

**Comments of the
NATIONAL CONSUMER LAW CENTER¹
on behalf of its Low Income Clients
on**

**Proposed Rules
National Credit Union Administration (NCUA)
12 CFR Parts 712 and 741
RIN 3133-AD93
Credit Union Service Organizations
76 Fed. Reg. 44866 (July 27, 2011)**

Submitted Sept. 26, 2011

Thank you for the opportunity to comment on NCUA's proposed credit union service organization (CUSO) rule. We support NCUA's proposal to protect the safety and soundness of the credit union industry by extending the federal CUSO accounting and reporting requirements to CUSOs owned by federally insured state credit unions (FISCUs); by requiring all CUSOs to file financial reports directly with NCUA; and by requiring subsidiary CUSOs to follow all applicable laws and regulations.

We are particularly concerned about a very small number of CUSOs (and credit unions) that are engaged in payday lending or activities supporting payday lending. Payday loans – short-term, high-rate small loans – lead borrowers into a destructive cycle of debt and lead to a number of adverse consequences.² This form of irresponsible lending creates a variety of compliance, safety and soundness and reputation risks for both the entity that makes the loans and any other entities associated with them.

We appreciate the actions that NCUA has taken to date to address payday lending and to encourage credit unions to offer responsible small loans. But more is needed, and the examination authority over CUSOs proposed in the present rulemaking is an important step. As NCUA examines CUSOs, it must identify their full range of activities and credit union relationships. We urge NCUA to:

- Stop CUSOs (and credit unions) from engaging in payday lending;
- Stop both federal and state credit unions from investing in, taking finder's fees from, or otherwise engaging with CUSOs that are involved with payday lending,

¹ The National Consumer Law Center, Inc. (NCLC) is a non-profit Massachusetts Corporation, founded in 1969, providing legal expertise on consumer law issues to public and private attorneys, policy makers, and consumer advocates across the country, with a special focus on low-income consumers. NCLC publishes a series of 18 practice treatises consumer laws, including Cost of Credit, Truth in Lending, and Unfair and Deceptive Acts and Practices. NCLC's attorneys have been closely involved with the enactment of and regulations under virtually all federal laws affecting consumer credit since the 1970s. These comments were written by Lauren Saunders.

² A longer discussion of the harms of payday loans can be found in National Consumer Law Center, *Stopping the Payday Loan Trap: Alternatives that Work, Ones that Don't* (June 2011), available at http://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/report-stopping-payday-trap.pdf, and in the comments filed today by the Center for Responsible Lending.

which would be unlawful, or would pose undue safety and soundness and reputation risks, if the credit union made the loans directly.

In these comments we will: (1) update our 2010 report detailing credit union involvement in payday lending, (2) describe CUSO rules that should be applied to prohibit payday lending by CUSOs, and (3) briefly outline the various laws that compel NCUA to rein in payday lending by CUSOs and credit unions.

A list of credit unions that we have identified that are still involved in payday lending is attached to these comments.

1. Payday Lending by CUSOs and Credit Unions

In our report last year, *Stopping the Payday Loan Trap: Alternatives that Work, Ones that Don't*,³ we identified a number of credit unions that have developed responsible alternatives to payday loans that have significantly lower rates, installment payments, longer repayment periods, and other features that make them truly helpful products for those in need of small dollar credit. Yet we also identified a number of credit unions, both federal and state, that are engaged in payday lending, either directly or, more commonly, through CUSOs. The accomplishments of the credit unions that offer affordable small loans, and the reputation of the credit union industry overall, risk being tarred by CUSO and direct credit union payday loans that differ little or not at all from destructive traditional payday products.

Last year's report identified 58 credit unions (31 federal and 27 state) that were offering short-term, high-rate loans with annual rates up to 400% or higher. The loans were primarily but not entirely made through CUSOs.

Since then – likely due to scrutiny by NCUA, which we applaud – the CUSO CU Access, which operated as e-accessloans.com, ceased operations and most of the federal and state credit unions that were offering loans through that CUSO appear to have ended their involvement in payday lending.⁴ A few other credit unions and CUSOs listed in our report also appear to have stopped offering payday loans. On the other hand, a few new credit unions have bucked the trend and have entered the payday business.

All told, we presently count 25 credit unions (14 federal and 11 state) that are still offering payday loans, again mostly through CUSOs. NCUA deserves credit for this drop in credit union payday lending, though these numbers (and those in our original report) are undoubtedly understated, as we do not have the capacity to identify all credit union or CUSO activities. We support NCUA's effort to gain more information and control over CUSO activities so that the full risk to credit unions from irresponsible lending practices can be understood and eliminated.

³ The report is available at http://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/report-stopping-payday-trap.pdf.

⁴ One of those credit unions, University of Hawaii Federal Credit Union, is now offering payday loans by CU on Payday, but we have not identified any continuing involved in payday lending by the other credit unions that were associated with CU Access. It is possible, of course, that we have missed it.

Although CU Access has ceased operations, other entities associated with CU Access remain in the payday lending business. CU Access was managed by America First Federal Credit Union and Capital Finance, LLC. The following related entities may be CUSOs and continue to offer payday loans to credit union members.

CU on Payday, LLC is a Washington limited liability corporation registered in Utah. Its managers are the same team that manages Capital Finance, LLC, which may own CU on Payday. CU on Payday has changed its website and it is no longer as easy to find the payday loans that it offers to credit union members. However, at least 10 federal⁵ and 3 state credit unions⁶ are letting CU on Payday use their names – and undoubtedly getting a finder’s fee in return – for 300% loans. In some cases, the payday loans are promoted on the credit union’s website.

Myinstacash is a dba of Capital Finance, LLC. It offers loans to credit union members at disclosed APRs of 146% to 876%.⁷ The website lists Mountain America Financial Services, a CUSO of Mountain America Credit Union (a federal credit union), in the masthead. The “about us” page states: “*Myinstacash, CU on Payday or Capital Finance LLC is licensed as a deferred deposit lender in Utah, Oregon, Washington, Colorado, North Dakota and Montana.*”⁸

In addition, **XtraCash LLC**, a subsidiary of Mazuma Credit Union, continues to offer payday loans to Mazuma members.⁹ The 261% to 392% APR XtraCash loans are also now offered by at least one FCU: Orlando Federal Credit Union.¹⁰

We would also be remiss in discussing CUSO payday lending if we did not point out that direct credit union payday lending remains a problem. **Kinecta Federal Credit Union** continues to flout the FCUA 18% usury rate and to make loans with a true annual rate, including the application fee, of 362%.¹¹ Another FCU, **Tri-Rivers Federal Credit**

⁵ University of Hawaii FCU: <https://www.uhfcu.com/loans/cuonpayday.html> (visited 9/21/11); Chetco FCU (Oregon): <http://chetco.cuonpayday.com> (visited 9/21/11); Clackamas FCU (Oregon): <http://clackamas.cuonpayday.com/> (visited 9/21/11); Rogue FCU (Oregon): <http://www.cuonpayday.com/rogue/> (visited 9/21/11); Pacific Crest FCU (Washington State): <http://www.cuonpayday.com/usuccu/> (visited 9/21/11); USU Charter Credit Union (FCU, Utah): <http://www.northernhillsfcu.org/borrow/other-loans/> (visited 9/21/11); Cyprus Credit Union (FCU, Utah): <http://cyprus.cuonpayday.com/> (visited 9/21/11); Heritage West CU (FCU, Utah): <http://www.cuonpayday.com/heritagewest/> (visited 9/21/11); People’s Community FCU (Washington State): <http://pccu.cuonpayday.com/index.php> (visited 9/21/11).

⁶ Marion And Polk Schools Credit Union (Oregon): <http://maps.cuonpayday.com/> (visited 9/21/11); Oregon Community CU: <http://oregoncommunity.cuonpayday.com/index.php> (visited 9/21/11); White River Credit Union (Washington State): <http://whiteriver.cuonpayday.com> (visited 9/21/11).

⁷ See <http://www.myinstacash.com/Fees.php> (visited 9/24/11).

⁸ See <http://www.myinstacash.com/AboutUs.php> (visited 9/24/11).

⁹ See http://www.mazuma.org/loans/micro_loans.php?loan_nav=micro (visited 9/21/11).

¹⁰ https://www.orlandofcu.org/services/payday_loan.asp (visited 9/21/11). The website promotes “the XtraCash program offered through Orlando Federal Credit Union.” The XtraCash website discloses APRs from 240% to 287% for loans made in Florida. http://www.xtracashllc.com/florida_fees.html (visited 9/24/11).

¹¹ See <http://nixcheckcashing.com/> (visited 9/24/11); *Stopping the Payday Loan Trap* at 38.

Union, is also offering payday loans at a cost of \$8.75 or \$11 per \$100, depending on the term of the loan (10 to 31 days), an annual rate of 160% to 401%. No APR is disclosed on the website.¹² It is also unclear whether **Northern Hills Federal Credit Union** is making payday loans directly or through a CUSO.¹³ These loans all likely violate both the Truth in Lending Act's APR rules and the Federal Credit Union Act's (FCUA) usury cap.¹⁴

At least seven FISCUs are also directly making payday loans.¹⁵ While FISCUs are not subject to the FCUA usury cap, the loans do pose various safety and soundness and legal issues, discussed briefly below.

2. CUSO Rules that Should Forbid Payday Lending

We are pleased that NCUA intends to take a closer look at CUSOs. We urge it to give payday lending by CUSOs – and directly by credit unions – especially close scrutiny. CUSO payday operations conflict with several rules governing CUSOs.

Purpose of CUSOs. The purpose of CUSOs is to enable credit unions to take advantage of “a level of expertise that may not be attainable by individual credit unions ...”¹⁶ Triple-digit loans are not part of the routine operations of credit unions, state or federal. Indeed, NCUA and the Eighth Circuit have found that payday loans are inconsistent with the FCU charter. Payday loans are not “promoting thrift” or “creating a source of credit for provident or productive purposes.”¹⁷

CUSOs are being used for payday loans not because they have expertise that credit unions lack, but rather to avoid the laws governing FCUs and to insulate credit unions from the taint of direct predatory lending. NCUA should put a halt to this improper use of CUSOs by federal or state credit unions.

¹² See <http://www.mtfcu.com/GoodMoney.htm> (visited 9/24/11). It is unclear if Tri-Rivers, like Kinecta, claims that the fees are properly excludable from the APR, but any such claim would be a sham.

¹³ Unlike most of the other CU on Payday loans, the loans do not appear to be made through the CU on Payday website and the credit union website provides a credit union application form and the credit union telephone number as the way to apply. See <http://www.northernhillsfcu.org/borrow/other-loans/> (visited 9/21/11).

¹⁴ NCUA's authority to interpret and enforce the FCUA usury cap is independent of Regulation Z. Even while looking to Reg. Z to calculate APRs, NCUA could prohibit FCUs from structuring their loans to have disproportionate application or other fees that manipulate the APR to evade the usury cap.

¹⁵ Frankenmuth Credit Union (Michigan):

https://www.frankenmuthcu.org/Payday_Lending_Center_42.html (visited 9/21/11); Delta County CU (Michigan): http://www.deltacountycu.com/Payday_Loans_66.html (visited 9/21/11); Guadalupe Credit Union (New Mexico): http://www.guadalupecu.org/portal/page/portal/Guadalupe/Accts_services/loans (visited 9/21/11); Salal Credit Union (Oregon): <https://www.salalcu.org/loans/personal-loans> (visited 9/21/11); Washington State Employees CU: <http://www.wsecu.org/x405.xml> (visited 9/21/11); Prospera Credit Union (Wisconsin): <http://www.goodmoneystore.com/contact.asp> (visited 9/21/11); Superior Choice CU (Wisconsin and Minnesota): <http://www.superiorchoice.com/goodmoney.htm> (visited 9/21/11).

¹⁶ NCUA, Final Rule, Credit Union Service Organizations, 73 Fed. Reg. 79307, 79308 (Dec. 29, 2008).

¹⁷ 12 U.S.C. § 1752(1); *accord* *Oiciyapi Federal Credit Union v. National Credit Union Admin.*, 936 F.2d 1007 (8th Cir. 1991) (affirming NCUA decision to dissolve credit union involved in payday lending).

Investments in, Loans to, or Contracts with CUSOs. The CUSO Rule states that “an FCU may invest in, loan to, and/or contract with only those CUSOs that are ... engaged in the preapproved activities and services related to the routine daily operations of credit unions.”¹⁸ Payday lending is not one of the preapproved activities in the CUSO Rule, and for good reason.¹⁹ Any FCU contract with a CUSO related to payday activities violates the CUSO Rule, including contracts relating to finders’ fees, loans to the FCU’s members, use of the FCU’s name on the CUSO’s website, or cross listing of a link to the CUSO’s website on the FCU’s website. NCUA should make clear that FCUs should never be involved in CUSO activities that would be unlawful for the FCU itself.

Though this part of the CUSO rule does not apply to FISCUs, the purpose behind the rule – to limit use of CUSOs to legitimate credit union activities – applies equally. Like FCUs, FISCUs should also be prohibited from investing in, lending to, or contracting with payday CUSOs.

Finders’ Fee. The Incidental Powers Rule permits FCUs to engage in certain activities that are “necessary or requisite to enable [the FCU] to carry on effectively” the credit union’s business.²⁰ Certain categories of activities are preapproved as incidental powers. One of these is “finder activities,” which includes bringing together two parties, endorsing a product or service, and offering third party products or services through the FCU website, among other finder activities.²¹ Most of the FCUs that are involved in payday lending appear to be doing so through “finder activities” through which they receive payment for promoting CUSO payday loans, letting the CUSO use the FCU name, and otherwise enabling payday loans to the FCU’s members. Other preapproved categories, such as marketing activities, may also cover certain aspects of FCU involvement in payday loans.²²

Though the general category of finder activities is preapproved as a permissible incidental power, enabling payday loans through finder activities does not meet the definition of “incidental powers activities.” An activity meets the definition of an incidental power activity only if it:

- (a) Is convenient or useful in carrying out the mission or business of credit unions consistent with the Federal Credit Union Act;
- (b) Is the functional equivalent or logical outgrowth of activities that are part of the mission or business of credit unions; and
- (c) Involves risks similar in nature to those already assumed as part of the business of credit unions.²³

Activities that promote or enable payday loans violate all three of these requirements. First, lending at 300% or higher is not part of the credit union mission and

¹⁸ 12 C.F.R. § 712.5 (emphasis added); *see* 12 U.S.C. § 1757(7).

¹⁹ Mortgage, student and credit card lending are the only approved consumer lending activities. *See* 12 C.F.R. § 712.5(c), (d), (n).

²⁰ 12 C.F.R. § 721.2.

²¹ 12 C.F.R. § 721.3(f).

²² 12 C.F.R. § 721.3(h).

²³ 12 C.F.R. § 721.2 (emphasis added).

would violate the FCUA. Second, triple-digit payday lending is not a functional equivalent or logical outgrowth of legitimate credit union activities. Finally, payday lending inherently involves very expensive, predatory lending to individuals without regard to ability to pay, and significant compliance, reputational and other risks. Any contractual relationship or involvement with entities engaged in payday lending involves risks that are radically different in nature to those assumed by a credit union as part of its regular business. Even if the credit union does not bear any of the risk of loss of the loans, the credit union does bear significant risks by marketing a loan made by a third party that it does not control and letting that third party use the credit union's name.

Though the Incidental Powers Rule does not apply directly to FISCUs, activities such as payday lending that do not meet the definition of "incidental powers activities" are highly likely to pose undue risks to the insurance fund for the same reasons discussed above and below and to be inappropriate for state credit unions as well. NCUA should declare that neither federal nor state credit unions may use their incidental powers to engage in finder, marketing or similar activities related to payday lending.

3. Risks That Compel NCUA to Rein in Credit Union Payday Lending.

Beyond the CUSO-specific rules and policies, in its capacity as insurer of both federal and state credit unions, NCUA should stop CUSOs and credit unions from taking on the long list of compliance, safety and soundness and reputation risks associated with payday lending. Those risks include strategic risk, reputation risk, transaction risk, credit risk, compliance risk, and others.²⁴ Those risks are not obviated and in fact increase if the lending happens through third parties.²⁵ Neither state nor federal credit unions should use CUSOs to distance themselves from lending practices that would be unsafe and unsavory for them to engage in directly.

In particular, a variety of other laws pose serious compliance risks to CUSOs and credit unions engaged in payday lending and compel NCUA to restrain payday lending to protect credit unions and the insurance fund. As detailed in our earlier legal analysis,²⁶ these include:

- *Federal Trade Commission Act (FTC Act)*: With respect to both federal and state credit unions, NCUA should use its FTC Act authority to prevent unfair or deceptive acts or practices to direct credit unions not to make unaffordable loans that borrowers are unable to repay without rollovers and not to structure their

²⁴ These risks are described in NCLC Letter to NCUA (Jan. 29, 2009), available at http://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/letter-ncua-payday-0109.pdf, and in the comments of the Center for Responsible Lending filed today.

²⁵ The Office of the Comptroller of the Currency noted that "authorizing third parties to conduct business in the banks' name is potentially the most problematic of the third-part relationships and often warrants significant additional supervisory scrutiny by the OCC." OCC Letter to CEOs re Third-Party Relationships Risk Management Principles, OCC 2001-47 (Nov. 1, 2001). In particular, franchising arrangements, in which the bank basically receives a fee in return for the use of its name, "often involve significant reputation, strategic, transaction, and compliance risk to the bank." *Id.*

²⁶ Letter from NCLC to NCUA (Jan. 29, 2009), available at http://www.nclc.org/images/pdf/high_cost_small_loans/payday_loans/letter-ncua-payday-0109.pdf.

loans in such a way as to evade interest rate caps. In addition, it is unfair and deceptive for a credit union to lend its name in connection with a loan that is not actually made by the credit union and would be illegal or unsound for the credit union to make. A mere disclosure that the credit union is not the lender is not sufficient to remove the credit union's association with the loan. Credit unions and CUSOs should also anticipate further rules against unfair, deceptive and abusive lending practices from the Consumer Financial Protection Bureau.

- *Electronic Funds Transfer Act (EFTA)*: EFTA prohibits conditioning credit on payment by preauthorized electronic funds transfer. The purpose is to protect the sanctity and security of deposit accounts and to prevent lenders from taking their cut of wages or benefits before the consumer buys food, rent or medicine. Credit union and CUSO payday loans routinely require preauthorized electronic payment. Though the EFTA's scope is limited to recurring payments and may not apply to a single-payment loan, payday loans that roll over are recurring payments.²⁷
- *Truth in Lending Act (TILA)*: Disproportionate application or participation fees intended to manipulate the APR disclosed for a payday loan do not meet the letter or spirit of Regulation Z. In addition, some loans purport to be open-end credit, and to be entitled to disclose no APR if they have no periodic interest, but in fact they are closed-end credit for which an APR must be disclosed. Some credit unions and CUSOs also fail to properly disclose the APR and emphasize instead the fee per \$100 loaned.
- *Equal Credit Opportunity Act (ECOA)*. Credit unions that offer loans at dramatically higher rates to one group of members than the loans offered to other members risk violating the ECOA.

Conclusion

We strongly support the NCUA's proposal to protect the safety and soundness of the credit union industry and the insurance fund by exercising greater scrutiny over CUSOs. We urge NCUA to use that authority to stop CUSOs, and credit unions, from engaging in payday lending and to focus their energies and the reputation of the credit union industry on affordable, responsible lending practices for which credit unions are rightly known.

²⁷ See National Consumer Law Center, Consumer Banking and Payments Law 4.11.1 (2011 Supp.); *Mitchem v. GFG Loan CO.*, 200 WL 294119 (N.D. Ill. Mar. 17, 2000); *Johnson v. Tele-Cash, Inc.*, 82 F. Supp. 2d 264 (D. Del. 1999), *rev'd in part on other grounds*, 225 F.3d 366 (3d Cir. 2000).

Credit Unions Engaged in Payday Lending*

| Credit Union | State | Type | Through CUSO | Directly | Website |
|-------------------------------|-----------------------|-------|--------------|----------|---|
| Tri-Rivers FCU | Alabama | FCU | | x | http://www.mtfcu.com/GoodMoney.htm |
| Kinecta FCU | California | FCU | | x | http://nixcheckcashing.com/ |
| Orlando FCU | Florida | FCU | ? | | https://www.orlandofcu.org/services/payday_loan.asp |
| University of Hawaii FCU | Hawaii | FCU | x | | https://www.uhfcu.com/loans/cuonpayday.html |
| Frankenmuth CU | Michigan | FISCU | | x | https://www.frankenmuthcu.org/Payday_Lending_Center_42.html |
| Delta County CU | Michigan | FISCU | | x | http://www.deltacountycu.com/Payday_Loans_66.html |
| Mazuma CU | Missouri | FISCU | x | | http://www.mazuma.org/loans/micro_loans.php?loan_nav=micro |
| Guadalupe CU | New Mexico | FISCU | | x | http://www.guadalupecu.org/portal/page/portal/Guadalupe/Accts_services/loans |
| Chetco FCU | Oregon | FCU | x | | http://chetco.cuonpayday.com/ |
| Clackamas FCU | Oregon | FCU | x | | http://clackamas.cuonpayday.com/ |
| Rogue FCU | Oregon | FCU | x | | http://www.cuonpayday.com/rogue/ |
| Marion And Polk Schools CU | Oregon | FISCU | x | | http://maps.cuonpayday.com/ |
| Oregon Community CU | Oregon | FISCU | x | | http://oregoncommunity.cuonpayday.com/index.php |
| Salal CU | Oregon South | FISCU | | x | https://www.salalcu.org/loans/personal-loans |
| Northern Hills FCU | Dakota | FCU | | ? | http://www.northernhillsfcu.org/borrow/other-loans/ |
| USU Charter CU | Utah | FCU | x | | http://www.cuonpayday.com/usuccu/ |
| Cyprus CU | Utah | FCU | x | | http://cyprus.cuonpayday.com/ |
| Heritage West CU | Utah | FCU | x | | https://www.heritagewestcu.com/LoanProducts/express_cash.php |
| Mountain America CU | Utah | FCU | x | | http://www.myinstacash.com |
| Pacific Crest FCU | Washington | FCU | x | | http://www.pacificcrestfcu.com/personal/extras/cu-on-payday/ |
| People's Community FCU | Washington | FCU | x | | http://pccu.cuonpayday.com/index.php_9/21/11 |
| White River CU | Washington | FISCU | x | | http://whiteriver.cuonpayday.com |
| Washington State Employees CU | Washington | FISCU | | x | http://www.wsecu.org/x405.xml |
| Prospera CU | Wisconsin | FISCU | | x | http://www.goodmoneystore.com/contact.asp |
| Superior Choice CU | Wisconsin & Minnesota | FISCU | | x | http://www.superiorchoice.com/goodmoney.htm |

*Payday lending refers to short-terms loans at high, usually triple-digit rates.