Louisiana Corporate
Credit Union

March 5, 2009

Ms. Mary F. Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Members of the Board:

We appreciate this opportunity to provide comment on NCUA's advance notice of proposed rulemaking and request for comment on corporate credit unions.

Losses in the corporate network resulting in the corporate stabilization program and the NCUA ANPR have transcended the corporate network itself and have clearly become an issue of vital concern to every individual credit union. The issues addressed in the ANPR not only have the potential to radically reshape the corporate network, they could dramatically and irreversibly impact the future of every natural-person credit union.

Despite the severe challenges we now face as a nation and as a credit union movement, the U.S. economy remains the strongest and most resilient economy in the world. Even in times of turbulence, it remains the preeminent safe haven for the world's investments. And in an economy based on free-market economic principles, the U.S. credit union movement has grown into a major force in the country's financial system. One of the most fundamental concepts that drove the development of America's financial strength was the principal that consumers and businesses, "voting" with their dollars in a free market economy, is the most efficient way to allocate resources.

As acknowledged in the NCUA ANPR, regulatory changes enacted after the purchase and assumption of Cap Corp sought to impact the structure of the corporate network. Highly expanded investment authorities, *combined* with national fields of membership, created increased rate competition and, for many, investment in higher-risk securities. While this created some consolidation among corporates focused on maximizing rates through the use of expanded authorities, *there remains no persuasive empirical evidence that economies of scale benefiting credit unions were achieved through consolidations*. Certainly, the losses now being reported outweigh any economy of scale benefits that are purported to have been realized. Over the past few years, corporates utilizing expanded investment authorities have failed to outperform the earnings ratios of corporates using base and base-plus authorities on any consistent basis.

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We suggest that the solution to the current crisis is not to create a system that makes it difficult, if not impossible, for corporates to operate that remain solvent, profitable, and continue to enjoy the support of their membership. Today's crisis was not caused by the three-tiered system; it was precipitated by the use of highly expanded investment authorities in an environment of increased rate competition. Bringing about structural consolidation of the corporate system by eliminating healthy corporates with proven ability to serve their members and operate soundly would not add a penny to the network's total equity. Better solutions lie not in further regulatory fine tuning of the structure, but in preserving credit unions' ability to choose where to place their deposits and investable funds in an informed manner with the benefit of full, fair and prompt financial disclosure.

Each corporate must earn (and in some cases, re-earn) its member credit unions' trust through sound financial risk-management and disclosure. Just like the loss of equity, the loss of trust cannot be restored by regulatorily mandated structural changes. It can come only from management accountability, and fair and prompt disclosure.

We support proposals to utilize the $4 billion in capital in the corporate network before requiring natural-person credit unions to utilize their earnings to restore the NCUSIF. We strongly believe that base and base-plus level corporates, like Louisiana Corporate, have an invaluable and irreplaceable contribution to make to the restoration of the corporate system. We are confident of our ability to continue to operate soundly and compete effectively in a market driven by credit union choice. Further, we believe it is critical that all credit unions have ample opportunity to express their views at this critical juncture in the evolution of our industry. Accordingly, we recommend a 30-day extension of the ANPR comment period to ensure that all credit unions have time to provide thoughtful responses to these complex issues.

We respectfully offer the following comments on issues under consideration:

Payment System:

We do not concur with a premise of the ANPR that the current crisis was caused by structural problems. These problems are attributable to intense competition among overlapping fields of membership *combined* with expanded investment authorities, and have been aggravated by late and erratic financial disclosure. Although no financial sector has been immune to the deterioration of the mortgage markets, the failure to promptly disclose and address investment portfolio deterioration is a failure of management and not of structure. The separation of institutions into payment systems and investment charters will not address the underlying management and capital problems. The feasibility of this approach is questionable, as these services are interdependent: Payment systems require settlement, settlement requires credit and the ability to concentrate funds as complementary services, and both settlement and credit services require investment for treasury management and collateral purposes.

A payment systems-only charter presumably would not perform the basic purposes of credit unions as originally defined in The Federal Credit Union Act, which was to establish a further market for U.S. securities and to make credit more available for people of small means. Likewise, the primary and founding purpose of corporate credit unions was to make credit available to natural-person credit unions, especially in times when credit may be restricted from other sectors of the financial services industry. Consequently, the tax exempt status of payment systems only charters may be called into question. Such an institution conceivably could be viewed as a form of credit union service organization operating with a tax exemption. The loss of the current tax-exempt structure housing payment systems would only serve to increase costs, ultimately to the persons of small means that the exemption was meant to benefit. Even without loss of the tax exemption, we do not believe that a payment systems-only charter would possess a sufficient earnings base to constitute a successful business model.

The corporate network has held ongoing discussions with the Office of Corporate Credit Unions over the past few years to recommend establishing a risk-based capital system. Such a system, which appropriately recognizes the differences in levels of capital necessary for varying types and degrees of operational and investment risk, would directly address the current problems, while structural changes would only address ancillary issues.

Liquidity and Liquidity Management:

Providing liquidity was the founding purpose of corporate credit unions, as well as the primary reason for their classification as credit unions and their tax exemption. The founders of the corporate system foresaw the need to ensure that in times of liquidity shortages, credit unions would not be at the mercy of competing sectors of the financial services industry. The elimination of liquidity as corporates' core service would be potentially threatening to the viability of the credit union system during periods of tight liquidity.

Currently, corporates with base and base-plus authorities have not experienced liquidity problems. These issues seem to be related to the use of expanded investment authorities, combined with the lack of a risk-based capital system. A proper risk-based capital system, as is used by most financial institutions, could provide a sufficient disincentive for expanded-authority corporates to invest in terms that are beyond their capacity to support deposits with sufficient liquidity. These issues also could be addressed through an examination of whether the current NEV requirements for expanded-authority corporates are still sufficient and have been enforced in a timely manner.

Field of Membership Issues:

While nearly all corporates currently possess national fields of membership, base and base-plus corporates with national FOMs have not suffered a critical deterioration of equity. Regional FOMs would not reduce risk, but they would reduce the ability of credit unions to exercise choice in their selection of correspondent and investment services. The structure of corporates can best be addressed by competition in a free-market environment. The most valuable role that the regulatory agencies can play in this environment is to ensure the availability of prompt, fair and accurate financial disclosure, and to take prompt action when capital and NEV requirements are breached.

Expanded Investment Authority:

Expanded investment authorities have not yielded consistently higher earnings ratios than base and base-plus corporate authorities. Further, the losses generated at the expanded-authority levels more than outweigh any purported gains both in terms of income and reputation damage to the credit union system. Operations at the expanded-authority levels have also called into question the corporate network's ability to perform its primary liquidity function. Competition based on reasonable rate differences at base and base-plus levels, quality of service, and availability of liquidity, combined with prompt and accurate financial disclosures, would best serve natural-person credit unions, and ultimately, their members.

Structured, Two-tier System:

The two-tier corporate system functioned without undue risk until the combination of expanded authorities *and* national FOMs were added to the structural mix. As far as we are aware, the vast majority, if not all, base and base-plus corporates, utilize the services of a wholesale corporate as an integral part of their current business model. These corporates have the highest percentage participation levels in the current wholesale corporate. At this point, the elimination of the wholesale tier would likely result in the "survival of the *unfittest*." This would be potentially damaging to many small- and medium-sized credit unions that rely on the current structure for access to settlement, financial and credit markets. The process of conversion to a radically altered structure could raise unanticipated operational risks and create unforeseen disruptions in payment systems at a time when the credit union system should be striving to prevent damage to its reputation for reliable services.

Corporate Capital:

Revision of corporate capital requirements should be undertaken in conjunction with the implementation of a risk-based capital system and a review of the empirical results of expanded investment authorities. A risk-based capital system would have the additional advantage of allowing the agency, corporates and credit unions to view a corporate's capital strength through the same prism used by rating agencies and counterparties. It would lessen the incidence of unexpected credit downgrades.

The erosion of trust in the corporate system caused by late and erratic financial disclosure by some corporates has created an environment in which it would be extremely difficult to raise additional member capital. Disclosure deficiencies must first be addressed through regulatory supervision and sound management to recreate an environment in which both corporates and credit unions can confidently rely on financial transparency to evaluate capital offerings. Revision of the current capital requirements and structures should not be undertaken absent consideration of a form of risk-based capital sufficient to recognize varying degrees of operational and investment risk.

Permissible Investments:

An empirical review comparing the results of operations and equity levels of corporates operating at the base and base-plus levels of investment authority with corporates operating at expanded investment authority levels should be undertaken to guide the process of reevaluation of permissible investments. A risk-based capital system would also act as a potent self-regulatory force by matching appropriate investment risk levels to an institution's capital levels.

Credit Risk Management:

Despite the dismal record of the major rating agencies in the current market situation, they possess an abundance of analytical resources that corporates could not realistically duplicate. While Congress will likely review the performance and regulation of rating agencies, duplication of their function by corporates or outside contractors would not be feasible. A properly configured risk-based capital system would directly address the credit risk issue in relation to each institution's capital levels.

Asset Liability Management:

The constraints of current NEV regulations properly result in an environment in which corporate credit unions hold a large percentage of their holdings in floating-rate investments and relatively short-term, fixed-rate securities. Consequently, widening credit spreads have benefitted the net income of most corporates. Widening credit spreads are a symptom of the lack of confidence in the investment markets and not a primary cause of the problems in the corporate network. Most corporates shock test their NEV measurements for widening of credit spreads as a part of their supplemental NEV testing. It would be advisable to make supplemental testing for widening of credit spreads a required part of current NEV shock testing.

Corporate Governance:

The IRS Form 990 filing currently provides transparency of executive compensation for most state-charted corporate credit unions that are subject to the filing requirements. The requirement of a form 990 filing, or its equivalent, by all corporates, would create a level playing field in this area and contribute to a restoration of trust in the corporate network. Greater transparency in this area would also provide member credit unions a more appropriate amount of information for use in evaluating the accuracy of economies of scale claims in merger proposals. We believe the issues of compensation and term limits for corporate directors is properly a matter for comment by the natural-person credit unions that own the corporates. We would offer the observation that the voluntary service of corporate and credit union directors has long been held forth as a part of the "credit union difference" and a defense of the tax exemption. We believe the introduction of outside directors would be antithetical to the fundamental nature of credit unions as member-owned and democratically controlled financial cooperatives. It would also present regulatory challenges in guarding against inappropriate interlock relationships. Currently, credit union directors consist of management and officials of natural-person credit unions and are qualified by virtue of their education, training, and experience in that capacity. While we support training for corporate officials, we recommend that requirements in this area take into account existing training requirements for credit union management and officials.

We appreciate the opportunity to provide our comments to the Board as it faces unprecedented challenges in the governance of the credit union system. While corporates often function cooperatively, we respectfully ask the Board to recognize that we are individual, member-owned financial institutions with primary fiduciary responsibilities to our individual member/owner credit unions. We pledge to do everything in our power to contribute to the restoration of trust in the corporate system and to provide any future input that the Board may find helpful in the administration of its duties.

Sincerely,

David A. Savoie

David A. Savoie, CPA, CFE
President / CEO