FORT KNOX FEDERAL
CREDIT UNION

WILLIAM J. RISSEL
PRESIDENT/CEO

CAROLYN F. DRAKE
EXECUTIVE VICE PRESIDENT

RAYMOND SPRINGSTEEN
SENIOR VICE PRESIDENT

March 2, 2010

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

Re: Proposed Corporate Credit Union Regulation 704

Dear Ms. Rupp:

On behalf of the Board of Directors and management of Fort Knox Federal Credit Union, I would like to express our appreciation to the NCUA Board for allowing us to comment on the proposed corporate credit union Regulation 704. Fort Knox Federal Credit Union is over $800 million in assets and has over 72,000 members.

We are currently a capitalized member of Kentucky Corporate Federal Credit Union. We also have transactional relationships, deposits, investments, and/or lines of credit with Southeast Corporate Federal Credit Union, Corporate One Federal Credit Union, and Members United Federal Credit Union.

While the proposed NCUA Regulation Part 704 contains some beneficial changes that will reduce risk and augment the value of corporate credit unions going forward (i.e. stronger capital standards, limits on investment concentrations, prohibitions on certain securities, and enhanced liquidity processes), the proposed rule contains several provisions which, left unchanged in the final rule, will significantly limit the value that corporates will be able to provide and even threaten the very existence of the entire corporate credit union system. We address each of these provisions below.

704.2 Definitions – Available to cover losses that exceed retained earnings
To the extent that any contributed capital funds are used to cover losses, the corporate credit union must not restore or replenish the affected capital accounts under any circumstances.

We do not understand the rationale for this definition. If the intent of this definition is not to reduce the capital level of a corporate credit union then this could be achieved by replacing the phrase, "under any circumstances" with the phrase "until a corporate credit union meets the well-capitalized level and any

P. O. BOX 900 RADCLIFF, KENTUCKY 40159-0900
PHONE (502) 942-0254 • FAX (270) 351-0258

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return of capital will not lower the corporate credit union's capital position below the well-capitalized level". If the agency's concern is safety and soundness, once a well-capitalized level is achieved, there will no longer be a safety and soundness issue.

Additionally, the regulatory mandate to permanently deplete capital based on estimated losses created by OTTI models with no ability for corporates to replenish capital back to existing capital holders, if actual losses are less than projected, is a major concern. GAAP does not require the treatment being applied by the NCUA, which is covered in the Letter to Credit Unions 09-CU-10 and now included in the revised definitions in the proposed rule. Further, as part of its Accounting for Financial Instruments project, it is likely that the FASB will change the credit impairment model standards in 2010 to allow OTTI reversals as loss projections improve. NCUA regulatory accounting treatment should allow for the same accounting treatment as national standards and not permanently deplete credit union capital based on projections which will continually change.

704.3 Corporate credit union capital
Effective [INSERT DATE 12 MONTHS AFTER DATE OF PUBLICATION OF FINAL RULE IN THE FEDERAL REGISTER], revise §704.3 to read as follows:
(a) Capital requirements. (1) A corporate credit union must maintain at all times:
(i) A leverage ratio of 4.0 percent or greater;
(ii) A Tier 1 risk-based capital ratio of 4.0 percent or greater; and

We have been told in several of your town hall meetings that the "leverage ratio" would not become effective until 36 months after the final rule has been published. However, in this section of the regulation (pages 152 and 153), it states that this part of the regulation would become effective 12 months after the final rule has been published. We ask that you make regulation to reflect the 36 month time frame, as it continues to be communicated to all credit unions by you, the NCUA.

In addition to the leverage ratio, we ask the NCUA to make the effective date of the Tier 1 risk-based capital ratio 36 months, the same as the leverage ratio. To require corporates to bring in new capital, or at a minimum convert existing MCA to the new PCC, could be difficult during a time when significant issues still remain with regards to legacy assets for some corporates. Raising contributing capital in such a short time frame will be challenging until corporate credit unions can demonstrate their business model will succeed under the revised regulation 704. Since it will be necessary to raise PCC for both the leverage ratio and the Tier 1 risk-based ratios, it makes sense to extend the effective date of both ratios to 36 months.

704.8(h) Two-year average life
(h) Weighted average asset life. The weighted average life (WAL) of a corporate credit union's investment portfolio, excluding derivative contracts and equity investments, may not exceed 2 years.

The impact of this part of the proposed regulation negatively affects a corporate credit union's ability to earn an adequate yield on its investment portfolio. One way a corporate credit union adds yield to its portfolio is to extend out the maturity ladder. This strategy has merit during certain interest rate environments. The current NEV testing required of corporate credit unions adequately measures and limits this risk. This WAL restriction will lower the yield a corporate credit union will be able to earn on its portfolio and will lead to lower rates available to natural person credit unions on corporate credit union certificates. We might note that this will be a significant competitive disadvantage to the banking industry; credit unions will be much more restricted in their investing choices than other deposit takers in the US economy.

A second effect from this part of the proposed regulation will be on the asset mix of a corporate credit union's investment portfolio. This weighted average life limit will make it very difficult for a corporate credit union to invest in agency mortgage-backed securities (MBS). While we realize certain MBS are the cause of the corporate losses, it was the private issue, non-agency mortgages that were the problem. Agency MBS are highly liquid instruments that can be easily sold if liquidity is needed. Unlike non-agency MBS, agency pass through securities continue to have very low credit risk and pose very little risk to a widening of credit spreads. There are very active and liquid markets for borrowing using agency MBS as collateral should liquidity needs arise. Had U.S. Central or other corporates bought agency MBS, my credit union would not be experiencing large insurance premiums or writing off our capital at my corporate. Agency MBS, used properly, are a prudent investment alternative for corporate credit unions just as they are for natural person credit unions.

We urge you to amend this section to allow a weighted average life of 3 years and that Agency and government-guaranteed securities be treated separately with a longer weighted average life restriction of 5 years.

Ability to grow retained earnings under the proposed investment and ALM limitations

Pages 99-101 of the NCUA proposed rule preamble contains an example of the ability to grow earnings under the proposed investment and ALM limitations. We believe this example does not represent an attainable or realistic outcome. The NCUA's example does not include any cost for new capital that must be attained. This capital should be well above market rates thus causing lower net income than reported in the NCUA's example. The assumptions on spreads and other factors appear to be unreasonable or unachievable.

We ask that you review the example provided and verify with outside sources to ensure these regulations allow for a viable business model for corporate credit unions.

704.8(k) Deposit Concentrations
(k) Overall limit on business generated from individual credit unions. On or after [INSERT DATE 30 MONTHS AFTER DATE OF PUBLICATION OF FINAL RULE IN THE FEDERAL REGISTER], a corporate credit union is prohibited from accepting from a member or other entity any investment, including shares, loans, PCC, or NCAs if, following that investment, the aggregate of all investments from that

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member or entity in the corporate would exceed 10 percent of the corporate credit union's moving daily average net assets.

The stated objective for limiting deposits from any one source to no more than ten percent of a corporate's assets is to reduce risks that arise from placing undue reliance on a single entity. However, if this limit is imposed, the only possible scenario going forward is that the credit unions will withdraw funds from the system. Of course, this decreases the liquidity in the corporate credit union network.

A credit union can choose to invest an unlimited amount of funds in a bank if they conduct proper due diligence. Why, then, should they be precluded from investing the same funds in another credit union (corporate or otherwise) if they conduct the same due diligence?

This part of the regulation should be removed.

Legacy Assets

This regulation does nothing to address the legacy assets that U.S. Central and some corporates hold on their books today. This is not a comfortable position for corporates or credit unions. NCUA's delay in detailing their plans for these legacy assets causes a corporate to defer any decisions or plans to move forward until this is resolved. These delays could cause issues for our corporates to meet the several capital goals in the near future, as mandated by the regulation.

Conclusion

There are a number of good proposals in these regulations in its current state, including: raising the capital requirements for entities with higher investment risks; reducing the use of short-term funding to finance longer term assets; and improving portfolio diversification. These provisions should remain.

However, there are also serious issues that must be addressed, as listed above. Any one of these new rules on its own would cause a major change to the operations of corporate credit unions which may threaten their very existence. Please consider my comments carefully to ensure a safe and sound corporate credit union network.

Again, thank you for providing us with the opportunity to respond to the proposed regulation.

Sincerely,

William J. Rissel
President/CEO