April 6, 2009

The Honorable Michael E. Fryzel
Chairman, National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

The Honorable Rodney E. Hood
Vice Chairman, National Credit Union Administration

The Honorable Gigi Hyland
Board Member, National Credit Union Administration

Re: Comments on Advanced Notice of Proposed Rulemaking for Part 704

Chairman Fryzel, Vice Chairman Hood, and Board Member Hyland:

Comments:

1. The Role of Corporates in the CU System: a corporate model is needed that can compete against other providers of similar services.
    - Payments and Liquidity
        - It would be prudent for allocation of capital to all business lines including payments.
        - Preserve the ability of corporate credit union to safely offer multiple product and service offering to all member credit unions.
        - A key factor forgotten by corporate leadership is risk that is not adequately capitalized for will first show up in liquidity.
    - Field of Membership Issues
        - Strongly disagree that the current economic calamity facing the corporate credit union system is, in part, a result of NCUA's longstanding policy of allowing corporate credit unions to complete with national fields of membership as that goes right in the face of American's long standing success with capitalism.
        - A very clear risk to PEFCU prior to NCUA stepping in with the Corporate Share Insurance Guarantee Program in January was concentration risk. Increased overnight liquidity placed additional capital at risk. The national field of membership provision allowed us to access an alternative corporate to reduce concentration risk. Returning to defined or regional fields of membership will clearly result in the restriction of competition and the removal of choice from the credit union system.
    - Expanded Investment Authority
        - Now is not the time to remove or limit the ability of a corporate credit union that can sufficiently demonstrate its ability to effectively manage and operate within expanded investment authority. To do so would significantly hinder the ability of the corporate network to compete in the financial marketplace and would most likely force natural person credit unions to seek other avenues for investments outside the industry.
        - Preserve the ability of corporates to safely engage in expanded investment authorities. Improved capital standards within a risk-based capital structure for corporate credit unions should be considered as part of this process. A properly weighted risk-based capital structure would enable NCUA to equate capital expectations with the expanded authorities granted to particular corporates.
        - Require corporate credit unions to sufficiently demonstrate their ongoing ability to manage the expanded investment authorities they have been granted. Reapplication and approval at reasonable intervals appears sound to ensure that the corporate has the appropriate management structure and sophistication to maintain the expanded investment authority going forward.
    - Structure: 2-tiered System
        - I urge the agency to carefully evaluate any proposed structural changes not solely from a perspective of safety and soundness, but also from a member service perspective. Therefore, any changes to the current structure must preserve the ability of retail corporate credit unions to provide a service and economic value to NPCUs. It remains critical that whatever structure that emerges through the rulemaking process must foster long term competition and at the same time promote cooperation where economies of scale can make a difference.
2. Corporate Capital:
        - I am pleased that the ANPR contemplates the revision of various definitions and standards for determining appropriate capital requirements for corporate credit unions.
        - Such changes are necessary from a regulatory point of view and are absolutely critical if credit unions are going to be able to be recognized as long term competitive players in the financial marketplace.
        - The current capital system for corporates is insensitive to the underlying risks and fails to properly align capital retention, because of this there is less incentive for corporate credit unions to engage in risk reducing activities.
        - Corporate capital requirements should be based upon appropriately weighted risk.
        - The implementation of a risk-weighted capital system would more effectively assist NCUA in identifying those corporate credit unions with higher levels of risk and would in turn enable the agency to more effectively allocate its resources. In addition, the implementation of a risk-weighted capital standard would place corporates on a more comparable playing field for auditors, rating agencies, counterparties, legislative bodies, other regulatory bodies, government agencies, and their NPCU owners.

3. Permissible Investments:
    - To limit a corporate credit union to the same investment options as PEFCU would virtually eliminate the capital producing value for such services from the corporates and raises the question of the need for their existence. Absolutely crucial that the agency not overreact and prescribe a "one-size-fits-all" approach to industry investment powers.
    - Not in the long term best interest of NPCUs to have corporate investment authority unduly restricted. A more prudent approach appears to include the combination of new risk weighted capital system discussed above, review and possible revisions to some expanded authority standards, and improved credit risk management techniques by corporate credit unions.
    - I would not be supportive of any proposal to unfairly restrict the ability of a corporate credit union to engage in prudent investment instruments currently permitted in regulation and statute.
4. Credit Risk Management:
    - It is important that all levels of risk in a portfolio be diligently managed and mitigated to extent possible.
    - Reliability on rating agency information has proven to be questionable to the extent utilized. While the financial industry requires uniform change in the interaction and use of agency data, new standards in corporate regulations for credit risk management are needed. Until an acceptable alternative is identified, continued reliance will be placed on the ratings provided by Nationally Recognized Statistical Rating Organizations (NRSROs). As an added measure a prudent change would be the use of multiple agency reports before making investments.
    - Whether a need exists in regulation for additional stress modeling tools is debatable, but the data likely would feed risk capital standards. Depending upon the changes made with rating agencies, a combination of changes is warranted.
    - Compile a list of best practices for effective credit risk management. Should the agency determine that stress modeling tools should be mandated in the regulation then I urge the agency to be flexible and reasonable in the implementation of this requirement and sensitive to the costs and complexities associated with the utilization of such tools.
    - Guidance on when and how to use independent evaluations would be beneficial. It would also be helpful if minimum requirements for the independent contractors conducting the evaluations were established to include, among other criteria, minimum experience levels, years in business and industry references.
    - Rather than mandate the use of independent evaluations, our suggestion would be to include scenarios where the use of independent evaluations would be recommended within a compilation of best practices guidelines designed to assist the corporate credit union in the mitigation of risk, including credit risk.
5. Asset Liability Management
    - It is essential that *all* aspects of risk be properly addressed so as to avoid a "managing to the last crisis" mentality that often results in failing to recognize the next crisis. Corporate professionals need to be utilizing new best practices in measuring interest rate, liquidity, and credit risk over time against capital. If required by regulation, the mandate should be reasonable, include minimum requirements and should afford corporate credit unions the flexibility to take into account such factors as cost, practicality and overall effectiveness.
6. Corporate Governance:
    - The implementation of minimum standards for corporate board members on a collective basis has merit and should be carefully considered.
    - Some advantage in establishing term limits for corporate board members.
    - Suggest that the terms of the board members be staggered with board members being allowed to serve for no more than three consecutive terms.
    - There appears some benefit in having a director from outside the credit union community on the board of a corporate credit union.
    - If compensation for directors is authorized it should be for all directors and not just the "outside director."
    - The decision of whether or not to compensate directors, however, should be a decision of an individual corporate credit union.
    - An alternative to outside directors could be instituting a process across corporates for peer reviews. This has long been a practice within the public accounting profession as a means for policing the industry and could help to improve collaboration as well.
    - Executive compensation and greater access to salary and benefit information are not at the heart of the current corporate crisis and are not widely viewed as significant areas of concern for corporate credit unions and their members.