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September 5, 2017

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

Cooperative Credit Union Association, Inc. Comments on Notice and Request for Comment on Closing the Temporary Corporate Credit Union Stabilization Fund and Setting the Share Insurance Fund Normal Operating Level

Cooperative Credit Union Association, Inc. Comments on Notice and Proposed Rulemaking on Requirements for Insurance; National Credit Union Share Insurance Fund Equity Distributions RIN 3133-AE77

<u>BY EMAIL ONLY</u>

Dear Secretary Poliquin:

On behalf of the member credit unions of the Cooperative Credit Union Association, Inc. ("Association"), please accept this letter relative to the National Credit Union Administration Board's ("NCUA") Request for Comment on Closing the Temporary Corporate Credit Union Stabilization Fund and Setting the Share Insurance Fund Normal Operating Level, and Notice and Proposed Rulemaking on Requirements for Insurance; National Credit Union Share Insurance Fund Equity Distributions. The Association is the state trade association representing credit unions located in the states of Delaware, Massachusetts, New Hampshire and Rhode Island, serving approximately 195 credit unions which further serve approximately 3.8 million consumer members.

In preparation for the development of the present comment letter and to foster a local consensus, the Association conducted a survey of all credit union members in order to obtain member credit union input across four states on the NCUA's proposed plan to close and merge the Stabilization Fund into the Share Insurance Fund, and how member credit unions envisioned an equitable distribution within the bounds of safety and soundness.

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In summary, the Association and its members support the closure of the Stabilization Fund and merger into the Share Insurance Fund, with a raising of the normal operating level to 1.39 percent, with a planned glide path return to 1.30% over time.

I. The NCUA Board Should Merge the Funds and Set the NOL at 1.39 Percent

The Association supports closing the temporary corporate stabilization fund ("SF") and thereby merging it with the National Credit Union Share Insurance Fund ("SIF"). Survey respondents unanimously indicated that they would like to see the SF closed prior to the currently scheduled date of June 2021. Nearly all members agreed that the SF should be closed this year and merged into the SIF. While one member did express concern over moving too quickly simply to close the SF in 2017, the Association understands the motivation behind and administrative need to move forward with the closure of the SF this year. While we also echo the concern that the turnaround time for the industry to respond to the NCUA's proposal was shorter than would be ideal, the Association continues to support closing and merging the SF as proposed this year.

The reasons behind member support for the closure and merger of the SIF are various, and reflect the Association's position of support. Member credit unions expressed: desire to reduce the possibility of a SIF assessment; belief that the SF has exceeded expectations, and that combining the two will enhance efficiencies, strengthen the Fund, and provide for some refund to the credit unions; support for the projected performance of legacy assets and the subsequent need to refund overpayments made by credit unions to the SF; the need for the capital by credit unions that are operating today, rather than a forward-looking projection which entails unknowns; and the equitable solution of returning the current surplus of funds to credit unions so that they can serve their members better in the here and now.

Under the proposal, the NCUA is asking credit unions to forego some of their returns from the SF in order to provide funding now for the SIF to handle projected problems in the future. Through this process, credit unions should be able to avoid having to pay insurance premiums for the foreseeable future, absent catastrophic economic events.

Members were asked to respond to the premise that while merging the SF and the SIF in 2017 guarantees there will not be an SIF premium assessment in 2017, there is a possibility that an assessment could be necessary at some point in the future if the assets in the stabilization fund deteriorate between now and 2021 when they fully mature. 76% percent of respondents indicated that they would rather see the funds merged sooner to guarantee no assessment in 2017 and manage a potential premium assessment in future years if the stabilization fund assets deteriorate.

Member credit unions were also asked that if legal authority exists to make distributions to insured credit unions from the SF, whether they would prefer that the Board make such a distribution, or close/merge the two funds. Input on this concept varied. While the Association reiterates its understanding of the significance of the overall plan and support of the basic approach of merger and temporary increase of the NOL, member credit union input is of highest priority, and the following comments from members may prove illuminating to the NCUA Board.

Nearly 60% of member respondents indicated that they would support an immediate distribution. Those members' comments reflected the Association's concerns that the 1.39% level on a permanent basis is too high, and is based on uncertain events for an uncertain time; therefore, an immediate distribution, allowing credit unions immediate access to capital to provide better services to members, was the desired outcome. Comments revealed that there is support for returning the funds to credit unions now to better serve members than waiting for a deterioration that may never happen. Operating in a flat yield curve further compresses member credit union margins; credit unions need relief sooner rather than later. In addition, the NCUA can impose an assessment on credit unions when they feel it is needed, and at a level determined appropriate.

Members further noted that the two concepts should be treated separately and distinctly: if the purpose of the Fund has been met, then the remaining funds should be returned to credit unions, who need the funds sooner rather than later.

Of the nearly 40% of members who indicated support for a closure/merger, comments again expressed the Association's position that a safe operating level is necessary and must be set at an appropriate threshold to comfortably cover any economic downturns. In addition, this approach provides an opportunity to further strengthen the SIF and eliminate the need for an assessment.

The Association appreciates the significance of the overall plan proposed and supports the basic approach presented, which we believe reflects prudent planning on the NCUA's part and could facilitate the ability of credit unions to perform well during a recession to the extent they are able to avoid additional expenses of insurance premiums. There are also benefits of this approach which should resonate well with key government policymakers, because we believe it demonstrates the agency's ability to be forward thinking and plan well ahead of anticipated problems.

In supporting the closure and merger of the SF, the Association also supports setting the normal operating level ("NOL") of the SIF at an appropriate amount to provide an additional cushion of resources for a reasonable period of time. Without question, our members are concerned that an appropriate safety and soundness balance is struck in the selection of an adequate NOL that would avoid excess funding for the SIF, which could result in unnecessary, negative consequences for the agency and for insured credit unions.

We note that the agency undertook rigorous analyses to derive its numbers relative to the NOL and the components included in the increase: (a) 4 basis points over 1.30% to account for legacy asset volatility; (b) another 2 basis points for the expected decline in the equity ratio of the SIF over the next two years due to insured share growth and low yields on the Fund's investments; and (c) another 3 basis points to keep the equity ratio from falling below 1.2% over the next five years if there is a moderate recession.

While future recessions are inevitable, no one knows for sure when the next one will happen, how acute it will be, or its impact on credit unions. The Board has attempted to take that factor into consideration by using projections based on a moderate recession but even with its comprehensive analysis, at the end of the day, the proposed increase to 1.39 percent is based on uncertain events for an uncertain time.

Even so, we strongly agree that the SIF must be prepared for the next down cycle. However, we request that the NCUA provide assurance to credit unions that there is no redundancy in taking account for the impact of a potential the recession regarding these components resulting in excessive funds in the SIF. Therefore, the Association would not support the proposed NOL if it is based on inflated assumptions that may result in overcompensating for the unknown impact of a recession which may already have been built into the increases tied to the volatility of legacy assets as well as to a decline in the equity ratio to the 1.2 level. In supporting the 1.39% NOL, the Association acknowledges, quite frankly, that credit unions remain concerned that if faced with more than ample resources, the agency will be enticed into over spending and justifying additional costs, to the detriment of the publicly stated goal of Chairman McWatters of enhanced accountability and transparency for federally insured credit unions.

For these reasons, the Association supports an increase in the NOL to 1.39 percent, which we believe will produce adequate funding for the SIF to be well positioned for the next several years. This level also allows federally insured credit unions to have access to a sizeable portion of their assessments, which they can make use of to meet members' needs and support their own operations.

At the same time, the Association opposes keeping the NOL at that level any longer than is actually needed, and as discussed below, urges the Board to make the increase temporary with a plan to return to 1.30% by 2021.

II. <u>The NCUA Board's Final Plan for the NOL Must Include A Glide-Path to Return to the Current 1.30%</u>

The Association is very concerned that at whatever level the NOL of the SIF is set, that it not become the new normal. Since the NCUA Board may not charge an SIF premium when the NOL exceeds 1.30%, there is some credence to the argument that the Federal Credit Union Act generally recognizes 1.30% as the standard, although the Board may raise it to 1.50%.

Nearly all member credit unions agreed that while a temporary increase in the NOL may be necessary, they also believe that a tiered path back down to 1.30% in 2021 when assets mature is essential.

To address the concern that the NOL return to 1.30% as soon as possible, the Board should, as part of the final rule, include requirements that it will revisit the increased NOL after two years. The final rule should state that at that time, the Board will specifically consider whether the NOL can be returned to 1.30% or reduced somewhat as a step toward returning to 1.30%. The final rule should provide that the Board will rely on comprehensive economic analyses relative to a recession, the performance of the legacy assets, and the financial condition of the SIF in revisiting the NOL.

Unanimously, member survey respondents indicated that the NCUA should revisit the NOL periodically given it can be changed at any time. The proposal is based on a five-year time horizon, equating generally to the historic life cycle of recessions. However, no one knows when the next recession will start or stop. In light of the uncertainties regarding a future rescission, we urge the Board not to commit to a five-year time frame but to gear the NOL to two years, after which the return of NOL to its current 1.30% would have to be reconsidered by the Board.

Members also supported either a public comment period, or a mandatory notice period for credit unions. All indicated that greater transparency and credit union participation in agency reviews are positive and should continue. While a rule change will likely be necessary at that time, the Association believes that the process should be expedited as the agency has done in raising the NOL.

Finally, the Association notes that members were asked to consider that given that a higher overhead transfer rate ("OTR") could reduce the dividends that credit unions will receive back from the SIF due to a merger of the funds, should the agency treat the OTR calculation differently during this time of an elevated operating level. 74% of respondents indicated that the NCUA should adjust the OTR based on the merging of the funds. Comments included the following:

> -Given the volume of funds under discussion, I would certainly expect that NCUA would review and revise the OTR calculation as necessary to ensure that the merger does not provide cover for any unnecessary adjustment.
>
> -Yes, the OTR should be about the same amount in dollars as the prior year and not a percentage.
>
> -It appears obvious there would be less risk.

III. <u>Share Insurance Fund Distributions Should be Last In, First Out</u>

In a separate rulemaking, the Board is requesting comments on how to make distributions from the SIF, including those that result from closing the SF and transferring its assets to the SIF. For greater efficiency, the Association is including its comments on some of those key issues in this letter, and respectfully requests the Board to consider them.

Closing the SF and winding down the Corporate System Resolution Program will require NCUA to transfer all remaining funds, property, or other assets remaining in the SF to the SIF, which will trigger a significant SIF equity distribution. Winding down of the Corporate System Resolution Program will also trigger future SIF equity distributions as the NCUA Guaranteed Notes ("NGNs") mature. Given the potential size and complexity of these transactions, the Board proposes to adopt a temporary provision to NCUA's share insurance requirements rule to govern an SIF equity distribution resulting from the Corporate System Resolution Program.

The Association supports the Board's position that any SIF equity distribution related to the Corporate System Resolution Program should first go towards repaying those federally insured credit unions that paid special premiums, rather than taking the form of a general proportionate distribution to current federally insured credit unions. In response to the Board's specific request regarding equity distributions related to the Corporate System Resolution Program, projected to be in the form of a series of SIF equity distributions repaying any corporate assessments against federally insured credit unions that paid them, the Association strongly supports a last-in, first-out ("LIFO") approach.

Under a LIFO approach, the Board would make an SIF equity distribution to each FICU up to the total dollar amount of assessments paid by that federally insured credit union during the relevant assessment period beginning with the last period. The Association and its members favor the LIFO method because it ensures that FICUs receive SIF equity distributions for their most recent corporate assessments first, with smaller assessments that took place at the start of the Corporate System Resolution Program being repaid over time as the NGNs mature.

The Association supports the agency's efforts to make distributions from the SIF as fair as possible to all federally insured credit unions. In that connection, the Association agrees that limiting distributions made possible by closing the SF to those federally insured credit unions who actually paid corporate stabilization assessments is reasonable. We also agree that there are no impediments in the Federal Credit Union Act that would prevent the agency from using the LIFO approach. We do not think that liquidation estates that have been closed should receive distributions resulting from the SF transfer since the decision to liquidate such credit union likely did not anticipate a possible distribution.

The Association considers this overall distribution approach to also be the most equitable as it is not contingent on asset size. Therefore, it ensures that all credit unions, especially smaller credit unions, have an equal return on assessments they paid in an orderly manner.

IV. Greater Transparency of Legacy Assets and Increased Reporting is Required

The Association recognizes that NCUA is committed to ensuring full transparency throughout the Corporate System Resolution Program. To that end, two websites were launched to provide up-to-date information on both the Corporate System Resolution and the NGN Program. In particular, NCUA created the NGN Program to provide long-term funding for distressed investment securities ("legacy assets") from five failed corporate credit unions. NCUA designed both websites to distill complex information and convey it in simple terms to stakeholders, using graphics and visual charts in addition to data tables and descriptive text.

While these efforts, combined with quarterly NCUA Board reporting, are steps in the right direction, the Association strongly urges NCUA to further promote greater transparency with legacy assets and therefore, greater integrity in the system as it draws to conclusion. More regularly reporting and replenishment of updated information on the websites should be adopted and made readily available to stakeholders. Such changes will serve to reinforce the NCUA's safety and soundness responsibilities and primary fiduciary responsibility to credit union members.

V. Conclusion

In sum, the Association and its members support the closure of the SF and merger into the SIF, as well as raising the normal operating level of the SIF to 1.39%, as long as there is a planned glide path to return to 1.30%. Finding a path back to 1.30% should be a high priority for the agency given the system's strong historical performance, the extraordinary commitment credit unions made to the cooperative system by funding the SF and supporting its originally intended goal to use only as much funds as necessary to stabilize the corporate system, and in recognition that credit unions have shown the ability to fund an assessment when the NOL approaches 1.20% as they did most recently in 2009 and 2010. The path back to

1.30% should include frequent engagement with the credit union system and a vigilance to transparency on not only the performance of the SF and SIF, but into the agency's strategy to ultimately reduce costs to credit unions by creating a more efficient and effective regulatory framework. Technological advances, decades of experience regulating credit unions, and a vision to create a modern regulator of credit unions provide NCUA with a strong and stable base to find continued savings which ultimately puts less demand on the resources of the SIF and reduces overall costs to the system.

Thank you for your consideration of these views. The Association appreciates the opportunity to provide input and I remain available to address any questions or concerns at pgentile@ccua.org that you or your staff may have at your convenience.

Sincerely,

Paul Gentile

Paul C. Gentile
President/CEO

PCG/mabc/kb