7535-01-U

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 712

RIN 3133-AE95

Credit Union Service Organizations (CUSOs)

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The NCUA Board (Board) is issuing a final rule that amends the NCUA's credit union service organization (CUSO) regulation. The final rule accomplishes two objectives: expanding the list of permissible activities and services for CUSOs to include the origination of any type of loan that a Federal credit union (FCU) may originate; and granting the Board additional flexibility to approve permissible activities and services.

DATES: The final rule is effective [**INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER**].

FOR FURTHER INFORMATION CONTACT: *Policy and Analysis:* Office of Examination and Insurance, (703) 518-6360; *Legal:* Office of General Counsel, (703) 518-6540; or by mail at National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314.

SUPPLEMENTARY INFORMATION:

I. Introduction

Legal Authority and Background

The Board is issuing this rule pursuant to its authority under the Federal Credit Union Act (FCU Act).[1] Under the FCU Act, the NCUA is the chartering and supervisory authority for FCUs and the federal supervisory authority for federally insured credit unions (FICUs). The FCU Act grants the NCUA a broad mandate to issue regulations governing both FCUs and FICUs. Section 120 of the FCU Act is a general grant of regulatory authority and authorizes the Board to prescribe regulations for the administration of the FCU Act.[2] Section 209 of the FCU Act is a plenary grant of regulatory authority to the NCUA to issue regulations necessary or appropriate to carry out its role as share insurer for all FICUs.[3] Accordingly, the FCU Act grants the Board broad rulemaking authority to ensure that the credit union industry and the National Credit Union Share Insurance Fund (NCUSIF) remain safe and sound.

Under the FCU Act, FCUs have the authority to lend up to one percent of their paid-in and unimpaired capital and surplus, and to invest an equivalent amount, in CUSOs.[4] The NCUA

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[1] 12 U.S.C. 1751 *et seq.*
[2] 12 U.S.C. 1766(a).
[3] 12 U.S.C. 1789.
[4] 12 U.S.C. 1757.

regulates FCUs' lending to, and investment in, CUSOs in part 712 of its regulations (CUSO rule).[5] In general, a CUSO is an organization: (1) in which a FICU has an ownership interest or to which a FICU has extended a loan; (2) is engaged primarily in providing products and services to credit unions, their membership, or the membership of credit unions contracting with the CUSO; and (3) whose business relates to the routine daily operations of the credit unions it serves.[6] The CUSO rule provides a list of preapproved activities and services related to the routine daily operations of credit unions.[7]

The list of preapproved activities and services in the CUSO rule has not been substantively revised since 2008.[8] The 2008 final rule added two new categories of permissible CUSO activities: (1) credit card loan origination and (2) payroll processing services. The 2008 final rule also added new examples of permissible CUSO activities and clarified that FCUs may invest in, and loan to, CUSOs that buy and sell participations in loans they are authorized to originate. In the 2008 final rule, commenters requested that FCUs be permitted to lend to or invest in CUSOs involved in broader types of lending; specifically, car loans, including direct lending and the purchase of retail installment sales contracts from vehicle dealerships, and payday lending. The NCUA, however, declined to provide such authority at that time.[9]

II. Proposed Rule

[5] 12 CFR part 712. All sections of part 712 apply to FCUs. Sections 712.2(d)(2)(ii), 712.3(d), 712.4, and 712.11(b) and (c) apply to federally insured, state-chartered credit unions (FISCUs), as provided in § 741.222 of the chapter. FISCUs must follow the law in the state in which they are chartered with respect to the sections in part 712 that only apply to FCUs. Corporate credit union CUSOs are subject to part 704. Any amendments to part 704 would occur through a separate rulemaking and are not included in this final rule.
[6] *See* 12 CFR 712.1(d), 712.3(b), and 712.5.
[7] 12 CFR 712.5.
[8] 73 FR 79307 (Dec. 29, 2008).
[9] The NCUA's rationale for not extending CUSO lending authority more broadly is discussed in detail in Section III, Final Rule.

At its January 14, 2021 meeting, the Board issued the proposed rule to amend the NCUA's CUSO regulation.[10] The proposed rule would accomplish two objectives: Expanding the list of permissible activities and services for CUSOs that FCUs may lend to or invest in to include origination of any type of loan that an FCU may originate; and granting the Board additional flexibility to approve permissible activities and services. The NCUA also sought comment on broadening general FCU investment authority in CUSOs based on the FCU Act's provision that authorizes FCUs to invest in organizations providing services associated with the routine operations of credit unions, which is codified in a separate provision from the authority for FCUs to lend to "credit union organizations." The proposed rule provided for a 30-day comment period that closed on March 29, 2021. To allow interested persons more time to consider and submit comments, the Board extended the comment period for an additional 30 days. The extended comment period closed on April 30, 2021.[11]

The Board received over 1,000 comments on the proposed rule. Comments were received from credit unions, both state and federal, CUSOs, credit union leagues and trade associations, banking trade organizations, individuals, consumer organizations, and an association of state credit union supervisors. In general, consumer organizations, banking trade organizations, and individuals who participated in a form letter writing campaign were opposed to the proposed rule. Credit unions were not unanimous, with some credit unions supporting the rule and others opposing it. CUSOs, credit union leagues, and trade organizations were generally in favor of the proposed rule.

[10] 86 FR 11645 (Feb. 26, 2001).
[11] 86 FR 16679 (Mar. 31, 2021).

III. Final Rule

The final rule adopts the proposed rule without any substantive change. Under the final rule, therefore, CUSOs are permitted to originate any type of loan that an FCU may originate and grants the Board additional flexibility to approve permissible CUSO activities and services outside of notice and comment rulemaking.[12] The final rule and a discussion of the Board's responses to the comments are discussed in detail subsequently. First, however, the Board explains the general principles and approach it has taken to examine and reconcile the competing viewpoints of commenters as well as past statements by the NCUA and individual Board Members on risks relating to CUSO activity.

As detailed in response to commenters' different points, which are grouped by subject matter in the following sections, the Board has re-examined several key statutory and policy principles to engage in a thorough, balanced review of the comments. These points include the following:

1. The Board's views regarding safety and soundness and risk to the NCUSIF. On this critical issue, the Board has considered key reference points, including the statutory definition of a "material loss" to the NCUSIF and requirements for NCUA insurance of member accounts. These authorities do not define all losses as material or involving undue risk to the NCUSIF. This preamble elaborates on these reference points in considering the degree of risk the rule may pose.

[12] Originate means to fund or make loans. This is separate from the already permissible activity for FCUs to lend to or invest in CUSOs that engage in loan support services that include loan processing and servicing under § 712.5(j).

2. The need to balance predicted risks against predicted benefits. Many commenters opposing the proposed rule made, for the most part, generalized predictions of harm to the NCUSIF, to consumers, or to the reputation of credit unions. While the Board recognizes the need to consider these concerns, it also finds that they do not account for the potential benefits that the regulatory changes may bring to FCUs by enhancing efficiency and supporting innovation, and to consumers by expanding lending options and access through credit union-affiliated lenders. The Board also finds this expansion in FCU authority appropriate for parity purposes because the Board currently does not restrict the activity of CUSOs in which only FISCUs lend or invest.
3. Some of the policy concerns invoked by commenters, as well as the Board at times in the past, have been both qualified and conditional. Most notably, some commenters and the Board in past CUSO rulemakings have considered the potential for FCUs lending to or investing in CUSOs with expanded authorities to dilute the FCU common bond and introduce more competition to small credit unions. The Board continues to recognize that these issues raise concerns for some parties, but has found that neither rests on clear statutory authority in the FCU Act. That is to say, nothing in the FCU Act binds CUSOs to FCU field of membership common bond provisions, and the Board itself has invoked this concern only conditionally in past rulemakings, allowing it to yield to the needs of credit unions to avail themselves of expanded CUSO lending activity. Further, the FCU Act does not require a CUSO to serve credit unions and members exclusively, but rather primarily, which balances a focus on credit union members while expressly authorizing CUSOs to serve others. Similarly, the Board does not believe it is prudent to allow concerns over legitimate competition in the marketplace to restrain regulatory changes that may benefit many credit unions and the system as a whole. Accordingly, to the

extent these factors are appropriate regulatory considerations, the Board believes they must yield to the benefits of expanded FCU authority about CUSO activity and other factors.

4. Application of the Board's judgment to reconcile differing viewpoints. Commenters opposing the rule raised several concerns, and in a few cases, cited past examples or incidents. But the Board does not believe that commenters opposing the rule provided substantial evidence to support their predictions that adopting the proposed rule would result in various harm. Commenters supporting the rule provided reasons they believe the rule would be beneficial. In considering these competing viewpoints, the vast majority of which are general policy views, the Board has applied its own judgment to make the best conclusions it can about the potential benefits and risks of the proposed rule. Throughout this review, the Board has concluded that limiting expansion and innovation indefinitely based only on generalized concerns would result in regulatory stagnation, which may harm the credit union system in the long term.

After considering the mixed viewpoints, the Board has determined that the overall weight of the factors in the record favor moving forward to enhance opportunities for FCUs CUSOs to engage in all types of lending permitted for FCUs.

Expansion of Permissible FCU Lending and Investment in CUSOs Engaged in Lending Activity

The Board has reconsidered its 2008 position on permitting FCUs to invest in or lend to CUSOs that engage in all types of lending. The Board now believes that permitting FCUs to

invest in or lend to CUSOs that originate any type of loan that an FCU may originate may better enable FCUs to compete effectively in today's marketplace and better serve their members.

As discussed in the preceding section, the FCU Act permits an FCU to lend to or invest in a CUSO that provides services associated with the routine and daily operations of credit unions. The NCUA has interpreted this statutory authority broadly to permit an FCU to lend to, and invest in, a CUSO that does most of the same activities and services permissible for an FCU.[13] To date, however, FCUs have not been permitted to invest in, or lend to, CUSOs that originate certain kinds of loans.[14]

As discussed in the proposed rule, the NCUA historically has been reluctant to grant FCUs authority to invest in or lend to CUSOs with broad lending authority. First, the NCUA has been hesitant because CUSOs may serve those who are not members of a member credit union . The NCUA has been concerned about FCUs benefiting from CUSO profits generated from non-members.[15] Second, the NCUA has also expressed concern that if member loans were being made by CUSOs, the NCUA would have a duty to examine such loans and that would necessitate greater NCUA examination authority over CUSOs.[16] Finally, the NCUA has also had concerns that permitting CUSOs to engage in a core credit union function could negatively affect affiliated credit union services.[17]

Due to these concerns, the NCUA has previously found compelling justification for permitting FCUs to invest in or lend to CUSOs engaged in only four types of loans: (1)

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[13] 12 CFR 712.5.
[14] *See*, 62 FR 11779 (Mar. 13, 1997).
[15] *Id.*
[16] *Id.*
[17] 68 FR 16450 (Apr. 4, 2003).

business; (2) consumer mortgage; (3) student; and (4) credit cards.[18] In permitting these types of lending, the NCUA has considered factors specific to each type of lending, such as whether these activities require specialized staff or economies of scale, and, as discussed subsequently, whether loan aggregation was prevalent in the marketplace for the particular type of lending.

Upon reexamination, the Board now believes it is appropriate to permit FCUs to invest in, or lend to, CUSOs that engage in all types of lending permitted for FCUs. As discussed previously, the Board received extensive comments on the proposed rule. The commenters, including credit union commenters, were split on whether permitting CUSOs to originate any loan that an FCU can originate would be ultimately beneficial to credit unions, particularly small credit unions, or detrimental to the long-run interests of credit unions. Comments are discussed in detail in the following paragraphs.

Safety and Soundness

Some commenters who supported the proposed rule generally stated that the rule would not cause safety and soundness concerns and that the current CUSO regulatory framework sufficiently protects FCUs and the NCUSIF. Commenters pointed to several existing authorities to manage the potential risk from CUSO lending. First, commenters noted that under the current regulation, the NCUA may at any time, based upon supervisory, legal, or safety and soundness reasons, limit any CUSO activities or services, or refuse to permit any CUSO activities or services. Commenters further stated that the NCUA can exert pressure on FCUs if CUSOs engaged in unsafe or unsound behavior. Second, an FCU may invest in, loan to, and/or contract

[18] *Id. See also,* 73 FR 79307 (Dec. 29, 2008).

with only those CUSOs that are sufficiently bonded or insured for their specific operations and engaged in preapproved activities and services. Third, FCUs are bound by an aggregate limit of loans and investments in CUSOs to two percent of paid-in and unimpaired capital and surplus. Fourth, FCUs (as well as FISCUs) are required to include provisions in contracts with CUSOs in which they lend or invest to give the NCUA complete access to any books and records of the CUSO and the ability to review the CUSO's internal controls. Finally, other commenters noted that CUSOs are subject to state lending laws and federal consumer protection laws. In addition, some CUSOs may be subject to supervision at the state level by way of state licensing requirements or third-party oversight authority.

Some commenters discussed that CUSOs currently have extensive lending authority and there have not been any extraordinary losses.

A few commenters also discussed that the bigger safety and soundness risk may arise from not adopting the proposed rule as it permits FCUs to remain competitive and build capital. Commenters also discussed that FCUs could be subject to reputational harm if they cannot provide members the necessary services.

In response to a question in the proposed rule about potential safety and soundness conditions, one commenter urged caution on the potential to apply risk retention requirements to participation loans originated by wholly owned CUSOs. The commenter stated that, since the balance sheets of the CUSO and its parent are consolidated, the participation becomes effectively nonexistent, so a risk retention requirement becomes unnecessary.[19]

[19] Note that a CUSO's balance sheet would be consolidated with a credit union's if required by applicable accounting principles. Generally, the NCUA requires credit unions to consolidate a CUSO's balance sheet with the credit union's when the credit union wholly owns or owns a controlling interest in the CUSO. *See* NCUA Call Report Form 5300 Instructions, Statement of Financial Condition, at 2, effective Sept. 2021, *available at https://www.ncua.gov/files/publications/regulations/call-report-instructions-september-2021.pdf*.

In contrast, some of the commenters who opposed the proposed rule believed that the proposal would have substantial unintended consequences and affect the safety and soundness of FCUs and the NCUSIF. Commenters primarily focused on the NCUA's lack of examination or oversight authority and the systemic risk that arises from a few CUSOs providing services to a large portion of credit unions.

Commenters generally discussed that the NCUA has no examination or oversight authority over CUSOs. One commenter noted that several federal agencies, including the Government Accountability Office and the Financial Stability Oversight Council, have recommended that the NCUA be given supervisory oversight of CUSOs and that the Chairs of every NCUA Board over the past decade, as well as the NCUA's Inspector General, have called for vendor authority. These commenters believed expanding CUSO lending authority at the same time the NCUA has acknowledged an existing risk related to CUSOs would exacerbate the current problems that arise from the inability to supervise CUSOs. One commenter questioned why the NCUA would propose providing CUSOs with all the powers of FCUs, but with none of the commensurate prudential supervision or consumer safeguards to mitigate the risk. One commenter recommended a hybrid approach that would enable the NCUA to review a CUSO's loan origination activities, but not permit a complete NCUA examination.

The Board does not believe that the limited expansion of FCUs' ability to lend to, or invest in, CUSOs engaged in lending permissible for an FCU contradicts its long-stated need for additional examination and enforcement authority of CUSOs and other third-party vendors.[20] It is the Board's continuing policy to seek third-party vendor authority for the agency from

[20] The Board also notes that its request for third-party vendor authority is more expansive than examination and enforcement authority over CUSOs. The term third-party vendors include any third-party service provider regardless of credit union ownership, a larger category of institutions than just CUSOs. The NCUA currently has very limited oversight of non-CUSO third-party vendors.

Congress. The Board does not believe this rule undermines its request for such authority as the rule provides only a modest expansion of FCU authority to lend to, and invest in, CUSOs and results in only an incremental amount of additional risk to the NCUSIF.

The Board also believes there are several factors that may mitigate the risk to the NCUSIF, though the Board acknowledges that despite these mitigating factors CUSOs have caused more than $500 million in losses to FICUs since 2008. First, as commenters in favor of the rule discussed, even though the NCUA does not have examination or enforcement authority over CUSOs, FCUs only have the authority to lend up to one percent of their paid-in and unimpaired capital and surplus, and to invest an equivalent amount, in total to CUSOs. These investment and lending limits mitigate risk to the NCUSIF. Additionally, § 712.3(d) requires all FICUs that obtain an ownership interest in a CUSO to ensure by contract that the NCUA has access to the CUSO's books and records and other information and reports. CUSOs are also subject to state lending laws and federal consumer protection laws. These and the other regulatory requirements discussed above mitigate the potential risk to the NCUSIF due to the modest expansion of FCU authority to lend to and invest in CUSOs engaged in all lending activities.

The Board also notes that it has broad investigative subpoena authority that agency staff can use to obtain records and testimony in certain extraordinary circumstances.[21] This broad authority is not limited to credit unions and may permit NCUA staff to obtain information from third parties in connection with the agency's examinations of credit unions.[22] The Board does not currently use this authority broadly to obtain information from CUSOs, but the Board could

[21] 12 U.S.C 1784(a), 1786(p).
[22] 12 U.S.C. 1784(a); *see United States v. Inst. for Coll. Access & Success*, 27 F. Supp. 3d 106, 112 (D.D.C. 2014) (an agency Inspector General's administrative subpoena to third party in an investigation was enforceable even though third party was not an entity subject to agency's regulatory jurisdiction).

potentially instruct NCUA staff to employ these oversight tools to their full potential to guard against risks to the NCUSIF associated with CUSO activity in the absence of direct statutory examination and enforcement authority over CUSOs.

Further, regarding its enforcement authority, the Board also notes that it may have statutory enforcement authority in certain cases over CUSOs that commit misconduct. Specifically, an insured credit union's independent contractor may be subject to the Board's enforcement powers under the FCU Act if it knowingly or recklessly participates in certain violations that cause or are likely to cause more than a minimal financial loss to, or a significant adverse effect on, the insured credit union.[23] Thus, the Board may have greater power in certain circumstances than opposing commenters acknowledge.

The Board also believes that the risk to the NCUSIF is mitigated because in its experience most CUSO loans are sold to credit unions, which are subject to NCUA enforcement and examination authority. In addition, the Board also believes that the additional risk is mitigated because most CUSOs are wholly owned by the parent credit union (as of the end of 2020, for instance, approximately 72 percent of natural person CUSOs were wholly owned by credit unions),[24] which provides the NCUA additional leverage if a CUSO is engaging in unsafe or unsound lending practices. In both situations, the NCUA would likely have additional insight into the risk of the CUSO's lending. The Board acknowledges, however, that there may be gaps in its jurisdiction for certain CUSOs that may retain its loans, sell them to third parties, or are not wholly owned by credit unions.[25] It is the Board's belief that this risk is limited and is outweighed by the potential benefits of the final rule.

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[23] 12 U.S.C. 1786(r).
[24] CUSOs at a Glance (2020), *available at* https://www.ncua.gov/analysis/cuso-economic-data/cusos-glance.
[25] The Board notes that such risk is already present in the credit union system as the NCUA insures FISCUs that may be subject to substantially less restrictive CUSO requirements. For example, many states do not restrict, or have higher limits for, FISCU investments in CUSOs.

As some commenters supporting the proposed rule observed, the expanding lending authority may be beneficial to FCUs by enhancing their competitiveness and ability to generate capital. Increased credit union capital would strengthen the NCUSIF by reducing the potential for losses due to credit union failures. The Board believes that the potential benefits of the expanded authority for FCUs to lend to or invest in CUSOs engaged in all lending activities may outweigh the potential costs of the rule including additional risk to the NCUSIF, decreased credit union lending due to increased competition, and increased consolidation, particularly among smaller credit unions. In any event, the Board considers the potential benefit to credit unions and the NCUSIF to be at least a partial mitigating factor against the potential incremental risks.

Other commenters expressed concerns about systemic risk. For example, one commenter quoted former NCUA Board Chair Mark McWatters to highlight how CUSOs contribute to systemic risk: "Since 2008, CUSOs have caused more than $500 million in losses to federally insured credit unions, and they have contributed to the failure of 11 credit unions…more than half of the NCUA's institutions hold less than $33 million in assets and average approximately three to four full-time employees per institution. These institutions are heavily dependent on third-party outsourced services and do not possess the resources to independently perform full due diligence on all of their critical services providers." Another commenter stated that a large CUSO operating as a loan originator and selling participations or whole loans could produce systemic risks within the industry as evidenced by prior events caused by single originators, a concentrated group of originators, or by overconcentration within a sector.

As discussed in its responses to other comments in the preceding section, the Board has considered the potential benefits and risks of FCUs lending to or investing in CUSOs engaged in broader types of lending. The Board recognizes that several present and prior Board Members, the Inspector General, and other government bodies have found that the NCUA needs statutory

enforcement authority over third-party vendors, including CUSOs, to manage the associated risks appropriately. The NCUA has also documented significant previous losses to the NCUSIF that were attributed to CUSOs, particularly between 2008 and 2015.

The Board, however, does not find it necessary to continue to limit FCUs' authority to invest in, or lend to, CUSOs engaged in lending activities permissible for FCUs until the FCU Act is amended to add enforcement authority over CUSOs. Such a response is disproportionate to the modest expansion permitted in this final rule.

The Board also finds that prior statements about losses to the NCUSIF do not support any firm prediction that similar losses will occur in the future because of this final rule (or even with a mere continuation of the current authorities).[26] For example, the Board considers what has occurred since 2015, as reflected in the Inspector General's regular reports. Under the FCU Act, the Inspector General must submit a written report to the Board, the Comptroller General of the United States, and other parties when the NCUSIF incurs a "material loss" an insured credit union, with material loss defined as one exceeding $25 million and 10 percent of total assets of the credit union.[27] These reports must include a description of the reasons that the problems of the credit union resulted in a material loss to the NCUSIF and recommendations for preventing any such loss in the future.[28] For losses that are not material as defined in this section of the FCU Act, the Inspector General must identify losses occurring in each 6-month period and report semi-annually to the Board and Congress on whether any of those losses warrant an in-depth

[26] The Board also notes that there have been significant changes to laws, regulations, and industry practices for loan underwriting and credit administration since the 2008 financial crisis. Therefore, the Board also believes that the historical losses attributed to CUSOs that were discussed in the comments are not reflective of the current standards and practices, so the referenced historical losses may not necessarily be predictive of future losses.
[27] 12 U.S.C. 1790d(j)(1), (2).
[28] 12 U.S.C. 1790d(j)(1).

review.[29] Since 2015, the NCUA's Inspector General has not issued any Material Loss Review reports in which CUSO activity was cited as the reason, or part of the reason, for the losses. The NCUA also looked at the total losses due to CUSOs in failed FICUs from 2015 to June 30, 2021. The Board found that failed FICUs lost approximately $4 million due to CUSOs during this period. And, the NCUSIF lost only an amount estimated to be under $1 million due to CUSOs during this period as most of the failed FICUs with CUSO-related losses were merged into other institutions without substantial loss to the NCUSIF.

The Board finds the absence of material CUSO-related losses during this period noteworthy; however, the Board acknowledges it excluded losses that occurred during the 2008 banking crisis and looked at data that occurred during a relatively robust economy. This absence does not guarantee that material losses will not occur in the future, but it illustrates the uncertainty associated with predictions by some commenters. A past pattern of material losses is not, in the Board's opinion, sufficient evidence that the pattern will continue.

In reconciling these competing perspectives, the Board also has considered the general principles discussed in the introduction to this preamble. Neither the FCU Act nor the NCUA's regulations or policies require the agency to ensure all potential losses to the NCUSIF are avoided. The FCU Act requires the Board to consider whether a credit union applying for insurance of member accounts poses "undue risk" to the NCUSIF and to deny the application if the financial conditions and policies are unsafe and unsound or if the applicant poses undue risk to the NCUSIF.[30] In its regulations in § 741.204(d), the Board has further defined "undue risk "to the NCUSIF as a condition that creates a probability of loss in excess of that normally found

[29] 12 U.S.C. 1790d(j)(4). This discussion provides only a general description of these requirements and the Inspector General's duties and activities. More information is available on the Inspector General website and in its Semi-Annual Reports to Congress.
[30] 12 U.S.C. 1781(c).

in a credit union and which indicates a reasonably foreseeable possibility of insolvency and a resulting claim against the NCUSIF. Similarly, in considering whether a credit union's practices are unsafe and unsound for chartering and field of membership purposes, the Board considers whether the action or lack of action would result in an "abnormal risk of loss" to the credit union, its members, or the NCUSIF.[31]

The Board also notes that the ongoing trend of credit union consolidation is already increasing systemic risk. On an aggregate basis, the total number of credit unions has been cut in half over the prior two decades as smaller credit unions have merged or consolidated. There were over 5,000 fewer credit unions with less than $1.0 billion in total assets in 2020 than there were in 2000. As the number of credit unions has declined, loan portfolios have become increasingly concentrated within the largest credit unions. Expanding FCUs' authority to lend or invest in CUSOs engaged in all lending activities may allow smaller credit unions to combine their resources to remain more competitive within the changing lending landscape, which could result in a reduction of systemic risk.

Separately, the Board already insures FISCUs that may, depending on state law, lend or invest in CUSOs that engage in all lending activities. In its role as insurer, the Board finds it would be unreasonable to decline to expand FCU authority on a risk basis when it currently allows the activity for FISCUs.

Based on these standards and principles, the Board does not find that the expanded FCU authority to lend to or invest in CUSOs engaged in all lending activities provided by this rule are likely or more likely than not to result in material losses to the NCUSIF or unsafe and unsound practices posing an undue risk to the NCUSIF.

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[31] 12 CFR 701, App. B, Glossary.

Regarding the concern over concentration risk, the Board believes that existing limitations in §§ 701.22 and 701.23 on the amount of eligible obligations that FCUs may purchase and on the amount of loan participations that all federally insured credit unions may purchase from a single source will provide significant protection against this concern. Additionally, the Board believes there is some potential benefit to small credit unions buying loans from CUSOs. In such a case, many credit unions may be purchasing loans from the same entity leading collectively to enhanced due diligence on the CUSO.

Commenters also discussed the risk for reputational harm. For example, the ownership structure of CUSOs may result in the public's linking any aggressive or improper CUSO lending activity with the lending activity of FCUs themselves.

The Board agrees that confusion over the status of CUSOs or mistaken belief that they are federally insured and subject to the NCUA's full oversight would be problematic. The Board notes that certain FCU practices related to the promotion of CUSO services or CUSOs with names related to their FCU parents may raise unfair, deceptive, or abusive acts or practices issues.[32] FCUs should pay particular attention to their marketing and ensure that members are informed and understand the legal significance between FCU-originated loans and CUSO-originated loans. For example, FCUs should ensure that members clearly understand that the NCUA may have a more limited ability to address member complaints related to CUSO-originated loans. The Board notes that standardized disclaimers in loan origination documentation may be insufficient to address this concern. The Board, however, finds that the current regulations, including the prohibition on unfair, deceptive, or abusive acts or practices, reasonably guard against the concern about member confusion. First, § 712.4(a) specifies that an

[32] Dodd-Frank Wall Street Reform and Consumer Protection Act, Title X, Subtitle C, § 1036; Pub. L. 111–203 (July 21, 2010).

insured credit union must take several steps to ensure corporate separateness from a CUSO, including that each is held out to the public as separate enterprises. Adherence to this requirement, and proper enforcement of it by the NCUA, is likely to mitigate much or all of the concern regarding confusion. Second, and similarly, the NCUA's advertising regulation in § 740.2 requires, among other matters, that an insured credit union using a trade name in advertising must use its official name in loan agreements and account statements. This requirement may further safeguard against the risk of confusing a credit union with an associated CUSO with a similar name because the official loan documentation would disclose which entity or entities are involved. Each of these provisions on their own, therefore, and when considered in concert, may work to address this concern.

Commenters also noted that CUSO lending activities are currently considered complex or high risk. The Board acknowledges that CUSO lending activity has the potential to create material financial risk. This is why lending CUSOs are currently subject to additional reporting requirements in § 712.3(d). As discussed above, however, the Board does not believe this rule represents an undue safety and soundness risk; rather, the Board believes it only represents an incremental risk to credit unions and the NCUSIF. This relatively modest, incremental risk is further mitigated, as discussed above, by the existing regulatory and supervisory controls and standards in place.

Finally, one commenter recommended that loans purchased from a CUSO be subject to the same limitations as loans purchased from other credit unions and recommended that the NCUA have a process to ensure the quality of CUSO loans.

The Board has considered this recommendation and declines to adopt it. First, regarding new limitations on loans, the Board underscores that currently, §§ 701.22 and 701.23 of the Board's regulations restrict loan and loan participation purchases by credit unions. Subject to

various exceptions, including those provided in the temporary COVID rule in effect through December 31, 2021,[33] FCUs may purchase only eligible obligations of its members for loans the FCU would itself be empowered to grant.[34] Section 701.22, most of which applies to FISCUs as well as to FCUs, restricts the types of loan participations that a credit union may purchase to those the credit union is empowered to grant and also requires the originating lender, including a CUSO, to retain at least five percent of the outstanding balance of the loan through the life of the loan (10 percent is required if the originating lender is an FCU).[35]

The Board believes that these existing restrictions are sufficient to ensure that the loans or loan interests purchased by credit unions from CUSOs will have reasonable terms. At the same time, the Board acknowledges that CUSOs may originate loans that parties other than credit unions purchase. In turn, this would make the restrictions discussed in the preceding paragraph inapplicable. This is, however, the current situation for loans originated by CUSOs. The commenter who recommended this new restriction did not present persuasive evidence that this new restriction is necessary and further provided no analysis or evidence regarding how the restrictions might hamper CUSO activities and thus decrease the value of credit union interests in CUSOs. Accordingly, the Board declines to adopt this recommendation.

Second, regarding the quality of loans, the Board believes that credit unions and other parties who purchase CUSO-originated loans can perform due diligence and ensure that loans are underwritten and documented appropriately. Further, as part of the examination process, NCUA examiners can continue to request documentation on credit unions' due diligence and other policies and procedures associated with their investment, lending, and other interaction with

[33] 85 FR 22010 (Apr. 21, 2020); 85 FR 83405 (Dec. 22, 2020).
[34] 12 CFR 701.23(b).
[35] 12 CFR 701.22(b)(3).

CUSOs. As with the recommendation on the terms of loans, the Board finds no persuasive evidence or analysis of the benefits and risks of such new oversight and declines to adopt the recommendation.

Consumer Protection

Commenters who supported the rule did not extensively discuss consumer protection issues. Several commenters stated that CUSOs would likely only issue loans that comply with the NCUA's loan origination rules as generally CUSO-originated loans would be sold to the parent credit unions. Another commenter stated that the proposed rule would expand financial inclusion due to the potential for collaboration to develop new technologies. Finally, commenters noted that CUSOs are subject to state lending laws and federal consumer protection laws.

In contrast, commenters who were against the proposed rule generally expressed concerns that the proposed rule would create risk to consumers. Several commenters expressed concerns that CUSO-originated loans are not subject to the same restrictions as loans originated by FCUs. For instance, the FCU Act limits interest rate, maturity, and prepayment terms for FCU-originated loans. Commenters were concerned that this rule change would enable an FCU to circumvent statutory lending restrictions through a CUSO subsidiary. Commenters were especially concerned about abuses because the proposed rule would principally allow payday and auto lending, which may be more likely targeted towards members in low-to-moderate-income communities and underserved areas. Furthermore, several commenters stated that CUSOs have been responsible for abusive lending in the past. One commenter noted that CUSOs were marketing payday loan products to state-chartered credit unions with triple digit interest rates in Texas until restrictions were implemented on the state level. One noted a 2010 National

Consumer Law Center report, which documented that over 40 credit unions were involved with payday lending through CUSOs. This prompted the NCUA to issue a letter to credit unions. Another commenter stated that the proposal will disproportionately harm communities of color and exacerbate financial exclusion, even as the Board elsewhere emphasizes racial equity and financial inclusion. Another commenter stated that investing in CUSOs that violate the FCU Act usury ceiling creates not only reputation risk, but compliance and legal risk as loans that exceed the usury cap in the FCU Act should not be considered part of the routine operations of credit unions.

Commenters raised several potential solutions to potential consumer harm. One commenter stated that any expansion of CUSO lending activity should be limited to loans FCUs are themselves empowered to make. Another commenter recommended changes to the Payday Alternative Loans (PALs) program if the goal is to encourage more small-dollar lending and included ideas on how to increase credit unions' adoption of PALs. Another commenter suggested requesting examination findings from the Consumer Financial Protection Bureau, which has requisite authority to examine CUSOs to determine whether consumer protection laws are being followed.

The Board has considered the comments on this point and finds that overall, they provide support for proceeding with adopting the regulatory change to CUSO lending authorities as proposed.

As commenters in support of the expansion of FCU authority with respect to loans to and investments in CUSOs engaged in all lending activities stated, more collaboration and use of financial services technology may positively affect financial inclusion. By authorizing more parties to offer an array of consumer loans, the Board may increase beneficial competition and expand consumer choice. The Board also believes that CUSOs would likely adhere to the

statutory and regulatory restrictions on loans that FCUs are empowered to grant in order to be able to sell these loans to FCUs (though the Board notes that the purchasing authority provisions may vary for FISCUs because the Board's eligible obligation purchase regulation in § 701.23 applies to FCUs only) and that CUSOs may not be under the same liquidity pressure for auto and payday loans as other types of loans currently authorized by the CUSO rule. The Board also notes that it recently relaxed some of these protections in light of the COVID-19 pandemic.[36] As a whole, however, it is the Board's belief that the current authorities governing FCU purchases of loans would likely result in a substantial amount of CUSO loans being issued on terms equivalent to those in the FCU Act, or what is already permitted for FISCUs.

The Board is, of course, concerned about the risk of unfavorable terms for consumers. As one commenter noted, in 2009, the NCUA Chairman issued a letter to all FCUs on consumer lending, including consumer protection issues.[37] The Board has also established two payday alternative loans (PALs) programs for FCUs to promote short-term, small-dollar loans for FCUs and their members that can serve as an alternative to loans with less favorable terms. The Board's concerns are partially mitigated, however, by state usury laws and other consumer protection laws that may be enough to curtail the risk of predatory lending by CUSOs. The Board acknowledges, however, that the majority of states permit payday lending and therefore state laws only provide some mitigation relating to the concern of CUSOs offering loans at excessive interest rates.[38] The Board plans to monitor new practices closely and take aggressive action when it can to protect consumers from abusive terms that are contrary to law. When the Board lacks direct authority, it can partner with other federal agencies, such as the CFPB, or state

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[36] 85 FR 83405 (Dec. 22, 2020).
[37] Payday Lending, 09–FCU–05, July 2009, *available at* https://www.ncua.gov/regulation-supervision/letters-credit-unions-other-guidance/payday-lending.
[38] See the CFPB final rule, Payday, Vehicle Title, and Certain High-Cost Installment Loans, 85 FR 44382, 44383 (July 22, 2020).

authorities to address any such situations. Ultimately, the Board and other parties, in combination, have tools available to protect consumers and curb abusive practices.

At the same time, the Board disagrees with commenters who believe that the expanded FCU authority to lend to or invest in CUSOs engaged in all lending activities would open up a new area of lending above the FCU interest rate cap and that such activity is contrary to the FCU Act.

First, the Board finds greater competition in the consumer loan market from FCU-owned entities is likely to introduce better consumer options and greater choice. If the Board decides to limit innovation and expansion out of concern for potential consumer harm, it may actually perpetuate a lack of consumer choice and access. Regardless of what action the Board takes, other parties will continue to lend in the marketplace and may lack the same grounding in the credit union mission and industry that would tend to mitigate the risk of abusive lending practices. Confronted with this choice, the Board's judgment is that CUSOs will be more likely than other lenders to offer only reasonable terms to consumers and be held accountable by the NCUA, other federal agencies, or state authorities. Second, regarding one commenter's opinion about the "daily operations of credit unions" not including lending above the FCU interest rate ceiling, the Board finds that the FCU Act's broad wording should not be read so narrowly. Reading this limitation into the phrase would, if applied to other areas of CUSO activity, such as trustee and fiduciary activity that is not generally within the power of an FCU, limit CUSOs to only those activities that FCUs may perform within all limitations of the FCU Act. CUSOs have long been permitted to engage in activities that are not specifically bound by these limitations. In particular, since originally authorizing CUSOs to engage in limited lending activity, the Board has not imposed the interest rate ceiling or other restrictions applicable to FCU-made loans to

CUSO-made loans. The concern, therefore, that some commenters raise is not specific to this rulemaking and has long stood as the agency's position on CUSO activities, including lending.

Ultimately, when faced with the choice between limiting or proceeding with this expansion of FCU authority to lend to, or invest in, CUSOs engaged in all lending activities, the Board finds in its judgment that the regulatory changes carry the potential to benefit consumers and FCUs through greater choice. At the same time, the Board will closely monitor the expanded activity given the importance of consumer protection.

In addition, the Board notes that amending the PALs program is beyond the scope of the CUSO rulemaking but will take commenters' input on that program into account in any future action on that program.

Innovation

Some of the commenters who supported the proposed rule generally stated that CUSOs enable necessary innovation. Many commenters discussed how CUSOs can pool resources for various projects each credit union could not afford to embark on individually, especially smaller credit unions. With innovation and technology continuously evolving at a significant pace, giving FCUs the option to start or partner with a CUSO to advance their technology capabilities would help FCUs remain competitive as they often lack the resources to build and maintain the technology infrastructure. Commenters stated that CUSOs are currently helping credit unions survive in the rapidly changing financial industry and several credit unions credited CUSOs with assisting them in reaching members, including low-to-moderate income members. Many commenters mentioned fintechs and that CUSOs are enabling credit unions to compete with fintechs and large banking organizations that have the resources to develop new technologies.

Several commenters stated that credit unions must continue to innovate, reduce costs, and generate income, especially as traditional sources of income, like net interest margins, are no longer sufficient.

Some of the commenters who were opposed to the proposed rule stated that CUSOs are already able to facilitate FCUs' collective investment in technology without having their lending powers broadened. CUSOs' permissible activities include "loan support services, including loan processing, servicing, and sales," which means CUSOs can currently play a support role in FCU lending according to one commenter.

When discussing current CUSO authorities to do indirect lending, another commenter stated that small FCUs struggle to engage in indirect lending, which requires significant investment and oversight. The commenter further stated that managing relationships with dealers and monitoring the quality of loans an FCU receives is paramount to the success of an indirect lending program. As a result, the indirect lending channel is often closed to small FCUs.

The Board has considered the wide variety of viewpoints on this issue. As several commenters noted, broadening the permissible CUSO lending categories may foster innovation and partnerships. Conversely, some commenters contended that the rule change is not needed for this purpose because credit unions already partner effectively with CUSOs to develop technology to support FCU lending. The Board views this difference of opinion and predictions similarly to how it views other general predictions about the risks and benefits of the rule change. The Board recognizes that the expanded FCU authority to lend to or invest in CUSOs engaged in all lending activities may not result in enhanced partnerships and cooperation with CUSOs and other credit unions because it is not possible to predict the future of the marketplace with certainty. Alternatively, the regulatory changes may enhance this collaboration for some credit unions in some type of lending but not in all.

However, the Board in its judgment also finds that expanded areas of activity and investment would naturally tend to increase collaboration and cooperation. Affording greater opportunities for FCUs to lend to and invest in CUSOs engaged in a broader range of lending may facilitate more partnerships that position FCUs better to work with new entities and technologies in financial services. For this reason, the Board continues to find this a good basis to proceed with the regulatory changes.[39]

Credit Union Mission

Some of the commenters in favor of the proposed rule broadly stated that CUSOs enable FCUs to fulfill their mission by enhancing their ability to serve members. Several commenters stated there is no evidence that the proposed rule would hurt the industry, members, or the NCUSIF.

In contrast, some of the commenters opposed to the proposed rule stated that the proposed rule undermines fundamental principles of the FCU Act. Principally, in their view, the proposed rule would dilute the common bond by permitting lending outside of FCUs' fields of membership. These commenters stated that allowing FCUs to directly profit from loans that are originated to non-members is contrary to the intent of the FCU Act. Many commenters generally stated that the profit FCUs would derive from non-members calls into question the rationale for the exclusion from federal income taxation.

[39] The Board also notes that innovation and collaboration were not the sole basis for the proposed rule. As discussed in the preamble to the proposed rule, another basis for the rule was to enable FCUs to better serve their members. The Board views the various bases in the proposed rule as independently sufficient to support the rule. 86 FR 11645, 11646 (Feb. 26, 2001).

The Board finds that concerns about diluting the FCU common bond do not warrant modifying or declining to adopt the proposed rule.

First, the Board does not agree with commenters who believe the FCU Act requires consideration of this factor in evaluating proposed CUSO activities. The FCU Act's field of membership and common bond provisions apply to FCUs, not to CUSOs.[40] The loan authority for CUSOs in the FCU Act specifically defines a "credit union organization" in part as an organization "established primarily to serve the needs of its member credit unions, and whose business relates to the daily operations of the credit unions they serve."[41] Thus, the FCU Act does not require that CUSOs be established exclusively to serve credit union members or credit unions. Accordingly, any objection based on a claim that expanded FCU authority to lend to or invest in CUSOs engaged in all lending activities violates the FCU Act is unfounded.

Second, apart from the statutory provisions, in this rulemaking the Board has re-examined its prior policy-based concern regarding dilution of the common bond through CUSO lending authorities. As the proposed rule recounted, historically the Board has been hesitant in granting CUSOs authority to make consumer loans because it may be perceived as diluting the common bond. In a 1998 final rule in which it granted CUSOs authority to make student loans, but not other types of consumer loans, the Board elaborated that it limited the expansion because Congress and the public may perceive it as a dilution of the common bond.[42] In the same discussion, the Board explained that it would grant authority to CUSOs to make student loans because they required more specialized staff and experience, whereas general consumer loans did not.[43]

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[40] 12 U.S.C. 1759 and the NCUA's Chartering and Field of Membership Manual, 12 CFR 701, App. B., set forth common bond definitions and requirements for FCUs.
[41] 12 U.S.C. 1757(5)(D).
[42] 63 FR 10743, 10752 (Mar. 5, 1998).
[43] *Id.*

The 1998 final rule is, therefore, best read as relying on two bases for limited expansion at that time: perception of dilution of the common bond and the need for credit unions to partner with CUSOs for certain types of loans. And in that rule, the determination that one type of new loan authority would be beneficial to credit unions overcame the generalized concern about perceived dilution. In fact, in the same final rule, the Board refuted in detail the contention by a commenter that CUSOs are subject to the statutory common bond requirement,[44] demonstrating further that the perceived dilution concern was not viewed as an absolute or particularly strong counterweight to other policy rationales. That is to say, incremental expansion of FCU authority about CUSO lending authorities based on the Board's judgment and experience have in the past outweighed this concern. Based on this re-examination, the Board concludes that the concern over perceived dilution of the common bond is relatively weak and has not historically been given great weight or decisiveness in evaluating the reasons for and against an expansion of FCU authority related to this activity.

Given this background and context for the perceived common bond dilution concern, the Board finds that it does not warrant refraining from adopting this final rule. The commenters who cited this concern provided only generalized predictions or policy arguments that lack specific evidence even to predict with any certainty that the regulatory changes would appear to dilute the common bond. Other commenters predicted that the expanded authority might instead bring credit union membership to more people. The Board believes this result is at least as likely as one in which the common bond is perceived by some subjectively as being diluted. For example, non-credit union members who are eligible for membership may decide to join a credit union after obtaining a loan from an affiliated CUSO. And in any event, a CUSO engaging in

[44] *Id.* at 10745.

this type of lending would still be required to primarily serve credit unions, its membership, or the membership of credit unions contracting with the CUSO.[45]

Accordingly, based on this re-examination of the perceived dilution concern and the limited support offered by commenters opposing the rule on this basis, the Board concludes that this concern does not weigh against adopting the rule as proposed.

Another commenter stated that FCUs would profit from loans exceeding usury caps in the FCU Act, and this is against the spirit of the FCU Act.

The Board does not find this generalized concern persuasive. Currently, CUSOs are not subject to the interest rate ceiling in the FCU Act.[46] This provision applies to loans made by an FCU. By regulation, subject to some exceptions, an FCU may not buy a loan it is not empowered to grant.[47] However, the Board recognizes that an FCU investing in a CUSO may receive revenue derived from loans the CUSO makes but does not sell to an FCU. This is true under the current regulation, but the customer base requirement discussed in the preceding section tends to limit this effect by requiring that CUSOs primarily serve credit unions, CUSO members, and members of credit unions contracting with the CUSO. The same requirement will apply to CUSOs engaged in new types of consumer loans. For this reason, the Board finds this concern lacks sufficient support and weight to warrant not adopting the rule as proposed.

Growth or Competition

[45] 12 CFR 712.3(b).
[46] 12 U.S.C. 1757(5)(A)(vi).
[47] 12 CFR 701.23(b).

Some of the commenters who supported the proposed rule generally stated that the CUSOs would not compete with credit unions because CUSOs do not have enough liquidity to originate and hold loans. These commenters stated that CUSOs will originate loans only as a mechanism to secure more loans for their lending partners and will then sell the loans to credit unions. Several commenters pointed to credit union loan growth in mortgages, student loans, credit cards, and business lending. One credit union trade organization acknowledged credit unions and CUSOs would likely compete for loans; however, it believed the greater threat comes from fintech and banks.

Several commenters also stated that the proposed rule would help FCUs because it would result in increased lending opportunities. One of the reasons for increased lending discussed was CUSOs' potential to lower costs through economies of scale. Several commenters stated that CUSOs enable FCUs to share costs, distribute risk, and provide scale. A few commenters specifically stated that the proposed rule would enable smaller FCUs to continue their lending activities but, instead of keeping their lending operations in-house, utilize the services of a CUSO to generate loans.

In contrast, several commenters who opposed the proposed rule believed that CUSOs would bring unnecessary competition, particularly for smaller credit unions. Some commenters stated that the proposed rule could benefit certain, larger FCUs, but it could hurt other, smaller credit unions as well-funded CUSOs could capture potentially significant market share. One commenter noted that past NCUA Boards have been concerned that CUSOs only benefit large credit unions and once noted that smaller credit unions have been unable to meet minimum eligibility requirements in order to partake of CUSO services. One commenter noted there is no evidence FCUs need help with non-complex consumer loans or auto loans. Other commenters

stated that the proposed rule would not result in increased lending and that CUSO-originated loans sold to credit unions do not drive credit union loan growth.

A few other commenters believed that the rule could be anti-competitive as it may result in additional industry consolidation because small credit unions could lose market share.

The Board has considered the differing viewpoints on this issue and determined that this concern does not warrant refraining from adopting the rule as proposed. As discussed in the introduction to this preamble, the Board has re-examined its historical stance on competition as it relates to CUSO activity and small credit unions.

First, it is not clear that the Board should, as a matter of principle, consider shielding credit unions from competition as an important consideration in its rulemaking.[48] Doing so may result in stagnation and could produce overall negative results for the credit union system and the NCUSIF over time.

Second, the NCUA currently does and will continue to provide significant support and flexibility to small credit unions through various regulatory and supervisory programs. These efforts recognize the challenges that these small credit unions face by reducing regulatory burdens. For example, the NCUA has a small credit union examination program that streamlines the examination process for small FCUs with a record of solid performance.[49]

The Board believes the final rule presents an opportunity for all credit unions to work collaboratively. It is the Board's belief that the final rule has the potential to benefit all credit unions, especially smaller credit unions, if they can effectively pool their resources to form new technology. The Board also believes the final rule would likely be a net benefit to the entire

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[48] *See Fed. Comm'cns Comm'n et al. v. Prometheus Radio Project et al.*, No. 19–1231 (Apr. 1, 2021), Thomas, J., concurring (discussing whether the FCC should have considered a non-statutory factor in its rulemaking).
[49] *See*, 12-FCU-03 (2012).

system. The Board acknowledges there would likely be additional competition for credit unions, particularly certain smaller credit unions, but this rule provides additional flexibilities to permit the credit union system to offer enhanced lending products. The Board believes that under the final rule, credit unions will have an enhanced ability to collaborate and create better lending products for their members.

For each of these reasons on their own, and in their totality, the Board finds that it is prudent to proceed with this final rule despite this objection.

Types of Loans

Some of the commenters who favor the rule encouraged the NCUA to finalize expansive lending authorities for CUSOs as lending opportunities are always evolving. Several commenters stated that there are currently companies looking for FCU partners that originate solar, renovation, boat, and airplane loans. One commenter expressed concern that these types of loans might cause credit unions to focus on loans for luxury items to the detriment of low- and moderate-income members.

The Board has not limited the types of loans a CUSO can originate provided that the loans are the type of loan an FCU is able to originate. Contrary to the concern of one commenter, the Board does not believe that focused CUSO activity would detract from individual credit unions' focus on providing financial services to all their members, as required by fair lending laws.

Auto Loans and National Lending

Several commenters who support the proposed rule stated that the proposal is necessary for FCUs to remain competitive as lending becomes more standardized and consumers move online for more of their financial services. Many commenters discussed a recent trend to point of sale financing. According to these commenters, consumers are acquiring credit at the point of sale, instead of acquiring credit through a credit union first. Commenters were particularly concerned about this trend for auto loans. These commenters expressed concerns that point of sale sellers are not interested in working with credit unions. The challenge, according to some commenters, is that a large, nationally focused seller is unlikely to secure relationships with thousands of individual credit unions. This presents an opportunity for CUSOs to help the credit union industry with their collaborative business model. Some commenters believed credit unions risk diminishing market share if CUSOs are not permitted to contract with national lenders. One CUSO commenter stated that CUSOs could easily use a common platform and participate out loans to credit unions within the geographic area in which members are located.

A few of the commenters who opposed the rule highlighted the established relationships some credit unions have with local dealers. These commenters were concerned that national lending CUSOs would threaten these existing relationships.

The Board finds that the comments on this issue generally support the regulatory changes. The Board agrees that expanding CUSO lending authority to cover auto loans may help credit unions compete at the point of sale. Existing data also supports the Board's belief that small credit unions are struggling to compete in auto lending and that the final rule may support small credit union auto lending efforts. The largest 150 credit unions have seen significant expansion of their auto lending market share over the prior two decades, while smaller credit

unions have lost market share almost every year.[50] The data indicates that smaller credit unions are becoming increasingly less competitive in the auto lending space.

The Board also recognizes that, despite the stated intent of the proposal, some credit union relationships with local dealers could be displaced by this rule, as they equally could be by other market forces. As discussed previously in response to concerns regarding additional competition for some small credit unions, the Board believes it would be inappropriate for the Board to attempt to restrain competition. The Board also believes that in the long-term, the benefits to the entire credit union system through this enhanced authority and competition will exceed costs associated with disruption to existing credit union-dealer relationships. Indeed, these costs are not certain or inevitable to occur.

Impact Analysis

Several commenters who were opposed to the proposed rule requested that the NCUA conduct an independent economic analysis to weigh the advantages and disadvantages of the proposal. Other commenters recommended an impact analysis specifically to determine the impact on small credit unions.

The Board is aware of the challenges that face small credit unions. As discussed previously regarding growth and competition, the Board does not believe it is prudent or necessary to adopt rules that prevent market-based competition. In response to this specific recommendation for an impact study, the Board also notes that the Administrative Procedure Act

[50] The Board notes, however, that during this period, the number of credit unions with less than $1 billion in assets also decreased by over fifty percent.

does not require agencies to engage in studies before adopting regulatory changes.[51] The Board also believes an impact analysis is unnecessary. The Board believes the final rule will likely benefit credit unions. In the Board's experience, CUSOs generally benefit credit unions through additional capital and the sale of CUSO-originated loans to credit unions. For these reasons, the Board will proceed with the proposed changes without delaying them further to conduct a general impact study. As a separate reason to decline taking this step now, the Board observes that the commenters did not provide any specific studies of their own that would give the Board empirical evidence to support delaying these regulatory changes now.

Loan Pools, Aggregation, and Securitization

A few commenters discussed the issue of securitization and whether the proposed rule would facilitate credit union securitizations. A few commenters asked for the NCUA to specifically permit CUSOs to aggregate credit union loans and issue securities on the secondary market as many credit unions do not have the available resources and volume necessary to originate the requisite amount of loans to securitize assets on their own. The Board will take this comment into consideration for future action.

Another commenter expressed concerns about CUSOs aggregating loans for sale to credit unions. The commenter stated that CUSO-generated loan pools may increase short-term operational efficiency; however, it also transfers the credit risk to smaller credit unions while the ancillary income is generated and retained by the CUSO. This commenter stated that the low

[51] *Fed. Comm'cns Comm'n et al. v. Prometheus Radio Project et al.*, No. 19–1231 (Apr. 1, 2021), slip op. at 12 (holding that the Administrative Procedure Act imposes no general obligation on agencies to conduct or commission their own empirical or statistical studies).

margin and credit risk would be passed to the credit union with the higher margin income retained at the CUSO and ultimately benefit the largest credit union equity partners of the CUSO. This commenter added that historically, when there is market disintermediation, risk and credit losses are passed back to the passive participants with a disproportionate impact. The Board does not believe it is good policymaking to restrict credit union authorities on the potential for credit unions to enter unfavorable business deals. The Board does not believe that a few examples of unfavorable contracts with CUSOs sufficiently justify reducing the flexibilities afforded to the credit union system as a whole. Each credit union is responsible for its own due diligence prior to purchasing assets and entering into a contractual arrangement. Credit unions should exercise business judgment before making purchases and entering any contractual arrangement, even for counterparties that are part of the credit union industry. As part of good governance, credit unions with ownership in a CUSO are encouraged to monitor the length of time all loans remain on the books of the CUSO.

Accordingly, for the reasons discussed in the proposed rule and this final rule, the final rule is adopting the proposed rule without substantive change. Under the final rule, CUSOs are permitted to originate, purchase, sell, and hold any type of loan permissible for FCUs to originate, purchase, sell, and hold. CUSOs, therefore, could originate types of loans previously prohibited by the CUSO rule, including general consumer loans, direct auto loans, and unsecured loans and lines of credit. CUSOs could also purchase vehicle-secured retail installment sales contracts (RICs) from vehicle dealers.

Under the final rule, CUSO originated loans are not subject to the same restrictions as loans originated by FCUs. For example, part 701 of the NCUA's regulations imposes conditions

on FCU lending relating to loan terms such as interest rate, maturity, and prepayment.[52] These restrictions would not apply to CUSO-originated loans because CUSOs, even wholly owned CUSOs, are separate entities from FCUs and are not subject to direct NCUA supervision. However, an FCU may not purchase a loan from a CUSO unless the loan meets the requirements of the NCUA's eligible obligations rule.[53] Similarly, an FCU may not purchase a loan participation from a CUSO unless it complies with the NCUA's loan participations rule.[54]

Loan Participations

Besides specifically permitting CUSOs to engage in consumer mortgage, business, and student loan origination, the current CUSO rule also permits CUSOs to buy and sell participation interests in such loans. The inclusion of this authority to buy and sell participation interests in such loans stems from the FCU Act and the NCUA's loan participation rule, which classifies a CUSO as a "credit union organization" authorized to engage in the purchase and sale of loan participations.[55] The NCUA's loan participation rule, however, does not permit the sale to FCUs of participation interests in open-end, revolving credit.[56] Therefore, the current CUSO rule only permits CUSOs to originate credit card loans, but not the authority to buy and sell participation interests in credit card loans. To remain consistent with the NCUA's loan participation rule, this final rule grants CUSOs the authority to only purchase and sell participation interests that are permissible for FCUs to purchase and sell. There were no comments specifically objecting to this provision, and the Board adopts it without change.

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[52] 12 CFR part 701.
[53] *See*, 12 CFR 701.23(b).
[54] 12 CFR 701.22.
[55] 12 U.S.C. 1757(5)(E); 12 CFR 701.22(a).
[56] 73 FR 79307 (Dec. 29, 2008).

CUSO Registry

Under the current CUSO rule, a FICU must obtain a written agreement from a CUSO the FCU loans to or invests in that the CUSO will annually submit to the NCUA a report containing basic registration information for inclusion in the NCUA's CUSO registry (CUSO Registry).[57] CUSOs that are engaged in complex or high-risk activities have additional obligations with respect to the CUSO Registry.[58] Under the current CUSO rule, complex or high-risk activities are defined to include credit and lending, including business loan origination, consumer mortgage loan origination, loan support services, student loan origination, and credit card loan origination.[59] For consistency, the final rule removes the specific subcategories of lending and instead refers to all loan originations as complex or high risk. Lending activities are considered complex or high risk because they can present a high degree of operational or financial risk.[60] Specifically, FICUs making loans to and investments in CUSOs engaged in credit and lending activities may be exposed to significant levels of credit, strategic, and reputation risks.[61]

Commenters also noted that the CUSO Registry requires all CUSOs to provide data to the NCUA. Several commenters stated that the current reporting requirements are sufficient and the NCUA should not expand reporting requirements, as proposed. The Board is not expanding what

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[57] 12 CFR 712.3(d).
[58] *Id*. Complex or high-risk CUSOs must agree to include in their report: (1) a list of services provided to certain credit unions, and (2) the investment amount, loan amount, or level of activity of certain credit unions. Complex or high-risk CUSOs must also agree to provide the CUSO's most recent year-end audited financial statements to the NCUA. CUSOs engaged in credit and lending services are also required to report the total dollar amount of loans outstanding, the total number of loans outstanding, the total dollar amount of loans granted year-to-date, and the total number of loans granted year-to-date.
[59] 12 CFR 712.3(d)(5)(i).
[60] 78 FR 72537 (Dec. 3, 2013).
[61] *Id.*

must be reported by CUSOs engaging in complex or high-risk activities, but as proposed is incorporating all types of lending in the definition of complex or high-risk activities.

An association of state credit union supervisors expressed concern that state CUSOs with authority to engage in all forms of lending would be required to report additional information under the proposed rule. The organization requested that the NCUA consult with state regulators. The Board notes that when it adopted this provision in 2013, it broadly described credit and lending activities as complex or high-risk and applied this requirement to FICUs.[62] Further, some FISCU-owned CUSOs are reporting the number and dollar amount of their lending activities, even if those lending activities are not explicitly listed in § 712.3(d). The Board, therefore, does not believe the effect of this rule on CUSOs in which only FISCUs have an ownership interest represents a policy change from that final rule.

Expansion of Permissible CUSO Activities to Other Activities as Approved by the Board in Writing

Currently, the list of permissible CUSO activities in § 712.5 includes many of the core services and activities associated with the daily and routine operations of credit unions. The list, however, does not provide the Board flexibility to consider additional activities and services without engaging in notice and comment rulemaking. In contrast, part 704 permits corporate CUSOs to engage in any category of activity as approved in writing by the NCUA and published on the NCUA's website.[63] Amending part 712 to be similar to part 704 has the potential to

[62] 78 FR 72537, 72542 (Dec. 3, 2013).
[63] 12 CFR 704.11(d)(3)(ii). Approved activities are listed on the NCUA's website at: https://www.ncua.gov/regulation-supervision/corporate-credit-unions/corporate-cuso-activities/approved-corporate-cuso-activities.

reduce regulatory burden by allowing the rule to expand as technology shapes the routine and daily operations of credit unions.

Several commenters supported the proposed change to permit the NCUA to approve of new activities outside of notice-and-comment rulemaking. Commenters mentioned the current authority in part 704 for corporate CUSOs. Other commenters generally stated that the proposed process would be more efficient and that the advantages outweigh the public input received through notice-and-comment rulemaking. One commenter stated that the change would allow the Board to be more responsive to shifting market dynamics. Another commenter encouraged the NCUA to periodically review the list for updates and to post any additional activities on its website. A few commenters noted that a technical change is necessary in the regulatory text.

A few commenters who opposed the proposed rule generally discussed that enabling the Board to approve new activities without notice-and-comment rulemaking would eliminate regulatory transparency and opportunity for the public to review and comment on newly proposed CUSO activities. One banking trade organization stated that the authority to approve rules without notice and comment is exacerbated by requiring formal rulemaking to revoke or reform the approved activity, but not adding the same activity. The commenter stated that this policy places a regulatory obstacle to address potentially unsafe and unsound activities, or activities that may be harming consumers, members, and underserved areas and low-to-moderate income communities. One credit union trade organization that supported the rule overall nonetheless encouraged the NCUA to do notice-and-comment rulemaking to add approved activities and suggested limiting the comment period to thirty days as a balance between speed and transparency. Another consumer stated that emerging technologies often pose risks to members and other consumers that should be evaluated through the public notice and comment process.

The Board has considered the comments on this issue and is finalizing the changes to the approval process as proposed. As commenters supporting the change observed, a streamlined process may help CUSOs keep pace with innovation. The Board has considered the opposing comments and notes that its intent is to use this authority only for approving activities that are related to the existing authorities in § 712.5. If the Board believes a new authority is sufficiently novel, and that notice and comment is advisable or required under the Administrative Procedures Act, then the Board would use notice and comment rulemaking.

The Board also believes it is reasonable to add new approved activities without issuing the matters for public comment but to solicit public comment before removing activities. The Board has had this process in place in part 704 for corporate credit unions since 2011 without any indication that the process is unworkable or leads to inadequately considered policy choices. Using notice-and-comment procedures when removing an approved activity is sound policy to ensure that the Board considers parties' serious reliance interests when changing a policy.[64] While the removal of any given approved activity may not rise to the level requiring an in-depth analysis of reliance interests before removing it, the general policy of following this process will help the Board ensure it conducts this analysis in appropriate cases.

Second, the Board has considered, but disagrees with, the suggestion to use a 30-day comment period when adding new activities as a blanket policy. While a 30-day comment period would naturally tend to lead to a prompter conclusion than a 60-day comment period, it would still generally result in several months or more from the time the activity is proposed until it is approved by the Board when taking into account the need to review and respond to public

[64] *See Dep't of Homeland Sec. v. Regents of the Univ. of Calif. et al.*, 591 U.S. ___ (2020), slip. op. at 23 (holding that, when an agency changes course, it must recognize that longstanding policies may have engendered serious reliance interests that must be taken into account).

comments and prepare a final Board action in response. The Board, therefore, finds this suggestion would not implement the proposal as it was intended. Regarding the commenter's transparency concern, the Board notes that it would have discretion to take action to add activities in a public forum, such as open Board meetings, or alternatively, undertake notice-and-comment proceedings if it deems them appropriate or desirable under the circumstances of any particular request to approve a new activity.

Accordingly, under the final rule, the list of permissible activities in § 712.5 includes a catchall category for other activities as approved in writing by the NCUA and published on the NCUA's website. The final rule also provides that once the NCUA has approved an activity and published that activity on its website, the NCUA would not remove that particular activity from the approved list, or make substantial changes to the content or description of that approved activity, except through formal rulemaking procedures.

IV. Investment Authority

An FCU's authority to lend to and invest in a credit union organization is provided for in two separate provisions of the FCU Act. The NCUA has historically interpreted the lending and investment authority under the FCU Act as referring to the same types of organizations.[65] The Board solicited comment about adopting separate definitions for the types of organizations that an FCU may invest in or lend to, which potentially would expand the types of organizations eligible for FCU investment. Several commenters supported the Board's decision to reconsider its longstanding interpretation of FCU investment and lending authority. Commenters in support

[65] 12 U.S.C. 1757(5)(D).

of the reinterpretation generally discussed the benefit of broadly permitting FCUs to invest in financial technology companies. Several commenters stated that FCUs can get left out of the development of new financial technology because of the requirement to primarily serve members. Some commenters stated that additional investment authority would ensure the industry has better leverage, control, and influence in the development of new technologies. Three commenters provided sample safety and soundness conditions that could be applied to these lending authorities.

One commenter recommended that certain de minimis investments be exempt from CUSO requirements. This commenter recommended that the NCUA permit FCUs to make a 25 percent investment in CUSOs of FISCUs without those CUSOs being subject to part 712. Currently, the preapproved activities and most other requirements of part 712 do not apply to CUSOs with only FISCU investment. Accordingly, if the only credit unions that have an ownership in a CUSO are state-chartered, then the CUSO may be able to engage in activities beyond those that are preapproved in § 712.5. Thus, any investment in, or loan to, a CUSO (which § 712.1 generally describes as ownership interests) from an FCU subjects the CUSO to all of part 712's requirements. The commenter's suggestion is that some amount of such investment should be allowed without invoking those requirements. The Board appreciates this recommendation and will take it into consideration when evaluating future action on the investment issue. The Board observes, however, that any future expansion of FCU investment authority would need to be in organizations providing services associated with the routine operations of credit unions, which could vary from some types of entities in which state-chartered credit unions may invest.

Another commenter recommended that the proposed interpretation be adopted and extended to corporate credit unions.

In contrast, one banking trade organization stated that expanding FCU investment authority in CUSOs would be outside the routine operations of credit unions, which are statutorily confined to serving their fields of membership. The commenter stated that the NCUA's position would exceed the agency's legal authority under the FCU Act.

The Board will consider these comments in determining whether to propose any change to its existing interpretation and regulatory definition of a CUSO. The Board notes, however, that it does not find persuasive the contention that the possible reinterpretation is inconsistent with the FCU Act. As set forth in the preamble to the proposed rule, the investment provision of the FCU Act contains distinct wording from the loan provision. The preamble discussion in the proposed rule discussed the statutory wording and possible interpretation in careful detail. The Board, therefore, declines to withdraw this portion of the proposed rule, as recommended by the commenter, and will consider this issue for potential future action.

V. Other Comments

The Board also received other comments outside the scope of the proposed rule, which are discussed briefly in this section.

One commenter recommended that where a CUSO is making a loan that involves tax credits the CUSO should be permitted to acquire and syndicate the tax credits, whether among taxable (non-credit union) members of the CUSO and/or third-party investors. The Board will consider this issue for potential future action for CUSO investment authorities but notes that these authorities have historically been narrow.[66] The NCUA has, however, previously found a

[66] *See* 12 CFR 712.5(r), 712.6.

CUSO's proposed acquisition and sale of tax credits in connection with approved lending activity to be permissible.[67]

One commenter asked that CUSOs be permitted to engage in both debt and equity aspects of financing sale-leaseback transactions for credit unions, whether those credit unions are members of the CUSO or not. The Board will consider this request in connection with future action on CUSO authorities.

One commenter suggested the NCUA offer periodic dialogue sessions akin to those recently launched by the Federal Deposit Insurance Corporation, and recommended a CUSO compliance guide. The Board will consider these suggestions as part of its ongoing supervisory program.

VI. Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) generally requires that, in connection with a final rulemaking, an agency prepare and make available for public comment a final regulatory flexibility analysis that describes the impact of a rule on small entities (defined for purposes of the RFA to include credit unions with assets less than $100 million).[68] A regulatory flexibility analysis is not required, however, if the agency certifies that the rule will not have a significant

[67] OGC Op. Ltr. 03–0647, FCU and CUSO Participation in New Markets Tax Credit Program (July 2003), *available at* https://www.ncua.gov/regulation-supervision/legal-opinions/2003/federal-credit-union-and-credit-union-service-organization-participation-newmarkets-tax-credits.
[68] *See* 80 FR 57512 (Sept. 24, 2015).

economic impact on a substantial number of small entities and publishes its certification and a short, explanatory statement in the *Federal Register* together with the rule.

This rule does not have a significant economic impact on a substantial number of small entities. The rule imposes no requirement or costs on small entities and only expands the list of permissible activities for CUSOs. The rule expands the list of activities that are considered complex or high risk for purposes of the CUSO Registry, however, the Board does not expect the additional reporting requirements to entail substantial regulatory burden. Accordingly, the NCUA certifies that the final rule does not have a significant economic impact on a substantial number of small FICUs.

Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3501 et seq.) requires that the Office of Management and Budget (OMB) approve all collections of information by a Federal agency from the public before they can be implemented. Respondents are not required to respond to any collection of information unless it displays a current, valid OMB control number.

Consistent with the PRA, the information collection requirements included in this final rule has been submitted to OMB for approval under control number 3133-0149.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. Per fundamental federalism principles, the

NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the principles of the Executive order. This rulemaking will not have a substantial direct effect on the states, on the connection between the National Government and the states, or on the distribution of power and responsibilities among the various levels of government. The NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the Executive order.

Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105-277, 112 Stat. 2681 (1998).[69]

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA) generally provides for congressional review of agency rules.[70] A reporting requirement is triggered in instances where the NCUA issues a final rule as defined in the Administrative Procedure Act.[71] An agency rule, besides being subject to congressional oversight, may also be subject to a delayed effective date if the rule is a "major rule." [The NCUA does not believe this rule is a "major rule" within the meaning of the relevant sections of SBREFA]. As required by SBREFA, the NCUA will submit this final rule to OMB for it to determine if the final rule is a "major rule"

[69] Pub. L. 105–277, 112 Stat. 2681 (1998).
[70] 5 U.S.C. 551.
[71] *Id.*

for purposes of SBREFA. The NCUA also will file appropriate reports with Congress and the Government Accountability Office so this rule may be reviewed.

List of Subjects in 12 CFR Part 712

Administrative practices and procedure, Credit, Credit unions, Insurance, Investments, Reporting and recordkeeping requirements.

By the National Credit Union Administration Board on October 21, 2021.

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Melane Conyers-Ausbrooks,

Secretary of the Board.

For the reasons stated in the preamble, the Board amends 12 CFR part 712 as follows:

PART 712—CREDIT UNION SERVICE ORGANIZATIONS (CUSOs)

1. Amend the authority for part 712 by revising the citation to read as follows:

Authority: 12 U.S.C. 1756, 1757(5)(D) and (7)(I), 1766, 1782, 1784, 1785, 1786, and 1789(a)(11).

2. Amend §712.3 by revising paragraphs (d)(5)(i), (d)(5)(ii) introductory text, and (d)(5)(iii) to read as follows:

§ 712.3 What are the characteristics of and what requirements apply to CUSOs?

* * * * *

(d) * * *

(5) * * *

(i) Credit and lending:

(A) Loan support services, including servicing; and

(B) Loan origination, including originating, purchasing, selling, and holding any loan as described in § 712.5(q).

(ii) Information technology:

* * * * *

(iii) Custody, safekeeping, and investment management services for credit unions.

* * * * *

3. Amend §712.5 as follows:

a. Revise paragraph (a) introductory text;

b. In paragraph (a)(4), add a semicolon at the end of the paragraph;

c. Revise paragraph (b) introductory text;

d. In paragraph (b)(11), remove the period and add a semicolon in its place;

e. Remove paragraphs (c), (d), (n), and (s);

f. Redesignate paragraphs (e) through (t) as paragraphs (c) through (p);

g. Revise newly redesignated paragraphs (c) introductory text, (d) introductory text, (e) introductory text, (f) introductory text, (g) introductory text, and (h) introductory text;

h. In newly redesignated paragraph (h)(3), remove the word “and”;

i. Revise newly redesignated paragraphs (i) introductory text, (j), (k), (l), and (m) introductory text;

j. In newly redesignated paragraph (m)(3), remove the period and add a semicolon in its place;

k. Revise newly redesignated paragraph (n);

l. In newly redesignated paragraph (o), remove "*CUSO investments in non-CUSO service providers:*" and remove the last period and add a semicolon in its place;

m. In newly redesignated paragraph (p), remove the period and add a semicolon in its place; and

n. Add new paragraphs (q) and (r).

The additions read as follows:

§712.5 What activities and services are preapproved for CUSOs?

* * * * *

(a) Checking and currency services:

* * * * *

(b) Clerical, professional and management services:

* * * * *

(c) Electronic transaction services:

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(d) Financial counseling services:

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(e) Fixed asset services:

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(f) Insurance brokerage or agency:

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(g) Leasing:

* * * * *

(h) Loan support services:

* * * * *

(i) Record retention, security and disaster recovery services:

* * * * *

(j) Securities brokerage services;

(k) Shared credit union branch (service center) operations;

(l) Travel agency services;

(m) Trust and trust-related services:

* * * * *

(n) Real estate brokerage services;

* * * * *

(q) Loan origination, including originating, purchasing, selling, and holding any type of loan permissible for Federal credit unions to originate, purchase, sell, and hold, including the authority to purchase and sell participation interests that are permissible for Federal credit unions to purchase and sell; and

(r) Other categories of activities as approved in writing by the NCUA and published on the NCUA's website. Once the NCUA has approved an activity and published that activity on its website, the NCUA will not remove that particular activity from the approved list or make substantial changes to the content or description of that approved activity, except through formal rulemaking procedures.