

January 05, 2015

National Credit Union Administration  
Office of General Counsel  
1775 Duke Street  
Alexandria, VA 22314-3428

RE: Comments on Proposed Rule—Corporate Credit Unions

Dear Office of General Counsel,

Thank you for the opportunity to comment on the proposed changes to 12 CFR Part 704 Rules and Regulations for corporate credit unions. As presented in the summary, the proposal clarifies certain provisions of the rule and makes several non-substantive and technical corrections. By way of background, the League of Southeastern Credit Unions & Affiliates (LSCU) is one of the nation's largest credit union advocacy organizations. LSCU currently represents more than 285 state and federal chartered credit unions which serve more than 6 million members.

Overall, we generally agree with the proposal as presented. However, a review of the proposal indicates to us the need to consider several additional items that address technical issues or are revisions we believe the NCUA Board would be well served by considering. While not currently included in the proposed rule, however, we would ask that the Board consider their overall benefit and consider their merit. Corporate credit unions have long provided critical payment, liquidity, and investment services to our affiliate credit unions and our comments are aimed at improving their ability to provide these services while at the same time mitigating risks.

NEV-related measures including the weighted average life - 704.8(j)

We agree that the current language in 704.8(j) is in need of additional clarification. As currently written, the regulation is not clear as to when a WAL violation has taken place. The regulation seems to offer a safe haven via a 10 day cure period, and if corrected within this time a notice of violation to its Board of Directors or the NCUA appears unnecessary. Given the role of corporates as payment providers to credit unions, there are regular and significant share balances fluctuations occurring throughout the month. The change in share balances understandably effect the cash of a corporate credit union. As a result, the WAL of a corporate's assets often fluctuate significantly based on nothing

more than the day of the week, the month or quarter ends.

Section 704.8(j) of the regulation currently provides 10 days for a corporate credit union to adjust the balance sheet to satisfy the requirements of the WAL and other NEV-related measurements. The clarification in the proposed rule recognizes the role corporates play with respect to payments processing and reiterates that the 10 days is part of the testing period. The regulation was obviously written to address the volatility in the WAL and other NEV-related measures due to the specific day of the week that the testing occurs.

Given that the NCUA has urged corporates to become more liquid and more focused on settlement payments, a reasonable solution to address the volatility in settlement dollars resulting from the day of the week the testing occurs is warranted. A WAL measurement based on a snapshot of one day is obviously an inappropriate regulatory tool, especially one for which prompt corrective action can be invoked. Based on these circumstances, we support the rule clarification as presented in the proposal.

#### Secured Borrowings - 704.9(b)(1)

This section of the rule contains a rigid prohibition on secured borrowing for periods in excess of 30 days. It is our understanding is that this is based on the desire to avoid the widespread use of borrowing to finance long-term assets. The consequence of the 30-day limit however, is a limitation on a corporate's ability to fund seasonal outflows of liquidity and it also removes a source of liquidity for credit unions in the event of an unforeseen liquidity crisis. The proposed rule seeks to maximize the borrowing limit from 30 days to 120 days. We consider the 30 to 120 days a fair adjustment but would not be averse to an even longer period. Additional time made available to corporates would server to improve their ability to fund affiliate credit unions' liquidity needs. Many industry leaders consider a time period of from 6 months to 2 years as reasonable. We believe the most appropriate time frame to be somewhere in this range. In addition, the liquidity challenges of 2008-09 taught us that there are times when an even longer period may be appropriate, with special approvals issued.

Based on this information, we support a rule revision for Section 704.9(b)(1) and urge the NCUA to expand the limit from the currently proposed 120 days to up to 2 years. We also strongly recommend that this section be rewritten to include language providing the NCUA Board or Office of National Examinations and Supervision (ONEs) the authority to suspend the rule to allow for longer secured borrowing periods in order to support potential systemic liquidity event in the future.

## Issues Not Present in Current Proposed Rule that Warrant Additional Consideration

### 1. Weighted Avg. Life (WAL) Treatment for Govt. Issued/Guaranteed Securities - 704.8(h)

Part 704.8(h) of the NCUA Rules and Regulations states that the WAL of investments that are issued or fully guaranteed as to principal and interest by the U.S. Government, its agencies or sponsored enterprises, including investments that are fully insured or guaranteed (including accumulated dividends and interest) by the NCUSIF or the Federal Deposit Insurance Corp, will be multiplied by a factor of .50 for purposes of the WAL tests of paragraphs (f) and (g) of this section.

Government guaranteed securities exhibit little or no credit risk, are considered highly liquid in the marketplace, often serve as buffers in times of economic stress, and are valuable collateral for liquidity in the capital markets and at the Federal Reserve Bank. With this in mind, we believe that the one-half WAL treatment is insufficient incentive for buying these securities. We think the factor included in section 704.8 (h) would be more effective if it is weighted as a cash equivalent and this is a consideration worth review by the board.

We are not seeking a revision by the NCUA Board of the WAL measurement for credit related securities or NCUA Rules and Regulations Part 704.8(f) and Part 704.8(g), but we are urging the Board to consider an exclusion of government guaranteed securities from this risk measurement in NCUA Rules and Regulations Part 704.8(h). It is reasonable to us that assigning WAL limits on government guaranteed instruments can be viewed as technically flawed. The longer WAL government guaranteed securities can exhibit more interest rate risk than credit exposed shorter WAL securities, but the NEV ratio and NEV impairment testing required within NCUA Rules and Regulation Part 704.8(d) already capture and limit the amount of interest rate risk a corporate credit union is permitted to take.

We therefore urge the Board to modify section 704.8(h) to multiply the WAL of government issued or guaranteed securities by a factor of zero. Further, we ask that all asset-backed securities comprised of collateral issued or insured by the US Government, or one of its Agencies, be provided a WAL treatment similar to government securities, up to the portion of the collateral that is guaranteed.

### 2. Investments - Section 704.5

The ability of corporates to invest in Government Sponsored Entity (GSE) mortgage-backed securities is currently permitted via section 704(c)(1), where it refers to the Federal Credit Union Act as to our permissibility of agency securities: (1) Securities, deposits, and obligations set forth in Sections 107(7), 107(8), and 107(15) of the Federal Credit Union Act, 12 U.S.C. 1757(7), 1757(8), and 1757(15), except as provided in this section; Section 1757(7)(c) of the Federal Credit Union Act states: "in obligations of the United States of America, or securities fully guaranteed as to principal and interest..."

This definition was based on past issuance rules for agency securities. However, the recent financial crisis and the changing regulations that continue to this day can be expected to change how GSE mortgage-backed securities are issued going forward. It is expected that in the future most, if not all, GSE mortgage-backed securities will have some form of credit sharing with investors. If corporates are not authorized to participate in the purchase of any of the credit sharing deals in the future, they will be excluded from providing liquidity to the mortgage market, including providing liquidity for natural person credit unions as well. Current regulations do not permit corporates to engage in an agency risk sharing structure because the arrangement must reflect a 100% guaranteed by a GSE.

As a requirement of Dodd-Frank, GSE's must now create risk sharing structures and as a result have to this point only issued subordinate certificates in which the performance and cash flows are tied to a pool of mortgage collateral. With that in mind, it is our understanding that the GSE's are now also required to structure other types of deals, such as insured, senior/sub, etc. A recent quote from a Barclay's research piece offers more detail:

"The FHFA has set a \$90 billion target for risk transfer in 2014. Each enterprise must utilize at least one transaction type in addition to the STACR or CAS structures (e.g., insurance, upfront credit risk transfers, and senior/subordinated securitizations). FHFA will provide extra scorecard credit for completing any additional types of transactions beyond the first two. This suggests that risk transfers other than CAS/STACR and insurance policies (senior-sub, for example) are likely." *The STACR and CAS are FNMA and FHLMC's subordinate certificates that have been issued to date.*

Without a modification to Regulation 704, corporates will likely see increased limits on access to government issued mortgage-backed securities. The impact of this is magnified by the fact that the mortgage market is a very big contributor to our nation's economy and a big component in how corporates provide liquidity to credit unions that sell to the GSE's. We are not requesting the approval of additional GSE structural rules; however, we urge the agency to

consider this opportunity for corporate credit unions when the market is more clearly defined.

With GSE mortgage-backed securities currently being re-structured they may, upon completion, no longer meet the definition provided in the Federal Credit Union Act. Should this occur, we request that NCUA consider adding to 704.5(c)(1) the following: "or a senior tranche of a credit risk sharing GSE security as long as it has no more than a minimal amount of credit risk."

## Conclusion

We appreciate the opportunity to comment on this proposal and hope our views are helpful in crafting a reasonable and efficient rule through which corporate credit unions can effectively operate. If you have questions regarding our comments, please feel free to contact me directly at (205) 437-2165.

Thank you for the opportunity to comment on this Proposed Rule and for considering our views on corporate credit unions.

Sincerely,

Scott Morris  
Director of Regulatory Advocacy  
League of Southeastern Credit Unions

cc: CUNA, CCUL