Special Report: CUSOs

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How to Start a CUSO

5 steps from planning to
ongoing operational success

PLUS:

How to *Start a CUSO*

5 STEPS FROM PLANNING TO ONGOING OPERATIONAL SUCCESS

BY KAREN BANKSTON

Maybe your credit union is considering forming a wholly owned CUSO to provide insurance or investment services to members, or maybe you're looking to partner with other CUs to rein in operating expenses or collaborate on new technology.

Either way, Guy Messick, general counsel with the National Association of Credit Union Service Organizations (*nacuso.org*) and attorney with Messick Lauer & Smith (*cusolaw.com*), Media, Pa., has guided the formation of many credit union service organizations. He offers these five steps from conception through continual improvements to keep CUSOs running smoothly and on target.

1 Identify the problem or opportunity. What goals does your CU hope to achieve? For wholly owned insurance or investment CUSOs, for example, the primary goals are typically to provide an alternative revenue source for the CU and a full range of financial services for members. Many multiple-owner CUSOs are organized with a primary goal of trimming operating expenses or sharing the costs of developing expertise that is only available to financial institutions of a certain scale. As an example of the latter, CUSOs focused on new technology and business intelligence solutions are on the rise, Messick notes. Two key questions to consider in early planning stages are:

• **In what areas are you willing to collaborate?** Many CEOs rope off member-facing functions as off-limits to collaboration because they are central to brand and market differentiation. On the other hand, they are open to opportunities to work with other CUs to streamline back-office functions and reduce costs.

• **Are there existing CUSOs you can join or learn from to accomplish your aim?** Joining a CUSO that has a track record in solving the problem you've identified may be a cost-effective alternative to starting from scratch. Even if you don't find a close match, consulting with existing CUSOs and their CU owners can still provide useful information on your next moves. NACUSO also offers advice to CUs considering a CUSO launch and is looking to formalize that support, Messick says.

2 Develop your business plan. Where will the necessary resources, in terms of finances and expertise, come from? In some cases, the CUs forming a CUSO may be able to tap into the competencies on their executive and management teams, at least to get the new venture up and running. But it may be necessary to hire professionals with specific expertise or contract with third parties to provide that know-how.

On the financial front, CUSO partners need to identify how to divvy up expenses and income. "How will the CUSO share revenue, and just as importantly, how will you cover initial losses?" Messick asks. "Every business plan must account for a start-up period until a new venture breaks even. The business plan will identify how much capital will be needed before the CUSO is self-sustaining."

3 Agree on a structure. A basic decision is what sort of business entity to form. Most CUSOs are structured as limited liability companies, he notes. Beyond that issue, owner credit unions must agree on leadership, governance and scope of operations:

• **Who will manage operations?** In the case of a wholly owned CUSO, a CU executive may take on those duties. When multiple credit unions are planning to launch a CUSO, they will likely need to work together to hire a CEO to lead the venture. "If you envision a significant operation, you'll need to find someone with the expertise to lead the organization so the owners on the CUSO board don't need to micromanage," Messick advises.

• **How will management and sharing rights be handled?** In the case of multiple-owner CUSOs, typically the CEO or another senior executive represents each owner CU on the CUSO board. Another decision point is voting power: Some CUSOs are structured so that CUs contributing significantly more capital than other owners have more votes on the board. But others apply the "one member, one vote" standard of the cooperative movement. "When you have peer credit unions—that is, credit unions of similar size—collaborating in an operational CUSO with one credit union, one vote tends

RESOURCES

New 'Merger' Option: CU Holding Companies (*cues.org/0318newmerger*)

Magnifying Effectiveness (*cues.org/0917magnifying*)

CUES on CUSOs (*cues.org/cuesoncusos*)

Canadian CUs Think Big About Collaboration (*cues.org/bccusos*)

Compensating CUSO Directors (*cues.org/0916 compensating*) to be the best model," Messick suggests.

• **Who will the CUSO serve?** The customer base could be limited to members or owner CUs, or the venture could serve non-owner CUs and their members. Up to 49 percent of a CUSO's customer base can be persons who are not CU members and entities that are not credit unions.

One additional consideration at this stage is determining in advance how to handle the potential for the departure and addition of owner credit unions. "Keep in mind that all things are not permanent," Messick says. "How will you unwind ownership of a credit union that decides to step away or respond to credit unions that want to join as owners? If you need to buy out one or more owners, you might figure out how to do that over a number of years so that the CUSO is not strapped for cash."

4 **Launch.** At this stage, owner CUs implement all their carefully laid plans: filing the orders of incorporation, holding the first board meeting, funding operations, hiring staff, conducting RFPs and negotiating vendor agreements. If the plans call for CU staff to divide their time between their existing responsibilities and new roles with the CUSO, a system should be developed so that the new venture reimburses the owner CU(s) for staff time.

A high trust factor among CUSO owners is often cited as a key success factor, Messick says. CUSOs sometimes falter when there's a change in leadership at an owner credit union and the new CEO doesn't have the same commitment to CUSO collaboration that his/her predecessor did.

5 **Measure and adjust, where necessary, to stay on track.** "You're always making adjustments. Maybe things didn't go exactly as you planned, or partners have differing ideas. So many things go into the mix when you start up that you need to continually adjust," Messick says. "Go back regularly to that problem you were trying to solve. Many credit unions start CUSOs with a good idea of what they want to do and how they're going to do it, but they may need to make changes along the way to accomplish their original goal."

For example, "some CUSOs start out with the goal of reducing operating costs, but along the way, some board members may shift to a goal of wanting to make money over and above expense containment. There are big differences between pricing services to make money and aiming to contain costs. I've seen that tug of war end poorly."

Karen Bankston *is a long-time contributor to CU Management and writes about CUs, membership growth, marketing, operations and technology. She is the proprietor of Precision Prose, Eugene, Ore.*

Thinking Big *With CUSOs*

Chuck Fagan, president/CEO for CUES Supplier Member PSCU (*pscu.com*), St. Petersburg, Fla., appreciates the impact CUSOs have on their owners. "We can aggregate our services and talent and work closely with many partners across the financial services industry," he explains. "Take Apple; it doesn't want to work with 58,000 separate entities. But it is happy to collaborate with key partners like PSCU."

CUSO partnerships enable you to follow financial trends all over the world. "The U.S. financial services system is extremely complex," says Fagan. "As a CUSO, we are continually following world trends and applying those key learnings."

Most CUSOs invest heavily in research, innovation and fraud prevention. "We have to be good stewards of our owners' data by monitoring for fraud," notes Fagan. "And we have the absolute obligation to protect a CU's assets during the transaction process. When we see fraudulent activity occurring in one part of the country, as a CUSO, we can apply strategic initiatives to protect all our owner CUs."

Aligning with a CUSO enables you to stay connected and follow developments without missing a beat; for PSCU, it's about observing spending and payment trends. "We've seen a dramatic shift in consumer spending," reflects Fagan. PSCU owners saw a 9 percent increase in holiday credit card spend. Additionally, there was a $14 billion shift nationally from in-store to e-commerce during that time. "This indicates consumers are comfortable with the security of shopping with their cards, in-store, online and in the mobile space."

GROW LOANS EFFICIENTLY

Consider CUES Supplier member CU Direct (*cudirect.com*), Ontario, Calif. The company's AutoSMART car-buying website, along with CUDL, the nation's largest credit union auto lending platform, providing point-of-sale financing, have become a catalyst for car loan growth. Its lending network includes 1,100 CUs, 15,000 car dealers and a potential member base of 50 million nationwide.

"We're continually seeking new ways to meet consumer loan demand," says Tony Boutelle, the CUSO's CEO/president. He points to CU Direct's Innovation Lab, a place where CU leaders meet to explore trends, collaborate on opportunities and debate emerging products. One product on its radar is "Subscription Services," a form of high-end leasing, enabling buyers to drive a variety of vehicles—rotating up to 18 different vehicles annually—at one set payment.

"Product innovation is critical for us," adds Boutelle. "We review new products in a 12-month window, a 24-month window and innovations beyond three years. Staying abreast of emerging products, we analyze the risk and gauge if there is a way for CUs to participate."

Auto loans continue to be good for CUs says Boutelle—with more than 25 percent of all auto loans in the U.S. closed by credit unions.

CU Direct offers a turnkey loan process, including loan tools members can use via mobile and POS financing at more than 15,000 dealers. "The process covers everything, from loan approval to risk management, underwriting, form creation and contracts with dealers," says Boutelle. Also impacting operational efficiencies is the explosion of artificial intelligence, with much of the back-end work now completed by machine learning. "Still, the future is mobile," he adds, "and we're helping CUs connect with more members than ever with the mobile tools they desire."

INCREASE NET INCOME

Creating income for their member-owners is a priority for CUSOs, and Tampa-based Trellance (*trellance.com*) is no exception. "Our role is to increase credit card spend, along with interchange, finance revenue and fee income," says Bill Lehman, SVP/managed services. And regardless if balances roll over, increased spend is good for all CUs. The CUSO, a CUES Supplier member, considers itself "processor-agnostic," so any CU can tap into its portfolio management strength. "We assist with portfolio management along with consulting and education for CUs," says Lehman. "We're also here to share our most valuable asset—our people—who have a wealth of industry knowledge and insights."

Lehman believes it's essential to leverage your CUSO's experience relevant to the market. "As credit card growth increases, up nationally 5 percent since 2016, it's important for credit unions to tap into our experiences, and the positive trends in spending and consumer confidence."

Watching transaction data enables CUs to tailor their products and services to consumer spending habits, adds Lehman. Here, targeted programs can support or stimulate spending and increase consumer confidence in your program.

He also sees a lot of CUs that "spray and pray" with their card marketing, which is both expensive and ineffective. "CUs can tap into our Card Portfolio Growth Solutions, a 12-month card growth plan offering segmentation and targeted communications. Participating CUs have seen an average of 14 percent revenue growth year-over-year when comparing 2017 to 2016."

Lehman also implores CUs to consider card loyalty programs. "For example, on credit and debit cards, there is an active market that expects rich rewards on card transactions. As rewards programs gain traction, consumer confidence and demand increase, making it even more imperative for CUs to compete."

Ultimately, the benefit of working with any CUSO is relying on its strengths, with the ability to think big and take advantage of an increased level of intimacy.

Stephanie Schwenn Sebring *established and managed the marketing departments for three CUs before launching her business, Fab Prose & Professional Writing. Follow her on Twitter@fabprose.*

It's a Fierce Job Market—Is Your CU Keeping Up?

Your credit union's future depends on its leaders, and competitive compensation is key to hiring and retaining the best talent.

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CUES
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Creating the CUSO *of Tomorrow Today*

CREATING AN UNPARALLELED MEMBER EXPERIENCE

BY PSCU

For more than 40 years, PSCU, as a credit union service organization, has delivered an exceptional and memorable service experience at every CU and member touchpoint. Targeted investments in payments solutions, risk management, analytics, loyalty programs, marketing, consulting, mobile platforms and call center support give all our owners a competitive edge. PSCU is proud to serve our industry and celebrates credit unions.

Our Venture. Your Gain.

But the times, they are a-changin'— and dramatically so. With digital disruption raising the bar on members' expectations and new competition emerging, CUSOs must reinvent themselves as agile, visionary, innovative venture partners to help CUs meet the challenges head on. That is why everyone at PSCU is embracing the entrepreneurial mindset to create transformational products and pioneering solutions that CUs need.

Living Our Values

PSCU acts as an extension of a CU's own staff. Our access to industry-leading partners gives our owners the opportunity for early adoption of new payment technologies like EMV chip cards and the latest digital wallet offerings. The depth of resources within PSCU relieves owners of the burden of managing dozens of endpoints as well as providing access to services and expertise at far less cost than credit unions would incur by hiring individual experts.

Reinventing the CUSO

To truly support the CUs of tomorrow, CUSOs must continue to evolve. PSCU is on a quest to work hand-in-hand with our owners as venture partners to create the next generation of CUSO services that will ultimately benefit the entire CU industry. Five areas of focus include:

1. Tomorrow's digital solutions: Digital transformation is revolutionizing every part of CU operations at warp speed, spanning mobile payments technology, voice search, chatbots, the internet of things and artificial intelligence. PSCU is leveraging its technology leadership to develop vendor partnerships that provide access to emerging technology while managing risk.

2. Entrepreneurial employees: As digital transformation expands product delivery options, it is changing the definition of what a product is. That is why PSCU is embracing the "minimum viable product" concept and adopting the agile development team approach. By sponsoring team development contests, PSCU is creating an entrepreneurial culture that delivers timely, innovative results.

3. Next-generation service excellence: Member service is where it all comes together — the branches, the call center, digital and mobile, social media, the loyalty programs, and the fraud-prevention technology. But without impeccable execution, it is the stuff of nightmares.

PSCU is investing in next-generation information technology and member engagement platforms that can take already exceptional member experiences to the next level while providing seamless wrap-around back office support.

4. Data-driven digital insights: Real-time behavioral insights from analytics help CUs craft the right offers for the right members at the right times, while tracking ROI. To that end, PSCU has built a data warehouse and suite of analytics that gives CUs a 360-degree view of members. This data can be accessed on demand through dashboards.

5. Security assurance: Nothing erodes confidence in a financial institution like a data breach or fraud. To protect CUs, PSCU is partnering with vendors to develop biometrics and dark web scrutiny.

Join Us

Here at PSCU, we built our CUSO on the belief that CUs' greatest assets are collaboration and strength in numbers. We invite you to join us on our exciting and vital mission to create the CUSO of the future.


Understand Your Market
Our Venture. Your Gain.

CU DIRECT

LENDING TECHNOLOGY & SOLUTIONS FOR TODAY.

THE NETWORK OF TOMORROW.

Leveraging A Digital Lending System to Help Drive Indirect Auto Loans

CU Direct recently partnered with Visions Federal Credit Union on a case study that took a close look at the credit union's success in the indirect lending marketplace, and the steps the credit union took to overcome the challenges it had in growing loans through the indirect channel.

Visions' indirect lending program had been a manual process. Dealers would fax purchase orders to the credit union, and employees would manually enter the information into its loan origination system. The credit union's loan officers would then have to call the dealership with loan approval or denial. In 2013, the credit union began researching loan origination systems, as well as what dealers were looking for from them as an auto lender. Simply, the dealers were looking for a digital process.

The credit union was looking to implement a digital indirect lending system that would enable it to meet current and future loan growth goals, while fostering and supporting a relationship with dealers that made the credit union a valuable business partner.

At the time, Visions had agreements with approximately 80 dealers to provide indirect financing. However, only a small percentage of the dealers sent the credit union applications, and even fewer produced loans that were eventually funded, creating a look-to-book issue. A lack of quick, digital loan decisioning was partly responsible.

Visions was also competing against other lenders that offered markup incentives to dealers, something it firmly believes goes against the credit union philosophy. The credit union needed an indirect partner that would provide it with attractive market differentiation that wasn't tied to paying any markup.

Visions looked at many indirect lending systems, and ultimately selected CU Direct's CUDL lending platform for several reasons. CUDL provided Visions with the ability to fund and retain more auto loans, increase profitability and fuel membership growth. Additionally, CU Direct's superior business model allowed Visions to protect its look-to-book ratio.

The first year using the CUDL system, the credit union experienced a 60% increase in indirect auto loans, achieving $11 million in new originations. Over the next three years, loans through the indirect channel continued to increase, with $28 million in loan originations in 2014, $79 million in 2015, and $90 million in 2016.

In 2017, the year the credit union hoped to reach a once unthinkable goal of $100 million in auto loans, Visions ended the year with over $120 million in new indirect loan originations. In total, Visions' overall indirect portfolio grew from $30 million at the outset to nearly $250 million. In addition to dramatic year-over-year growth in loans, the credit union has also grown membership 1,000 -1,600 members annually since implementing CUDL in 2013.

Another important aspect to Visions' indirect lending success was its commitment to seek out annual dealer feedback and use the data to make program enhancements that strengthened dealer relationships and increased originations. Taking advantage of CUDL's wide dealer network helped fuel immediate growth for Visions' indirect lending program.

When Visions committed to its goal of originating $100 million in new indirect loans per year, it took an "all-in" approach for three primary reasons:

- *It could be used as a strategy to achieve new market penetration*
- *It was a way to serve members in a non-branch environment*
- *It supported loan growth goals*

After five years of strong commitment to indirect lending, the credit union pointed to these major benefits for incorporating the CUDL indirect lending platform and executing its new lending strategy:

- *Increased member and loan opportunities at the point-of-sale*
- *Joint marketing opportunities*
- *Loan portfolio diversification*
- *Opportunity to strengthen partnerships with community businesses*

Visions' "all-in" indirect lending strategy has been so successful, the credit union has increased its cap of how much indirect lending it can hold compared to other loan assets. "It used to be $300 million, and they thought we'd never hit that," notes Tom Novak, Visions' Director of Digital Banking. "But we recently increased it to $500 million, and we're already halfway there as an overall indirect loan portfolio."

Discover more, start the journey at **CUDIRECT.com**

Dedicated *To Card Growth*

CUSO AIMS TO HELP CREDIT UNIONS INCREASE CREDIT CARD SPEND.

BY TRELLANCE

Trellance (*trellance.com*), a Tampa, Fla.-based CUSO, is making a splash with its focus on debit and credit card marketing initiatives. This "processor-agnostic" credit union service organization can provide services to any CU, regardless of their processing relationships.

"Our goal is to serve as a platform for credit unions by granting access to expertise and proven programs that provide results," says Bill Lehman, SVP/managed services at the CUES Supplier member CUSO. "We also help our credit unions with effective program management to cultivate their growth."

Trellance helps credit unions increase the penetration, activation and usage of their card programs. "Our experienced card portfolio consultants help CUs to leverage our specific experience relevant to the CU market," adds Lehman. "For example, I've personally managed large portfolios, and growth in credit card volume nationally is up 5 percent. I encourage our member credit unions to leverage not just our experience but also find ways to exploit this positive trend in consumer confidence."

The CUSO seeks to increase credit card spend for its member credit unions, thus increasing interchange income, finance revenue and fee income. "Increased spend is always a positive for credit unions," says Lehman. Trellance can also assist with debit card activity, and Lehman sees the volume of debit transactions holding steady. "This shows the consumer being confident in using their cards over cash or checks."

CARD TRENDS TO WATCH

Lehman notes these trends:

- ***Consumer spending is up in the U.S.*** over 3 percent across the board, using all payments vehicles. This is indicative of strong consumer confidence.
- ***Growth in credit card volume is up 5 percent,*** which fuels growth in interchange revenue (the second largest line item in the credit card space) and finance revenue. Interchange income continues to be an important part of a profitable card program.
- ***With the growth in volume,*** consumers may be ripe for credit line increases or balance transfer offers.
- ***Debit card volume is remaining steady,*** but the number of transactions is increasing. Consumers have confidence in using their debit card in place of cash or checks.
- ***20 to 30 percent*** of all credit and debit card volume is in e-commerce.
- ***Rewards programs on both the credit and debit side*** continue to grow and must be embraced to remain competitive in the marketplace. Consumers now expect rich rewards on card transactions.
- ***CUs will seek more upscale Signature credit cards*** and look for ways to spark product differentiation.

Trellance can also assist in the war on loyalty. This war, notes Lehman, is based on high-value rewards and impacts spend and consumer confidence. And as these rewards programs gain traction, consumer confidence increases.

CUSOs are designed to take the headaches away. "Through our Optimized Managed Services and Card Portfolio Growth Solutions, we assist our member-owners with marketing, analysis, charge-offs and virtually all functions of portfolio management," explains Lehman.

There are many positives in working with a CUSO such as Trellance, including to:

- provide greater understanding of the market;
- offer terrific experience with products and services;
- leverage intimacy with the CU industry;
- assist with selection and management of vendors; and
- improve operational efficiencies and profitability and keep costs down.

Trellance is holding its immersion18 (*immersion18.com)* conference May 8-11, in Fort Lauderdale, Fla. The conference is designed for CUs of all sizes to share ideas and hear from industry leaders.

Your growth. Our guidance.

We're Trellance, a new company sprouted from years of payments experience to provide powerful new solutions to credit unions. Trellance was created to provide the structure and solutions to help credit unions not just compete, but thrive. We provide next-generation insights, resources, expertise and execution capabilities to credit unions. We're talking about vibrant strategies to grow your community and attract new members, along with powerful tools to keep current members even more engaged. Trellance is here to support your growth.

Join us at our immersion18 conference, May 8-11th in Ft. Lauderdale, FL.

Register at **immersion18.com.**

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For more info visit trellance.com.