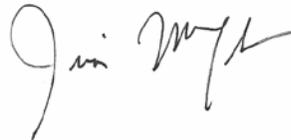
rule. That said, the provisions in 712.4(b) that address the legal opinion as to whether a CUSO can amend its structure and the factors concerning piercing the corporate veil should be clarified. We are concerned that practitioners who represent credit unions will have difficulty providing an adequate opinion on future or potential structures of a CUSO. For example, in the case of an LLC, the attorney reviewing the management agreement and related documentation will be limited to what is before him/her at that time. Any opinion about future structures is likely to result in warnings that may have little value. It is questionable whether a practitioner could even opine on future structures absent some manifestation of intent by the CUSO to amend its structure and an explanation of what the new structure would be. Piercing the corporate veil carries a heavy burden of proof in the litigation context. Analysis and explanations of piercing the corporate veil in an opinion letter offers minimal assistance to a credit union that is entertaining a CUSO transaction.

Conclusion

The Committees see safety and soundness benefits in the proposed rule. Greater awareness of the risk that might be associated with CUSO activity enhances the safety and soundness of credit unions. Establishing uniform due diligence standards through which federally insured credit unions can obtain the information required to make a rationalized business decision serves transparency interests. NCUA or state regulators can then obtain that information through the exam process which satisfies supervisory concerns. The requirement for a CUSO to submit financial reports directly to NCUA by means of a contract with investing credit unions is at odds with the Federal Credit Union Act. The proposed rules for separate corporate identities between the CUSO and credit unions are prudent; however, the requirements for analysis of piercing the corporate veil in the legal opinion should be deleted from the final rule.

Sincerely,

PENNSYLVANIA CREDIT UNION ASSOCIATION



James J. McCormack
President/CEO

JJM:RTW:llb

cc: Association Board
Regulatory Review Committee
State Credit Union Advisory Committee
M. Dunn, CUNA