PEOPLES Choice Federal Credit Union

February 26, 2010

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

RE: Proposed Changes to NCUA Regulation 704

Dear Mrs. Rupp:

As a $60 Million natural person community-chartered credit union with 13,200 members, we are concerned by the idea that proposed Regulation 704 would increase capital requirements and introduce a risk-based capital scheme in addition to stricter forms of capital. Corporate credit unions may also require capital as a condition of membership. Another issue is the requirement that capital must be depleted when needed to cover losses by a corporate credit union. Further, as proposed, Regulation 704 gives NCUA the authorization to also establish stricter capital requirements at their discretion.

At a high level, the proposed NCUA Regulation 704 will result in price increases our credit union will have to pay to SunCorp Corporate FCU, lower the dividend rates we receive, that in turn will be passed on to our members. Along with the new capital requirements of Regulation 704, we do not believe credit unions will support this business model and as a result, corporate credit unions will cease to exist and credit unions will be forced to find new providers for settlement services, likely from our competitors in the for-profit banking industry.

As presented, it appears proposed Regulation 704 assumes it can prevent global systemic capital market failure and implies that capital investments and ownership are too risky. It is our opinion that risk should be managed, not eliminated. We ask that NCUA consider permitting corporate credit unions to assume some risk and higher return *OR* if the risk is to be reduced, require less return. We would also ask that the NCUA Board offer more choices and more flexibility in the proposed regulation related to risk.

One of the items referred to in proposed Regulation 704 deals with a Net Interest Income ("NII") Model (pgs. 99-101). The model makes the assumption that the deposit mix is 30% in overnight funds and 70% in term deposits, which appears to be counter to the goal of reducing longer-term investments in corporate credit unions. As presented, the model showed a positive net income of 0.21%. However, the model ignores the cost of new capital investments from credit unions. If this model included an allocation for new capital investments from credit unions to a level of "adequate capital" of 4%, we estimate net income would be reduced to 0.12%, below the rate of required capital as proposed. Using the assumptions presented, 10% of the investments held by the sample corporate were in Private Student Loan Asset Backed Securities with a Total Weighted Average Life of 0.500 and a yield of LIBOR + 200 basis points ("bp"). We do not believe this type of investment is appropriate for a corporate credit union and we do not believe the yield used in the example is representative of a long-run attainable return. Based upon a Bank of America historical analysis of other securities of this type, their spread history shows a six-year average of LIBOR + 157 bp with pre-August 2008 spread of LIBOR +30 bp. If an average yield of LIBOR + 50 bp was inserted into NCUA's model, net income would then result in a negative 0.03%. In other words, 10% of the model portfolio drives 59% of the net interest income and 39% of the bottom line. This modeling inconsistency is a key issue for us and we feel it should be addressed before any final action is taken on this proposed regulation. The proposed regulation states the model used shows that a corporate credit union can make sufficient money to become adequately capitalized. We believe the modeling assumptions used are not reflective of reality and if applied with more realistic assumptions, would result in corporate credit unions loosing money.

The Asset Liability Management ("ALM") area of the proposed regulation states that a corporate credit union must have a "sufficient amount of cash to support payment systems" yet "sufficient" is not defined in the proposed Regulation 704. An additional area of concern in this area is the requirement that the borrowing limit will be changed from the *greater* of ten times capital or 50% of capital and shares to the *lesser* of the same accounts. If rapid changes in the market occur as we have experienced in the not to distant past, this funding constraint could not only impact the corporate network, but also have an impact on natural person credit unions who are seeking liquidity from their corporate credit union.

Another area of concern in the ALM portion of proposed Regulation 704 is the limit that borrowing would be restricted to 30 days. This short time frame is very limiting and would be inefficient in certain market conditions. In reviewing an overview of areas addressed by proposed Regulation 704, only one percent was devoted to liquidity issues even though it impacts a critical amount of a corporate and natural person credit union day-to-day viability.

In reviewing proposed Regulation 704 on a "before and after" basis, it appears that NCUA is asking that corporate credit unions move from a "co-op pricing model" to a "market price, for profit model." While that may be fine for an ordinary business, these model assumptions are contrary to the founding and existing credit union philosophies and as a result, our credit union might have difficulty supporting.

It is our belief that another portion of the business model appears to be flawed. This deals with a fundamental investment principal that return is derived from risk taking. These "risks" include interest rate risk, credit risk, and liquidity risk. As proposed, the ability to obtain return from all three of these risks would be eliminated. Interest rate risk

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is eliminated by proposed stricter Net Economic Value ("NEV") tests. Also eliminated is credit risk as a result of the institution of concentration risk limits. Finally, liquidity risk is eliminated by the weighted average life constraint.

To address interest rate risk noted above, suggested solutions include the requirement of more capital, a reduction of the credit spread shock test from 300 bp to 100 bp and an increase in NEV volatility limit from 15% to 30-50%. With regard to liquidity risk, even a high level member of NCUA's staff stated, "if assets and liabilities are perfectly matched, it is almost impossible to generate a positive spread." With these types of comments from within NCUA, how does NCUA expect corporate credit unions meet the objectives outlined in the proposed regulation?

Based upon our services utilized and current account balances, our credit union pays approximately $25,000 per year in processing charges and spreads on deposits on our accounts at SunCorp Corporate FCU. In order to meet the new 4% requirement included proposed Regulation 704, it is estimated our credit union would either receive less income and or pay higher fees in the range of $6,000 to $12,000 per year to meet the new requirements. As a $60 Million credit union, this reduction of income or increase in expenses can and does make a difference in our bottom line and overall ROA.

In addition to the measurable dollar impact of the proposed regulation, natural person credit unions like ours will likely be required to hire additional staff and incur higher personnel costs to support some of those services previously provided by SunCorp if it ceases to exist.

SunCorp also provides us with no-cost staff training and timely information on many topics including proposed regulations such as NCUA Regulation 704, BSA and OFAC compliance, ACH compliance and audit review, funds transfer security, sessions providing economic updates and investment strategies, check conversions, branch capture options, in addition to other training needed for us to meet our regulatory requirements in addition to serving our members. Without SunCorp, we would have to look elsewhere in the financial services market place for this type of training and assume the cost of this needed training.

We would recommend that proposed Regulation 704 would 1): allow for managed risk and require more capital or 2): eliminate risk, but require much lower levels of capital. In addition, we would suggest NCUA consider the allowance for increased portfolio diversification to ensure dependable liquidity sources.

We recognize that some changes are necessary with the existing NCUA Regulation 704 and we support these efforts. This includes the need for more capital, tighter Asset Liability Management ("ALM") practices, more diversification of investment portfolios and more liquidity sources.

On the other hand, we believe there are some inherently significant errors and questions raised by NCUA's modeling techniques used in the proposed regulation. One very large issue for us as a [illegible] million credit union [illegible] is the fact that proposed Regulation 704 is [illegible] pages in length and NCUA is providing us only [illegible] days to read, understand, and project its long-term consequences.

Thank you for your time and consideration to review the important information contained in this letter.

Respectfully submitted,

Dale B. Springer
President/CEO

CC: Board of Directors, Peoples Choice Federal Credit Union
Senator Mike Johanns, Nebraska
Senator Ben Nelson, Nebraska
Representative Jeff Fortenberry

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