April 30, 2021

Ms. Melane Conyers-Ausbrooks
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Submitted electronically via regulations.gov

Re: Comments on Proposed Rule: Credit Union Service Organizations (CUSOs), RIN 3133-AE95

I. Introduction

The **Center for Responsible Lending (CRL)**, **Self-Help Federal Credit Union**, **Self-Help Credit Union**, and the **National Consumer Law Center (on behalf of its low income clients)** write to oppose the National Credit Union Administration (NCUA or the Board)'s proposal to expand the activities in which credit union service organizations (CUSOs) are permitted to engage.[1] This proposal will authorize predatory lending by credit unions, hampering household security at a time when greater security is badly needed. We believe it will also increase racial discrimination, as families of color are disproportionately targeted with these harmful loans.

For 40 years, Self-Help has created asset-building opportunities for low-income individuals, rural communities, women, and families of color. In total, Self-Help has provided over $9 billion in financing to 172,000 homebuyers, small businesses, and nonprofit organizations and serves more than 185,000 mostly low-income families through 65 credit union branches in North Carolina, California, Florida, Illinois, South Carolina, Virginia, Washington and Wisconsin.

Since 1969, the nonprofit National Consumer Law Center® (NCLC®) has worked for consumer justice and economic security for low-income and other disadvantaged people in the U.S. through its expertise in policy analysis and advocacy, publications, litigation, expert witness services, and training. Our multi-volume consumer law treatise series includes Consumer Credit Regulation.

This proposal is deeply problematic for the following reasons, which we address further throughout these comments:

- The proposal will do significant harm by permitting more high interest rate lending to credit union members and consumers more broadly, at rates prohibited for federal credit unions:
  - Credit unions have historically used CUSOs to engage in predatory payday lending.
  - Payday and other high-cost consumer lending inflicts severe harm on financially vulnerable consumers.
  - The subprime auto lending market is rife with exploitative practices.

[1] NCUA, Credit Union Services Organizations (CUSOs), Proposed Rule, 86 Fed. Reg. 11645 (Feb. 26, 2021).

- The proposal will disproportionately harm communities of color and exacerbate financial exclusion, even as the Board elsewhere emphasizes racial equity and financial inclusion.

- The proposal undermines fundamental principles of the FCU Act:
  - It allows lending that exceeds the FCU Act's interest rate ceiling.
  - It broadly permits lending outside of the credit union field of membership.
  - It poses safety and soundness risks to the credit union system.

- The proposal is not necessary to accomplish its stated goals, as CUSOs are already able to facilitate collective investment in technology without broadened lending powers.

- The proposal fails to justify the Board's change in position on this very issue.

A theme throughout our comments is that the proposal fails to acknowledge, much less wrestle with, the profound risks it poses.

We urge the Board to abandon this proposal. Should the Board proceed, we urge it to amend the proposal with changes that are critical to protecting credit union members and the credit union system. Most critically, any expansion of CUSO lending activity must be limited to loans FCUs are themselves empowered to make.

II. The proposal will do significant harm by permitting more high interest rate lending to credit union members and consumers more broadly.

A. Credit unions have historically used CUSOs to evade the FCU usury ceiling as well as state laws.

Credit unions have used CUSOs to engage in practices hostile to consumers, particularly in the area of payday lending. In January 2009, the National Consumer Law Center (NCLC) documented and communicated to NCUA that a number of credit unions, both state-chartered and federal, were involved in high-cost payday lending through CUSOs.[2]

Some made the loans directly through CUSOs they owned. For example, Kinecta Federal Credit Union purchased Nix Check Cashing and created a CUSO, which operated under the d.b.a. Nix Check Cashing. Kinecta touted its exemption from state payday loan laws, including the laws of its home state of California, which does not permit payday loan repayments, including fees, to exceed $300. Nix used an evasive pricing model – an "application fee" of up to $37.95, plus a 15% periodic interest rate – for a loan due in full on the borrower's next payday, resulting in an effective 262% APR.[3] Despite continued

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[2] *See* Letter from Lauren Saunders, NCLC, to Michael E. Fryzel, NCUA (Jan. 27, 2009), https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/letter-ncua-payday-0109.pdf.

[3] Regulation Z is clear, and the Board has acknowledged, that the application fee, while it may be excluded from an APR disclosure, may not exceed the cost of processing the application. It was highly unlikely that Kinecta's fee represented only the processing cost, and not marketing costs, loan losses, collection costs and other costs. Rather, it was likely that the fee represented an evasion of the federal credit union interest rate limit.

calls for NCUA to address this product, Kinecta continued it through NIX for nearly a decade, until at least 2018.[4] By 2019, NIX no longer appeared to be in operation.

A 2010 NCLC report documented that many more credit unions – over 40 – were involved with payday lending through CUSOs.[5] Credit unions facilitated payday loans by implementing products the CUSOs designed; by earning finder's fees for referring members to CUSO-issued payday loan products; or by funding and selling payday loans to a CUSO they owned.

One leading CUSO product that made high-cost payday loans in the name of federal credit unions was the CUSO e-Access loan. E-Access loans carried a $59 per month "participation fee" on top of a purported 18% APR on a 30-day loan. The fee varied by loan and credit union, ranging from $30-$105, resulting in a true APR of 138%-378%.[6] E-access Loans made triple-digit payday loans in the name of at least 12 FCUs.[7]

Another product was CUonPayday, with true APRs ranging from 141% to 876% APR.[8]

Several federal and state-chartered credit unions were participating in payday lending by earning a finder's fee for loans made to their members through CUSOs (either by promoting the loan through a link on the credit union's website and/or by using the credit union's name on the CUSO website). One state-chartered credit union worked with a credit union technology CUSO, CU*Answers, to develop a turnkey payday lending program to sell to other credit unions for $3,750.[9] That product, "GoodMoney," reportedly carried rates reaching 252% APR.

Some credit unions were also funding or selling triple-digit CUSO payday loans, possibly for the purpose of evading state laws. For example, one Missouri-based credit union had a CUSO with a payday lending division, XtraCa$h, which was making loans with APRs from 214%-391%. It appeared that the credit union was making the loans and then selling them to the CUSO. The loans did not appear on the credit union's call report, and it appeared unlikely that XtraCa$h was registered as a payday lender in any state.[10]

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[4] *See* Comments of the authors of the letter to NCUA on its Proposed Rule on Payday Alternative Loans at 6, Aug. 3, 2018, https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-comment-ncua-aug2018.pdf.

[5] *See* Lauren Saunders, Leah Plunket, NCLC, Stopping the Payday Loan Trap: Alternatives that Work, Ones that Don't. Appendix A-2 and A-3 (June 2010) ("Stopping the Payday Loan Trap"), https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/report-stopping-payday-trap.pdf.

[6] *See* Letter from Lauren Saunders, NCLC, to Michael E. Fryzel, NCUA (Jan. 27, 2009), https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/letter-ncua-payday-0109.pdf.

[7] Stopping the Payday Loan Trap at 27.

[8] *See* Letter from Lauren Saunders, NCLC, to Michael E. Fryzel, NCUA (Jan. 27, 2009), https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/letter-ncua-payday-0109.pdf.

[9] *Id*.

[10] *Id.*

From 2009 to approximately 2013, NCUA evidently worked hard to stop credit unions' involvement in payday lending. In July 2009, it issued a supervisory letter on payday lending that addressed evasive pricing through application fees and participation fees; emphasized that consumer loans were not a preapproved activity for CUSOs ("if a CUSO makes payday loans, then an FCU must divest itself of its ownership interest in the CUSO and may no longer invest or lend to the CUSO"[11]); and warned of the risks to credit unions involved in payday lending, including through finder's fee arrangements – credit risk, transaction/fraud risk, reputation risk, and compliance risk.[12]

Even following this letter, some credit unions were slow to dissociate themselves from payday lending. But the number steadily declined. By 2011, the number of credit unions NCLC identified as being involved in payday lending had dropped to 25 (including 14 FCUs).[13] By 2013, nine FCUs were involved, along with state-chartered CUs.[14] By 2018, we knew of only one credit union, Kinecta. And by 2019 and through today, we know of none.

One lesson here is that extricating credit unions from involvement with payday lending was no easy exercise. It was undoubtedly made easier by the bright-line rule that consumer loans were not preapproved activities for CUSOs, and that FCUs were not permitted to invest in CUSOs making consumer loans, regardless of term. Policing terms of consumer loans in an area historically exploited for purposes of evasion is not a task NCUA should bring upon itself.

B. The proposal will facilitate payday and high-cost installment lending, which inflicts severe harm on financially vulnerable consumers.

High-cost lending causes severe harm to financially vulnerable borrowers and communities. An interest rate limit, like the FCU Act's bright line cap, currently 18%, is the single most effective way to prevent predatory lending.

The notion that higher-cost loans should be allowed because they expand financial inclusion – an argument often heard from lenders and others seeking deregulation – is not supportable. That is predatory inclusion, not real inclusion. Some so-called "fintechs" using the kind of technological advances the proposal seems to contemplate are among the loudest pushing for the ability to avoid state interest rate caps in the name of "access to credit." These lenders, using "soaring rhetoric,"[15] portray their loans as better alternatives to payday loans, but their loans often lead to similar problems. They often carry extremely high rates, with repayment still tied to a borrower's payday, with little regard

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[11] The letter also noted that "state-chartered credit union investment and divestiture requirements in such a CUSO will be governed by applicable state law." NCUA Letter to All Federal Credit Unions, 09-FCU-05, July 2009.

[12] NCUA Letter to All Federal Credit Unions, 09-FCU-05, July 2009.

[13] NCLC, Press Release, Credit Unions Are Still Peddling High Cost Payday Loans: National Credit Union Administration Considers Rule Changes (Sept. 26, 2011), https://www.nclc.org/images/pdf/pr-reports/pr_credit_unions_payday_lending.pdf.

[14] *See* Letter from Lauren K. Saunders, NCLC and Michael D. Calhoun, CRL to Chairman Debbie Matz, NUCA (May 16, 2013), https://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/letter-ncua-cu-payday-may2013.pdf.

[15] *See* Christopher K. Odinet, *Predatory Fintech and the Politics of Banking* 19, 20, 22-28 (Iowa Law Review (2021 Forthcoming)) (Aug. 2020), https://papers.ssrn.com/sol3/Papers.cfm?abstract_id=3677283.

for the borrower's ability to repay while meeting other expenses – all part of a business model where lenders can profit despite high borrower defaults.

Data show time and again that high-cost credit, like that offered by many of these so-called "fintechs," does not drive out other, higher-cost unaffordable credit. It simply piles more unaffordable credit onto already financially vulnerable borrowers.[16] For example, Hope Credit Union described this example in a recent set of comments on rent-a-bank installment loans offered by so-called fintechs offering high-cost loans online laundered through a bank to evade state rate caps:

> [O]ne of HOPE's members, a disabled veteran on a fixed income, received a rent-a-bank loan in July 2019 with no previous high cost lending activities. By May 2020, not even a year later, he is now saddled with an additional six payday loans, owing over $1,000 in monthly payments. Between April 29, 2020, the day he received his $1,200 stimulus check, and May 1, 2020, five lenders extracted $1,004 with the original rent-a-bank lender extracting the largest payment. For another member, at the beginning of the year, the payments on four outstanding consumer loans, inclusive of a high-cost rent-a-bank loan, accounted for 32% of her monthly take home pay. By the end of the year, she was still making payments on all four debts plus two new additional loans, such that the payments now accounted for 60% of her monthly take home pay.[17]

Harm caused by high-rate loans extends far beyond the higher cost itself. High-cost lending turns incentives on their head, so that lenders succeed when borrowers fail – that is, lenders can easily profit even when large portions of borrowers default.[18] Once even small portions of principal are paid down, lenders aggressively push refinances to borrowers to keep them on a high-cost debt treadmill.[19] Even with these high refinance rates, defaults on high-cost loans are extraordinarily high. Elevate is an online lender that touts its "cutting-edge machine learning-powered algorithms"[20] and describes its mission as

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[16] *See* Comments of CRL, NCLC and other consumer and civil rights groups on the FDIC's Request for Information on Small-Dollar Lending at 5-8, Jan. 22, 2019, https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-fdic-smalldollar-rfi-22jan2019.pdf.

[17] *See* Comments of Hope Enterprise Corporation / Hope Credit Union/Hope Policy Institute in response to the OCC Notice of Proposed Rulemaking, National Banks and Federal Savings Associations as Lenders, OCC-2020-0026, RIN-1557-AE97 (Sept. 2, 2020), https://www.regulations.gov/comment/OCC-2020-0026-0168.

[18] *See generally*, NCLC, *Misaligned Incentives: Why High-Rate Installment Lenders Want Borrowers Who Will Default* (July 2016), https://www.nclc.org/issues/misaligned-incentives.html.

[19] The CFPB found that for online payday installment loans (the channel for most new "fintech" loans) refinance rates were very high. CFPB Supplemental Findings on payday, payday installment, and vehicle title loans (June 2, 2016) at 15 (35% for storefront, 22% for online); *see also* Elevate Credit, Inc., Form 10K, 2019, https://www.sec.gov/Archives/edgar/data/1651094/000165109420000010/elevate10-kx2019.htm, at 15 (noting "[a]pproximately 55% of Rise installment customers in good standing had refinanced or taken out a subsequent loan as of December 31, 2019, with 40% of the outstanding Rise installment loan balances on that date consisting of new customer loans and 60% related to returning customer loans."). While mainstream lenders also often have substantial rates of refinancings, those lenders also charge rates that permit reasonable amortization of loan balances.

[20] https://www.businesswire.com/news/home/20171003005423/en/Elevate-Customers-Save-More-Than-2-Billion-Thanks-to-Advanced-Tech-Enabled-Underwriting

"Good Today, Better Tomorrow."[21] But Elevate's loans average 103% APR[22] and it has net charge-offs as a percentage of revenues of 41%.[23]

Thus, interest rate limits are an essential component of responsible lending – indeed, an essential characteristic of "credit for provident or productive purposes" – because they better align lender incentives with borrower incentives by making it more difficult for a lender to build a business model with high defaults. Lower interest rates enable borrowers to make progress on paying down principal and make the loan cost reasonable for the borrower. Yet this proposal does not consider the risks to consumers posed by facilitation of lending above the FCU Act rate ceiling.

Enabling higher-cost lending is particularly ill-timed in light of the pandemic and the related economic crisis. We would urge the Board to focus its attention resources on how credit unions can provide relief to members during this time, rather than exposing consumers to additional risks. As Chairman Harper has noted, because of this rule, some consumers "may end up paying much more for their loans."[24]

C. The proposal will facilitate exploitative auto lending.

The proposal poses similar concerns related to auto lending. The subprime auto loan market is rife with abuses. The collapse of the subprime mortgage lending market in 2008 sent investors seeking higher yields to the subprime auto lending market. In order to make their loans more attractive to auto dealers, lenders relaxed their underwriting standards, reflected in rising loan-to-value (LTV) ratios and lengthening loan terms, both of which are more pronounced in the subprime market. Lenders routinely allow dealers to make loans that substantially exceed the value of the car, often allowing dealers to finance additional insurance products such as extended warranties and credit insurance policies. Delinquency and repossession rates in the subprime market over the last decade have reflected this less prudent underwriting.[25]

This proposal will permit FCU investment in CUSOs making auto loans at any rate. The rates on subprime auto loans reach as high as 30 percent.[26] There is no reason for NCUA to be expanding credit union involvement in auto loans above the rates FCUs are permitted to charge, creating substantial reputation and financial risk for those FCUs as investor-owners of CUSOs that originate subprime auto loans.

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[21] Elevate Form 10K, 2020, at 6; *see also* Elevate's website at https://d18rn0p25nwr6d.cloudfront.net/CIK-0001651094/e87f1c36-f251-4ff6-bded-860ecf59f594.html.

[22] Elevate Form 10K, 2020, at 84.

[23] Elevate Form 10K, 2020, at 70; *see also* CFPB Supplemental Findings on payday, payday installment, and vehicle title loans (June 2, 2016) at 9 (the CFPB found that 55% of online loan sequences ended in default).

[24] Board Member Todd M. Harper Statement on Credit Union Service Organizations Proposed Rule, Jan. 14, 2021, https://www.ncua.gov/newsroom/speech/2021/board-member-todd-m-harper-statement-credit-union-service-organizations-proposed-rule.

[25] *See* Telis Demos, *Auto Loans Are Running on Fumes*, Wall Street Journal, Apr. 29, 2020, https://www.wsj.com/articles/auto-loans-are-running-on-fumes-11588158000

[26] Michael Corkery, *As Auto Lending Rises, So Do Delinquencies,* New York Times, Nov. 30, 2016, https://www.nytimes.com/2016/11/30/business/dealbook/as-auto-lending-rises-so-do-delinquencies.html.

D. The proposal will disproportionately harm communities of color and exacerbate financial exclusion, even as the Board elsewhere emphasizes racial equity financial inclusion.

High-cost lenders peddling unaffordable loans cause particular harm to communities of color,[27] often in the same geographic areas that experienced redlining. Storefront high-cost lenders have long targeted borrowers of color, more likely to locate stores even in more affluent communities of color than in less affluent white communities.[28] Online high-cost lenders may focus more on subprime credit score than geography, although we understand that some lenders use zip codes to target online marketing. But historical discrimination against communities of color is also reflected in credit scores.[29] Lenders that focus on borrowers with subprime credit scores will inevitably disproportionately target borrowers of color. The algorithms and big data that "fintech" lenders use may also result in disparate impacts on these communities.[30]

Moreover, when online lenders promote their models as expanding economic inclusion, this often puts borrowers of color among their target borrowers. Communities of color have historically been disproportionately left out of the traditional banking system, a disparity that persists today. Some defend the high-cost "fintech" loans as bringing communities of color into the economic mainstream. But high-cost loans, particularly with their high association with lost bank accounts,[31] drive borrowers

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[27] *See* CFPB Payday Rule, 82 Fed. Reg. at 54556-57 (African Americans are payday borrowers at three times the rate, and Hispanics at twice the rate, of non-Hispanic whites (citing 2015 FDIC National Survey of Unbanked and Underbanked Households (calculations using custom data tool)). Vehicle title borrowers are also disproportionately African American and Hispanic. *Id*.)

[28] Li, et al., *Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California,* Center for Responsible Lending (2009), http://www.responsiblelending.org/payday-lending/research-analysis/predatory-profiling.pdf; Brandon Coleman and Delvin Davis, *Perfect Storm: Payday Lenders Harm Florida Consumers Despite State Law*, Center for Responsible Lending at 7, Chart 2 (March 2016); Delvin Davis and Lisa Stifler, *Power Steering: Payday Lenders Targeting Vulnerable Michigan Communities*, Center for Responsible Lending (Aug. 2018), https://www.responsiblelending.org/research-publication/power-steering-payday-lenders-targeting-vulnerable-michigan-communities; Delvin Davis, *Mile High Money: Payday Stores Target Colorado Communities of Color*, Center for Responsible Lending (Aug. 2017; amended Feb. 2018), https://www.responsiblelending.org/research-publication/mile-high-money-payday-stores-target-colorado-communities-color.

[29] *See* Chi Chi Wu, *Past Imperfect: How Credit Scores and Other Analytics "Bake In" and Perpetuate Past Discrimination*, National Consumer Law Center (May 2016), https://www.nclc.org/images/pdf/credit_discrimination/Past_Imperfect050616.pdf.

[30] *See* Testimony of Chi Chi Wu, National Consumer Law Center, Before the U.S. House Committee on Financial Services Task Force on Financial Technology Regarding "Examining the Use of Alternative Data in Underwriting and Credit Scoring to Expand Access to Credit" (July 25, 2019); Carol A. Evans, *Keeping Fintech Fair: Thinking about Fair Lending and UDAP* Risks, Consumer Compliance Outlook (2017), https://consumercomplianceoutlook.org/2017/second-issue/keeping-fintech-fair-thinking-about-fair-lending-and-udap-risks/; *see also* Christopher K. Odinet, *Predatory Fintech and the Politics of Banking* 19-20 (Iowa Law Review (2021 Forthcoming) (Aug. 2020), https://papers.ssrn.com/sol3/Papers.cfm?abstract_id=3677283.

[31] CFPB found that about half of borrowers with online payday or other high-cost online loans paid a nonsufficient funds (NSF) or overdraft fee. These borrowers paid an average of $185 in such fees, while 10% paid at least $432. It

out of the banking system and exacerbate this disparity. By sustaining and exacerbating an existing precarious financial situation, high-cost lending reinforces and magnifies existing income and wealth gaps – legacies of continuing discrimination – and perpetuates discrimination today.

Racial discrimination is also of particular concern in the auto market. Data has long showed that Black and brown car buyers are more likely to have their interest rates marked up through discretionary dealer mark-ups than similarly-situated white borrowers, and that those who do have their interest rates marked up more than white borrowers.[32] A 2018 study by the National Fair Housing Alliance paired white and non-white testers to visit auto dealerships and shop for the same car within 24 hours of each other. More often than not, the better qualified non-white applicant was offered higher cost financing options than the less qualified white applicant, resulting in those non-white borrowers paying on average $2,662 more than the white borrowers over the life of the loan.[33] Erosion of the consumer protections on the auto loans with which FCUs may be involved only heightens the risk of discriminatory impact on credit union members and other consumers of color. Investing in CUSOs that serve non-members and members with loans that violate the FCU usury ceiling creates not only reputation risk, but compliance and legal risk for the investing FCUs.

Over the last year, the Board has elevated its commitment to racial equity and inclusion. When Board Member Hood served as Chairman, he stated that "perhaps the most important [thing] is doing everything we can to embrace the strengths of diversity, equity, and inclusion — and in particular, encourage greater financial inclusion for all."[34] Chairman Harper recently stated that equity and inclusion will be guiding priorities in NCUA decisions addressing current economic and marketplace realities.[35] This proposal, by facilitating lending that has always been racially discriminatory, is squarely at odds with these commitments.

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further found that 36% of borrowers with a bounced payday payment later had their checking accounts closed involuntarily by the bank. CFPB Online Payday Loan Payments at 3-4, 22 (April 2016).

[32] For discussion of discrimination uncovered by lawsuits in the 1990s, *see* NCLC, *Racial Disparities In Auto Loan Markups State-by-State Data* (June 2015), https://www.nclc.org/images/pdf/car_sales/ib-auto-dealers-racial_disparites.pdf. In addition, the Consumer Financial Protection Bureau's investigations found that borrowers who identified as African American, Latino, and Asian/Pacific Islander paid between 20 and 30 basis points more for their loans than similarly situated white borrowers, adding between $200 and $300 in additional interest over the life of those consumers' loans. *See*, *e.g.*, CFPB Takes Action Against Fifth Third Bank for Auto-Lending Discrimination and Illegal Credit Card Practices, Sept. 28, 2015, Attorney General Tong weighed in with Congress last week, along with 24 other AGs, urging members of Congress to support this resolution overturning that rule.

[33] National Fair Housing Alliance, *Discrimination When Buying A Car: How the Color of Your Skin Can Affect Your Car-Shopping Experience* (Jan. 2018), http://nationalfairhousing.org/wpcontent/uploads/2018/01/Discrimination-When-Buying-a-Car-FINAL-1-11-2018.pdf.

[34] NCUA Chairman Rodney E. Hood's Remarks before the World Council of Credit Unions/Credit Union National Association Webinar: "An International Perspective on Financial Inclusion, Social Justice and Credit Union Regulatory Advocacy", As Prepared for Delivery on Sept. 21, 2020, https://www.ncua.gov/newsroom/speech/2020/ncua-chairman-rodney-e-hoods-remarks-world-council-credit-unionscredit-union-national-association.

[35] Chairman Harper: Focus on Diversity, Equity, Inclusion, and Social Justice, March 9, 2021, https://www.ncua.gov/newsroom/press-release/2021/chairman-harper-focus-diversity-equity-inclusion-and-social-justice.

III. The proposal undermines fundamental principles of the FCU Act.

A. The proposal allows lending that exceeds the FCU Act's interest rate ceiling, including illogically permitting FCUs to own CUSOs that make loans that FCUs may not originate or purchase.

The proposal states that under the proposed rule, "CUSO originated loans would not be subject to the same restrictions as loans originated by FCUs," including those related to loan terms like interest rate, maturity, and prepayment.[36] It notes this is true even for CUSOs wholly owned by FCUs because they "are separate entities" and "are not subject to direct NCUA supervision."[37]

The idea that lack of NCUA supervision is a justification for permitting and enabling high-cost lending is illogical. Lack of supervision is a reason for even more guardrails, not fewer. As discussed below, allowing risky lending though CUSOs poses safety and soundness risks for the credit union.

The proposal notes that an FCU may not purchase a loan from a CUSO unless the loan meets the requirements of NCUA's eligible obligations rule,[38] and may not purchase a loan participation from a CUSO unless it complies with the NCUA's loan participations rule.[39] Those rules limit FCU loan purchases and loan participations, respectively, to loans that FCUs are "empowered to grant."[40] Loans FCUs are empowered to grant "refers to the authority of an FCU to make the types of loans permitted by the [FCU] Act, NCUA regulations, FCU Bylaws, and its own internal policies."[41] NCUA has stated that "[b]ecause FCUs can only participate in loans they are empowered to grant, FCUs cannot participate in loans with an interest rate greater than the maximum allowable interest rate, which is currently 18%."[42]

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[36] Proposed Rule, 86 Fed. Reg. at 11647.

[37] *Id.*

[38] *Id.*, citing 12 CFR 701.23(b).

[39] *Id.*, citing 12 CFR 701.22.

[40] 12 CFR 701.23(b): *Purchase.* (1) A Federal credit union may purchase, in whole or in part, within the limitations of the board of directors' written purchase policies:

> (i) Eligible obligations of its members, from any source, if either:
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> > (A) They are loans it is empowered to grant or
> >
> > (B) they are refinanced with the consent of the borrowers, within 60 days after they are purchased, so that they are loans it is empowered to grant….

[41] NCUA, Meaning of the Phrase Empowered to Grant in NCUA Regulations, 04-0713, Oct. 2004, https://www.ncua.gov/regulation-supervision/legal-opinions/2004/meaning-phrase-empowered-grant-ncua-regulations.

[42] NCUA, Supervisory Letter, Evaluating Loan Participation Programs, "Exhibit A: Summary of NCUA Rules Applicable to Loan Participations," LCU2008-26, https://www.ncua.gov/files/supervisory-letters/LCU2008-26Enc-2.pdf ("Interest Rate. Because FCUs can only participate in loans they are empowered to grant, FCUs cannot participate in loans with an interest rate greater than the maximum allowable interest rate, which is currently 18%.").

Thus, it appears the proposed rule produces the incongruous effect that an FCU may not purchase a loan or a participation in a loan that exceeds the FCU rate cap but can partially or even wholly own – and profit from – a CUSO that may make such loans. It also would permit CUSOs to originate loans in which they would not be permitted to purchase or sell participations.[43]

These results are both illogical and, as discussed below, at odds with the FCU Act. The FCU Act provides that ''[f]ederal credit union means a cooperative association organized in accordance with the provisions of this [Act] for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes."[44] The FCU Act limited the credit it intended to facilitate to that subject to its usury ceiling. FCU involvement in loans that exceed that ceiling, whether directly or via investment in a CUSO, clearly violates Congressional intent. Both NCUA and the Eighth Circuit have taken the position that payday lending is inconsistent with an FCU charter. In *Oiciyapi Federal Credit Union v. National Credit Union Admin.*, 936 F.2d 1007 (8th Cir. 1991), the court affirmed the NCUA's decision to dissolve a FCU on the grounds, *inter alia*, that it failed to promote thrift as required by the credit union charter:

> The NCUA argues in response that Oiciyapi is not serving any purpose relevant to the goals of the FCUA, and that the very things that keep Oiciyapi solvent and profitable demonstrate that it fulfills no useful function as a federal credit union. Oiciyapi's primary activity, according to testimony and documents in the record, is granting payday loans…. Payday loans are not "credit for provident or productive purposes," [12 U.S.C. § 1752(1),] as they are not used for investment.[45]

This same logic should apply to any loans, whether single-payment or installment loans, made in evasion of the FCU usury ceiling.

Moreover, NCUA defines a CUSO in part as an organization "whose business relates to the routine daily operations of the credit unions it serves."[46] Loans above the FCU Act usury cap are not part of the routine operations of credit unions. In addition, CUSO engagement in higher-cost loans than permitted for FCUs creates reputational risk to credit unions that the NCUA has an obligation to minimize.

B. The proposal broadly permits lending outside of the credit union field of membership.

As the proposal notes, NCUA has long been concerned that expansion of CUSOs' authority to lend would be perceived as dilution of the FCU common bond requirement.[47] NCUA has been concerned about "FCUs benefiting from CUSO profits generated from non-members."[48] Yet the proposal fails to

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[43] 86 Fed. Reg. 11647 ("To remain consistent with the NCUA's loan participation rule, this proposed rule would grant CUSOs the authority to only purchase and sell participation interests that are permissible for FCUs to purchase and sell.").

[44] 12.U.S.C. 1752(1).

[45] 936 F.2d at 1011.

[46] 86 Fed. Reg. at 11645 (citing 12 CFR 712.1(d), 712.3(b), and 712.5).

[47] 86 Fed. Reg. at 11646.

[48] *Id*.

meaningfully address this longstanding, legitimate concern or to explain why it should no longer preclude the agency from dramatically expanding CUSO-originated loans far beyond the credit union field of membership.

C. The proposal fails to consider that unsupervised expansion of CUSO activities poses risk of loss to the National Credit Union Share Insurance Fund.

The current CUSO rule reflects and the proposal broadly acknowledges that "[l]ending activities are considered complex or high risk" and that CUSOs engaged in credit and lending activities "may be exposed to significant levels of credit, strategic, or reputation risks."[49] But the proposal fails to wrestle with these risks – particularly in light of the lack of NCUA supervision of CUSOs. In particular, the proposal does not consider the risks to the National Credit Union Share Insurance Fund (NCUSIF) posed by expansion of CUSO activities.

Indeed, the NCUA Inspector General (IG) has cited CUSO activity as a primary reason for prior credit union failures and consequent drains on the fund. For example, the IG found that Eastern New York Federal Credit Union's 2011 failure, which cost the NCUSIF an estimated $3.6 million, was due primarily to its CUSO activity.[50] It separately found that the 2012 demise of California-chartered Telesis Community Credit Union, causing estimated losses to the fund of $77 million, was caused in part by missteps in acquiring certain CUSOs,[51] failure to do due diligence related to CUSOs,[52] and a dependence on fee and service income from its CUSOs.[53]

IV. The proposal is not necessary to accomplish its stated goals, as CUSOs are already able to facilitate collective investment in technology without broadened lending powers.

The proposal does not offer any compelling rationale for permitting CUSOs to offer any type of loan an FCU may originate. Its primary rationale for this expansion, which it acknowledges would "principally result in CUSOs originating automobile loans and small dollar consumer loans,"[54] is technological advancement in lending. It cites "consumer expectations for financial services" as "expanding with unprecedented speed."[55] And it notes increased targeting by nonbank firms of these products "traditionally provided by credit unions."[56]

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[49] 86 Fed. Reg. at 11647.

[50] *See* NCUA Office of the Inspector General, Material Loss Review of Eastern New York Federal Credit Union at 8 (Nov. 19, 2012), https://www.ncua.gov/files/audit-reports/OIG-12-14_MLREasternNYFCU.pdf.

[51] NCUA Office of the Inspector General, Material Loss Review of Telesis Federal Credit Union at 5 (March 15, 2013), https://www.ncua.gov/files/audit-reports/OIG-13-05MLRTelesis.pdf.

[52] *Id.* at 13.

[53] *Id*.

[54] 86 Fed. Reg. at 11646.

[55] *Id.*

[56] 86 Fed. Reg. at 11647.

The proposal notes that in the past, a "primary rationale" for permitting CUSOs to engage in a certain kind of loan origination is that certain lending requires an expertise that FCUs may not possess.[57] It notes that NCUA has found in that past that vehicle loans and general consumer loans required less expertise than "other more sophisticated lending categories permissible for CUSOs."[58] Indeed, it had found that general consumer loans were "relatively easy to offer and process."[59] It suggests that in light of today's technological advancements, the Board's conclusion has changed.

This argument is not compelling. Credit unions that wish to better digitize their consumer or auto lending do not need this rule in order to do so. They can purchase technology from third parties, including from CUSOs. CUSOs' permissible activities already include "loan support services, including loan processing, servicing, and sales,"[60] which means that CUSOs can play a support role in credit unions' consumer lending without revising the CUSO rule at all. By no means do CUSOs need to "originate, purchase, sell and hold" any type of loan an FCU may originate, sell, and hold, in order to facilitate technological advancements among credit unions. And they certainly do not need to originate high-rate loans that are illegal for the FCU to offer directly.

In terms of small dollar lending, NCUA already has a rule that facilitates "payday alternative loans" (PALs) by permitting significant upfront fees outside of the FCU cap and a higher interest rate. NCUA recently made that rule more flexible, including by eliminating the 30-day membership requirement on PALs II Loans.[61] PAL pricing is limited; its features are clearly prescribed; and its frequency is limited to six loans in a twelve-month period, all of which serve to make PALs far less likely to inflict harm on borrowers than loans enabled by CUSOs that exceed the FCU Act limit on interest rates. The Board should not be taking any steps that will expand small dollar lending at a cost that exceeds those permitted by the FCU or by the Board via the PALs program.

The proposal cites a 2018 U.S. Treasury report for the notion that technological developments "lower[] the cost of credit as well as providing greater access to credit."[62] But lower cost of credit is an argument for lower interest rates, not higher ones.

Moreover, it should be noted that this 2018 report pushed for broad deregulation of non-bank lenders and severe erosion of longstanding protections at the federal and state level. Senator Sherrod Brown noted that the Treasury report "embraces the shortsightedness of pre-crisis regulators," "exalt[ing] the benefits of 'financial innovation' while "recommend[ing] gutting important consumer protections."[63]

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[57] 86 Fed. Reg. at 11646.

[58] *Id.*

[59] *Id.*

[60] 12 CFR 712.5(j)(2).

[61] NCUA, Payday Alternative Loans, Final Rule, 84 Fed. Reg. 51942, 47 (Oct. 1, 2019).

[62] 86 Fed. Reg. at 11646 (citing U.S. Treasury, "A Financial System That Creates Economic Opportunity: Nonbank Financials, Fintech, and Innovation," July 2018, https://home.treasury.gov/sites/default/files/2018-07/A-Financial-System-that-Creates-Economic-Opportunities---Nonbank-Financi....pdf.

[63] Brown Opening Statement at Banking Committee Hearing on Fintech, Sept. 18, 2018, https://www.banking.senate.gov/newsroom/minority/09/20/2018/brown-opening-statement-at-banking-committee-hearing-on-fintech.

The report included a suite of policy proposals, which the federal financial regulators under the Trump Administration followed through on, and that have placed consumers at much higher risk of predatory lending than they were prior. The report's recommendations included the CFPB rescission of its rule to address unaffordable payday and car title lending; an OCC rule to reverse the 2015 *Madden v. Midland* decision in order to promote bank/non-bank partnerships that evade state laws; and the OCC "fake lender" rule that blesses "rent-a-bank" schemes and threatens to gut the effectiveness of state interest rate limits in all 50 states.[64]

Thus, the Board should not take at face value this report's suggestion that use of new technologies or increased access to credit is desirable at any cost. Indeed, technological developments also pose very real risks involving evasion of state interest rate limits, fair lending violations, floods of unaffordable credit, and ultimately severe harm to consumers. This is particularly true when promoting "fintech" comes at the expense of consumer protections, which fintech lenders often urge be rolled back in order to facilitate their "innovative" products. This rule appears to be another example of erosion of consumer protections that will enable "fintech" lending without adequate consumer safeguards.

V. The proposal fails to justify the Board's change in position.

The Board has not demonstrated that the concerns about expanded CUSO lending activity it has raised previously can be overcome. The Board states that it has "reconsidered its 2008 position" and that the proposed rule "may better enable FCUs to compete effectively in today's marketplace and better serve their members."[65] It notes that its historical reasons for not granting CUSOs general lending authority included (1) concern about a perceived dilution of the FCU common bond requirement; (2) concern that if member loans were being made by CUSOs, the NCUA could have a duty to examine such loans, leading to stricter NCUA examination authority over CUSOs; and (3) concern that CUSO engagement in a core credit union function could negatively affect affiliated credit union services.[66]

The Board asserts or suggests that these concerns have not materialized as a result of CUSO's existing lending activities.[67] But it does not address why these concerns still would not apply to lending activities the Board has affirmatively chosen *not* to authorize for CUSOs in the past, including vehicle and general consumer lending.

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[64] U.S. Treasury Report, *supra.* The rent-a-bank lending that these rules endorse has led to an explosion of predatory lending that harms consumers. *See* Testimony of Lauren K. Saunders, NCLC, on behalf of its low income clients, before the House Financial Services Committee on Rent-A-Bank Schemes and New Debt Traps: Assessing Efforts to Evade State Consumer Protections and Interest Rate Caps (Feb. 5, 2020), http://bit.ly/debt-trap-schemes; Comments of Center for Responsible Lending, National Consumer Law Center (on behalf of its low income
clients), and several additional consumer and civil rights organizations, on the OCC's proposed so-called "true lender" rule Sept. 3, 2020,
https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/comment-occ-truelender-3sep2020.pdf.

[65] 86 Fed. Reg. at 11646.

[66] *Id.*

[67] *Id.*

It is particularly striking that NCUA has failed to address the concern that CUSOs would need to be more strictly examined if they engage in vehicle and general consumer lending. As noted above, supervision would be all the more important given the proposal's position that CUSOs need not comply with FCU Act interest rate limits, and the fact that CUSOs have been engaged in high-cost, high-risk lending in the past.

VI. Should the Board proceed, it should significantly strengthen the rule and avoid weakening it.

A. Any rule expanding CUSO lending should be limited to loans FCUs are permitted to make directly.

Any rule permitting CUSOs to engage in expanded lending practices should limit loan activity not to "any *type* of loan permissible for Federal credit unions" but rather to any *loan* FCUs are empowered to grant – that is, only loans carrying terms that are permitted for FCUs to originate. Should the Board not limit CUSO lending to loans FCUs are empowered to grant, it should at a minimum make clear that FCUs may not be involved in any way in CUSO lending activity that would be unlawful for the FCU to engage in itself. Importantly, this prohibited involvement should include FCUs' contracts with CUSOs, whether through the finders' fee arrangements we have seen in the past, through loans to the FCUs' members, or through links from an FCU's website to a CUSO's website. The CUSO Rule states that "an FCU may invest in, loan to, *and/or contract with* only those CUSOs that are … engaged in the preapproved activities and services related to the routine daily operations of credit unions."[68] Thus, the CUSO Rule does not merely restrict FCU investments in or loans to CUSOs, but also their contracts. Any FCU contract with a CUSO engaged in lending that an FCU could not engage in directly violates the CUSO Rule because, again, such activity is not a service "related to the routine daily operations of credit unions."[69]

B. NCUA should emphasize that CUSOs may not use arrangements with credit unions to evade state laws.

Non-bank lenders are increasingly seeking to evade state interest rate limits. Unfortunately, during 2020, the OCC and FDIC sought to oblige by attempting to preempt state laws as applied to non-bank lenders via those entities' relationships with banks.[70] The agencies' rules to that end are all being challenged by state Attorneys General.

NCUA should remind credit unions and CUSOs that neither NCUA nor any other banking agency has ever extended the preemptive effect of federal banking laws to subsidiaries of credit unions, whether state-

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[68] 12 CFR 712.5.

[69] *Id.*

[70] *See* Testimony of Lauren K. Saunders, NCLC, on behalf of its low income clients, before the House Financial Services Committee on Rent-A-Bank Schemes and New Debt Traps: Assessing Efforts to Evade State Consumer Protections and Interest Rate Caps (Feb. 5, 2020), http://bit.ly/debt-trap-schemes; Comments of Center for Responsible Lending, National Consumer Law Center (on behalf of its low income clients), and several additional consumer and civil rights organizations, on the OCC's proposed so-called "true lender" rule Sept. 3, 2020, https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/comment-occ-truelender-3sep2020.pdf.

chartered or federal. For CUSOs subject to the FCU Act CUSO Rule, this should already be clear, as the rule specifies: "A CUSO must comply with applicable Federal, state and local laws."[71] No federal law preempts applicable state law for CUSOs, and thus state law is applicable to loan transactions in a given state. Accordingly, NCUA should remind all credit unions and CUSOs that CUSOs must comply with licensing, usury, and other state laws that apply to other non-bank lenders.

C. NCUA must mitigate risks by more closely examining CUSO's lending activities.

Expansion of CUSOs' permissible lending activities poses increased safety and soundness risks, as noted above, as well as consumer protection, compliance, and other risks. Should the Board proceed with a rule, it should mitigate those risks in a number of ways. First, as discussed above, it should limit those activities to ones legal for the FCU itself. Second, NCUA should collect additional data about CUSO lending activities, including the interest rate and other loan terms of all loan products offered. Third, NUCA should seek Congressional authority to directly examine CUSOs.

D. NCUA should not expand permissible activities further without additional notice and comment.

We oppose enabling the Board to approve further permissible CUSO activities without notice and opportunity to comment. The proposal suggests that this change is warranted in light of changing technology that will affect credit union operations.[72] But emerging technologies often pose risks to members and other consumers that should be evaluated through the public notice and comment process.[73]

We also oppose what the Board floats as an alternative approach – requiring FCUs to petition the Board for permission to lend or invest in CUSOs that do additional activities or services not already listed in the CUSO rule. Petitions from individual actors typically involve a closed process in which the public lacks the opportunity to participate and leads to gradual erosion of consumer protections. A one-off approach also disadvantages competitors. For further discussion of these concerns, see the 2020 comments from NCLC, CRL, and a number of other groups to the CFPB on its advisory opinion process.[74]

VII. Consider the interaction of the proposed rule with state laws, consistent with Executive Order 13132.

As the Board notes, Executive Order 13132 encourages agencies to consider the impact of their actions on state and local interests. The Board concludes that this proposal "would not have substantial direct effects on the states, on the connection between the national government and the states, or on the

[71] 12 CFR 712.3(e).

[72] 86 Fed. Reg. at 11646.

[73] *See, e.g.,* Lauren K. Saunders, NCLC, Fintech and Consumer Protection: A Snapshot (Mar. 2019), http://bit.ly/2Tx9BmG.

[74] Comments of NCLC, et al. on CFPB's Advisory Opinions Proposal, Aug. 21, 2020, https://www.nclc.org/images/pdf/regulatory_reform/advisory-opinion-cfpb-consumer-comments-2020.pdf.

distribution of power and responsibilities among the various levels of government."[75] Thus, the Board concludes, the proposal does not have federalism implications.

We disagree with the Board's legal assessment, as the proposed rule indeed has significant implications for state law. Most states regulate the interest rates permitted on consumer loans, and non-depository lenders are all subject to those rate limits. Where very high-rate payday loans are permitted, states also regulate the size and, in some cases, the frequency of those loans.[76] Eighteen states plus the District of Columbia limit the cost of short-term loans such that payday lenders don't have active markets there,[77] and the majority of states have caps on longer-term loans as well. Those laws reflect value judgments by legislators and voters about what the cost of credit in those states should be. To the extent credit unions or CUSOs attempt to use their credit union/CUSO relationship to evade state laws governing high-cost lending, the proposal undermines and threatens state laws.

VIII. Conclusion

We appreciate your consideration of our comments and would be happy to discuss them further.

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[75] 86 Fed. Reg. at 11650.

[76] For example, California limits the size of payday loans, including fees, to $300, and Washington limits payday loans to eight per year.

[77] This figure includes Illinois, where a 36% rate cap bill was signed by the governor on March 23, 2021.