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National Association of Federally-Insured Credit Unions

March 31, 2023

Comment Intake— Nonbank Registration
of Certain Agency and Court Orders,
c/o Legal Division Docket Manager
1700 G Street NW
Washington, DC 20552

RE: Request for Comment on Nonbank Registration of Certain Agency and Court Orders (Docket No. CFPB-2022-0024)

Dear Sir or Madam:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing in response to the request for comment (RFC) issued by the Consumer Financial Protection Bureau (CFPB or Bureau) regarding its proposed rule to require certain nonbank covered person entities that are under certain final public orders obtained or issued by a Federal, State, or local agency in connection with the offering or provision of a consumer financial product or service to report the existence of such orders to a Bureau registry. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 134 million consumers with personal and small business financial service products. NAFCU appreciates the Bureau's efforts to provide transparency to consumers and credit unions regarding the risk that some nonbank entities pose and to monitor repeat offenders and bad actors more comprehensively. NAFCU supports the Bureau's proposal to make these orders public and hold covered entities accountable through annual attestations of compliance. However, the Bureau can and should do more to regularly supervise these underregulated market players, both through its risk-based supervisory authority and its "larger participant" authority.

General Comments

NAFCU agrees with the Bureau's assertion that there are a significant number of nonbank providers of consumer financial products and services that lack consistent monitoring by any federal regulator. The Bureau estimates that there are approximately 155,043 covered nonbank entities currently in operation, and although the vast majority of these entities may be compliant with federal, state, and local consumer financial protection laws, those that are noncompliant, and even those that are repeat offenders, often lack any meaningful oversight from federal regulators and are capable of inflicting serious harm.[1] The creation of a central repository that catalogs entities which have violated consumer financial protection laws would represent a meaningful first step toward uncovering the extent of nonbank malfeasance and provide

[1] 88 Fed. Reg. 6088 (Jan. 30, 2023).

consumers and regulated financial institutions such as credit unions with a much-needed baseline of confidence and transparency as they interact with these entities. Although NAFCU appreciates the potential of the proposed registry to bring the extent of nonbank noncompliance to light, the Bureau must do more to address the indisputable truth, that for unsupervised and underregulated fintechs to offer the same consumer financial products and services as well regulated and supervised financial institutions creates an unlevel playing field and puts consumers at risk. The Bureau, in recognition of its mandate to protect consumers, should feel obligated to supervise those fintechs that represent a risk to consumers or that represent a larger participant in their market.

Risks of Nonbank Entities and Fintechs

Although the proposed registry would have broad applicability to nonbank covered persons, the majority of nonbank persons engaged in the provisions of consumer financial products and services could accurately be categorized as fintech companies, that is, non-chartered, nonbank institutions that reach consumers through digital channels. For many years, credit unions have partnered with fintech companies to improve operations, deliver new products and services, and enhance member experiences. NAFCU advocates for a regulatory environment that promotes competition and responsible innovation; however, the risk of arbitrage remains a concern as fintech companies continue to operate on the periphery of traditional supervisory domains. The addition of this registry has the potential to capture the conduct of those fintechs and nonbanks that lack supervision, and in cases in which they demonstrate inability or unwillingness to comply with consumer financial protection laws, to help identify entities that should be brought under federal supervision.

The growth of fintech market share and the adoption of fintech products and services by consumers has been explosive. In 2019, 64 percent of consumers worldwide had used one or more fintech platforms, up from 33 percent in 2017.[2] In terms of lending, nearly half of all personal loans in the U.S. are originated by fintechs, up from 22 percent in 2015, as estimated by the Consumer Bankers Association. The five leading providers of buy-now-pay-later (BNPL) installment loans, are all fintechs. Use of fintechs by consumers is even more prevalent for payments, with 71 percent of consumers indicating that they leverage the services of fintech companies such as PayPal or Venmo for payments.[3] Finally, digital banking, the largest segment within the fintech space has grown steadily in adoption year-over-year from 61.3 percent in 2018 to 65.3 percent in 2022.[4] Without question, fintechs have become major players in the consumer finance market and could easily be categorized as "larger participants." While NAFCU continues

[2] Ernst & Young, "Global FinTech Adoption Index 2019" *available at* https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/banking-and-capital-markets/ey-global-fintech-adoption-index.pdf.
[3] MX Technologies, "COVID-19's Impact on the Fintech Landscape" (July 14, 2020) *available at* https://www.mx.com/infographics/fintech-landscape-amid-covid-19/.
[4] Exploding Topics, "Fintech Market Size & Future Growth (2023-2027)" (January 3, 2023) *available at* https://explodingtopics.com/blog/fintech-market.

to encourage the Bureau to utilize its "larger participant authority" over nonbank providers of consumer financial products or services,[5] the Bureau should also exercise its risk-based supervisory authority under Section 1024(a)(1)(C) of the *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* (Dodd-Frank Act). The creation of the proposed registry should be used, among other indicators, by the Bureau to inform its decision-making regarding which entities to place under its risk-based supervisory authority.

NAFCU encourages all relevant regulators to ensure that when fintechs compete with traditional financial institutions, they do so on a level playing field where smart regulations and consumer protections apply to all actors in the consumer marketplace. Regulations and laws have evolved in a piecemeal fashion as both traditional and non-traditional financial institutions transition to a world of faster payments, alternative data, and machine learning. While most fintech products and services already fit within the existing scope of federal consumer financial law, which addresses the core banking activities of lending, payments, and deposit taking, significant supervisory gaps exist that fail to address certain fintech business models—particularly those that raise consumer compliance risks. Nonbank lenders are not subject to the same safety and soundness regulations as banks and credit unions. This disparity poses serious, systemic risks given the growing market share that these firms represent and could have carry-on effects that impact consumers directly. This is especially concerning in the mortgage lending market, with nonbank mortgage lenders originating 68.1 percent of all mortgages originated in 2020, a staggering jump in market share from 2009, when nonbank mortgage lenders originated only 8.9 percent of all mortgages.[6] In 2016, when the market share of nonbank mortgage lenders was a mere 24.2 percent, the Government Accountability Office (GAO) rightly raised the alarm over the lack of a safety and soundness regulator for these lenders and called for them to be supervised and examined by the Federal Housing Finance Agency (FHFA). "GAO has previously determined that a regulatory system should ensure that similar risks and services are subject to consistent regulation and that a regulator should have sufficient authority to carry out its mission."[7] Now, seven years later and with nonbank mortgage lenders representing more than two-thirds of the market for originations, the risks to the system have been dramatically increased and federal regulators have failed to step in. With the clarity afforded to the Bureau by the proposed registry, it should move quickly and proactively to begin supervising and examining fintechs, and especially fintech lenders, to protect consumers and the system as a whole.

Also in the lending space, fintechs, displaying their capacity to adapt, have begun to offer financial products and services such as BNPL that fall outside the scope of some consumer protection laws. The failure of the firms offering these products to adhere to consumer protection laws and traditional financial institution norms raises concerns over data protection, lack of disclosures

[5] 12 U.S.C. 5514(a)(1)(B).
[6] Wall Street Journal, "Nonbank Lenders Are Dominating the Mortgage Market" (June 22, 2021) *available at* https://www.wsj.com/articles/nonbank-lenders-are-dominating-the-mortgage-market-11624367460.
[7] US Government Accountability Office, "Nonbank Mortgage Servicers – Existing Regulatory Oversight Could be Strengthened" (March, 2016) *available at* gao.gov/assets/gao-16-278.pdf.

and dispute resolution protections as well as late fees and policies that expose consumers to greater risk of financial harm. More specifically, the absence of standardized disclosures in BNPL fintech lending combined with misleading marketing creates concerning potential for hidden fees and expenses. Firms that offer these types of products would seem to be engaging in the exact type of conduct that poses risks to consumers, as described in Section 1024(a)(1)(C), and could benefit from supervision. In cases where these risks rise to the level of violations of consumer financial protection laws, the proposed registry will help to compile and track violations and provide a basis from which to initiate risk-based supervision.

For traditional financial institutions such as credit unions, these risks are particularly troubling, and have a real-world impact for credit unions that must deal with the fallout from their members being harmed by the insufficient regulatory framework for fintechs. Furthermore, when credit unions partner with third-parties such as fintechs, they expose themselves to the risk of malfeasance by those third-parties. This tool could help to mitigate those risks and assist credit unions in conducting due diligence prior to entering into a third-party relationship. The Bureau's creation of a registry to better understand the scope and nature of nonbank covered persons, and in particular fintechs, will allow increased transparency for all parties and aid the Bureau in exercising its supervisory authority over entities that pose risks to consumers.

Incentive for Compliance

Although the vast majority of financial services providers, whether traditional or not, operate conscientiously and work hard to avoid violations of consumer financial protection law, there are a variety of reasons that entities do not or cannot comply. First and foremost is the cost of compliance, with the ever-growing number of consumer financial protection laws and regulations making compliance burdensome for even the largest financial institutions. As nonbank entities offer new products and services, they must establish and maintain appropriate compliance mechanisms, which include developing compliance processes and training and retaining compliance staff, and with each additional product or service, new laws and regulations come into play, increasing the cost and complexity of the endeavor. Nor are the laws and regulations static, they change constantly and require vigilance to ensure that the organization stays abreast of new developments. For newer nonbank entities such as fintechs, this burden may be overwhelming and staff may lack the expertise to ensure compliance or lack the experience to understand that their compliance program is inadequate. As a threshold matter, many of tech-first companies also struggle to recruit and retain staff necessary to implement the appropriate consumer financial protection knowledge and experience to build a comprehensive compliance management system. When faced with these tremendous costs and practical difficulties, some nonbank entities may choose to invest less in their compliance program. The fact that these entities are largely unsupervised by federal financial regulators may make an inadequate focus on compliance appear to be a relatively low-risk strategy.

The proposed registry would provide the much-needed disincentive of a stick in the "carrot and stick" metaphor. Nonbank entities that, all else being equal, might consider skimping on their compliance programs would be much more likely to focus on consumer financial protection with the knowledge that any violations thereof would be compiled in a public registry. Although these violations are already public, violating entities may view the prospect of a centralized repository as having greater visibility to consumers and therefore greater potential to damage the reputation of the entity among consumers. Additionally, beyond reputational risk, as the Bureau monitors activity in the market to determine which entities to subject to its risk-based supervisory authority, violating entities that repeatedly appear on the registry will likely increase compliance to avoid Bureau supervision. Finally, for those entities that have committed violations, the registry could serve as a motivating force for future compliance and ensure that efforts to comply with orders are not forgotten or lacking priority within the organization.

NAFCU supports the creation of the proposed registry but agrees with the sunset provisions of the proposal to create "an outer limit on the time period during which the existence of a covered order would subject a registered entity to the requirements" of the proposed registry.[8] If the purpose of the proposed registry is, as stated, monitoring risks to consumers and reducing corporate recidivism, the Bureau should provide the ability for entities to rehabilitate their compliance with consumer financial protection laws and remove themselves from the registry.

Benefits of Transparency

The creation of a registry for entities subject to orders for violations of consumer financial protection laws would represent a beneficial movement toward transparency into the conduct of nonbank covered persons and fintechs, with a number of positive impacts. The registry would provide traditional financial institutions such as credit unions with a central repository of information regarding the conduct of nonbank covered persons, allowing credit unions to engage in more informed decision-making when deciding whether to partner with these entities. This benefit would also extend to all financial institutions by providing them with more, clear examples of the types of acts and practices that constitute violations of consumer financial protection laws. Finally, the proposed registry would benefit consumers by making public orders centrally located, thereby providing consumers with more information on which to base their choice as they shop for financial products and services.

Credit unions would benefit from a clearer picture of the nonbank landscape when determining whether to partner with a third party. To remain competitive and provide exceptional service to their members, virtually all credit unions rely to some extent on partnerships to improve operations, deliver new products and services, and enhance member experiences. Unfortunately, just as with the search for any product or service, the marketplace is extensive, and reliable data on the quality of third-party offerings is often hard to come by. Many credit unions report entering into relationships with third parties only to find out after the fact that the

[8] 88 Fed. Reg. 6088 (Jan. 30, 2023).

product or service is not of the expected quality, that costs are much higher than expected, and that due to contractual obligations, ending the relationship can be difficult or costly.[9] Furthermore, in the event that a service provider violates consumer financial protection laws, consumers will often hold their traditional financial institution responsible, leaving the financial institution with a breach of contract claim against the service provider as their only recourse. Finally, the credit union industry, which includes institutions of many sizes, including many smaller institutions, is often overlooked by third-party service providers and may deal with providers refusing to work with institutions below a certain asset size or being more responsive to big banks. Although the proposed registry would not catalog the quality of service, it would provide value to credit unions by ensuring a baseline level of consumer protection compliance from prospective partners and narrowing the seemingly endless field of nonbank financial service providers.

As credit unions and other traditional financial institutions evolve with the times and begin to offer new products and services, the body of precedent provided by the registry would also help to guide credit unions in the decision to adopt new models or enter new spaces. For example, the use of alternative data has attracted scrutiny as potentially problematic. The use of non-traditional indicators of borrower creditworthiness offers an avenue for improving access to credit for credit invisible consumers and credit unions value opportunities to help their members build their credit and obtain the financial assistance they need. However, without further clarity, the use of such data may present potential fair lending violations. Similarly, the proliferation of BNPL, while attractive to consumers and financial institutions alike, may conflict with consumer protections laws and regulations.

Additionally, the formal rulemaking process used by federal financial regulators often lags the pace of technological evolution in the financial sector. As a result, the Bureau's approach to fintechs may exhibit the limitations of reactionary policy, failing to account for new products and services such as decentralized finance platforms offering products that evade easy regulatory classification.[10] The steady, consistent accumulation of data regarding violations of consumer financial protection law would better inform the market and better protect consumers.

Future Applicability to Traditional Financial Institutions

As noted in the proposed rule, the Bureau would not include insured depository institutions, credit unions, or related persons in the proposed registry. The Bureau's reasoning behind this decision is sound; credit unions are a known commodity, with comprehensive supervision, examination, and reporting requirements. Federal credit unions (FCUs) are regulated by the

[9] Credit Union Advisory Council Meeting, November 3, 2022.
[10] *See* President's Working Group Report on Stablecoins (November 2021) ("Despite some asserted distinctions from more traditional or centralized financial products, services, and activities, DeFi arrangements often offer the same or similar products, services, and activities, and raise similar investor and consumer protection, market integrity, and policy concerns.")

National Credit Union Administration (NCUA), which regularly publishes orders related to violations of consumer financial protection laws. Consumers seeking information on the characteristics of a credit union or the credit union's track record of compliance with consumer financial protection laws need only look to the NCUA to find an answer. Furthermore, federally-insured state-chartered credit unions (FISCUs) are subject to rigorous supervision and examination - far beyond that of fintechs regulated by state supervisory authorities. Finally, credit unions over $10 billion in assets are already subject to examination by the Bureau for compliance with consumer financial protection laws. Credit unions are closely regulated and examined and they do not suffer from the opacity and lack of supervision found in the nonbanks subject to the proposed registry.

Although NAFCU supports the exclusion of credit unions from the proposed rule, it strongly objects to the Bureau's indication that it "might at some point consider collecting or publishing the information described in the proposal" from credit unions.[11] The stated purposes of the proposed rule are, "assessing compliance with the requirements of Federal consumer financial law"; "obtaining information about the activities and compliance systems or procedures of such person[s]"; and "detecting and assessing risks to consumers and to markets for consumer financial products and services."[12] These are reasonable objectives when directed at the shrouded market of nonbank covered persons, but lack any discernible function when applied to the transparent and well-regulated credit union industry. All of these objectives are currently carried out by the NCUA, and for credit unions over $10 billion in assets, by the Bureau, and to require this additional level of reporting from credit unions would be burdensome, duplicative, and wholly unnecessary.

Furthermore, credit unions service organizations (CUSOs) should be exempt from the registry, as they are good-faith actors with a track record of compliance with consumer financial protection laws. Through its supervision of credit unions, the NCUA is already able to obtain information about CUSOs— which are, at least in part, owned by regulated, supervised credit unions. Including CUSOs in the proposed registry would be, just as it would with credit unions, duplicative and burdensome. Additionally, the rule as proposed would provide little utility to consumers if CUSOs were subject to the rule's reporting requirements. CUSOs provide services to credit unions by providing for example, lending support services, IT services and compliance services. Consumers that are concerned about a service received through their credit union are much more likely to contact the credit union or the NCUA than they would be to search for the name of the individual service provider and then search the Bureau's registry for instances of consumer financial protection violations. The one certain impact that would come from CUSOs inclusion in the proposed registry is increased costs for CUSOs, which would mean increased costs for credit unions. This would tax the resources of institutions that are already threatened by extraordinarily thin margins, undermining their ability to offer affordable, core deposit products like free

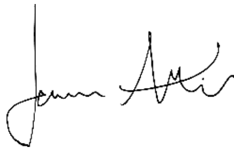
[11] 88 Fed. Reg. 6088 (Jan. 30, 2023).
[12] Id.; 12 U.S.C. 5514(b)(1)

checking, damaging their ability to compete in an era where virtually all operational costs are rising, and eroding their ability to serve underserved communities.

Conclusion

NAFCU appreciates the opportunity to provide comments on this proposed rule. NAFCU supports the Bureau's decision to require certain non-banks to register with the agency when they become subject to a public written order or judgment imposing obligations based on violations of certain consumer protection laws. NAFCU also supports the creation of a public online registry of those nonbanks subject to agency or court orders, to "limit the harms from repeat offenders." Finally, the Bureau should exercise its risk-based and larger participant authorities over entities that are unwilling or unable to comply with consumer financial protection laws. If we can answer any questions or provide you with additional information, please do not hesitate to contact me at 703-615-5109 or jakin@nafcu.org.

Sincerely,



James Akin
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