CUNA
Credit Union National Association

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The Honorable Rick Metsger
Chairman
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

Dear Chairman Metsger:

On behalf of America's credit unions and the millions of consumers in need of small dollar credit, I am writing to encourage you to consider and address with the Consumer Financial Protection Bureau (the Bureau) the very significant impact its recently released proposed rule for payday loans, vehicle title loans, and small dollar loans ("proposed rule") will have on credit unions.

Credit unions are the original consumer protectors in the financial services industry. Owned by their members and operated as cooperatives, credit unions' core mission is to promote thrift and provide access to credit for provident purposes. Some of the earliest credit unions were formed for the purpose of making small loans, and we are quite concerned that the Bureau's proposal sweeps in and threatens the stability of these consumer-friendly products offered by credit unions. This action, in our view, is uncalled for given credit unions' history of, and approach to providing short term, small dollar credit to their members. We have specific concerns that the proposal will discourage credit union participation in the National Credit Union Administration's (NCUA) Payday Alternative Loan (PAL) program because of the additional compliance and regulatory burdens it places on credit unions participating in it.

Predatory or abusive lending practices deserve increased scrutiny; however, as the Bureau works to address the issues in the for-profit payday and title lending space, it is critical that they do so in a manner that ensures consumers can continue to access safe and affordable credit from credit unions, which have no history of abusive behavior. As you know, credit unions that offer these types of loans to their members generally do so as a service to members who may have a one time or unexpected expense such as a flat tire, medical expense, or high utility bill. Those interested in protecting consumers from abusive lending practices should want active credit union participation in this market because credit unions often serve as the liberator to consumers who have fallen into the cycle of debt or have been the victims of predatory lending practices. Indeed, there have been many cases in which a credit union's assistance to its members has helped bring them out of an abusive lending situation and back into mainstream financial services.

In his remarks at the field hearing on the proposed rule, CFPB Director Richard Cordray stated that, "In particular, we are not intending to disrupt existing lending by community banks and credit unions that have found efficient and effective ways to make small-dollar loans to consumers that do not lead to debt traps or high rates of failure. Indeed, we want to encourage other lenders to follow their model."

We encourage you to carefully consider whether the proposal would disrupt existing lending by credit unions. After you have had a chance to review the proposal, we hope you will address the impact it will have on credit unions with Director Cordray, and encourage him to use the Bureau's statutory powers to ensure the rule does not disrupt consumers' ability to access safe and affordable short term, small dollar credit from credit unions.

Frankly, we believe that if the intention of the Bureau's proposal was not to disrupt credit union lending, then the proposal has badly missed the mark. Not only will this proposed rule disrupt, and arguably crush, the ability of credit unions to offer small dollar loans, it also sweeps in and detrimentally impacts the ability to offer other types of loans such as refinanced auto loans. The good news is that the Bureau has the statutory authority to protect consumers from losing access to safe and affordable short term, small dollar credit from their credit union. We believe the best solution to protect credit union consumer friendly small dollar and other covered loan products is for the Bureau to use its authority under Section 1022 of the Dodd-Frank Wall Street Reform and Consumer Protection Act to exempt credit unions from its proposed rule in entirety.

As you examine the proposal, there are a number of issues we encourage you to consider, including the fact that the PAL program is not exempted by the proposal notwithstanding the Bureau's claim that it is; the proposal's underwriting requirements are unnecessarily complex; the scope of the proposal is overly broad and will sweep in other products and services that consumers need; and the final result of this proposal, if implemented, will be a reduction in the availability of consumer credit.

The NCUA PAL Program is Not Exempt and Would Be Adversely Impacted by the Proposed Rule

Recent NCUA data showed that federal credit unions originated $123.3 million in payday alternative loans over the four quarters ending in the fourth quarter of 2015. This showed an increase of 7.2 percent from the fourth quarter of 2014, and CUNA was encouraged by this interest in participating in the PAL program. We are extremely disappointed that the Bureau's proposed rule, if it moves forward in its current form, is very likely to not only impede this growth of the PAL program, but will force many credit unions to abandon their participation in it. In Congressional testimony, in conversations with CUNA, and in other public releases, the Bureau has stated the NCUA PAL program is exempt from the proposed rule. However, that is not the case. In reality, the proposed rule adds a number of new conditions to offer PAL loans (please see the attachment for our analysis of changes the proposed rule would make and the compliance changes it would require). This is problematic for several reasons and credit unions have continually warned the Bureau that adding more compliance burdens to the PAL program will force credit unions to stop offering these loans. We have already heard from credit unions that they will be unable to sustain their PAL programs after the Military Lending Act made changes to the number of application fees allowed for PAL loans, and arguably that change was not as complex as what the Bureau has proposed.

Not only do we believe that some of the new conditions the Bureau proposed in the rule would make PAL loans unsustainable, we believe the sheer complexity of the proposed rule alone will force credit unions to stay out of this market. As the NCUA has recognized, credit unions are facing an unprecedented amount of regulatory burden, and just over the past several years they have been forced to comply with thousands of pages of regulations from the Bureau and other regulators. This proposed rule is more than 1300 pages. As such, it is important to understand that credit unions, who make little or no profit on PAL or other similar loans but usually offer them as a service or courtesy to members, are being asked to voluntarily navigate compliance with a rule that is hundreds of pages long with many complexities. Furthermore, changes to payment transfers and collection processes found in the proposed rule could subject a credit union to safety and soundness issues.

The Underwriting Requirements Are Unnecessarily Complex for Credit Unions

The proposed rule would make it an abusive and unfair practice for a lender to make a covered short-term or longer-term loan without determining upfront that the consumer will have the ability to repay the loan, in what the Bureau calls the “full-payment test.” The requirements outlined in this test are extremely complex and prescriptive, and inconsistent with how credit unions that know their members typically underwrite a loan as small as $200. As an alternative to this “full-payment test” or ability to repay analysis, the proposed rule offers as a solution two alternatives. One, which was already discussed, is mirrored after the NCUA PAL program, and the second is based on maintaining a default rate of below 5 percent. This second exemption, called the “Portfolio Approach,” mandates an underwriting method designed to result in a default rate that will be less than or equal to 5 percent per year, among many other complex conditional requirements. Credit unions that provide small dollar credit alternatives have stated that these riskier loans often have default rates much closer to 10 percent or above. Accordingly, this limitation alone, notwithstanding all of the other complexities of the exemptions, would eliminate this exemption alternative for many credit unions. Furthermore, as you know the NCUA is vigilant in its rules and examination process to closely monitor delinquency ratios in credit unions as a matter of safety and soundness. This diligent oversight is virtually ignored by the Bureau in this rulemaking.

The significant point is that credit union loans do not fit into one specific category subject to a lengthy list of requirements. This is one reason credit unions have already expressed concerns to the NCUA that the PAL program should be more flexible.[1] The Bureau's proposed rule, however, is a step in the opposite direction and will actually make it more difficult to offer PAL or similar loans. Credit union programs that are extremely consumer friendly, and unquestionably a member's best option, could be eliminated because of these onerous rules.

It is perplexing to us that the Bureau would claim it does not want to disrupt credit union lending to this market and then propose a rule that makes it considerably more difficult to serve this market.

The Overly Broad Scope of the Rule Will Likely Sweep in Other Products Consumers Need and Want

Another initial concern we have about the overly broad scope of the rule is that it sweeps in products and services offered by credit unions that are not even similar to a payday or small dollar loan. For example, the Bureau has stated that auto refinance loans are included in the proposed rule if they exceed a rate of 36 percent when other products are included with the loan. As you know, in most circumstances when consumers are refinancing auto loans at a credit union, they are getting a more consumer friendly and favorable interest rate then what they had originally. Making it more difficult to offer these refinanced auto loans would essentially be making it harder for consumers to get an improved interest rate on an auto loan. It is hard to see how this is beneficial to consumers, and even harder to explain why this requirement is found in a rule that should be focused on predatory practices in the payday lending market.

Moreover, the research supporting this proposed rule focuses primarily on online and storefront payday and title lenders, and deposit advance products. Since little, if any, of this research focused on credit union products, is not clear to us why the Bureau believes credit union members need more consumer protection from the consumer friendly products offered by the credit unions they own. In our estimation, there is no evidence of a pattern of harm to credit union members using credit union products and services. In the alternative, credit union members see credit unions as a lifeline and the safest and best solution when in difficult financial situations.

[1] CUNA Comment Letter to NCUA regarding payday loan alternative loans, http://www.cuna.org/Legislative-And-Regulatory-Advocacy/Track-Regulatory-Issues/Comment-Letters/Archive---2012-Comment-Letters/#NCUA (Nov. 26, 2013).

Consumers Will Lose Access to Credit Under the Proposed Rule

We urge the NCUA to carefully consider how this proposed rule could harm credit union members and make it difficult for credit unions to serve as the solution for consumers. As the Bureau has acknowledged, credit unions are one of the best options for consumers in need of this type of credit. If credit unions and other depository institutions are regulated out of this market, we are very concerned about the options credit union members will be left with, which could include unregulated and unlicensed predatory lenders.

It is pertinent that the NCUA act on behalf of federally-insured credit unions to ensure that this proposal does not adversely impact credit union members' ability to get safe and affordable short term, small dollar loans from their credit unions. We hope you will encourage the Bureau to produce a final rule that excludes credit unions.

Thank you for your attention to these important concerns.

Sincerely,

Jim Nussle
President & CEO

Attachment

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Attachment

CUNA STAFF ANALYSIS OF CFPB CHANGES TO THE NCUA PAL PROGRAM

- A covered longer-term loan that is made under the exemption for PAL loans under the rule must satisfy the following conditions:

  1) The loan is not structured as open-end credit;
  2) The loan has a term of not more than six months;
  3) The principal of the loan is not less than $200 and not more than $1,000;
  4) The loan is repayable in two or more payments due no less frequently than monthly, all of which payments are substantially equal in amount and fall due in substantially equal intervals;
  5) The loan amortizes completely during the term of the loan and the payment schedule provides for the credit union allocating a consumer's payments to the outstanding principal and interest and fees as they accrue only by applying a fixed periodic rate of interest to the outstanding balance of the unpaid loan principal every repayment period for the term of the loan;
  6) And, has the same interest rate as the PAL loan of no more than 28 percent allowing a $20 application fee.

- **Underwriting**

  - The credit union must maintain and comply with policies and procedures for documenting proof of recurring income – this can be done by obtaining two recent paycheck stubs or other procedure for documenting recurring income that satisfies the lender's own underwriting obligations.
  - Credit union must assume that the consumer will utilize the full amount of credit as soon as it is available.
  - Specific to lines of credit – the credit union must not permit a consumer to obtain an advance under the line of credit more than 180 days after the initial ability to repay determination. After 180 days there would have to be a new assessment of the ability to repay.
  - May not make a covered loan subject to the ability-to-repay determination if the consumer has a covered short-term loan made under the conditional exemption.
  - Must determine that affiliates have not also offered loans under this section, so that there are not more than three outstanding loans within a period of 180 days. This will require pulling a credit report or using the new tracking system under the rule.

- **Collection**

    - Credit unions may not impose a prepayment penalty; or
    - If the credit union holds funds on deposit in the consumer's name, in response to an actual or expected delinquency or default on the loan: sweep the account to a negative balance, or exercise a right of set-off to collect on the loan, including placing a hold on funds in the consumer's account, or close the account.

- **Reporting**

    - Must report the loan in the next regularly scheduled furnishing, or within 30 days, to a nationwide consumer reporting agency or to the information systems for tracking covered loans registered in accordance with the new rule.

How are these requirements different from NCUA PAL loans?

- The NCUA PAL loan minimum length is 30 days, the proposed rule has a minimum of 45 days.
- Under the PAL program, credit unions may make only one loan at a time to a member and no more than three loans in any rolling six-month period. Under the proposed rule, the credit union would additionally have to check with a credit reporting agency or the new tracking system to see what other loans borrowers have. Under the proposed rule, credit unions could only make three outstanding loans, including the loans of <u>its affiliates,</u> within a period of 180 days. So, if borrower has other outstanding loans, the credit union cannot offer the 6 PAL loans allowed under the NCUA program.
- PAL loans do not require specific debt collection requirements. The proposed rule provides some exemptions for collection of loans made under this section, but also adds that credit unions cannot exercise the right to set-off to collect from a consumer's deposit account.
- PAL loans must be fully amortized and must be underwritten. However, the NCUA does not set underwriting standards. It also does not require as specific amortization requirements as found in the Bureau's rule.
- The proposed rule includes specific requirements for lines of credit.
- The proposed rule includes new requirements for reporting to credit reporting agencies or the new tracking system.