



## National Credit Union Administration

Office of the Chairman

October 12, 2007

**VIA FACSIMILE to (202) 452-3819  
and U.S. MAIL**

Jennifer J. Johnson, Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue, N.W.  
Washington, DC 20551

Re: Docket No. R-1286.

Dear Ms. Johnson:

On behalf of the National Credit Union Administration (NCUA), we are taking the opportunity to provide comments in response to a request for comment by the Board of Governors of the Federal Reserve System (Federal Reserve) on proposed changes to the open-end credit rules in Regulation Z. This comment letter addresses proposed changes in Regulation Z Official Staff Commentary on multi-featured open-end plans.

NCUA, an independent federal agency within the executive branch, is the chartering authority for federal credit unions and provides federal account insurance to all federal credit unions as well as state-chartered credit unions upon application. As such, NCUA is the federal regulator for approximately 8,200 federally-insured credit unions (FICUs). NCUA's mission is to ensure safety and soundness as well as compliance with applicable federal regulations. While NCUA has enforcement authority for Regulation Z only for federally chartered credit unions, the potential impact of proposed changes in the rule on all FICUs informs our comments given NCUA's role as the federal account insurer for credit unions.

In the financial services industry, credit unions are individually, on average, smaller than other financial institutions, and changes in regulatory requirements, particularly those requiring retooling of procedures and processes, can have a greater cost for them as compared to other financial institutions. The average FICU is small compared to other types of financial institutions: 85% of all FICUs have assets under \$100 million and about half of those under \$100 million have less than \$10 million in assets. NCUA is concerned that changes the Federal Reserve is proposing to make affecting multi-featured open-end plans could place a substantial burden on a significant number of credit unions.

Many credit unions use multi-featured, open-end plans as a lending option and members find them to be a flexible, timely, and efficient way to obtain financing. The plans enable members to qualify for several loan products with a single, one-time loan application. Members receive all of the required Regulation Z disclosures, including initial disclosures, periodic statements, and change-in-terms notices, regardless of whether the member actually takes an advance for a particular product. Thus, while each advance or sub-account does not require a new application, consistent with current Regulation Z commentary, 12 C.F.R. Part 226, Supp. 1, 2(a)(20)5, a credit union generally will verify the member's credit information if a member activates a previously unused feature of the plan. NCUA's experience regulating credit unions with these plans reveals no problems that appear to be generated by or inherent to the multi-featured aspect of these plans. NCUA performs risk-focused examinations and supervision as part of its statutory enforcement and oversight responsibilities. Examiners utilize questionnaires in the agency's Automated Integrated Regulatory Examination Software program to guide and document reviews, including federal credit union compliance with Regulation Z.

*Disclosures Under Regulation Z.*

The Federal Reserve has proposed numerous changes to the general Regulation Z disclosures that also would apply to multi-featured open-end plans. The proposed changes do not identify any specific, disclosure problems unique to multi-featured open-end plans and NCUA wants to highlight that it is unaware of any specific disclosure problems through its supervision of credit unions related to closed-end features that are part of a multi-featured open-end plan. Given that the cornerstone for consumer protection is disclosure, NCUA believes that requiring additional disclosures in connection with a "closed-end feature" could be appropriate and accommodate the Federal Reserve's concern -- without displacing a product that has proved beneficial to a small but significant segment of the financial services landscape available to consumers.

NCUA respectfully encourages the Federal Reserve to carefully consider the significant detriment to credit unions and their members if they could no longer benefit from the convenience and efficiencies of including a so-called closed end feature in multi-featured open-end plans. As a typical example, the closed end feature permits a credit union member to use the plan to finance an auto purchase. Under a multi-featured open-end plan, a member can contact his or her credit union and obtain approval, even while at the dealership, and obtain funding for an auto loan within minutes. If credit unions cannot process the auto loan under the multi-featured plan, members may be persuaded to agree to financing through the auto dealership. A member's ability to obtain financing quickly from his or her credit union enhances a member's ability to negotiate with an auto dealership, obtain optimal pricing on the auto and the loan, and timely complete the purchase.

In addition, NCUA believes the Federal Reserve should not ignore the identity of the creditor in considering the appropriateness of disclosures because doing so ignores the reality of the circumstances in which disclosures are made. Multi-featured open-end plans in credit unions involve circumstances where there is an ongoing relationship between the consumer-member and a regulated financial institution, usually involving various depository account and other credit relationships at the credit union. These circumstances are different in important and meaningful ways for a consumer-member as compared to a single, closed-end transaction with a creditor with which a consumer may have no prior or continuing financial relationship, such as an auto dealership.

*The Proposed Changes: Self Replenishment & Separate Underwriting.*

The Federal Reserve's proposed changes to the Commentary, if adopted without change, would narrow the types of products available to credit union members under a multi-featured open-end plan. The proposed changes appear to require that each sub-account meet a self-replenishment criterion to continue to qualify as open-end credit, meaning funds must be made available to the consumer as a loan balance is paid down in that sub-account.

The proposal uses an auto loan example to illustrate its point: if the consumer makes two, \$500 payments, the proposal states \$1,000 should be available for the consumer's use. The example indicates credit limits must be established for the overall plan and the sub-account, a requirement that currently does not exist. However, the example fails to consider that the sub-account is secured by an auto, which is, of course, depreciating collateral.

To permit or require "replenishment," i.e., continued draws for this sub-account, against specific, depreciating collateral, would negatively alter the plan's overall risk exposure. Replenishment does occur in these plans, however, by allowing a member to take another advance secured by different collateral and this approach supports the risk posture of the overall plan. NCUA encourages the Federal Reserve to view the replenishment criterion as met in multi-featured open-credit plans where another advance is permitted, for example with different collateral, based on the overall limit of the plan.

The proposed change shifts the focus from the conduct and operation of an overall plan and, instead, focuses on each, specific, loan product --or sub-account-- covered by a plan. NCUA believes the current focus on whether the conduct and operation of an overall plan are consistent with the characteristics of open-end credit is the appropriate approach and not whether a particular sub-account, if offered independently, would be considered an open-end or closed-end product. The current approach is similar to that applied to home-equity plans where the focus is

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not on how the consumer uses advances under the plan but on proper disclosures to the consumer regarding how the plan works.

The impact of the proposed changes are considerable for credit unions offering these plans and would require wholesale system changes, including changes in information technology and marketing materials. Most significantly, there would be a negative impact on the convenience and efficiencies these plans provide to credit unions, and, thereby, their ability to offer competitive pricing and efficiency to their members. The benefit to members as consumers from this proposed change is not clearly discernible.

A primary issue discussed in the preamble to the proposal is the Federal Reserve's concern that a sub-account is separately evaluated and this concern exists whether the sub-account being activated is an overdraft line of credit or an auto loan under a multi-featured open-end plan. As noted in the preamble, however, the Truth in Lending Act contemplates that creditors can verify credit information from time to time in open-end credit plans without being deemed closed-end credit. 15 U.S.C. §1602(i).

NCUA agrees with the Federal Reserve that this provision, however, is not intended to permit creditors to separately underwrite and require separate applications for each sub-account in a multi-featured open-end plan. As noted above, the convenience of the multi-featured plans in credit unions is that members can qualify for several loan products with a single, one-time loan application. Credit unions do not require a separate application to activate a sub-account but, given the passage of time between initial application and subsequent activation of a sub-account, credit unions should be able, as noted as appropriate in the preamble, to verify that the member's creditworthiness has not deteriorated. NCUA encourages the Federal Reserve to focus any changes in the commentary to Regulation Z on the distinctions between a credit verification versus a credit evaluation as a more appropriate and less burdensome response to its concerns.

If Federal Reserve staff believes it would be helpful to consult or obtain further information regarding multi-featured open-end plans in credit unions, we hope you will free to call on Sheila Albin, Associate General Counsel, or Linda Dent, Staff Attorney, in the NCUA's Office of the General Counsel, (703) 518-6540.

Sincerely,



JoAnn M. Johnson  
Chairman