

Filed via: regcomments@ncua.gov

September 27, 2011

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

Re: Comments on Notice of Proposed Rulemaking - CUSOs

Dear Ms. Rupp:

As a member and owner of a CUSO, I appreciate the opportunity to comment on NCUA's proposal to expand the reporting requirements for credit union service organizations (CUSOs). We are a member of a collaborative CUSO, NCCU, which is a CUSO formed by a group of small credit unions to gain economies of scale.

In general, as a member/owner I oppose the proposed amendments and respectfully ask NCUA to completely withdraw the proposals. Comments below outline my concerns.

General Concerns

1. We believe that NCUA already has adequate authority to manage and mitigate risks posed to the share insurance fund by CUSOs. This includes its broad authority to stop credit union actions to resolve any safety and soundness issues, as well as its authority to order credit unions to divest themselves of ownership of a CUSO and to discontinue doing business with any vendor, including CUSOs. Further, pursuant to §712.3(d)(3) of its Rules and Regulations, NCUA currently has the authority to examine the books and records of CUSOs. With all due respect, even with NCUA's full on-site supervisory and regulatory access to WesCorp and US Central and their financial records, this access did little to identify the recent systemic risk to the share insurance fund.
2. We do not believe NCUA has the statutory authority to examine CUSOs in the manner outlined in the proposal. With this proposal, we believe NCUA is exceeding its statutory authority by moving NCUA closer to direct examination and regulation of CUSOs, which has not been authorized by Congress. Bank and thrift operating subsidiaries are subject to examination by the appropriate federal banking agency pursuant to the Bank Service Company Act, but NCUA has not had similar statutory authority to fully examine CUSOs since 2001, when its temporary CUSO examination authorities were not renewed by Congress after Year 2000 conversion. In our view, the fact that the authority was not made permanent is a clear expression from Congress that it did not intend the agency to regulate CUSOs directly as the proposal would do. NCUA should not require by regulation what Congress does not permit it to do by statute. The agency has expressed a desire for parity with banks' regulatory authority over bank operating subsidiaries. Yet there is no evidence that this regulatory authority mitigated bank losses in the current economic crisis. Moreover, subsidiaries are entities where a single financial institution holds a controlling or greater than 50% ownership interest. CUSO investment is not the automatic equivalent of subsidiary ownership.

3. The costly, unnecessary, and burdensome reporting and audit requirements will hinder the ability of CUSOs and cooperatives like CURoots to continue to innovate and provide cost-effective products and services. If CUSOs are regulated differently from other vendors (i.e., their competitors) they will be placed at a competitive disadvantage, which will curtail the impact they have in the marketplace of keeping a competitor's pricing lower for the industry. Ironically, the proposed rule-making discourages the very collaboration and cooperation that promises to foster credit union profitability and protect the share insurance fund.
4. While we understand that there have been some problems in a small number of CUSOs and their credit union owners, these problems have generally stemmed from a combination of poor economic factors, excessive lending concentrations, and/or lack of adequate and timely use of existing supervisory oversight authority. Such isolated incidents do not warrant NCUA's claim that CUSOs constitute a systemic risk within the credit union industry.

Additional Comments on Proposed Changes

- Access to Information from the CUSO by Regulators
Under the proposal, CUSOs would be required to submit their balance sheets, income statements, and confidential business plans and customer lists to NCUA. These documents comprise a corporation's intellectual property, and could potentially expose private business secrets to public dissemination through Freedom of Information Act requests. Such risks would not be faced by CUSO competitors and could, in fact, be exploited by them. This would be of substantial concern even as a standalone issue.
- Tying CUSO Rule Compliance to Conditions for NCUSIF Coverage
The proposal would condition National Credit Union Share Insurance Fund coverage on a credit union's CUSO agreeing to provide financial statements and conduct financial audits as required under the CUSO regulation. As stated earlier, we believe that NCUA already has adequate authority to manage and mitigate any risks posed to the share insurance fund by CUSOs.
- Paperwork Reduction Act Analysis
We are concerned that while NCUA's Paperwork Reduction Act analysis provides paperwork-related regulatory burden estimates for credit unions, it does not provide estimates of the proposal's regulatory burden on CUSOs. Since CUSOs face significant new costs under the proposal, and costs incurred by a CUSO ultimately reach their credit union owners, leaving out the regulatory burden on CUSOs seriously underestimates the significant economic impact that this proposal will actually have on credit unions. CURoots' objective is to reduce a credit union's operating costs by providing shared back-office services. These additional regulatory requirements will require CUSOs and cooperatives, like CURoots, to incur these additional costs which will ultimately be passed on to member owner credit unions, the exact opposite of what CURoots was organized to do.

Recommended Changes to Current Regulation

While we urge NCUA to withdraw this rulemaking, we believe that a clarification should be made in the current CUSO regulation. Specifically, we ask NCUA to make a distinction with regard to the risk of "piercing the corporate veil" of a CUSO wholly owned by a single credit union versus a CUSO owned by multiple credit unions. For CUSOs with many shareholders, it is unlikely that a court would find the type of circumstances present that would warrant piercing its corporate veil. Where such a risk does not exist as a matter of fact or law, there is no justification for regulatory action. We believe NCUA should define and distinguish multi-credit union-owned entities and exempt them from regulatory burdens directed at single credit union-owned entities (i.e., true subsidiaries). CUSOs vary widely in complexity and ownership structure so "one size" does not fit all. We believe it is misguided to treat all CUSOs as if they are the same.

Current regulation requires “prior to an FCU investing in a CUSO, the FCU must obtain written legal advice as to whether the CUSO is established in a manner that will limit potential exposure of the FCU to no more than the loss of funds invested in, or lent to the CUSO” (§712.4 (b)). Although we agree this may be prudent for a wholly owned CUSO, it should not be required for a CUSO or a cooperative such as CURoots with multiple owners, and with little risk of piercing the corporate veil. Indeed, California state law specifically states “a member of a corporation is not, as such, personally liable for the debts, liabilities, or obligations of the corporation” (CA Corporations Code 12440(a)). In addition, requiring this written legal opinion does nothing to protect the credit union going forward and merely adds additional costs and burdens to credit unions. Therefore, we ask that NCUA change its current requirement for a legal opinion to be applicable only to wholly owned CUSOs.

In closing, I ask NCUA to carefully consider the very real benefits CUSOs provide, and to thoughtfully assess the very real, and negative, impact these proposed changes, as well as existing regulatory burdens, have on CUSOs and the credit unions that depend on them for innovative, cost effective solutions. We believe it is reasonable for NCUA as a safety and soundness regulator to consider whether additional rules are required to address current or potential problems. However, this proposed rule is unreasonable and inappropriate, and is not based on authority under the Federal Credit Union Act.

Thank you for the opportunity to comment.

Sincerely,

Diana Michaels
President & CEO
Western Healthcare FCU

cc: WHFCU Board of Directors