CUNA REGULATORY ADVOCACY

CUNA REGULATORY COMMENT CALL

December 22, 2011

ANPR – Maintaining Access to Emergency Liquidity

Executive Summary

- The National Credit Union Administration Board (NCUA) has issued an advance notice of proposed rulemaking (ANPR) regarding how credit unions should maintain access to emergency liquidity.
- Specifically, NCUA is seeking comments on the scope and requirements of a potential new regulation to require all federally-insured credit unions (FICUs) to have access to backup federal liquidity sources in times of financial emergency and distressed economic circumstances. The new regulation, if promulgated, would be added to NCUA's regulation on requirements for share insurance and would apply to both federal and federally-insured state-chartered credit unions.
- NCUA believes a credit union could demonstrate that it has access to emergency liquidity in one of four ways:
    1. becoming a member in good standing of CLF directly;
    2. becoming a member in good standing of CLF through a corporate credit union;
    3. obtaining and maintaining demonstrated access to the Federal Reserve Board's Discount Window; <u>or</u>
    4. maintaining a certain percentage of assets in highly liquid Treasury securities.
- CUNA is interested in your comments and the CUNA Corporate Credit Union Task Force will also be reviewing the ANPR. Comments for the proposal are due to NCUA by February 21, 2012; **please submit your comments to CUNA by February 10, 2012.**
- Please e-mail your comments to Regulatory Counsel Dennis Tsang at dtsang@cuna.com and SVP Deputy General Counsel Mary Dunn at mdunn@cuna.com or call (800) 356-9655 ext. 6733 if you have questions. Our comment call questions are also available on an online survey.
- For further information, please review the ANPR in the Federal Register.

Background

NCUA is seeking comments on the scope and requirements of a potential new regulation to require all federally-insured credit unions (FICUs) to have access to backup federal liquidity sources in times of financial emergency and distressed economic circumstances. NCUA believes that all credit unions should have access to emergency liquidity from both their own balance sheets and through credit facilities.

Liquidity is a credit union's capacity to meet its cash and collateral obligations at a reasonable cost. Liquidity risk is the risk that a credit union's financial condition or overall safety and soundness is adversely affected by an actual or perceived inability to meet its obligations. Credit unions can manage their liquidity risk by maintaining: 1) adequate levels of highly liquid marketable securities that can be used to meet liquidity needs in stressful situations; 2) an appropriately diverse mix of existing and potential future funding sources; and 3) access to a contingent liquidity provider, such as the Central Liquidity Fund (CLF) or the Federal Reserve Board's Discount Window (Discount Window).

In March 2010, NCUA, federal financial regulators, and the Conference of State Bank Supervisors, issued a Federal Financial Institutions Examination Council (FFIEC) Interagency Policy Statement on Funding and Liquidity Risk Management. Further, NCUA in August 2010 issued an updated Letter to Credit Unions (10-CU-14) that incorporated the FFIEC Interagency Policy Statement and described how FICUs should manage liquidity risk using processes and systems to account for their credit union's unique risk and operations profile.

Based on June 2011 Call Report data, NCUA believes most FICUs have no emergency liquidity beyond indirect CLF membership through their corporate membership and U.S. Central Bridge Corporate Federal Credit Union (USC Bridge). The data showed that approximately:

- 1.3 percent of FICUs have direct membership in CLF;
- 4.5 percent of FICUs have current access to the Discount Window;
- 14.6 percent of FICUs report being members of a Federal Home Loan Bank (FHLB) (however 27 percent of all FICUs do not hold any mortgage assets and would be not likely to rely on the FHLB for wholesale funding or liquidity); and
- 90 percent of FICUs do not currently hold any U.S. Treasury obligations.

Central Liquidity Fund

Most FICUs have access to the CLF to meet certain liquidity needs if they belong to a corporate credit union that is part of the agent group headed by USC Bridge, while some credit unions have direct regular membership with the CLF. The CLF provides liquidity advances to credit unions that have a valid liquidity need and meet minimum creditworthiness standards at the time of the request. As part of the wind down process, USC Bridge will soon discontinue its role as CLF agent group representative, and existing agent group arrangements will also terminate, so most credit unions will need to establish new indirect (through an agent or another corporate) or direct membership arrangements to continue to access the CLF. Further information about the CLF, such as the types of borrowing requirements, is available at NCUA's CLF resources webpage.

Federal Reserve Discount Window

Credit unions may also be eligible to use the Discount Window to meet certain liquidity needs. The Discount Window provides three credit programs to eligible depository institutions: 1) primary credit; 2) secondary credit; and 3) seasonal credit. Only depository institutions that maintain reservable transaction accounts (share draft accounts for credit unions) or nonpersonal time deposits (share certificates or money market share accounts held by a depositor other than an individual) may borrow from the Discount Window. Further information about the Discount Window, such as borrowing requirements, agreements, and types of acceptable collateral, is available at the Federal Reserve Board's Discount Window Resources webpage.

Questions to Consider Regarding the ANPR

1. Does your credit union believe there should be a new regulation to require all federally-insured credit unions (FICUs) to maintain access to backup federal liquidity sources in times of financial emergency and distressed economic circumstances? If so, what are the standards, provisions, and considerations that should be part of a potential new regulation?

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   a. Should credit unions under a certain asset threshold be exempt from these requirements? If so, what should that asset threshold be?

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2. Are there other sources of credit or liquidity beyond the CLF and Discount Window that credit unions could use for a backup federal liquidity source?

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   a. Do you have any recommendations regarding the current processes and requirements to apply for liquidity from the CLF or the Discount Window?

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   b. Should credit unions be able to satisfy potential liquidity requirements by holding a certain percentage of its assets in highly liquid (maturity of 90 days or less) Treasury securities? If so, what should the appropriate required percentage of liquid securities be? How should NCUA ensure these liquid securities are available to be pledged or sold?

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c. Should NCUA follow the Basel III international liquidity framework's guideline that a depository institution must maintain "an adequate level of unencumbered, high-quality liquid assets that can be converted into cash to meet is liquidity needs for a 30 calendar day time horizon under a significantly severe liquidity stress scenario specified by supervisors."?

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3. How should the CLF continue to operate after USC Bridge completes the wind down process to satisfy future credit union contingency liquidity needs?

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a. Do you recommend any changes to the CLF statute to modernize the CLF? Should the CLF become more like the Discount Window?

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4. What is the best way for credit unions to continue to access the CLF (e.g., directly or through an agent)? Should corporate credit unions continue to provide CLF access, and also be encouraged to purchase CLF stock as agents for natural person credit unions?

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5. Does your credit union have any recommendations on ways to minimize regulatory burden on credit unions regarding these potential new liquidity requirements?

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6. Any other comments or suggestions?

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