GEORGIA CREDIT UNION
Affiliates

6705 Sugarloaf Parkway, Suite 200
Duluth, GA 30097
(770) 476-9625 • (800) 768-4282 • (770) 497-9534 (Fax)

AMERICA'S
CREDIT UNIONS

July 25, 2013

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

RE: Comments on Derivatives Investment Authority

Dear Ms. Rupp,

The Georgia Credit Union League (GCUL) appreciates the opportunity to comment on NCUA's Derivatives Investment Authority. As a matter of background, GCUL is the state trade association and one member of the network of state leagues that make up the Credit Union National Association (CUNA). GCUL serves approximately 139 Georgia credit unions that have over 1.9 million members. This letter reflects the views of our Regulatory Response Committee, which has been appointed by the GCUL Board to provide input into proposed regulations such as this.

GCUL is generally supportive of credit unions being given authority to engage in derivative transactions as a means to hedge against interest rate risk ("IRR"). With that in mind, GCUL will support NCUA's efforts to authorize derivatives.

The proposal as issued limits credit unions' authority to "plain vanilla" derivatives instruments known as interest rate swaps and caps. These simple derivatives investments that NCUA is considering authorizing are transactions that have performed well over the last five or so years. And are not the kinds of financial transactions, such as credit default swaps that contributed to the financial crisis. We believe that the use of simple derivatives by eligible credit unions can be an important means to help manage risks associated with fixed-rate mortgage loans when rates begin to rise. In addition, the use of simple derivatives could likewise help to minimize risks to the NCUSIF and the credit union system generally. The fact that the agency has issued a proposal for comments indicates that NCUA recognizes the importance of tools such as derivatives to hedge IRR.

However, GCUL is concerned with the overall costs for credit unions to obtain derivatives bad authority. Several of the requirements are very costly and will be a huge barrier to credit unions applying for derivatives authority. GCUL believes that the approach laid out in the proposal requiring a credit union to comply with a number of

requirements before submitting an application to NCUA is unacceptable. This will front-load expenses and create huge start-up costs before the first transaction takes place.

GCUL opposes application and supervision fees, as the use of derivatives will help reduce risks to participating credit unions and to the National Share Insurance Fund. Credit unions should not be charged additional fees to take advantage of programs that will minimize risks. The imposition of separate activity fees would establish a dangerous precedent that could set the stage for fees for other activities that NCUA deems to be particularly risky.

The proposal, as is, would not permit a credit union that has less than $250 million in assets to apply for derivatives authority. Credit unions below the asset threshold have Interest Rate Risk and may benefit from using derivatives to hedge these risks The ability to meet reasonable requirements associated with derivatives authority will make the process self-selecting, and therefore NCUA should not establish an arbitrary asset-size prerequisite for otherwise qualified credit unions.

NCUA has not provided sufficient rationale for attaching investment limits to net worth. By tying limits to net worth, the credit unions that may need derivatives most will have lower limits. Another approach could be to allow credit unions to match derivatives to segments of their portfolios that create the IRR. GCUL urges NCUA to establish a meaningful and timely waiver process for any applying or participating credit unions that reasonably concludes it needs additional derivatives authority above what NCUA is proposing under Level II authority. We encourage NCUA to establish a Level III to provide more flexibility for credit unions to use derivatives. Duration limits should be extended under both Levels I and II to give credit unions more flexibility in matching derivatives to risks. We also believe the three business day settlement requirement is too restrictive and we oppose mark-to-market valuation limitations as a measurement of IRR management.

The experience requirements of the proposal are too rigid and inflexible for "qualified derivatives personnel." Level I and Level II credit unions should be allowed to contract with external service providers to conduct a wider range of services that the proposal would permit, and also help a participating credit union manage its derivatives program. We are concerned that very few credit unions will be able to meet all of the experience requirements.

The proposed rule would require that all applying and participating credit unions have an internal controls audit to be granted derivatives authority. This requirement is excessive and unnecessary for most credit unions. Experienced external auditors with derivatives experiences should be able to perform an appropriate audit that would provide reasonable assurances to NCUA that adequate internal controls are in place and that the credit union can safely engage in derivatives authority.

The limited number of pilot-program credit unions should be allowed to continue with their derivatives programs, to Level II authority, without having to reapply to NCUA. Reapplication would be needlessly expensive and unnecessary for credit unions that have already conduced derivatives transactions. Pilot-program credit unions should be allowed to use experience and other aspects of their participation in the pilot program to meet NCUA's regulatory requirements.

Credit unions should be able to outsource reporting requirements. The proposed rule creates reporting requirements for credit unions that will require expensive infrastructure and personal skill to maintain.

The proposed derivatives rule allows a wholly-owned CUSO to perform functions required by the proposed derivatives rule, but does not allow a CUSO owned by more than one credit union to perform similar functions. All CUSOs should be allowed to perform these functions regardless of how many credit unions own the CUSO. Level II credit unions should have the same ability to rely on ESPs (External Service Providers) as Level I credit unions. The proposed rule allows Level I credit unions to use ESPs to conduct far more activities than Level II credit unions. We feel this requirement is not necessary.

State chartered credit unions are required to comply with NCUA's derivatives rule or their state rule if that state rule is more stringent. GCUL opposes this requirement because it takes authority away from individual state regulators and would adversely impact the dual chartering system. We believe that some coordination between a state regulator and NCUA is important for the efficiency of the NCUSIF; however, we feel that NCUA should not override the authority of state regulators to impose its rule on state credit unions.

Finally, we believe the proposed legal review requirements are too restrictive and do not reflect the realities of the simple, plain vanilla type derivative transactions that would be authorized for credit unions. NCUA should minimize the legal review requirements and allow credit unions to detail for themselves in their board policy how they will implement legal review requirements.

In summary, GCUL does support allowing credit unions to engage in derivative transactions and we support the agency's efforts to move forward with a derivatives rule. But as we have mentioned above, we have many concerns with the proposed rule as drafted and would like to see some further revisions to the rule so that credit unions will consider using them as investments to their IRR.

GCUL appreciates the opportunity to present comments on behalf of Georgia's credit unions. Thank you for your consideration. If you have questions about our comments, please contact Selina Gambrell or Cindy Connelly at (770) 476-9625.

Respectfully submitted,

Selina M. Gambrell
Compliance Specialist