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To: _Regulatory Comments
Subject: [Dean Birge]- Comments on Advanced Notice of Proposed Rulemaking for Part 704

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Santa Clara County Federal Credit Union (SCCFCU) is a $480mm institution that serves over 43,000 members. The credit union is a capitalized member of Western Corporate Federal Credit Union, and utilizes this corporate credit union (CCU) as a primary provider of services, including check clearing and payment services, cash management, investments, and securities safekeeping. SCCFCU is also a non-capitalized basic member of Southwest Corporate Federal Credit Union, and uses this CCU only for investments. These CCUs provide many vital services for SCCFCU in an efficient, cost-effective and professional manner.

Payment Systems- The financial crises was not caused by problems with the current structure of CCUs that combines payment systems and investment functions. Separating these functions into two different charters seems to be an inefficient (due to the low margin nature of a commodity-like payment systems function) and unnecessary reaction. A better solution might be to set liquidity and operational targets, and then to monitor the CCUs as part of their normal examination process. Many of the services provided by CCUs can be obtained from other sources, and separating these two functions weakens the system and moves them closer to irrelevance in today's marketplace.

Liquidity and Liquidity Management- While one of the primary services provided by CCUs to SCCFCU is to provide liquidity and cash management, mandating liquidity requirement by regulation seems excessively burdensome. A possible solution would be to address adequate liquidity as part of the CCUs normal examination process (just like at natural persons credit unions) and to expand the capabilities of the Central Liquidity Facility to allow it to act as lender of last resort for CCUs, much like the Federal Reserve's Discount Window does with banks.

Field of Membership- The national fields of membership should be retained for CCUs, and limiting them would tend to promote inefficiencies within the credit union industry and limits competition between CCUs, which in turn hurts natural persons credit unions. Just as an average consumer has the opportunity to join several different credit unions due to community charters, a natural persons credit union should have the same choice.

Expanded Investment Authority- The expanded investment authority should continue, but higher capital standards should be required for higher levels of risk inherent in some types of investments. Concentration limits should be established, and CCUs must maintain those capital levels and requalify for the higher level of authority during their periodic examination.

Structure: Two-tiered System- The current system with US Central as the wholesale credit union for CCUs seems redundant and a problematic concentration of risk. In general, CCUs operate at very thin margins and this might have lead CCUs to take excessive risks with their investment portfolios (which is a direct cause of the current credit union financial crisis). The services provided by US Central could be received in other ways. Smaller CCUs could partner with larger ones to gain access to required services, or CCUs could merge to achieve economies of scale. Using a banking system analogy, there is no "wholesale" non-government bank that other banks turn to for liquidity or services. An added feature of the current share insurance program could be to separate the share insurance fund between natural person and corporate credit unions and to put

There was not an "inappropriate transfer of risk" between retail and wholesale corporates, but a systemic breakdown in the real estate mortgage market from aggressive lenders making risky underwriting decisions, consumer over-extending on housing, and rating agencies not recognizing the potential risk in the securities.

Corporate Capital- The current crisis has demonstrated that CCUs do not have adequate capital for the levels of risk they were assuming. Increasing capital requirements to a level on par with other types of financial institutions seems a prudent action. Possible changes could be to increase the amount of member capital that natural persons credit unions must contribute to CCUs in order use their services, basing the capital amount on asset size of the natural persons credit union, changing the structure of member capital to allow it to be included as tier two capital, and creating a risk-based capital requirement for CCUs. Most CCUs operate with higher leverage and narrower margins which make them inherently more risky. CCUs with a higher level of risk in their balance sheet should be required to have a higher level of capital.

Permissible Investments- CCUs should be able to continue to purchase investments that are prohibited for natural persons credit unions, but there should be concentration limits on higher risk investments or exclusion of certain extremely high risk investments. The higher risk investments would also trigger a higher required capital level if a risk-based requirement were in place.

Credit Risk Management- A requirement for more than one rating on an investment seems very reasonable as are concentration limits by sector and obligor.

Asset Liability Management- A review of a credit union's projections and modeling assumption for net interest income should be a standard part of every examination for both CCU or natural persons credit union. The expectation for credit unions is that more complex institutions should have more robust and extensive asset/liability management tools.

Corporate Governance- The Board of Directors for a CCU should have the same requirements and conditions as for the board of a natural persons credit union. The board should be non-paid volunteers that are elected by the members. The only requirement for a CCU director is that they must be an officer of a natural persons credit union that is a member of that corporate. Term limits should not be imposed by regulation, but may be set by each CCU if they desire.
Thank you for this opportunity to comment on this issue before the NCUA Board.

Sincerely,
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Santa Clara County Federal Credit Union

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