BCU

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April 3, 2009

Ms. Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Re: Comments on ANPR, Part 704 Corporate Credit Unions

Dear Ms. Rupp:

Baxter Credit Union provides the comments in the attached document regarding the National Credit Union Administration's (NCUA) Advance Notice of Proposed Rulemaking (ANPR) concerning its evaluation of the role of corporate credit unions.

Sincerely,

M. Val

Mike Valentine
President/CEO

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Baxter Credit Union

Response to NCUA Advance Notice of Proposed Rulemaking

This document presents Baxter Credit Union's positions.

1. The Role of Corporates in the Credit Union System.

The primary role for corporate credit unions should be to provide liquidity, investment, and settlement services to natural person credit unions.

Payment system

Since profits associated with the payment system are small, there is a need for consolidation in order to reduce competition and increase efficiency. We suggest establishing a CUSO to process all payments nationally. This would allow for efficiencies in scale operations. Competition would come from outside the corporate system.

Liquidity and liquidity management

Require liquidity policies that detail adequate cash flow and liquidity measurement and reporting. This would include cash flow gap modeling and monitoring various liquidity ratios against specified minimum requirements. Regular monitoring of standard liquidity measurements would allow for trend analysis and anticipation of potential problems. Reports should show diversified funding sources and adequate coverage for short term funding needs.

Require in-depth contingency funding plans, including stress scenarios for dealing with crises at individual corporates, the entire corporate system, the entire credit union system, and all financial institutions. This procedural documentation would specify the steps that should be taken in the event of a liquidity crisis. Mock scenarios should be run in order to test the viability of the strategies.

Limits should be placed on investing in certain asset classes that are prone to market disruptions, which could adversely affect the liquidity position.

Corporate credit unions should have direct access to the Central Liquidity Facility (CLF) for liquidity purposes.

Debt should be issued from the entire corporate system as a whole and then divided up as needed for individual corporates, rather than issuing debt by each individual corporate. This would require corporate cooperation and rely on the financial strength of the corporate system as a whole, rather than on the financials of any one corporate individually.

Field of membership issues

Allow each natural person credit union to do business with only one corporate. A natural person credit union can switch which corporate it does business with, as long as it moves all of its business to the new corporate. There is no true benefit to having natural person credit unions diversify among corporate credit unions because they behave in unison. This system would be more cooperative than the current competitive situation, without creating a monopoly. Each corporate should offer a full range of services. Membership capital should be transferable if a natural person credit union decides to switch from one corporate to another.

Expanded investment authority

Expanded investment authority should be allowed for corporate credit unions. CDOs should not be an allowed investment. Higher capital requirements and limits on the amount of concentration and credit risk will reduce the amount of risk taken

Structure; two-tiered system

Eliminate the wholesale corporate and reduce the number of retail corporates to between five and eight, distributed on a regional basis. This will promote efficiency while allowing for some choice by natural person credit unions. The current system encourages too much duplication of effort and cost.

2. Corporate Capital.

Core capital

Corporates should be required to have more capital than the current requirement, but not as much as the capital requirement for natural person credit unions. Somewhere in the range of 4-5% core capital, with a two-tier capital requirement for core and total capital. This will allow an adequate capital cushion for the activities of the corporate. The current level of capitalization required at corporate credit unions is too low.

Membership capital

Similar to the system used by FHLB, contributed capital should be based primarily on the amount of usage of the corporate credit union products and services by the natural person credit union. For example, the greater amount of a two-tiered criteria with one criterion being an appropriate percentage, based on capital requirements, of the amount borrowed from the corporate by the natural person credit union and the other criterion being a small percentage of the assets of the natural person credit union. Therefore, a small capital contribution, based on asset size, would be required from a natural person credit union to join a corporate if its borrowings from the corporate were small, and a larger capital contribution would be required if the amount borrowed by the natural person credit union from the corporate was large.

Risk-based capital and contributed capital requirements

Risk-based capital calculations and requirements, based on a Basel II framework, should be implemented as soon as possible. Capital should adequately account for credit, interest rate, liquidity, and operational risks. A risk-based capital requirement would represent a more accurate measurement of the risk at the institution and the appropriate level of capital.

Corporate credit unions should be allowed to access secondary capital representing up to 49% ownership. This capital would be nonvoting. In this way, interested investors would be able to participate in the corporate credit unions and another source of capital, besides natural person credit unions, would be utilized.

3. Permissible Investments.

Expanded investment authority should be allowed for corporate credit unions. CDOs should not be an allowed investment. Higher capital requirements and limits on the amount of concentration and credit risk will reduce the amount of risk taken

4. Credit Risk Management.

When a corporate takes on credit risk in the form of securities, it should not rely solely on the ratings from Nationally Recognized Statistical Rating Organizations (NRSROs), but should have its own internal system established for credit research, review, monitoring, and rating of the security, similar to the process that natural person credit unions use to rate originated loans for credit risk. Data sources exist to provide delinquency, default, and charge-off information for the collateral that is underlying a security, as well as outstanding credit support information in order to allow corporates to perform internal credit analysis in addition to obtaining NRSRO ratings.

The current NRSRO system should be fixed so that there is no incentive to give higher ratings to those who pay for the ratings. Concentration limits should be imposed on the corporates in order to limit risk. A third party review of the corporate credit union's investments should be required.

Corporates should credit risk rate the natural person credit unions that borrow from them and establish guidelines regarding the collateral needed to secure the borrowing.

5. Asset Liability Management.

Corporates should be required to perform regular, at least monthly, measurements of NII and NEV risk. Sensitivities to assumptions should be measured for various forms of spread and basis risk; yield curve movements in the form of shocks, ramps, and twists; shifts in implied market volatility; changes in credit spreads, prepayment speeds, etc. These processes should be validated annually by independent third party experts. The results of the monthly measurements and annual validation should be released to member credit unions for transparency. The NCUA should scrutinize the experience and background of the ALM staff in order to verify that they are qualified to perform accurate assessments of risk.

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6. Corporate Governance.

Corporates should be required to have some outside directors, even if they need to be compensated. Of course, corporate directors should be qualified, trained, and educated to hold these positions. Corporate directors should be actively involved at the appropriate subcommittee level in order to maintain control of the strategic decision making process. The requirements should be uniform for all corporates. Term limits should be imposed. There should be a peer review to encourage transparency. Training regarding asset liability management and investments should be required.

Other Issues

Require transparency including disclosure of policies, procedures, investments, sources of liquidity, and financial results on a timely basis to member credit unions.

Require reviews of significant policies and procedures by independent third party experts.

The NCUA should have an examiner resident at each corporate at all times in order to monitor activity on a continuous basis. The examiner assigned to a corporate should be rotated periodically. This would allow early intervention if any potential problems develop.

Issue debt from the entire corporate system and divide it up as needed for individual corporates, rather than issuing debt by each individual corporate. This would require corporate cooperation and rely on the financial strength of the corporate system as a whole, rather than on the financials of any one corporate individually.

Examine the possibility of setting up a "bad bank" that would absorb the assets that currently have large unrealized losses. The "bad bank" would hold the assets until they repaid.

Corporate credit unions should have direct access to the Central Liquidity Facility (CLF) for liquidity purposes.

The debt issued by corporate credit unions should have some quasi-governmental support in order to increase the sources of liquidity.

An enterprise risk management system should be put in place so overall risk is controlled. A transparent risk management evaluation should be required, including a third party review of credit risk with disclosure to natural person credit unions.

In order to encourage transparency, a periodic report to members and regulators should be required that shows results for and attests to the quality of internal controls, separation of duties, risk management practices, and policy compliance.