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January 24, 2011

Ms. Mary Rupp
Secretary
[redacted]
1775 Duke Street
Alexandria, VA 22314-3486

RE: NCUA Proposed Rule to amend Part 704 of the agency's rules on Corporate Credit Unions

Dear Ms. Rupp:

On behalf of the Credit Union National Association, below are our views on the National Credit Union Administration Board's proposal to amend Part 704 of NCUA's Rule and Regulations regarding corporate credit unions. CUNA's letter was developed with our Corporate Credit Union Next Steps Working Group, chaired by Terry West, President and CEO of VyStar Credit Union. By way of background, CUNA is the nation's largest credit union advocacy organization, representing about 90% of the nation's approximately 7,700 state and federal credit unions that serve more than 93 million members.

First, we appreciate the NCUA Board's decision to extend the comment period in response to the request from leagues and CUNA for additional time to formulate our comments in light of the significance of these issues and the numerous other regulatory proposals that are currently pending with NCUA and other agencies.

The Board issued the proposal in November 2010 to make further changes to the agency's regulation on corporate credit unions, subsequent to the dramatic amendments the Board adopted two months earlier. After careful consideration of the proposal, CUNA has a number of serious concerns that are addressed in this letter, and we urge the Board to make the significant changes we recommend before the rule is adopted in final form.

**Prohibition on Membership in More Than One Corporate Credit Union**

The proposal would prohibit natural person credit unions from maintaining membership in more than one corporate at any one time, with limited exceptions. One exception would be when a natural person credit union is transitioning from membership in one corporate credit union to another. Also, the prohibition would only apply prospectively and would not prohibit a natural person credit union from maintaining membership in multiple corporates so long as such relationships existed prior to the effective date of the final rule.

The proposal would prohibit a natural person credit union from making any new investment (including establishing a share or deposit account), loan to, or capital investment in a corporate credit union if the natural person credit union is not a member.

CUNA does not agree that this prohibition is sound public policy and urges the agency not to limit membership to one corporate credit union. We believe the better public policy would be to allow natural person credit unions to decide which corporates they want to join and to be able to support them without these membership limitations. This approach would benefit natural person credit unions as well as corporate credit unions and would not jeopardize the safety and soundness of either group of credit unions or the National Credit Union Share Insurance Fund.

In our view, only when an agency is directed by statute or imminent, overarching safety and soundness concerns should it impose regulatory limitations on activities that should otherwise be determined by the marketplace. This is certainly the case with the proposal to limit membership in corporate credit unions. These provisions needlessly remove the ability of each natural person credit union to have the latitude to exercise its business judgment to determine which corporates' services, rates, management, and record of financial performance fit with the credit union's business strategy. Flexibility for natural person credit unions to select more than one corporate would help them achieve their business goals and should be supported by the agency, not eliminated.

Also, allowing membership to be more open will help avoid a result in which natural person credit unions are held captive of an individual corporate, due to perpetual capital requirements and other considerations such as a natural person credit union having to move all accounts in order to get some services they find attractive from another corporate. We also think that limiting membership could ultimately serve to inhibit innovation at the corporates if they become complacent as a result of the natural person credit union membership restrictions.

In addition, allowing natural person credit unions to belong to more than one corporate will help provide broader support for corporate credit unions that are well-managed and are able to meet NCUA's requirements as well as the due diligence scrutiny of natural person credit unions.

It is our understanding that NCUA may be proposing this limitation to address competition among corporate credit unions regarding term deposit investments. We support and applaud that objective but believe the mechanisms to achieve the desired result have already been put in place with the earlier changes to the final rule. We also believe that it is unlikely that NCUA is overly concerned about whether a natural person credit union get its ATM services, for example, from one corporate and its check processing from another.

In consideration of these issues and concerns, we urge NCUA not to adopt the proposed prohibition on natural person credit union membership in more than corporate credit union.

If NCUA is convinced based on appropriate analysis that it must regulate in this area because its earlier amendments are insufficient, then we recommend that NCUA only prohibit a natural person credit union from obtaining term deposit investment services from multiple corporates, rather than adopting a general prohibition on multiple memberships. Natural person credit unions should be permitted to maintain existing relationships, as well as establish new ones, with more than one corporate for services other than such investments, such as settlement activities, overnight balances, and lines of credit.

**Corporate Credit Union Stabilization Fund Expenses – "Encouraging" Entities That Are Not Federally Insured to Contribute**

NCUA is proposing a regulatory process under which NCUA Corporate Credit Union Stabilization Fund expenses would be shared among all members of corporate credit unions—including all federally insured credit unions (FICUs) and non-FICUs. Under this process, when NCUA imposes a Corporate Credit Union Stabilization Fund (Stabilization Fund) assessment on FICUs, it would also require a corporate credit union to notify existing non-FICU members within 60 days, including non-FICUs and other entities such as credit union service organizations and credit union trade organizations that belong to a corporate credit union, that they should make a "voluntary" payment to the Stabilization Fund in an amount calculated as a percentage of the non-FICU's previous year-end assets. As proposed, if the non-FICU fails to pay the full amount within 90 days of the request, the corporate credit union must hold a membership vote on whether to expel the non-FICU member.

This proposal should be eliminated, first and foremost, because NCUA has no legal authority to assess a non-FICUs for any reason. Even if the equitable distribution of Stabilization Fund costs were a desirable goal, as addressed further below, in our view based on legal analysis, a process to impose assessments on non-FICUs will not withstand judicial review, also as discussed below.

Under the May 2009 and January 2011 amendments to the Federal Credit Union Act that established and modified the Corporate Credit Union Stabilization Fund, (*see* Pub. L. No. 111-22, Sec. 204 (2009), and Pub. L. No. 111-382 (2011), (both codified at 12 U.S.C. §1790e), NCUA may borrow funds from the U.S. Treasury to cover the costs of the Stabilization Fund , and federally insured credit unions must repay those borrowed funds; NCUA may also assess federally insured credit unions directly for the Stabilization Fund costs.

These statutory provisions could not be clearer that only federally insured credit unions may be assessed for such costs. For example, the newest provisions enacted this year, at 12 U.S.C. §1790e(d)(1),(2), and (3), lay out NCUA's authority to assess credit unions directly to pay for Stabilization Fund costs without having to borrow first from the U.S. Treasury. These provisions direct NCUA to assess each (federally) (parenthesis added) insured credit union -- and no other entities.

Also, the general mechanics of the Stabilization Fund as provided in the amendments reinforce the intent of Congress to confine the payment of its costs to FICUs. Prior to authorizing a payment from the Fund, the NCUA Board must certify that absent the existence of the Stabilization Fund, the payment would have been made from the NCUSIF. Clearly, only federally insured credit unions may be assessed for and contribute to the NCUSIF, and the funding mechanism of the NCUSIF was replicated by Congress in creating the Corporate Credit Union Stabilization Fund -- which functions in place of the NCUSIF to cover costs that would otherwise fall to the NCUSIF. Further, the assessments for Stabilization Fund payments are based on federally insured credit unions' insured shares.

Thus, there is no question that assessments cannot legally be levied on non-FICUs. To avoid direct conflict with the statue, the proposal seeks to dress up and present the assessments to non FICU members as "voluntary" payments. However, merely labeling the assessments as "voluntary" will not avoid the legal conflict, since the "contributions" would be treated by NCUA and considered by those paying them as assessments, since the proposal would impose sanctions, e.g., the loss of corporate credit membership, if desired payments from a non-FICU member are not made in a timely manner. In addition, the impact of the proposal for non-FICU members would be compounded if NCUA goes forward with the proposed provision to prohibit corporate credit union membership in more than one corporate.

Another concern regarding this provision is that it would require a corporate to serve as a “policeman” for NCUA and would place the corporate in a very burdensome and awkward position of having to pay for and executive a membership expulsion vote if the non-FICU does not pay its assessment. To avoid this situation, corporate credit unions may not want to provide services to non-FICUs, and non-FICUs could be forced to work with banks or other third parties. This result would be regrettable for the cooperative credit union system.

Despite CUNA’s strong opposition to this provision as proposed, CUNA recognizes that the provision raises an important issue of fairness and whether there should be some process for non-FICUs to contribute to the Stabilization Fund if they use the services of a corporate credit union.

This issue deserves careful consideration, including whether non-FICUs can or should be permitted to contribute, on a purely voluntary basis (both as to whether they will contribute and to the amount of their payments), to the Stabilization Fund, even though Congress could have included non-FICUs among those paying for corporate costs, and it did not. (The statute is silent as to whether contributions from non-FICUs for the Stabilization Fund should be permitted. Even though the statute does not address the issue of contributions from others for the Stabilization Fund, there is some support for the view that strictly voluntary contributions would be permitted under 12 U.S.C. §1772a, which authorizes gifts to NCUA.)

Thus, while CUNA strongly opposes the proposed, thinly veiled attempt to assess non-FICUs, which NCUA has no authority to do, we do support fairness for all credit unions, and in that context, we urge NCUA to work with the credit union system to consider a strictly voluntary system that would not result in any retributions, sanctions, or stigmas for those that do not chose to make a voluntary contribution or that base their contribution on their own evaluation of what is fair for them.

**Membership Fees**

Under the proposal, as a way to build retained earnings, a corporate credit union would be permitted to charge its members a mandatory one-time or periodic membership fee; the fee would need to be proportional to the member’s asset size. The corporate would have the ability to reduce the fee for members that have contributed capital to the corporate, and any reduction would be proportional to the amount of the member’s non-depleted contributed capital.

A corporate would be required to give its members at least six months' notice of any new fee, or material change to an existing fee. If the member fails to pay the fee within 60 days of being invoiced, the corporate would have the option to terminate the membership.

While each corporate should carefully determine the amount of such fees based on issues of need, efficiency, and fairness to its members, CUNA generally supports the ability of a corporate credit union to charge a one-time or periodic membership fee. In general, the characteristics of the fees should be determined by the corporate, in line with the views of its membership on such fees.

Also, as we have in the past, we urge the agency to revisit its interpretation that all federal credit unions (including corporates) are prohibited from charging membership fees; we can find no basis for the prohibition in the Federal Credit Union Act.

**Corporate CUSOs**

Under the final rule, a corporate credit union's auditor, board of directors, and NCUA would be permitted to have access to the corporate credit union service organization's (CUSO) personnel, facilities, equipment, books, records, and any other pertinent documents. Also, the corporate CUSO would be responsible for providing the corporate with data on the amount of compensation the CUSO paid to any of its employees who are also employees of the corporate.

Under the proposal, such highly compensated employees would be required to include in the annual disclosure, compensation paid from any corporate CUSO in which the corporate (employer) had invested or to which it had made a loan.

CUNA supports access to reasonable and appropriate information about a CUSO's operations for participating corporate credit unions. However, we still have a number of concerns about these requirements and about the proposal. One concern is that issues of piercing the corporate veil between a corporate and a corporate CUSO may arise because of the broad access to the operations of the CUSO.

There is also a concern that NCUA is attempting to expand its authority over corporate CUSOs without a sufficient legal basis or justification. Moreover, credit unions are concerned that the agency may also undertake this approach with natural person credit union CUSOs.

However, we understand that there may be circumstances in which NCUA has legitimate concerns about corporate CUSOs if safety and soundness issues arise. For those instances, we support increased access to information but only when there is a direct connection to materiality and risk, as opposed to a broad, across-the-board grant of authority.

In that regard we request that NCUA limit the reach of this provision to employees who receive “material” compensation, which we would leave to NCUA to develop a reasonable definition, and where the CUSO is wholly owned by the corporate.

**Board Responsibilities**

The proposal would require a corporate credit union to maintain a detailed record of each vote of its board of directors. The minutes reporting the vote would identify the board members, by name, who voted for or against the proposal, and any board members who abstained from or otherwise failed to vote. NCUA believes this provision is necessary to increase the transparency of corporate board actions.

NCUA also indicates that requiring recorded votes will help to ensure that corporate directors comply with their obligation to recuse themselves from deliberating and voting on items that may involve a conflict of interest.

CUNA fully supports board members fulfilling their responsibilities as required by their fiduciary duties and applicable laws and regulations consistent with reasonableness and practicality. However, we question the need to place these requirements in the rule because we are concerned they would subject corporate credit union directors to additional sanctions and fiduciary standards that do not apply to other corporate directors. Moreover, these are issues that should be addressed under a corporate credit union's bylaws, rather than by regulation.

**Audit and Reporting Requirements**

The proposal would make a number of detailed revisions to the audit and reporting requirements of corporate credit unions. A corporate would be required to ensure that its financial reports reflect all material adjustments necessary to comply with generally accepted accounting principles (GAAP) that were identified by the corporate’s independent public accountant (IPA).

Most notably, a corporate would need to prepare an annual management report, signed by the CEO and CFO, that contains:

- A statement of management’s responsibility for: (1) preparing financial statements, (2) establishing and maintaining an adequate internal control structure, (3) procedures for financial reporting, and (4) complying with safety and soundness laws and regulations designated by NCUA;

- An assessment of the corporate's compliance with such laws and regulations; and
- For corporates with over $1 billion, an assessment of the effectiveness of the internal controls and procedures over financial reporting, including identifying the internal control framework used to evaluate such internal control.

There would also be additional requirements imposed on a corporate regarding its IPA and a corporate would have to ensure that its Supervisory Committee: (1) consists of members who are not employees of the corporate; (2) supervises the IPA; and (3) ensures that audit engagement letters do not contain unsafe and unsound limitation-of- liability provisions.

NCUA currently requires that a corporate credit union's board of directors ensure the preparation of timely and accurate balance sheets, income statements, and internal risk assessments and that systems are audited periodically in accordance with industry standards. In addition, a corporate's supervisory committee must ensure that an external audit is performed annually in accordance with generally accepted auditing standards, and the audit report is submitted to the board of directors, NCUA, and the members.

In view of the accounting and report requirements that corporate credit unions must already meet, we believe these proposed provisions are unnecessary and unrealistic, and, we do not support them. While such requirements may be wholly necessary and appropriate for financial institutions that must directly comply with the FDIC rules and Sarbanes-Oxley, we disagree that their application to corporate credit unions is appropriate at this time.

**Enterprise Risk Management**

This provision would require corporates to develop and follow an enterprise risk management policy, and a corporate's board of directors would be required to establish an enterprise risk management committee to oversee the corporate's enterprise-wide risk management practices.

The committee would be required to include at least one "independent" risk management expert hired from outside the corporate with sufficient experience in identifying, assessing, and managing risk exposures. "Independent" would mean that the expert does not have any family relationships or material business or professional relationships with the corporate that would affect his or her independence as a committee member. In addition, the expert would be required to have: post-graduate education; an actuarial, accounting, economics, financial, or legal background; and at least five years' experience in identifying, assessing, and managing risk exposures.

Management of a corporate with at least $1 billion in assets would have the additional requirement of assessing and signing off on the effectiveness of the corporate's internal control structure and procedures for financial reporting.

Increasingly, enterprise risk management is being utilized by credit unions, particularly larger ones, as an important mechanism to ensure the organization has the proper, overall prospective on all of its risks and its capacity to manage those risks. We appreciate the value of enterprise risk assessments, and we agree that they can be very effective tools for management. This would include making sure the corporate has the ability to identify, manage, and correct material risks.

However, we do not think that the role of the Enterprise Risk Management Committee should be prescribed by the agency as it has done under the proposal. First, we do not think the Enterprise Risk Management Committee has been sufficiently distinguished from the function of the Supervisory Committee. Also, it is far from clear how the "independent" expert on the Enterprise Risk Management Committee would remain independent once he or she is compensated by the credit union. Further, we question whether a corporate credit union's use of enterprise risk management should more appropriately be included under the general assessment of the corporate credit union's management, as opposed to requiring a corporate credit union to follow the detailed directives under the proposal.

**<u>Conclusion</u>**

This proposal identifies several NCUA concerns regarding corporate credit unions. However, we believe a number of these issues have already been addressed sufficiently -- either in current requirements or in the new corporate rule adopted in September. CUNA supports key safety and soundness objectives that the proposal has raised but urges the Board to incorporate the improvements addressed in this letter when it approves the final regulation. Thank you for your consideration of our concerns and recommendations.

Sincerely,

Mary Mitchell Dunn

Mary Mitchell Dunn
CUNA SVP and Deputy General Counsel