



BOARD ACTION MEMORANDUM

TO: NCUA Board

DATE: December 8, 2020

FROM: Office of Examination and Insurance; Office of General Counsel

SUBJ: Final Rule – Subordinated Debt

ACTION REQUESTED: The NCUA Board’s approval to issue the attached final rule, which amends the NCUA’s rules in 12 CFR parts 701, 702, 709, and 741. Most significant to this proposal is the addition of a new subpart in part 702 – Subpart D – Subordinated Debt, Grandfathered Secondary Capital, and Regulatory Capital. The final rule will become effective January 1, 2022.

DATE ACTION REQUESTED: December 17, 2020.

BUDGET IMPACT, IF ANY: Based on the volume and complexity of the additional work associated with this final rule, staff estimates the need for internal training and outside counsel assistance. As such, staff requests the following:

- \$20,000 in 2021 for internal staff training;
- \$50,000 in 2021 for outside counsel services related to setting up the NCUA’s Subordinated Debt review process; and
- \$100,000 annually beginning in 2022 for outside counsel services related to the ongoing management of the Subordinated Debt review process.

SUBMITTED TO INSPECTOR GENERAL FOR REVIEW: Yes.

RESPONSIBLE STAFF MEMBER: Tom Fay, Manager, Capital Markets, Office of Examination and Insurance and Justin M. Anderson, Senior Staff Attorney, Office of General Counsel.

SUMMARY:

The attached final rule amends various parts of the NCUA’s regulations to permit low-income designated credit unions (LICUs), Complex Credit Unions, and New Credit Unions to issue Subordinated Debt for purposes of Regulatory Capital treatment. Specifically, this final rule



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creates a new subpart in the NCUA's final risk-based capital (RBC) rule¹ that addresses the requirements for and Regulatory Capital treatment of Subordinated Debt.

This new subpart, among other things, contains requirements related to applying for authority to issue Subordinated Debt, credit union eligibility to issue Subordinated Debt, prepayments, disclosures, securities laws, and the terms of a Subordinated Debt Note.

All secondary capital issued after the effective date of this final rule are subject to the requirements for Subordinated Debt. This change does not impact a LICU's ability to include such instruments in its Net Worth.

This final rule also grandfathers any secondary capital issued before the effective date of this final rule (Grandfathered Secondary Capital), and preserve such secondary capital's Regulatory Capital treatment for 20 years after the effective date. Grandfathered Secondary Capital, generally, remains subject to the requirements in current §§ 701.34(b) through (d) (Current Secondary Capital Rule). For ease of reference, the requirements in the Current Secondary Capital Rule are moved from their current location to a section in the new subpart.

In addition to the above-mentioned changes, the final rule also makes various additions and amendments to other parts and sections of the NCUA's regulations. Specifically, the proposed final rule includes: a new section addressing limits on loans to other credit unions; an expansion of the borrowing rule to clarify that federal credit unions can borrow from any source; revisions to the final RBC Rule and the payout priorities in an involuntary liquidation rule to account for Subordinated Debt and Grandfathered Secondary Capital; and cohering changes to part 741 to account for the other changes proposed in this rule that apply to federally insured, state-chartered credit unions.

Finally, this final rule includes several changes from the proposed rule, issued by the Board in January 2020. Such changes include amending the definition of Accredited Investor, providing a longer timeframe in which to issue Subordinated Debt after approval, reducing the required number of years of Pro Forma Financial Statements an Issuing Credit Union must provide with its application, clarifying the prohibition on Subordinated Debt issuances outside of the United States, and clarifying that the Board will publish a fee schedule only if it makes a determination to charge a fee.

RECOMMENDED ACTION: The NCUA Board approve the attached final rule for publication in the *Federal Register* with an effective date of January 1, 2022.

ATTACHMENT: Final Rule.

¹ On December 12, 2019 the NCUA Board approved a final rule to delay the effective date of a final RBC rule until January 1, 2022.