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February 19, 2010

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

Subject: Comments on Part 704 Corporate Credit Unions

Dear Ms. Rupp:

On behalf of Atchison Village Credit Union (AVCU), I appreciate the opportunity to comment on NCUA's proposed amendments to Part 704, which would make major revisions regarding corporate credit union capital, investments, asset-liability management, and governance. By way of background, AVCU is a small, (6 million dollars in assets) state chartered, low-income designated, 51 year old credit union with 1080 members.

AVCU thanks NCUA for its deliberative approach in this very important rulemaking. We recognize that the NCUA Board and staff have spent an enormous amount of time, effort, and consideration in researching, discussing, soliciting and evaluating input, and creating the Advanced Notice of Proposed Rulemaking and this proposed rule. NCUA's desire to improve and strengthen the corporate system is evident in the scope and breadth of this proposal. However, we regret to state that in our view the proposal raises several substantial concerns. There are several provisions that, if enacted as proposed, will make it essentially impossible for corporate credit unions to operate in a viable fashion. Further, many of these provisions will have harmful effects on natural person credit unions and, ultimately, their members.

After reviewing all comments, concerns and proposals, we strongly believe that there should be another round of proposed rule making for Part 704—with another 90 day comment period—before issuing final rules to govern corporate credit unions.

<u>1. Time Period for Capital Ratio Attainment</u>
As drafted. the one year window required by the proposal to attain the risk-based capital ratios (i.e., the 4% Leverage Ratio) will require corporates to bring in new capital or, at a minimum, convert existing MCA to the new PCC during a time when significant issues remain unresolved regarding legacy assets. Due to a lack of sufficient retained earnings at most corporates, especially WesCorp, our corporate, which is in conservatorship, and an inability to grow retained

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earnings at a rate required by the proposed rule, member credit unions will likely be asked to contribute approximately 4% of the corporate credit union deposits as perpetual capital within 12 months of the publication date of the final rule.

We doubt that credit unions will be willing to contribute additional capital in such a short time frame, and in such an uncertain environment. Indeed, some larger credit unions may decide to pull their deposits from the corporate system as the result of such a precipitous move to achieving a 4% Leverage Ratio via PCC. This, in turn, would lead to liquidity concerns for corporates.

We believe that many credit unions will need longer than one year before they will feel comfortable recapitalizing corporates and the proposal's time period for attaining the risk-based capital ratios must be extended to at least three years.

2. Retained Earnings Growth Model
We take issue with NCUA's assumptions regarding a corporate's ability to grow retained earnings.

In addition, the model assumes funding using a deposit mix of 30% overnight shares and 70% certificates. This assumption is not valid, as other provisions of the proposal (e.g., the early withdrawal premium provision for certificates) will serve to create a major disincentive for corporate term funding. Finally, the model does not provide any cost of capital in its assumptions. This baffling omission further weakens the credibility of the retained earning growth outcomes presented.

We believe the proposed model is far-removed from attainable, real-world results. Further, the model appears to provide little opportunity for diversification, which will make retained earnings growth that much more difficult to realize. It is apparent from these assumptions that NCUA is attempting to eliminate risk at the corporate level, as opposed to permitting corporate credit unions to manage risk. Such a business model is unreasonable and counterproductive and, ultimately, will be crippling to the corporate network. For example, without an ability to generate earnings from investment risk, corporates will not be able to keep payment system fees down, forcing a move from a cooperative payment system pricing model to a market-based, for-profit model. This will have a pronounced effect on small natural person credit unions, as we will be saddled with much higher fees, as well as the possibility of obtaining and maintaining new payment services relationships.

Beyond what we believe are obvious failings of the proposed retained earnings growth model, we are concerned about the broader implications of what is reflected. It appears that NCUA envisions the shrinking of corporates' balance sheets. Such movement would not only represent a fundamental change to the corporate business model but would also result in a shifting of the investment function to natural person credit unions. Obviously, corporates possess far more in the way of experience, expertise, and resources to manage this function than does the typical natural person credit union. We believe such a "managing down" of corporate balance sheets to the natural person credit union tier would introduce greater instability, risk, burden, and costs into the credit union system, and would pose ever greater risk and losses to the NCUSIF. Surely,

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NCUA cannot have intended to introduce greater risk at the natural person credit union level and greater losses to the share insurance fund.

3. Legacy Assets in Corporate Credit Unions

While we are aware that NCUA has made public statements indicating that it will announce plans in April 2010 for addressing legacy assets, why is this critical topic is not mentioned at all in the proposed rule? Dealing with investment securities remaining on corporates' books is vital to realizing any lasting, consequential changes to the corporate system. These toxic assets continue to create instability in the network, and serve as a major disincentive to credit unions providing any future capital contributions. No investor will invest unless the toxic assets are segregated so that new capital is not at risk.

4. Qualifications of Directors

The proposal requires, as qualification for directorship, that all candidates must currently hold the equivalent of a CEO, CFO, or chief operating officer (COO) position at a member institution. We do not agree that a particular job title necessarily makes for a better board member, and instead suggest that NCUA consider that directors of corporates that may not have full experience or training needed in a particular area be required to obtain training on an annual or other periodic basis as a condition of service on a corporate board. The goal should be that directors serving on a corporate credit union board have sufficient analytical ability to effectively look after member credit unions' interests.

We are of the opinion that a maximum of nine years (as compared to six) provides a more reasonable and useful time for training and developing directors as well as for benefiting from the investment in their development. Extending the term limit to nine years further allows for much needed continuity for a corporate without compromising the benefits that may be realized from bringing on new directors.

5. Risk-Based Net Worth for Natural Person Credit Unions

We support adoption of risk-based capital among corporate credit unions. Corporate credit unions and natural person credit unions, alike, have been operating in an outdated capital framework that is out-of-step with the broader financial sector and worldwide financial regulatory regimes. While it is beyond the scope of Section 704, we take this opportunity to ask that risk-based capital be extended to natural person credit unions. As the corporate credit union meltdown clearly reminded the entire credit union system, not all assets are created equal and NCUA should modernize its measurement of capital adequacy to reflect the degree of risk associated with different assets. This change is fully within NCUA's regulatory authority, is low risk, and would provide many credit unions with relief while still maintaining strong and credible credit union net worth standards.

6. Consolidation of Corporate Credit Unions

We believe that corporate consolidation could be beneficial to the system, and that NCUA should be more open, responsive, and supportive of such consolidation by removing unreasonable impediments and/or resistance to corporate credit union mergers. We recognize that the current number of corporates is less than ideal with respect to efficiency and effectiveness. While we understand NCUA's avoidance in dictating the number of corporates in

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the system, we would like to see more open dialogue between NCUA, corporates, and credit unions regarding consolidation scenarios including the effect it would have on the viability of the entire credit union system.

7. Premium for Early Withdrawals on Corporate Certificates

This proposed provision limits a corporate credit union's ability to pay a market-based redemption price to no more than par, thus eliminating the ability to pay a premium on early withdrawals. Such a change will pose a significant disincentive for member credit unions seeking liquidity, and will likely lead them to seek more competitive investing options than corporates. Many smaller credit unions take advantage of a non-penalty option to manage liquidity, especially if they do not invest in securities.

Such a change will also have the effect of increasing corporates' funding costs. Even if a corporate desired to raise their yield in order to compete, it would be unlikely that they could generate sufficient earnings to cover the increased rate. As a result, corporates' institutional funding market for term certificates will be severely impaired—or even wiped out—which will lead to a significant reduction in overall liquidity in the corporate credit union system.

8. Payment of Dividends

The proposal will prohibit an undercapitalized corporate, unless it obtains NCUA's prior written approval, from paying dividends on capital accounts. A blanket prohibition strikes us as counter-intuitive and potentially counter-productive for the future re-capitalization of the corporate credit union system. Capital accounts, as natural person credit unions have painfully learned, are riskier than insured deposits. To balance that higher risk, investing credit unions will be reluctant to contribute capital without the promise of a higher return to compensate for the added risk.

While we understand the operational questionability of paying dividends on paid-in capital when an undercapitalized financial institution needs to maximize retained earnings to build capital, we strongly believe that this is a case-by-case decision properly made by the board and management of a corporate credit union in the context of the interest rate environment at a given moment in time. Further, the proposed retained earnings target will serve as a built-in constraint on paying dividends.

9. Concentration Limits

As written, Federal Funds transactions are not specifically excluded from the sector concentration limits. As a result, corporates would have severely limited access to the federal funds market. This will have the harmful effect of reducing the overnight rates that member credit unions receive from their corporate. In addition, it would reduce natural person credit union ability to access or engage in a market-based overnight investment option.

10. Disclosure of Executive and Director Compensation

We believe it is sensible and desirable for NCUA to align its compensation disclosure requirements with IRS Form 990 guidelines.

11. An Extra Line of Defense between Corporates and Natural Person Credit Unions

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We urge NCUA to consider a more robust "firewall" or "buffer" between corporate credit union risk and natural person credit union (NPCU) safety. We suggest that NCUA might consider the creation of a separate insurance fund or separate insurance "system" for corporate credit unions in the future. We believe that NCUA should explore options for creating a line of defense between corporates and NPCUs.

Ultimately, 90 million credit union members rely on the corporate system to provide trading, payments, clearing, and settlement services for their local credit unions. Given this systemically important role that the corporate credit union network plays in our nation's "financial plumbing," it would appear that preservation of a corporate credit union option is tantamount to preserving the credit union option, locally, for everyday consumers in our country.

NCUA should utilize its regulatory authority to redefine the definition of "total assets" under §702.2(g) of the Prompt Corrective Action rule to exclude guaranteed or low/no-risk assets from net worth ratio calculations. We recommend that the following assets be excluded from "total assets" for the calculation of net worth:

- Cash
- Overnight investments in corporate credit unions
- CU SIP deposits in corporate
- Corporate CU CDs
- Insured institutional certificates of deposit
- Guaranteed student loans
- Share secured loans
- Guaranteed portion of SBA loans
- Shares and loans guaranteed by the government
- Other government/recourse loans
- Accrued interest of non-risk investments
- Loans purchased from liquidating credit unions
- Assets held with options to sell to government
- Loans under Corporate CU Loan Guarantee Program
- GNMA/FNMA/FHLMC (GSE) securities/bonds
- U.S. Treasuries
- Furniture, fixtures, and equipment
- Land and buildings

In closing, AVCU thanks the NCUA Board for the opportunity to provide our concerns and recommendations regarding this very important rulemaking. We urge the Board to strike an effective and fair balance between preventing a repeat of past corporate failures and allowing a viable corporate system to thrive. The gravity of possibly losing the corporate credit union system as an option for natural person credit unions justifies a comprehensive "reality check" on what NCUA has proposed for the future of corporate credit unions and, ultimately, natural person credit unions.

Sincerely,

Nancy Blackstock

Nancy Blackstock
CEO/manager
Atchison Village Credit Union