Standards for Investment Pilot Program –
Investment in Mutual Funds Containing Instruments Otherwise Prohibited by Part 703

1. STANDARDS FOR THE CREDIT UNION

(a) Financial Condition

At the time of approval, the credit union must:

- Be classified as Well Capitalized under Part 702 for at least the preceding six (6) quarters;
- Have positive, stable earnings for the preceding 12 months; and
- Receive a letter of "no objection" from its Regional Office. The Regional Office will formulate its letter on the basis of financial condition and prior examination and knowledge of the credit union and on verification that the credit union has met the following policy standards. To facilitate verification, the credit union will submit a copy of relevant policies in its request to the region.

(b) Board of Directors

The credit union board of directors must adopt policies that address, at a minimum:

- The stated objective and the expected benefit of the credit union's investment in the mutual fund;
- Limitations on the mutual fund investments, including at a minimum:
    - *Investment pilot program limits:* An investment concentration limit not to exceed 25 percent of net worth;
    - *Specification of instruments and activities:* A description of the instruments in which the fund may invest;
    - *Price risk limits:* Limits on price risk (e.g., duration, convexity, value at risk) of the mutual fund;
    - *Rate risk limits*: Limits to loss from changes in interest rates based on net asset value (NAV) shock analysis provided by the management of the mutual fund or, where relevant, the third party applicant on behalf of a mutual fund; and
    - *Stop-loss limits:* A reasonable and supportable NAV loss limit that triggers a required liquidation of mutual fund positions. This limit may either be a single limit relating to the credit union's investment in the fund, or a schedule of limits requiring successive withdrawals.
- Daily measurement and monitoring of NAV;
- Monthly reports to the board on listings of fund composition, NAV, and mutual fund returns. These reports will include comparisons of actual vs. expected returns; and
- In cases where the credit union utilizes borrowings to invest in the fund, a cash flow analysis and contingency funding plan demonstrating that the

credit union will have sufficient liquidity to continue operations, assuming investment at a level of 100% of the maximum exposure in the fund.

(c) Internal Controls

Internal control procedures must be established that require, at a minimum:

- Daily assessment of NAV and reporting in relation to board approved limitations (see above) to the Chief Executive Officer; and
- Segregation of duties between risk assessors and risk takers, e.g., staff responsible for measuring compliance with board risk limits are not supervised by staff with investment authority.

(d) Investment Advisor Due Diligence

Before investing in a mutual fund, a credit union must verify and annually update that the fund's investment advisor continues to meet the minimum requirement specified in these standards for the amount under the investment advisor's management.

(e) Accounting

The credit union must report all mutual fund positions in its financial statements in accordance with GAAP.

(f) Agreements and Contracts

The credit union must retain a prospectus of the mutual fund and document compliance with its approved policies, specifically limiting the instruments and activities to those specified by policy.

2. STANDARDS FOR THE MUTUAL FUND

The fund will:

- Qualify and register as an investment company under Securities and Exchange Commission (SEC) rules and regulations.
- Purchase only such instruments as are specifically described and listed in its prospectus and are either permitted by NCUA Rules and Regulations Part 703 or included in the table of additional permissible investments and investment transactions below:

TABLE OF ADDITIONAL PERMISSIBLE INVESTMENTS AND INVESTMENT TRANSACTIONS

ACTIVITY	DESCRIPTION
1. Call or put option contract on a permissible investment, a derivative or security listed in this table, or a US. interest rate	The buyer of a call (put) option acquires the right but not the obligation to purchase (sell) a specified quantity of the underlying instrument at a stated price on or before a particular date. The seller of the option contract has the obligation to sell the underlying instrument to, or buy it from, the option buyer at the exercise price if the option is exercised.

ACTIVITY	DESCRIPTION
2. U.S. dollar interest-rate swap, also called a forward rate agreement (and options on this derivative)	Two parties agree to exchange periodic interest payments, based on reference interest rates and a reference principal amount. The reference interest rates are any two U.S. dollar interest rates, both a fixed rate and a variable rate, or two different variable rates. The reference principal amount is not exchanged (i.e., a notional principal). A forward rate agreement involves a single interest payment, rather than periodic interest payments.
3. U.S. dollar denominated total return swap (and options on this derivative)	Two parties agree to exchange periodic interest payments, as in an interest rate swap, and agree to a make or take one or more cash payments based on the difference in price of a reference instrument between two or more dates.
4. U.S. dollar interest rate cap (and options on this derivative)	Also called a rate ceiling, an interest rate cap is a series of call options on an interest rate, with the options cash settled. The buyer acquires the right to receive cash payments at specific time periods if the reference interest rate exceeds a specified level (i.e., the cap rate).
5. U.S. dollar interest rate floor (and options on this derivative)	Similar to a rate cap, an interest rate floor is a series of put options on an interest rate, with the options cash settled. The buyer acquires the right to receive cash payments at specific time periods if the reference interest rate declines below a specified level (i.e., the floor rate).
6. U.S. dollar interest rate collar (and options on this derivative)	A combination of an interest rate cap and an interest rate floor.
7. Treasury futures contracts (and options on these derivatives)	For a physical delivery contract, the buyer agrees to take delivery at contract expiration, and the seller agrees to make delivery at contract expiration, of a U.S. Treasury security specified as deliverable under the terms and conditions of the contract. For a cash-settled contract, a cash payment is made at expiration, based on the difference in price between contract date and expiration. The underlying instruments on Treasury futures contracts are U.S. Treasury bills, notes and bonds.

ACTIVITY	DESCRIPTION
8. Eurodollar futures contracts (and options on these derivatives)	A cash-settled contract in which the buyer agrees to make (take) a cash payment if the reference interest rate increases (decreases) and the seller agrees to the opposite, based on the difference between the purchase interest rate and the interest rate on a time deposit in a prime London bank at contract expiration. The reference interest rate is the London interbank offered rate (LIBOR), often called the Eurodollar rate. The underlying instruments on Eurodollar futures contracts include one-month and three-month bank time deposits.
9. Federal funds futures contract (and options on these derivatives)	A cash-settled contract in which the buyer agrees to make (take) a cash payment if the reference interest rate increases (decreases) and the seller agrees to the opposite, based on the difference between the purchase interest rate and an average interest rate on Federal funds transactions at contract expiration.
10. Short sales	The sale of a security not owned by the seller. To sell short, sell a security to a buyer, obtain that security by borrowing the security (securities lending) or entering into an investing repurchase transaction, and deliver the security to the buyer. To close out the short sale, purchase the security and return the security to the lender or repurchase counterparty.
11. Stripped mortgage-related and public mortgage backed securities	A collateralized mortgage obligation (CMO) that receives only principal payments (e.g., a PO), a CMO that receives only interest payments (e.g., an IO), or a mortgage obligation that substantively receives only principal or interest payments, that meets the other requirements for a mortgage related security, or is otherwise a permissible investment for a federal credit union, e.g., Government National Mortgage Association (Ginnie Mae), Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac).
12. Forward settlement	The purchase of a security for deferred delivery, later than a regular way settlement date.

- Provide to the NCUA within 120 days of calendar year-end after inception of any fund:
    - An annual financial statement audit performed by a licensed independent accountant in accordance with generally accepted auditing standards (GAAS), and presented in accordance with generally accepted accounting principles (GAAP);
    - An annual assessment by the fund's management of the effectiveness of internal control over financial reporting as of year-end;
    - A report by the fund's licensed independent accountant on management's assertion concerning internal control following either: Section 501 of the American Institute of Certified Public Accountants (AICPA) attestation standards, Reporting on an Entity's Internal Control Over Financial Reporting, commonly referred to as "AT 501", or if the fund prefers, the more robust "Public Company Accounting Oversight Board (PCAOB) Auditing Standard No. 2, An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements; and
    - A written report of material weaknesses and/or reportable conditions (management letter), if any.
- Allow for daily purchases and sales from the fund.
- Permit NCUA full access to the premises, books and records of those funds in which credit unions are invested (e.g., the registered investment company and the registered investment advisor) for purposes of inspection and review.

3. STANDARDS FOR A THIRD PARTY VENDOR

The third party vendor will provide to the credit union, if necessary by obtaining this from the investment advisor to the fund:

- The impact to fund NAV under +/-300 basis point shocks prior to purchase and monthly after purchase, effective once the fund has been established; and
- A complete list of the end of month composition of the fund to the credit union.

The vendor will provide a quarterly report to NCUA specifying participant credit unions and the dollar amount of investment in the mutual fund.

4. STANDARDS FOR THE ADVISOR

The advisor will:

1. Be a Securities and Exchange Commission (SEC) registered investment advisor; and
2. Have at least $5 billion under management.

5. TERMINATION OF AUTHORITY

(a) Termination of a Credit Union Investment

If the credit union is classified as less than Well Capitalized, the credit union will close out all positions obtained under the pilot program in a commercially reasonable manner (typically, one business day after the effective date of classification), and report the disposition of the mutual fund investment to the appropriate Regional Director within 30 days of the effective date of net worth classification (in 702.101(b)) as less than Well Capitalized. Approval under the pilot program will be deemed terminated.

(b)Termination of a Third-Party Program

In the case of third-party programs, where the credit union has knowledge of non-compliance with these standards, participating credit unions will close out positions in the mutual fund in a commercially reasonable manner (typically, one business day after knowledge of non-compliance).

(c) OCMP reassessment of the Pilot Program

OCMP will reassess the pilot program 3 years after the mutual fund becomes invested and no more than 5 years after the program is approved.

6. PILOT PROGRAM LIMITS

The number of federal credit unions participating in the program, through a third-party vendor, will be limited to a maximum of 75 participants, and to an aggregate investment of $1.5 billion, for each third party.