America's Credit Unions

August 12, 2024

Jeanette Quick
Deputy Assistant Secretary for Financial Institutions Policy
U.S. Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, DC 20220

RE: Request for Information on Uses, Opportunities, and Risks of Artificial Intelligence in the Financial Services Sector; Document No. 2024-12336

Dear Deputy Assistant Secretary Quick:

On behalf of America's Credit Unions, I am writing in response to the request for information (RFI) issued by the U.S. Department of the Treasury (Treasury) regarding uses, risks, and opportunities of artificial intelligence (AI). America's Credit Unions is the voice of consumers' best option for financial services: credit unions. We advocate for policies that allow the industry to effectively meet the needs of their over 140 million members nationwide.

America's Credit Unions supports a financial marketplace that allows credit unions to grow and innovate through the responsible use of AI. As not-for-profit cooperatives, credit unions use AI to meet the needs of their members, such as by improving access to credit, preventing fraud, enhancing risk management, and improving customer service operations. AI can also grant a competitive edge to credit unions in a marketplace dominated by larger institutions. While AI holds promise for credit unions and the communities they serve, sustained innovation depends on a commitment from regulators to facilitate and encourage experimentation. To achieve this goal, policymakers should favor the application of principles-based frameworks for risk management while avoiding needlessly granular examination procedures designed to interrogate a single type of technology.

While generative AI has evoked concern around topics of bias and misinformation, it is important to recognize that the use of AI within the credit union industry is already highly regulated; consumer protections, anti-discrimination laws, and prudential safeguards continue to apply and remain tech-neutral. Accordingly, regulatory priorities should be oriented towards refining supervisory understanding rather than seeking new, one-size-fits all rules that would soon grow outdated in the quickly developing field of AI. With greater understanding of how this technology can benefit consumers, enhance business functions, and support healthy competition, regulators may find it easier to offer signals of support rather than skepticism.[1]

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[1] *See* CFPB, "Director Chopra's Prepared Remarks on the Interagency Enforcement Policy Statement on 'Artificial Intelligence'" (April 25, 2023), *available at* https://www.consumerfinance.gov/about-us/newsroom/director-chopra-prepared-remarks-on-interagency-enforcement-policy-statement-artificial-intelligence/ (alleging that

General Comments

America's Credit Unions supports non-regulatory approaches for supporting and evaluating the use of AI within the financial services sector. As with other technologies, consumer financial protections and anti-discrimination rules continue to have broad applicability and are not diminished by any particular mode of decision making. Existing regulations require credit unions to adopt robust risk management practices and compliance procedures to ensure that the use of any new technology does not jeopardize safety and soundness or the rights of individual members.[2]

As a preliminary matter, Congress and financial regulators should ensure that policy targeting financial institution use of AI accounts for existing regulation and is tailored to specific use cases, which are typically far narrower than the "generative AI" capabilities which have attracted the greatest share of public concern.[3] Policymakers should avoid developing guidance targeted at general AI behavior with the intent of applying it to narrow and already highly regulated banking applications—such as credit underwriting or customer service interaction. Doing so would overstate the perceived autonomy of AI agents while undervaluing the robust risk management processes already required by the National Credit Union Administration (NCUA) and other banking regulators.

Credit unions looking to partner with third parties to deploy AI are well aware of the risks that such technology could pose in the absence of proper due diligence and third-party risk management. Fine-tuned control, careful oversight, and an abundance of caution are prerequisites for putting any type of AI software into production. Accordingly, Treasury should generally defer to existing frameworks of risk management applicable to credit unions, which demand full compliance with all applicable laws and regulations relevant to the use of a particular technology.[4]

Confusion regarding the difference between types of AI (narrow versus generative) or use cases could contribute to uncertainty about how much control is vested between human and machine agents. The particular degree of control has relevance insofar as some financial regulators may

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"[w]hile machines crunching numbers might seem capable of taking human bias out of the equation, that's not what is happening.").

[2] *See* e.g., NCUA, Supervisory Letter, Evaluating Third Party Relationships, SL No. 07-01 (October 2007), *available at* https://ncua.gov/regulation-supervision/letters-credit-unions-other-guidance/evaluating-third-party-relationships-0; *see also* NCUA Examiner's Guide, Model Risk (last updated October 11, 2016) (citing FRB and OCC SR Letter 11-7, Supervisory Guidance on Model Risk Management (April 4, 2011)), *available at* https://publishedguides.ncua.gov/examiner/Content/ExaminersGuide/IRR/MeasurementSystems/ModelRisk.htm.

[3] *See* e.g., CFPB, "CFPB Joins Federal and State Agencies in Coordinated Statements on Tech & Enforcement" (March 26, 2024), *available at* https://www.consumerfinance.gov/about-us/newsroom/cfpb-joins-federal-and-state-agencies-in-coordinated-statements-on-tech-enforcement/.

[4] *See* NCUA Examiner's Guide, Risk Management Components (last updated August 23, 2022), *available at* https://publishedguides.ncua.gov/examiner/Content/ExaminersGuide/Risk-ManagementGovernance/RiskManagementComponents.htm#Policies.

perceive AI-driven outcomes as difficult to understand but are not sure how financial institution end users should validate their use of AI to demonstrate compliance with applicable law. In general, when a law or regulation prohibits specific conduct rather than prescribes a particular way of doing things, financial regulatory agencies tend to evaluate compliance by looking at policies and procedures and the sufficiency of an institution's compliance management system (CMS). These evaluations can be subjective and can result in lower supervisory ratings even when no violations of law are identified.[5] Given how AI appears to draw scrutiny from certain regulators, a balanced supervisory approach is paramount to ensure that assessments of AI are reasonably scoped and output oriented.[6]

Overregulation of emerging technologies can stifle innovation.[7] If regulators begin to demand excessive technical documentation regarding usage or training of AI in order to prove a negative (i.e., that an AI model is incapable of producing an erroneous result), this will likely discourage continued investment in such technology. For smaller, community institutions like credit unions, compliance burdens under existing law already present significant obstacles to innovation. Moreover, supervisory expectations born of inherent hostility towards AI will tend to reward the largest incumbent users of such technology whose business strategies may welcome regulatory gatekeeping as a means of reducing competitive pressure.[8]

An environment of regulatory skepticism or even hostility towards AI would harm credit unions and their members. AI has demonstrated a capacity to expand access to credit for underserved and minority populations; reduce competitive barriers for small, community institutions; and protect consumers when applied to the field of cybersecurity.

Uses and Opportunities of AI

Credit unions were created to offer provident credit to all members of their communities, and this organizing principle helps to explain the prevalence of robust relationship lending models across the industry. As cooperatives that are directly accountable to their member-owners, credit unions are focused on developing long-lasting, trusted relationships—an interest that is best

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[5] *See* CFPB, Supervision and Examination Manual, Examinations and Targeted Reviews, 11 (February 2019) *available at* https://files.consumerfinance.gov/f/documents/cfpb_examination-process-section.pdf ("An institution may receive a less than satisfactory rating even when no violations were identified, based on deficiencies or weaknesses identified in the institution's CMS").
[6] *See* CFPB, CFPB and Federal Partners Confirm Automated Systems and Advanced Technology Not an Excuse for Lawbreaking Behavior (April 25, 2023) *available at* https://www.consumerfinance.gov/about-us/newsroom/cfpb-federal-partners-confirm-automated-systems-advanced-technology-not-an-excuse-for-lawbreaking-behavior/ ("[T]he CFPB will work with its partner enforcement agencies to root out discrimination caused by any tool or system that enables unlawful decision making").
[7] *See* Aghion, Philippe, Antonin Bergeaud, and John Van Reenen, National Bureau of Economic Research Working Paper, The Impact of Regulation on Innovation (January 2021), *available at* https://www.nber.org/system/files/working_papers/w28381/w28381.pdf.
[8] *See* Jennifer Huddleston and Ian Adams, "Potential Constitutional Conflicts in State and Local Data Privacy Regulations" (December 2, 2019), *available at* https://rtp.fedsoc.org/wp-content/uploads/RTP-Cyber-and-Privacy-Paper-Constitutional-Conflicts-in-Data-Privacy-final.pdf.

served by adhering to core principles of equality and fairness. The use of AI, like other technologies, serves to complement these principles rather than displace them.

AI has shown promising results in a variety of different contexts. In the domain of credit decisioning, underwriting models that leverage AI and alternative data have expanded access to credit for underserved and minority populations.[9] In some cases, AI-driven assessments of applicants' creditworthiness can produce more accurate results than is possible when relying solely on traditional credit score lending models (traditional lending models).[10] Unlike traditional lending models reliant on discrete, backwards-looking data specific to an individual, algorithmic lending models use training data containing billions of observations from millions of individuals when assessing applicants' creditworthiness. AI tools that can reveal insights about alternative measures of creditworthiness can help applicants who are credit-thin or credit invisible, a benefit that regulators have already acknowledged.[11] AI models can also be used to quickly process a vast amount of data to render a timely credit decision, helping smaller institutions remain competitive with the largest, technologically sophisticated firms.

As the NCUA and the other federal banking agencies have recognized in prior requests for information, credit unions face considerable and wide-ranging competitive pressures from both larger financial institutions and non-bank financial technology (fintech) firms. Chief among these competitive pressures, and particularly important in this RFI's context, are technology driven expense compressions in core lines of business that present credit unions myriad immediate and long-term business risks.[12] Larger financial institutions and fintech competitors are increasingly leveraging AI's cost and operational efficiencies realized during loan application and origination processes to not only capture lending market share but also to introduce consumers to broader suites of financial products, including deposit and payment products.[13]

While AI usage is not yet widespread within the credit union industry, most credit unions have indicated that they are at least considering investments in AI. Some are already partnering with third parties to successfully implement AI-driven tools to facilitate access to credit for members, strengthen existing risk management processes, and improve customer service. In general, partnerships with third parties are preferred to in-house development of AI due to the significant costs associated with training a model from scratch. Industry experts have estimated that the

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[9] *See* CFPB, An update on credit access and the Bureau's first No-Action Letter, (August 6, 2019), *available at* https://www.consumerfinance.gov/about-us/blog/update-credit-access-and-no-action-letter/.

[10] *See e.g*., Zest, Zest AI announces FairBoost (June 26, 2023), *available at* https://www.zest.ai/insights/zest-ai-announces-fairboost.

[11] *See* Board of Governors of the Federal Reserve System, CFPB, FDIC, NCUA, OCC, Interagency Statement on the Use of Alternative Data in Credit Underwriting, Consumer Financial Protection Bureau, Blog: Report on the Bureau's Building Bridge to Credit Visibility Symposium, *available at* https://www.consumerfinance.gov/about-us/blog/report-credit-visibility-symposium/.

[12] *See* Deloitte, AI leaders in financial services (August 13, 2019), *available at* https://www2.deloitte.com/us/en/insights/industry/financial-services/artificial-intelligence-ai-financial-services-frontrunners.html.

[13] *See id*.

total cost to train even a narrow-purpose AI can easily reach into the millions of dollars for compute alone.[14]

Regulatory barriers that stand in the way of responsible AI innovation risk compromising the quality of member services and long-term industry viability by favoring larger companies that can absorb stringent compliance standards. On the other hand, thoughtful AI adoption coupled with a flexible regulatory framework that encourages responsible experimentation will allow credit unions to better and more cost-effectively serve present-day members and remain at the forefront of engaging unbanked and underbanked Americans.

AI Used by Credit Unions

AI helps credit unions meet member demand for modern financial services and compete more effectively with larger institutions. Although a significant advantage of AI involves the ability to automate manual processes, the technology has not fundamentally altered credit unions' historical role as relationship lenders committed to maintaining a close bond with the communities they serve. Instead, AI has allowed credit unions to elevate the roles of their employees to fulfill a greater range of consultative responsibilities that are critical to maintaining high member satisfaction, an essential element to their relationship banking model.[15]

AI deployed by credit unions tends to be a type of "narrow AI" derived from supervised machine learning.[16] Models built using supervised machine learning tend to exhibit predictable characteristics since their foundation consists of labeled training data grounded to a baseline expectation for what would be considered a correct response. Credit unions and other end users of AI in the financial sector often regard supervised AI models as more suitable for deployment in typical consumer finance applications like credit underwriting given their close supervision and regulation and because these types of models are easier to evaluate in terms of the correctness of their output.[17]

Models derived from unsupervised learning are typically designed to draw inferences from unlabeled data and produce outputs which relate to the perceived closeness or similarity of

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[14] *See* Deen Favaedi, Phoebe Zhou, "Evaluating AI adoption in financial crime programs," (May 16, 2024), *available at* https://www.crowe.com/insights/fincrime-in-context/evaluating-ai-adoption-in-financial-crime-programs.

[15] *See* Statement of Elizabeth Osborne before the House Financial Services Committee, "AI Innovation Explored: Insights into AI Applications in Financial Services and Housing," 6 (July 23, 2024), *available at* https://docs.house.gov/meetings/BA/BA00/20240723/117527/HHRG-118-BA00-Wstate-OsborneE-20240723.pdf.

[16] The Office of Management and Budget has characterized "narrow" AI as an algorithm that learns and performs "domain-specific or specialized tasks by extracting information from data sets, or other structured or unstructured sources of information." *See* OMB, Guidance for Regulation of Artificial Intelligence Applications, (November 17, 2020), *available at* https://www.whitehouse.gov/wp-content/uploads/2020/11/M-21-06.pdf.

[17] *See e.g*., Zest AI Testimony – Hearing on Banking Relationships and Regulatory Burdens (July 12, 2024), *available at* https://docs.house.gov/meetings/BA/BA20/20240712/117514/HHRG-118-BA20-Wstate-deVereM-20240712.pdf.

different data points, but without a ground truth to guide output towards an expected result.[18] These models may be harder to assess in terms of accuracy; however, they are well suited for discovering new patterns in large datasets. Models built on a foundation of unsupervised learning have shown promise in the field of cybersecurity and fraud prevention, where large amounts of network or transactional information can be quickly analyzed to detect anomalous behavior that could be indicative of criminal activity. In the context of preventing fraud or cybercrime, a model that is able to draw inferences about activity that does not fit known signatures or behavioral patterns is generally preferred to better anticipate and identify criminal behavior.[19] While such models may face challenges in terms of comprehensive explainability, regulators should avoid supervisory policies that would impair deployment of AI intended to protect institutions and the public from criminals.[20]

Some popular AI models, such as large language models (LLMs) capable of natural language responses, are built using a combination of supervised and unsupervised machine learning.[21] Other forms of generative AI may leverage self-supervised learning techniques "wherein the data itself provides a label (*e.g.,* the next word in a string of text) and the model returns a predicted value of that label as output."[22] Models built using combinations of different learning techniques can yield new insights across different domains while still retaining high reliability and accuracy, especially when they are fine-tuned (often through some supervised learning process) to reduce divergence from what is later deemed a "correct" response for a given input.[23]

Although generative AI has invited scrutiny when used in less regulated sectors of the economy, credit unions follow robust risk management requirements and take extreme precaution to minimize the chance of reputational risk when these tools are used in member-facing interactions. Although all AI systems are inherently predictive models, systems designed to

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[18] While there are different ways to distinguish between supervised and unsupervised machine learning, regulators outside the financial sector have offered a technical description of the relevant differences. The Office of the National Coordinator for Health Information Technology has addressed both supervised and unsupervised techniques in a final rule addressing certification requirements for health information technology developers. *See* 89 Fed. Reg. 1192, 1243 (January 9, 2024).

[19] *See* Cornerstone Advisors, "Banks Need Artificial Intelligence – It's Just a Matter of Picking the Right Technology," (July 13, 2023), *available a*t https://www.crnrstone.com/gonzobanker-blog/banks-need-artificial-intelligence-its-just-a-matter-of-picking-the-right-technology; *see also* Microsoft, "What is AI for cybersecurity?", *available at* https://www.microsoft.com/en-us/security/business/security-101/what-is-ai-for-cybersecurity.

[20] One major provider of AI-powered antifraud software has warned that overregulation of AI could counterintuitively grant criminals the greatest advantage. *See* Bloomberg Law, Nasdaq Warns Criminals May Win If AI Regulation Moves Too Fast (April 19, 2023), *available at* https://news.bloomberglaw.com/capital-markets/nasdaq-warns-criminals-may-win-if-ai-regulation-moves-too-fast.

[21] *See e.g*., Radford, A., Wu, J., Child, R., Luan, D., Amodei, D., & Sutskever, I. (2019), "Language models are unsupervised multitask learners," OpenAI Blog, *available at* https://cdn.openai.com/better-language-models/language_models_are_unsupervised_multitask_learners.pdf.

[22] *See e.g.,* ONC and DHS, Health Data, Technology, and Interoperability: Certification Program Updates, Algorithm Transparency, and Information Sharing, 89 Fed. Reg. 1192, 1243.

[23] *See* IBM, "What is fine-turning?", (March 15, 2024), *available at* https://www.ibm.com/topics/fine-tuning.

interact with consumers through natural language prompting leverage filtering and other self-supervision techniques to ensure that output is tightly orchestrated.

Most credit union AI usage falls into the following three buckets:

Underwriting Support

In testimony before the Financial Institutions and Monetary Policy Subcommittee on July 12, 2024, Commonwealth Credit Union (CWCU) in Kentucky highlighted the use of its third-party AI model to improve credit underwriting activities, both in terms of efficiency and in terms of approving a greater share of underserved applicants.[24] Using AI, CWCU is able to approve more loans outside of business hours, approve more members with little or no credit history, and increase lending and approvals to minority and disadvantaged populations, all while improving loan portfolio performance.[25] Other credit unions that are exploring the use of AI for credit decisioning purposes foresee similar benefits.[26] AI can assist in achieving faster and smarter decisions about loan applications by analyzing various data sources and factors beyond the credit score. These data points can include maintaining a positive account balance over a period, adherence to regular bill payments, and other positive account usage indicators.

As with any other technology used in conjunction with credit underwriting activity, credit unions ensure that AI tools comply with all applicable laws and regulations, including the Equal Credit Opportunity Act (ECOA), Fair Housing Act (FHA), and Fair Credit Reporting Act (FCRA). Credit unions engage in self-tests or self-evaluations as part of their ongoing monitoring of fair-lending risks.

While self-evaluations can vary in terms of their scope and sophistication based on a credit union's risk profile, they generally encompass review of denied applications, comparisons of loan files, analysis of Home Mortgage Disclosure Act (HMDA) data, and review of lending policy exceptions. Self-tests can be similarly varied and encompass a variety of analytical techniques (e.g., surveys, use of test applicants, review of credit transaction records). Both types of testing could function as methods for evaluating the results of AI-driven lending decisions. Analysis of lending decisions ensures that regulatory attention is appropriately focused on outputs rather than the technical training parameters of individual AI models.

Deconstructing the entirety of an AI algorithm to address explainability or overfitting risks would be costly and less productive for examination purposes. Furthermore, it is questionable whether a complete deconstruction of an AI model to satisfy regulator scrutiny would be feasible

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[24] *See* Statement of Karen Harbin, President and CEO of Commonwealth Credit Union, on behalf of America's Credit Unions, House Financial Services Committee, Financial Institutions and Monetary Policy Subcommittee, "Financial Institution-Fintech Partnerships: Leveraging Third-Party Relationships to Increase Access to Financial Services," July 12, 2024, *available at* https://docs.house.gov/meetings/BA/BA20/20240712/117514/HHRG-118-BA20-Wstate-HarbinK-20240712.pdf.

[25] *See id.*

[26] *Supra* note 15.

for institutions that rely on proprietary models provided by third parties. For smaller credit unions that cannot afford to train their own models, reliance on third parties depends on a marketplace for AI that can accommodate innovation and experimentation without the burden of open-ended or needlessly granular regulatory inquiries.

Risk Management and Financial Crime

AI-powered fraud analytics can enhance credit union risk management practices and efforts to prevent financial crime by improving detection of irregular financial behaviors. Many credit unions are already using third-party technology bundled with debit and credit card products to prevent fraudulent transactions or to flag suspicious transactions.[27] In some cases, this technology leverages AI and machine learning (ML) processes (e.g., neural networks) to develop predictive models for fraud mitigation purposes. Credit unions are eager to adopt more effective fraud management tools given the increasing prevalence of card not present fraud and the impossibility of manually monitoring transaction patterns.

AI also has the potential to reduce Bank Secrecy Act (BSA) and anti-money laundering (AML) compliance costs by reducing the burden of filing Suspicious Activity Reports. AI could also be used to satisfy regulatory notification standards if an institution experiences a reportable cyber incident. The contents of Suspicious Activity Reports and cyber incident notifications are usually driven by the output of automated risk scoring, analytic, or diagnostic systems, and the role of staff is to summarize this information in a coherent narrative. However, the development of a narrative is often a slow and mostly manual task, particularly for smaller institutions. Accordingly, the use of AI to summarize the output of automated systems for financial crime or cyber reporting purposes is a use case that Treasury and other regulators should support.[28]

Customer Service Improvements

One of the most publicly visible implementations of AI technology is the use of chatbots to enhance customer service. AI-enhanced call center services are becoming increasingly common among credit unions and offer a cost-effective means of responding to routine member questions while also elevating the role of human representatives to a more consultative position. The use of AI technologies to resolve member questions can enhance the consumer response function of a compliance management system, and regulators should encourage the use of such technology without prescribing AI-specific methods for escalation or resolution of consumer inquiries.

In testimony before the House Financial Services Committee, one member of America's Credit Unions shared that the introduction of an AI-powered conversational assistant had significantly

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[27] *Supra* note 19.

[28] *See* U.S. Department of the Treasury, Managing Artificial Intelligence-Specific Cybersecurity Risks in the Financial Services Sector, 42 (March 2024), *available at* https://home.treasury.gov/system/files/136/Managing-Artificial-Intelligence-Specific-Cybersecurity-Risks-In-The-Financial-Services-Sector.pdf (noting that "GenAI will facilitate the automation of analyzing threat actor behaviors and streamlining alerts, investigations, and responses").

improved call center performance, member satisfaction, and employee engagement.[29] Since launching in August 2023, the credit union AI assistant fully handles over 60 percent of total inbound calls during business hours and over 75 percent of all calls after business hours, compared to a less than 25 percent handling rate with the previous "telephone banking" solution.[30] The credit union is now looking to upgrade the AI assistant to speak Spanish, to better serve Spanish speaking members who represent a large percentage of membership.[31] As time progresses, the credit union plans to assess additional languages relevant to the credit union's field of membership.[32]

Conversational, multilingual chatbots are an example of how AI can build more inclusive financial services. However, regulators must ensure that supervisory policy does not chill adoption of these useful tools. For example, the Consumer Financial Protection Bureau (CFPB) has chosen to characterize financial institution chatbots as a poor substitute for human customer service representatives, claiming that consumers "may in fact be dealing with a very rudimentary system with little capacity to help beyond retrieving basic information and parroting it back or directing customers to policies or FAQs."[33] Credit unions do not intend to make it more difficult for their members to get answers to questions and continued investments in physical branches reflect this priority. In fact, recent industry research reveals that 12 percent of members switched to their current credit union primarily because their previous financial institution did not have branches nearby.[34] AI is meant to enhance routine call center operations, not displace a distinguishing factor of the credit union industry: community presence.

Managing AI Risk Within the Financial Sector

As the NCUA and the other federal banking agencies have recognized in prior requests for information, many of the potential risks associated with using AI are not unique to AI.[35] Furthermore, many of these risks are addressed by existing law, regulation, or supervisory guidance. For example, safety and soundness risk associated with the use of AI for credit underwriting purposes is largely accounted for in the NCUA's supervision policy for model risk management. The NCUA has noted in its examiner guidance that "[m]odel risk increases with

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[29] *See* Statement of Elizabeth Osborne, Chief Operations Office of Great Lakes Credit Union before the House Financial Services Committee, "AI Innovation Explored: Insights into AI Applications in Financial Services and Housing," (July 23, 2023) *available at* https://docs.house.gov/meetings/BA/BA00/20240723/117527/HHRG-118-BA00-Wstate-OsborneE-20240723.pdf.

[30] *Id.*

[31] *Id.*

[32] *Id.*

[33] CFPB, Chatbots in consumer finance, (June 6, 2023), *available at* https://www.consumerfinance.gov/data-research/research-reports/chatbots-in-consumer-finance/chatbots-in-consumer-finance/.

[34] *See* PYMNTS, "PSCU/Co-op Solutions Study Adds New Urgency to Credit Union Innovation," (March 11, 2024), *available at* https://www.pymnts.com/credit-unions/2024/pscu-study-adds-new-urgency-to-credit-union-innovation/.

[35] Board of Governors of the Federal Reserve System, CFPB, FDIC, NCUA, OCC, Request for Information and Comment on Financial Institutions' Use of Artificial Intelligence, Including Machine Learning, 86 Fed. Reg. 16837, 16839 (March 31, 2021),*available at* https://www.federalregister.gov/documents/2021/03/31/2021-06607/request-for-information-and-comment-on-financial-institutions-use-of-artificial-intelligence.

model complexity and with higher levels of uncertainty about the validity of inputs and assumptions," and advises credit unions to engage in a robust risk management process to ensure model validation and accuracy.[36]

In terms of assessing the adequacy of credit union model risk management, the NCUA references interagency guidance published by the Board of Governors of the Federal Reserve System (Federal Reserve) and Office of the Comptroller of the Currency (OCC). The interagency guidance casts a wide net, covering many different banking activities including underwriting credits, valuing exposures, measuring risk, and safeguarding client assets.[37] As stated in the guidance, "[a] guiding principle for managing model risk is 'effective challenge' of models, that is, critical analysis by objective, informed parties who can identify model limitations and assumptions and produce appropriate changes."[38] Additionally, the guidance contemplates a process of continuous monitoring, noting "[v]alidation activities should continue on an ongoing basis after a model goes into use, to track known model limitations and to identify any new ones."[39]

While certain applications of AI may be new (e.g., natural language interaction with consumers), the high-level principles contained in the interagency model risk management guidance remain broadly applicable. Most importantly, the guidance recognizes limits on risk management by emphasizing a standard of materiality. Similar to other domains of prudential regulation, effective regulation seeks to manage risk to an acceptable level based on the exposures and risk tolerances of individual institutions:

> As is generally the case with other risks, materiality is an important consideration in model risk management. If at some banks the use of models is less pervasive and has less impact on their financial condition, then those banks may not need as complex an approach to model risk management in order to meet supervisory expectations.[40]

Treasury should recognize that the question of whether risks are material is especially relevant in the context of evaluating AI systems. If an institution can demonstrate adequate risk management and exercise appropriate due diligence with respect to the selection of technology service providers, consistent with longstanding regulatory guidance, deployment of AI technology should not raise significant new concerns within the financial sector. Unlike unregulated sectors of the economy, where unsupervised companies may be exploring generative uses of AI that could introduce unique security or political risks, the use of AI by credit

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[36] *See* NCUA, Model Risk, *available at* https://publishedguides.ncua.gov/examiner/Content/ExaminersGuide/IRR/MeasurementSystems/ModelRisk.htm.

[37] *See* Federal Reserve, OCC, Supervisory Guidance on Model Risk Management, SR Letter 11-17 (April 4, 2011), *available at* https://www.federalreserve.gov/supervisionreg/srletters/sr1107a1.pdf.

[38] *Id*. at 4.

[39] *Id*. at 10.

[40] *Id*. at 5.

unions and other regularly examined financial institutions should not correspond with nearly the same level of concern.

Regulatory Use of AI

In contrast to the supervisory scrutiny that applies to credit union usage of AI, the deployment of such technology by federal banking regulators is subject to fewer explicit guardrails when it comes to transparency or explainability. The Office of Management and Budget's (OMB) directive to executive agencies to "annually submit an inventory of its AI use cases to OMB and subsequently post a public version on the agency's website"[41] represents a positive shift in terms of correcting for this imbalance. However, to account for the lack of clear obligations for independent agencies, financial regulators should clearly disclose when and how they are using AI for supervisory purposes.

While little information is known about how AI is being deployed within federal financial regulatory agencies, the CFPB has offered some hints. The CFPB's FY 2023 Annual Performance Report states that the CFPB continues "to assess sources and capabilities that will provide an enhanced data-driven approach to its areas of supervisory focus."[42] The report provides the specific insight that the CFPB is now "[l]everaging additional data sources as well as artificial intelligence within the supervisory prioritization process."[43] To date, the CFPB has shared very little information about its use of AI to perform supervisory prioritization.

Some important information regarding AI/ML projects comes not from the CFPB itself, but from vendors selected to perform data analysis contracts. For example, a press release from one company describes a "Data Analytics Blank Purchase Agreement" covering "machine learning, and natural language processing support."[44] However, the CFPB has never disclosed where machine learning or natural language processing support may be applied. One potential domain is the CFPB's consumer complaint database, where it is unlikely that manual analysis is feasible. Yet the CFPB does not state conspicuously whether AI/ML techniques are used in conjunction with complaint analysis. The opaque application of novel analytics to complaints which are, by the CFPB's own admission, not screened for factual accuracy, raises concerns about fairness and transparency.

America's Credit Unions supports the OMB's directive to executive agencies to "annually submit an inventory of its AI use cases to OMB and subsequently post a public version on the agency's

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[41] OMB, Advancing Governance, Innovation, and Risk Management for Agency Use of Artificial Intelligence, (March 28, 2024), *available at* https://www.whitehouse.gov/wp-content/uploads/2024/03/M-24-10-Advancing-Governance-Innovation-and-Risk-Management-for-Agency-Use-of-Artificial-Intelligence.pdf

[42] CFPB, FY 2023 Annual Performance Report, 85 (February 2023).

[43] *Id.*

[44] Analytica, CFPB Data Analytics BPA Prime Award (October 20, 2022), *available at* https://www.analytica.net/press-release/cfpb-data-analytics-bpa-prime-award/.

website."[45] In addition, the CFPB and other financial regulators should disclose on their websites all AI/ML applications, services, and contracts that might bear upon supervisory work or rulemaking activity. Accompanying these disclosures should be a description of each AI model, its purpose, and a reasonably specific explanation of how the model works. Credit unions and other regulated financial institutions deserve to know how they are being assessed for potential violations of federal consumer financial law. Opaque algorithms that dictate supervisory focus should be subject to the same level of transparency as other supervision and enforcement functions.

Conclusion

Credit unions are committed to using AI safely, securely, and with the goal of helping their members meet their financial needs. Regulators should recognize the tech-neutral applicability of existing laws with the aim of signaling acceptance—rather than skepticism—of responsible AI innovation. A balanced supervisory framework for AI should favor the application of flexible, principles-based risk management practices rather than a one-size-fits all policy of excessive scrutiny. Requiring production of source code or other technical parameters of AI models to satisfy regulatory curiosity would impair credit unions' ability to deploy AI in a cost-effective manner, impeding competition and depriving communities of modern financial services.

Given the demonstrable benefits of AI across a variety of business uses cases, regulators should seek opportunities to promote the use of this technology so that American consumers can enjoy greater inclusivity, speed, and convenience at credit unions. America's Credit Unions appreciates the opportunity to provide information in response to the RFI. If you have any questions, please do not hesitate to contact me at 703-842-2266 or amorris@americascreditunions.org.

Sincerely,

Andrew Morris
Director, Innovation and Technology

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[45] OMB, Advancing Governance, Innovation, and Risk Management for Agency Use of Artificial Intelligence, (March 28, 2024), *available at* https://www.whitehouse.gov/wp-content/uploads/2024/03/M-24-10-Advancing-Governance-Innovation-and-Risk-Management-for-Agency-Use-of-Artificial-Intelligence.pdf.