

May 8, 2017

Gerald Poliquin  
Secretary of the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, Virginia 22314-3428

RE: Comment on Advanced Notice of Proposed Rulemaking for Alternative Capital

Dear Mr. Poliquin:

The American Bankers Association appreciates the opportunity to provide comments on the National Credit Union Administration (NCUA) Board's (the Board) Advanced Notice of Proposed Rulemaking (ANPR) regarding alternative capital for federally insured credit unions.

The American Bankers Association believes that allowing credit unions to issue alternative capital would be inconsistent with the purpose of their charter, undermine the foundation of their tax exemption and introduce potentially significant safety and soundness concerns to their balance sheets. Furthermore, the NCUA lacks legal authority to allow complex credit unions that are not low-income designated to issue alternative capital to meet risk-based net worth ratio requirements. The ABA feels strongly that no further action should be taken and no proposed rule advanced. Instead, NCUA should be encouraging—and facilitating—conversions of credit unions to federal mutual savings bank charters should these institutions wish to expand their access to capital or their scope of operations.

### **NCUA Lacks the Legal Authority to Permit Issuance of Alternative Capital**

The FCUA defines a credit union's capital level based on a net worth ratio requirement for all credit unions and a risk-based net worth ratio requirement for credit unions the Board defines as complex. The FCUA specifically limits net worth to a credit union's retained earnings. This restriction was intentional, designed to restrict a credit union's ability to access capital markets. The definition was intended to carry throughout the FCUA and limits the discretion granted to NCUA in formulating the risk-based net worth requirement as well as the net worth ratio.

The risk-based net worth requirement specifically contains the language "net worth." By allowing alternative capital to be counted towards the risk-based net worth requirements for complex credit unions, the Board is seeking to rewrite the FCUA to expand the numerator of the risk-based net worth ratio to include items that are not part of the statutory definition of net worth. If Congress intended to allow complex credit unions to issue alternative capital, it would have authorized secondary capital when it enacted Section 1790d(d) of the FCUA in 1998.

### **Alternative Capital Threatens Tax Exempt Status of Credit Union Industry**

The FCUA specifically exempts federal credit unions from taxation by federal, state or local taxing authorities, with the exception of real and personal property taxes. Federally insured state

chartered credit unions are exempt from federal income tax under §501(c)(14)(A) of the Internal Revenue Code (IRC). Section 501(c)(14)(A) of the IRC provides for exemption from federal income taxes for state credit unions without capital stock and organized and operated for mutual purposes without profit.

The Board recognizes that supplemental capital could have an impact on the entire credit union industry's tax exempt status. The ANPR states "that part of the basis for the credit union tax exemption was that Congress recognized most credit unions could not access the capital markets to raise capital." If the credit union industry had the ability to access capital markets to raise capital, it would rightfully call into question the industry's tax exempt status.

Furthermore, alternative capital places an even greater risk to the tax exempt status of federally insured state chartered credit unions whose tax exemption is tied to being "without capital stock" through the IRC. The Board acknowledge that in some states it is possible that alternative capital instruments issued by federally insured state chartered credit unions could have characteristics of capital stock, which would subject these credit unions to taxation.

#### **Alternative Paths for Institutions Who Have Outgrown the Credit Union Charter**

Available data suggests there is little demand for alternative capital instruments. Credit unions have enough capital to meet healthy organic growth needs and do not need the threats that coincide with alternative capital, such as losing the industry's tax exempt status.

For the limited number of credit unions seeking alternative capital or unconventional growth strategies, there are other paths which would better serve their customers, better address safety and soundness concerns, and be within the legal boundaries of the FCUA. One such path: Allow credit unions who have outgrown the credit union charter to more easily convert to a federal mutual savings bank charter. Such a charter allows the credit union to maintain its cooperative ownership and mutual structure, while expanding its abilities to grow with its community.

#### **Conclusion**

In conclusion, the American Bankers Association believes that the NCUA lacks legal authority to allow complex credit unions that are not low-income designated to issue alternative capital to meet risk-based net worth requirements. Furthermore, the issuance of alternative capital would remove any remaining justification for the credit union tax exemption. Instead of manipulating the language of the FCUA to support unsanctioned growth of the credit union industry, the Board should support charter conversions as institutions outgrow their credit union charters.

Sincerely,



Brittany Kleinpaste  
Director of Economic & Policy Research