American Bankers Association
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Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314–3428

re: National Credit Union Administration; Corporate Credit Unions; 12 C.F.R. Part 704; 76 Federal Register 54991, September 6, 2011

Dear Ms. Rupp:

The National Credit Union Administration (NCUA) Board (the Board) issued proposed amendments to its rule governing corporate credit unions (corporates). One proposed amendment is to revise the definition of net assets, which is the denominator of the corporate credit union leverage ratio. The Board is seeking to exclude Central Liquidity Facility (CLF) stock subscriptions from the definition of net assets.

The American Bankers Association (ABA)[1] is opposed to the proposed change in the definition of net assets. Deducting CLF stock subscription is an accounting gimmick that would artificially inflate the leverage ratio for corporate credit unions, making them appear less risky than they really are. ABA believes that this would weaken the safety and soundness of corporate credit unions and could pose a risk to the National Credit Union Share Insurance Fund (NCUSIF) and to taxpayers who have recently been called upon to provide billions of dollars in financial backing for Temporary Corporate Credit Union Stabilization Fund. In addition, arguments that the proposed definitional change in net assets is necessary to meet the systemic liquidity needs of natural person credit unions ignores the fact that credit unions have other alternative sources of liquidity already available to them.

Background

In 2010, NCUA amended its capital regulations for corporate credit unions subjecting corporates to a minimum four percent leverage ratio to be adequately capitalized. NCUA defines the leverage ratio (beginning on October 21, 2013) as the ratio of adjusted core capital to moving daily average net assets. Currently, NCUA regulations define net assets as "total assets less loans guaranteed by the NCUSIF and member reverse repurchase transactions."

[1] The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $13.6 trillion banking industry and its two million employees. The majority of ABA's members are banks with less than $165 million in assets. ABA's extensive resources enhance the success of the nation's banks and strengthen America's economy and communities.

The Board proposes to modify the definition of net assets to the following: "total assets ***less CLF stock subscriptions***, loans guaranteed by the NCUSIF, and member reverse repurchase transactions."

The Board is proposing this change in the definition because it believes that credit risk associated with CLF stock subscription is negligible. Additionally, the Board believes that this adjustment will "encourage continued CLF participation by corporates, which in turn will facilitate corporates providing a systemic liquidity benefit to natural person credit unions through offering CLF access as agents."[2]

ABA's Position

ABA believes that the Board should ***not*** adopt the proposed revised definition of net assets as it will weaken the leverage ratio for corporate credit unions and is unnecessary for addressing systemic liquidity needs of natural person credit unions.

Revised Definition Weakens the Leverage Ratio

NCUA is proposing to deduct CLF stock subscription from net assets, because it believes it poses negligible credit risk.

The four percent leverage ratio requirement is intended to ensure that credit unions maintain a minimum amount of capital as protection against risks that are not captured by risk-based capital standards, risks that by definition are unknown or unknowable. The leverage ratio is a recognition that risk models are subject to significant error, which the recent financial turmoil affecting banks and credit unions alike made all too clear. The leverage ratio should not be influenced by fallible estimates of the riskiness of the assets.

By allowing corporate credit unions to deduct CLF stock subscription from assets, the Board would lower the denominator of the leverage ratio. This accounting gimmick would then inflate the leverage ratio for corporate credit unions. As a result, this could allow some more thinly capitalized corporate credit unions to comply with the new leverage capital requirements.

By weakening the capital requirements for corporates, this could pose a safety and soundness concern for corporate credit unions and a risk to the National Credit Union Share Insurance Fund (NCUSIF). ***Therefore, ABA recommends that NCUA replace the denominator of the leverage ratio with moving daily average of total assets.***

CLF Stock Subscription Should Be Addressed via Risk-based Capital Ratios

Additionally, if NCUA believes that the credit risk posed by CLF stock subscription, as well as loans guaranteed by the NCUSIF and member reverse repurchase transactions, is negligible, then this is best addressed through the ***risk-based capital requirements*** for corporate credit unions and not the leverage ratio.

[2] 76 Federal Register 172, September 6, 2011, p. 54991

NCUA corporate credit union regulations currently use net risk-weighted assets in the denominator for its corporate credit union risk-based capital requirements. By net risk-weighted assets, NCUA means risk-weighted assets less CLF stock subscriptions, CLF loans guaranteed by the NCUSIF and member reverse repurchase transactions.

But ABA opposes NCUA's netting of these items against the corporate's risk-weighted assets. These items should be incorporated into the calculation of the corporate's risk-weighted assets rather than netting these items against the risk-weighted assets.

Therefore, ABA recommends that the Board should not net these assets against the risk-weighted assets.

Revised Net Asset Definition Is Not Needed to Meet Systemic Liquidity Needs

NCUA attempts to justify this change in the definition of net assets further by arguing it would address systemic liquidity needs of natural person credit unions. This argument does not seem compelling, and it certainly does not outweigh the danger from undermining the leverage ratio capital standard.

First, credit unions can meet their liquidity needs by becoming members of the Federal Home Loan Bank (FHLB) system. As of June 2011, NCUA is reporting that 1,047 federally-insured credit unions were FHLB members.

Second, almost all credit unions, except for the smallest, can make arrangements with the Federal Reserve to access the discount window to meet emerging liquidity needs. The Federal Reserve's discount window, not the CLF, is the logical source of liquidity. During the financial crisis of late 2008 and early 2009, credit unions regularly tapped the discount window for liquidity needs, not the CLF.

In conclusion, ABA believes that the proposed definitional change in net assets represents a step backward as it would overstate the leverage ratio for corporates and makes it less robust as a regulatory guide. Moreover, arguments that this change in the definition is needed for the systemic liquidity needs of natural person credit unions ignore other available liquidity sources already available to credit unions.

Sincerely,

Keith Leggett
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