

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 Credit Union of Southern California ("CU SoCal"), 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, governance, and credit union service organization (CUSO) activities.

CU SoCal is deeply concerned that if the following issues are left unchanged, there will be severe, and possibly unrecoverable, repercussions to corporate credit unions, which in turn would have harmful effects on the natural person credit unions that rely upon them.

1. Payment Systems

While it is difficult to determine the best strategy to preserve the corporate system, CU SoCal believes that NCUA should ensure that new regulations foster an environment that is conducive for corporate credit unions, or other credit union based organizations, to provide payment system services, especially for smaller credit unions.

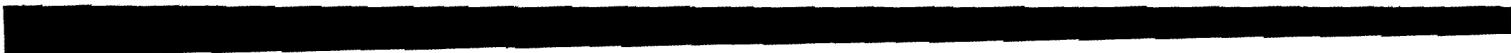
2. Time Period for Capital Ratio Attainment

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, and an inability to grow retained earnings at a rate required by the proposed rule, 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.

CU SoCal will likely never be willing to contribute additional capital and most certainly not be willing to contribute additional capital in such a short time frame, and in such an uncertain environment. Indeed, CU SoCal may decide to pull its deposits from the corporate system as the result of such a



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precipitous move to achieving a 4% Leverage Ratio via PCC. This, in turn, would lead to liquidity concerns for corporates.

We recommend that NCUA clarify its intention with respect to the time period for capital ratio attainment. Given the unavoidable reality that credit unions will need longer than one year before they will feel comfortable recapitalizing corporates, we urge NCUA to recognize that: (a) some kind of financing or capital note (equivalent to 4% of a corporate's balance sheet) will be required to meet corporates' operational needs; and (b) the proposal's time period for attaining the risk-based capital ratios must be extended to at least three years.

3. Retained Earnings Growth Model

With an investment mix that includes loans, ABS-Autos, ABS-Credit Cards, FFELP Student Loans, Structured Agency, Bank Floaters, Other Short-term, MBS-CMBS, and Overnight, it is projected that net income of 14 bps can be realized. However, I must point out that even this margin would be insufficient to meet the proposed capital targets. Even at 14 bps, a corporate would be short 7 bps of NCUA's model projected net income of 21 bps.

NCUA should provide independent, third-party "proof of concept" validation of the Agency's business model presented in this proposal or any alternative proposal. A proper assessment must do more than just "test the math." A credible assessment will test assumptions and ultimate viability of the proposed business model.

4. Legacy Assets in Corporate Credit Unions

While I am aware that NCUA has made public statements indicating that it will announce plans in April 2010 for addressing legacy assets, I am puzzled as to why 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 assets—by some estimates believed to represent as much as \$30 billion in eventual losses, or one-third of all natural person credit union net worth—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. I believe that failure to address this issue invites the weakening of even currently stable corporates, and would serve to negate the positive changes that NCUA and credit unions would like to see in the corporate system.

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CU SoCal strongly urges NCUA to cooperatively and transparently address the business and regulatory issues associated with these assets so that corporate credit union balance sheets can start with a "clean slate," rather than from a negative position. I would like to point out that, in addition to the proto-typical assets on corporate balance sheets, NCUA should also address any problem assets that may reside on the balance sheets of corporate credit union service organizations.

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

CU SoCal strongly supports 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, I 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.

I urge NCUA to exercise its regulatory authority to update the capital framework for natural person credit unions to align with the broader financial sector by extending risk-based net worth to natural person credit unions.

6. Disclosure of Executive and Director Compensation

The requirement to disclose all compensation between a corporate and its senior executives—defined as a chief executive officer, any assistant chief executive officer (e.g., any assistant president, any vice president or any assistant treasurer/manager), and the chief financial officer—goes deeper than industry requirements for banking counterparts and, for a large, complex corporate with many vice presidents and assistant managers, could mean disclosure of compensation for non-executive staff. CU SoCal believes that this requirement goes well beyond expected and necessary practice. As NCUA has indicated that this provision mirrors IRS Form 990 with regard to information and access process, I believe it is sensible and desirable for NCUA to align its compensation disclosure requirements with IRS Form 990 guidelines.

Per IRS practice, I recommend that the definition of "senior executive" in this provision be modified to conform with Form 990 definitions (e.g., "officers," "key employees") and limitations (e.g., only over \$150,000 reportable compensation for key employees). Consistent

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with the Form 990 disclosure requirements, I would also advise NCUA to require compensation disclosures *upon request only* rather than require annual outward reporting of compensation which can be abused by the press to the detriment of the credit union system. Furthermore, corporates should only be required to honor compensation disclosure requests made by bonafide members of the corporate. In lieu of outward annual reporting of compensation information, I would support a requirement to annually announce the *availability* of compensation information upon member request.

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

I believe that NCUA should explore options for creating a line of defense between corporates and NPCUs. Although a number of Federal Home Loan Banks are known to have invested in similarly toxic securities and have found themselves in highly weakened capital positions, no credit unions nor their bank counterparts have lost stock held in FHLBs—a looming contrast to capital lost by NPCUs in the credit union corporate system.

In closing, CU SoCal thanks the NCUA Board for the opportunity to provide our concerns and recommendations regarding this very important rulemaking. I 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.

Sincerely,

A handwritten signature in black ink, appearing to read "Dave Gunderson", with a long horizontal flourish extending to the right.

Dave Gunderson
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Credit Union of Southern California

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