



Credit Union National Association

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May 23, 2011

Mary Rupp  
Secretary of the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, VA 22314-3428  
[regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov)

Re: Net Worth and Equity Ratio Notice of Proposed Rulemaking

Dear Ms. Rupp:

The Credit Union National Association (CUNA) appreciates the opportunity to submit comments to the National Credit Union Administration Board regarding its proposal on federally-insured credit union (FICU) net worth and the National Credit Union Share Insurance Fund (NCUSIF) equity ratio, pursuant to Public Law number 111-382. By way of background, CUNA is the largest credit union advocacy organization in this country, representing approximately 90% of our nation's 7,400 state and federal credit unions, which serve about 93 million members.

### Summary of CUNA's Views

CUNA strongly supported the legislation to allow section 208 assistance to be treated as regulatory net worth and we support most aspects of the proposal. In particular, we support the inclusion of section 208 assistance in a credit union's net worth and the clarification that the NCUSIF's equity ratio is to be calculated using the financial statements of the NCUSIF alone.

CUNA, however, opposes the proposed "technical change" to deduct "bargain purchase gain" in certain credit union mergers. This aspect of the proposal should be further studied by the agency and be subject to additional notice and comment.

### Section 208 Assistance

CUNA believes that the agency's proposed approach of permitting section 208 assistance when a FICU is in danger of closing or other situations specified by section 208 of the Federal Credit Union Act will help maintain the safety and soundness of the credit union system and is consistent with statutory requirements, including those under Public Law number 111-382. Any restrictions on this authority beyond those required by statute—such as

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restricting the agency's option to use section 208 assistance to supervisory mergers or similar business combinations alone<sup>1</sup>—would be contrary to Congress's intent and could potentially threaten the credit union system's safety and soundness. Public Law number 111-382 revised section 216(o)(2) of the Federal Credit Union Act to include section 208 assistance in FICU net worth as follows:

[W]ith respect to any insured credit union, includes, at the Board's discretion and subject to rules and regulations established by the Board, assistance provided under section 208 to facilitate a least-cost resolution consistent with the best interests of the credit union system . . .

Section 208 of the Act permits the Board to establish accounts or make loans to FICUs "to reopen a closed insured credit union or in order to prevent the closing of an insured credit union which the Board has determined is in danger of closing or in order to assist in the voluntary liquidation of a solvent credit union . . ."

Congress clearly intended to give the Board a high degree of discretion with respect to using section 216(o)(2) authority to further the best interests of the credit union system by preventing the closing of a FICU and other situations specified by section 208. Had Congress intended to limit section 216(o)(2) to the context of, for example, supervisory mergers or similar combinations only, Congress would have included the term "supervisory mergers" or similar limitations as an express requirement in Public Law number 111-382. The lack of such an express requirement regarding mergers or other business combinations, in addition to Congress's broad grant of discretionary authority to the Board in section 216(o)(2), indicates that Congress intended for the Board to have significant flexibility with respect to using section 208 assistance and section 216(o)(2) to facilitate a least-cost resolution, including a resolution that does not involve a business combination.

CUNA therefore supports this aspect of the rule exactly as proposed and believes that any restrictions on the Board's discretion beyond those expressly included in section 208 and 216(o)(2) are not permissible under the statute.

### **NCUSIF Equity Ratio**

CUNA also supports the proposed clarification that the NCUSIF equity ratio is to be determined using solely the financial statements of the NCUSIF alone. The proposed rule incorporates the exact language of section 2 of Public Law number 111-382 into 12 C.F.R. § 741.4(b). Congress included this language to clarify that the NCUSIF is not to be combined for equity ratio accounting purposes with

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<sup>1</sup> The American Bankers Association's comment letter of April 29, 2011 (page 2) argues that the Board should limit the option of section 208 assistance so that it can only be used to facilitate mergers of failed credit unions even though Congress did not include such limitations in the law.

the National Credit Union Central Liquidity Facility, conserved credit unions, or any other entity. This aspect of the proposed rule is both consistent with congressional intent and sound public policy, and should be adopted as proposed.

### **Bargain Purchase Gain**

CUNA believes that the proposed “technical changes” to deduct “bargain purchase gain” in certain credit union mergers is outside the scope of Public Law number 111-382. If the agency chooses to proceed with this aspect of the proposal, the provisions should be subject to a separate rulemaking with additional opportunity for notice and comment.

The safety and soundness benefits of the proposed treatment of “bargain purchase gain” are questionable. The proposal may improve matters in some cases by reducing the difference between regulatory net worth and GAAP under a particular set of facts and circumstances, but would cause problems in other cases.

For example, in a FICU merger where the fair value of net assets acquired (such as \$11.0 million) is greater than the acquired credit union’s net worth, and the merger is a bargain purchase because the fair value of net assets acquired is greater than the fair value of the acquired entity (such as \$10.5 million), the Board’s proposal would reduce net worth, in this example, from \$20.5 million under current policy to \$20.0 million.

This is a problem for multiple reasons. First, in this example, the current regulation already produces a net worth that is \$0.5 million smaller than the credit union’s GAAP equity, and the proposed change would widen the gap to \$1.0 million in the example cited above. Second, the proposal would make this difference permanent, even after the acquired assets and liabilities no longer existed. We are concerned that, in practice, the deduction of “bargain purchase gain” in situations like this example would discourage mergers, including supervisory mergers, and therefore present possible safety and soundness concerns.

In addition to not being required by Public Law number 111-382 and having questionable safety and soundness benefits, this “technical change” does not seem consistent with Congress’s intent in adopting the Financial Services Relief Act of 2006, the law which last amended section 216 of the Act regarding net worth accounting in FICU mergers. Pub. L. No. 109-351, § 504 (2006). Congress’s intent in the 2006 amendments was to make credit union regulatory net worth more consistent with the GAAP treatment of retained earnings in mutual combinations that existed prior to the implementation of the FAS 141-R accounting standard. Congress did not contemplate deducting “bargain purchase gain” in the manner proposed in by the Board in this rulemaking.

Absent additional study of the impact of the proposal on credit union mergers, input from accounting experts, and/or further guidance from Congress, we urge the Board to eliminate the “bargain purchase gain” aspects of the proposed rule at this time.

Thank you for the opportunity to comment on the Board’s proposed regulation on FICU net worth and the NCUSIF equity ratio. If you have questions about our comments, please feel free to contact CUNA SVP and Deputy General Counsel Mary Dunn or me at (202) 508-6705.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael S. Edwards". The signature is fluid and cursive, with the first name "Michael" and last name "Edwards" clearly legible.

Michael S. Edwards  
CUNA Senior Assistant General Counsel