

## National Credit Union Administration

## § 704.2

704.21 Enterprise risk management.

704.22 Membership fees.

APPENDIX A TO PART 704—CAPITAL  
PRIORITIZATION AND MODEL FORMS

APPENDIX B TO PART 704—EXPANDED AU-  
THORITIES AND REQUIREMENTS

APPENDIX C TO PART 704—RISK-BASED CAP-  
ITAL CREDIT RISK-WEIGHT CATEGORIES

AUTHORITY: 12 U.S.C. 1766(a), 1781, 1789.

SOURCE: 62 FR 12938, Mar. 19, 1997, unless  
otherwise noted.

### § 704.1 Scope.

(a) This part establishes special rules for all federally insured corporate credit unions. Non federally insured corporate credit unions must agree, by written contract, to both adhere to the requirements of this part and submit to examinations, as determined by NCUA, as a condition of receiving shares or deposits from federally insured credit unions. This part grants certain additional authorities to federal corporate credit unions. Except to the extent that they are inconsistent with this part, other provisions of NCUA's Rules and Regulations (12 CFR chapter VII) and the Federal Credit Union Act apply to federally chartered corporate credit unions and federally insured state-chartered corporate credit unions to the same extent that they apply to other federally chartered and federally insured state-chartered credit unions, respectively.

(b) The Board has the authority to issue orders which vary from this part. This authority is provided under Section 120(a) of the Federal Credit Union Act, 12 U.S.C. 1766(a). Requests by state-chartered corporate credit unions for waivers to this part and for expansions of authority under appendix B of this part must be approved by the state regulator before being submitted to NCUA.

### § 704.2 Definitions.

*As used in this part:*

*Adjusted core capital* means core capital modified as follows:

(1) Deduct an amount equal to the amount of the corporate credit union's intangible assets that exceed one half percent of the corporate credit union's moving daily average net assets, but the NCUA, on its own initiative, upon petition by the applicable state regu-

lator, or upon application from a corporate credit union, may direct that a particular corporate credit union add some or all of these excess intangibles back to the credit union's adjusted core capital;

(2) Deduct investments, both equity and debt, in unconsolidated credit union service organizations (CUSOs);

(3) If the corporate credit union, on or after October 20, 2011, contributes any perpetual contributed capital (PCC), or maintains any NCAs, at another corporate credit union, deduct an amount equal to this PCC or NCA;

(4) Beginning on October 20, 2016, and ending on October 20, 2020, deduct any amount of perpetual contributed capital (PCC) that causes PCC minus retained earnings, all divided by moving daily net average assets, to exceed two percent; and

(5) Beginning after October 20, 2020, deduct any amount of PCC that causes PCC to exceed retained earnings.

*Adjusted trading* means any method or transaction whereby a corporate credit union sells a security to a vendor at a price above its current market price and simultaneously purchases or commits to purchase from the vendor another security at a price above its current market price.

*Applicable state regulator* means the prudential state regulator of a state chartered corporate credit union.

*Asset-backed commercial paper program* (ABCP program) means a program that primarily issues commercial paper that has received a credit rating from an NRSRO and that is backed by assets or other exposures held in a bankruptcy-remote special purpose entity. The term *sponsor of an ABCP program* means a corporate credit union that:

(1) Establishes an ABCP program;

(2) Approves the sellers permitted to participate in an ABCP program;

(3) Approves the asset pools to be purchased by an ABCP program; or

(4) Administers the ABCP program by monitoring the assets, arranging for debt placement, compiling monthly reports, or ensuring compliance with the program documents and with the program's credit and investment policy.

*Asset-backed security* (ABS) means a security that is primarily serviced by

## § 704.2

## 12 CFR Ch. VII (1–1–13 Edition)

the cashflows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to the security holders. Mortgage-backed securities are a type of asset-backed security.

*Available to cover losses that exceed retained earnings* means that the funds are available to cover operating losses realized, in accordance with generally accepted accounting principles (GAAP), by the corporate credit union that exceed retained earnings net of equity acquired in a combination. Likewise, *available to cover losses that exceed retained earnings and perpetual contributed capital (PCC)* means that the funds are available to cover operating losses realized, in accordance with GAAP, by the corporate credit union that exceed retained earnings net of equity acquired in a combination and PCC. Any such losses must be distributed *pro rata* at the time the loss is realized first among the holders of PCC, and when all PCC is exhausted, then *pro rata* among all nonperpetual capital accounts (NCAs) and unconverted membership capital accounts, all subject to the optional prioritization described in Appendix A of this Part. To the extent that any contributed capital funds are used to cover losses, the corporate credit union must not restore or replenish the affected capital accounts under any circumstances. In addition, contributed capital that is used to cover losses in a calendar year previous to the year of liquidation has no claim against the liquidation estate.

*Capital* means the same as *total capital*, defined below.

*Capital ratio* means the corporate credit union's capital divided by its moving daily average net assets.

*Collateralized debt obligation (CDO)* means a debt security collateralized by mortgage-backed securities, asset-backed securities, or corporate obligations in the form of loans or debt. Senior tranches of Re-REMIC's consisting of senior mortgage- and asset-backed securities are excluded from this definition.

*Collateralized mortgage obligation (CMO)* means a multi-class mortgage-backed security.

*Commercial mortgage-backed security (CMBS)* means a mortgage-backed security collateralized primarily by multi-family and commercial property loans.

*Compensation* means all salaries, fees, wages, bonuses, severance payments, current year contributions to employee benefit plans (for example, medical, dental, life insurance, and disability), current year contributions to deferred compensation plans and future severance payments, including payments in connection with a merger or similar combination (whether or not funded; whether or not vested; and whether or not the deferred compensation plan is a qualified plan under Section 401(a) of the IRS Code). Compensation also includes expense accounts and other allowances (for example, the value of the personal use of housing, automobiles or other assets owned by the corporate credit union; expense allowances or reimbursements that recipients must report as income on their separate income tax return; payments made under indemnification arrangements; and payments made for the benefit of friends or relatives). In calculating required compensation disclosures, reasonable estimates may be used if precise cost figures are not readily available.

*Consolidated Credit Union Service Organization (Consolidated CUSO)* means any corporation, partnership, business trust, joint venture, association or similar organization in which a corporate credit union directly or indirectly holds an ownership interest (as permitted by § 704.11 of this Part) and the assets of which are consolidated with those of the corporate credit union for purposes of reporting under Generally Accepted Accounting Principles (GAAP). Generally, consolidated CUSOs are majority-owned CUSOs.

*Contributed capital* means either perpetual or nonperpetual capital.

*Core capital* means the sum of:

- (1) Retained earnings;
- (2) Perpetual contributed capital;
- (3) The retained earnings of any acquired credit union, or of an integrated set of activities and assets, calculated

at the point of acquisition, if the acquisition was a mutual combination; and

(4) Minority interests in the equity accounts of CUSOs that are fully consolidated. However, minority interests in consolidated ABCP programs sponsored by a corporate credit union are excluded from the credit unions' core capital or total capital base if the corporate credit union excludes the consolidated assets of such programs from risk-weighted assets pursuant to appendix C of this part.

*Core capital ratio* means the corporate credit union's core capital divided by its moving daily average net assets.

*Corporate credit union* means an organization that:

- (1) Is chartered under Federal or state law as a credit union;
- (2) Receives shares from and provides loan services to credit unions;
- (3) Is operated primarily for the purpose of serving other credit unions;
- (4) Is designated by NCUA as a corporate credit union;
- (5) Limits natural person members to the minimum required by state or federal law to charter and operate the credit union; and
- (6) Does not condition the eligibility of any credit union to become a member on that credit union's membership in any other organization.

*Credit-enhancing interest-only strip.* (1) *Credit-enhancing interest-only strip* means an on-balance sheet asset that, in form or in substance:

- (i) Represents the contractual right to receive some or all of the interest due on transferred assets; and
- (ii) Exposes the corporate credit union to credit risk directly or indirectly associated with the transferred assets that exceeds its *pro rata* share of the corporate credit union's claim on the assets whether through subordination provisions or other credit enhancement techniques.

(2) NCUA reserves the right to identify other cash flows or related interests as a credit-enhancing interest-only strip. In determining whether a particular interest cash flow functions as a credit-enhancing interest-only strip, NCUA will consider the economic substance of the transaction.

*Critical accounting policies* means those policies that are most important

to the portrayal of a corporate credit union's financial condition and results and that require management's most difficult, subjective, or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

*Daily average net assets* means the average of net assets calculated for each day during the period.

*Derivatives* means a financial contract whose value is derived from the values of one or more underlying assets, reference rates, or indices of asset values or reference rates. Derivative contracts include interest rate derivative contracts, exchange rate derivative contracts, equity derivative contracts, commodity derivative contracts, credit derivative contracts, and any other instrument that poses similar counterparty credit risks.

*Dollar roll* means the purchase or sale of a mortgage-backed security to a counterparty with an agreement to resell or repurchase a substantially identical security at a future date and at a specified price.

*Eligible ABCP liquidity facility* means a legally binding commitment to provide liquidity support to asset-backed commercial paper by lending to, or purchasing assets from any structure, program or conduit in the event that funds are required to repay maturing asset-backed commercial paper and that meets the following criteria:

(1)(i) At the time of the draw, the liquidity facility must be subject to an asset quality test that precludes funding against assets that are 90 days or more past due or in default; and

(ii) If the assets that the liquidity facility is required to fund against are assets or exposures that have received a credit rating by an NRSRO at the time the inception of the facility, the facility can be used to fund only those assets or exposures that are rated investment grade by an NRSRO at the time of funding; or

(2) If the assets that are funded under the liquidity facility do not meet the criteria described in paragraph (1) of this definition, the assets must be

guaranteed, conditionally or unconditionally, by the United States Government, its agencies, or the central government of an Organization for Economic Cooperation and Development (OECD) country.

*Embedded option* means a characteristic of certain assets and liabilities which gives the issuer of the instrument the ability to change the features such as final maturity, rate, principal amount and average life. Options include, but are not limited to, calls, caps, and prepayment options.

*Enterprise risk management* means the process of addressing risk on an entity-wide basis. The purpose of this process is not to eliminate risk but, rather, to provide the knowledge the board of directors and management need to effectively measure, monitor, and control risk and to then plan appropriate strategies to achieve the entity's business objectives with a reasonable amount of risk taking.

*Equity investment* means investments in real property, equity securities, and any other ownership interests, including, for example, investments in partnerships and limited liability companies.

*Equity security* means any security representing an ownership interest in an enterprise (for example, common, preferred, or other capital stock) or the right to acquire (for example, warrants and call options) or dispose of (for example, put options) an ownership interest in an enterprise at fixed or determinable prices. However, the term does not include convertible debt or preferred stock that by its terms either must be redeemed by the issuing enterprise or is redeemable at the option of the investor.

*Examination of internal control* means an engagement of an independent public accountant to report directly on internal control or on management's assertions about internal control. An examination of internal control over financial reporting includes controls over the preparation of financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP) and NCUA regulatory reporting requirements.

*Exchangeable collateralized mortgage obligation* means a class of a collateralized mortgage obligation (CMO) that, at the time of purchase, represents beneficial ownership interests in a combination of two or more underlying classes of the same CMO structure. The holder of an exchangeable CMO may pay a fee and take delivery of the underlying classes of the CMO.

*Fair value* means the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. If there is a principal market for the asset or liability, the fair value measurement is the price in that market (whether that price is directly observable or otherwise determined using a valuation technique), even if the price in a different market is potentially more advantageous at the measurement date. In the absence of a principal market, the fair value measurement occurs in the most advantageous market for the asset or liability. The fair value of the asset or liability shall be determined based on the assumptions that market participants would use in pricing the asset or liability. In developing those assumptions, the corporate need not identify specific market participants. Rather, the corporate should identify characteristics that distinguish market participants generally, considering factors specific to all of the following: the asset or liability; the principal (or most advantageous) market for the asset or liability; and market participants with whom the corporate would transact in that market. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Examples of valuation techniques include the present value of estimated future cash flows, option-pricing models, and option-adjusted spread models.

*Federal funds transaction* means a short-term or open-ended unsecured transfer of immediately available funds by one depository institution to another depository institution or entity.

*Financial statements* means the presentation of a corporate credit union's financial data, including accompanying notes, derived from accounting records of the credit union, and intended to disclose the credit union's economic resources or obligations at a point in time, or the changes therein for a period of time, in conformity with GAAP. Each of the following is considered to be a financial statement: a balance sheet or statement of financial condition; statement of income or statement of operations; statement of undivided earnings; statement of cash flows; statement of changes in members' equity; statement of revenue and expenses; and statement of cash receipts and disbursements.

*Financial statement audit* means an audit of the financial statements of a corporate credit union performed in accordance with generally accepted auditing standards by an independent person who is licensed by the appropriate State or jurisdiction. The objective of a financial statement audit is to express an opinion as to whether those financial statements of the credit union present fairly, in all material respects, the financial position and the results of its operations and its cash flows in conformity with GAAP.

*Foreign bank* means an institution which is organized under the laws of a country other than the United States, is engaged in the business of banking, and is recognized as a bank by the banking supervisory authority of the country in which it is organized.

*Generally accepted auditing standards* (GAAS) means the standards approved and adopted by the American Institute of Certified Public Accountants which apply when an independent, licensed certified public accountant audits private company financial statements in the United States of America. Auditing standards differ from auditing procedures in that procedures address acts to be performed, whereas standards measure the quality of the performance of those acts and the objectives to be achieved by use of the procedures un-

dertaken. In addition, auditing standards address the auditor's professional qualifications as well as the judgment exercised in performing the audit and in preparing the report of the audit.

*Immediate family member* means a spouse or other family member living in the same household.

*Independent public accountant* (IPA) means a person who is licensed by, or otherwise authorized by, the appropriate State or jurisdiction to practice public accounting. An IPA must be able to exercise fairness toward credit union officials, members, creditors and others who may rely upon the report of a supervisory committee audit and to demonstrate the impartiality necessary to produce dependable findings. As used in this part, IPA is synonymous with the terms "auditor" and "accountant." The term IPA does not include a licensed person working in his or her capacity as an employee of an unlicensed entity and issuing an audit opinion in the unlicensed entity's name, e.g., a licensed league auditor or licensed retired examiner working for a non-licensed entity.

*Intangible assets* means assets considered to be intangible assets under GAAP. These assets include, but are not limited to, core deposit premiums, purchased credit card relationships, favorable leaseholds, and servicing assets (mortgage and non-mortgage). Interest-only strips receivable are not intangible assets under this definition.

*Internal control* means the process, established by the corporate credit union's board of directors, officers and employees, designed to provide reasonable assurance of reliable financial reporting and safeguarding of assets against unauthorized acquisition, use, or disposition. A credit union's internal control structure generally consists of five components: Control environment; risk assessment; control activities; information and communication; and monitoring. Reliable financial reporting refers to preparation of Call Reports that meet management's financial reporting objectives. Internal control over safeguarding of assets against unauthorized acquisition, use, or disposition refers to prevention or timely detection of transactions involving such unauthorized access, use,

or disposition of assets which could result in a loss that is material to the financial statements.

*Internal control framework* means criteria such as that established in *Internal Control—Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), or comparable, reasonable, and U.S.-recognized criteria.

*Internal control over financial reporting* means a process effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance regarding the preparation of reliable financial statements in accordance with accounting principles generally accepted in the United States of America. A corporate credit union's internal control over financial reporting includes those policies and procedures that:

(1) Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the entity;

(2) Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of the entity are being made only in accordance with authorizations of management and those charged with governance; and

(3) Provide reasonable assurance regarding prevention, or timely detection and correction, of unauthorized acquisition, use, or disposition of the entity's assets that could have a material effect on the financial statements.

*Leverage ratio* means, before October 21, 2013, the ratio of total capital to moving daily average net assets. This is the interim leverage ratio.

*Leverage ratio* means, on or after October 21, 2013, the ratio of adjusted core capital to moving daily average net assets. This is the permanent leverage ratio.

*Limited liquidity investment* means a private placement or funding agreement.

*Member reverse repurchase transaction* means an integrated transaction in which a corporate credit union pur-

chases a security from one of its member credit unions under agreement by that member credit union to repurchase the same security at a specified time in the future. The corporate credit union then sells that same security, on the same day, to a third party, under agreement to repurchase it on the same date on which the corporate credit union is obligated to return the security to its member credit union.

*Mortgage-backed security* (MBS) means a security backed by first or second mortgages secured by real estate upon which is located a dwelling, mixed residential and commercial structure, residential manufactured home, or commercial structure.

*Moving daily average net assets* means the average of daily average net assets for the month being measured and the previous eleven (11) months.

*Moving monthly average net risk-weighted assets* means the average of the net risk-weighted assets for the month being measured and the previous eleven (11) months. Measurements must be taken on the last day of each month.

*Mutual combination* means a transaction or event in which a corporate credit union acquires another credit union, or acquires an integrated set of activities and assets that is capable of being conducted and managed as a credit union.

*Nationally Recognized Statistical Rating Organization* (NRSRO) means any entity that has applied for, and been granted permission, to be considered an NRSRO by the United States Securities and Exchange Commission.

*NCUA* means NCUA Board (Board), unless the particular action has been delegated by the Board.

*Net assets* means total assets less Central Liquidity Facility (CLF) stock subscriptions, loans guaranteed by the NCUSIF, and member reverse repurchase transactions. For its own account, a corporate credit union's payables under reverse repurchase agreements and receivables under repurchase agreements may be netted out if the GAAP conditions for offsetting are met. Also, any amounts deducted from core capital in calculating adjusted core capital are also deducted from net assets.

*Net economic value* (NEV) means the fair value of assets minus the fair value of liabilities. All fair value calculations must include the value of forward settlements and embedded options. Perpetual contributed capital, and the unamortized portion of nonperpetual capital that is, the portion that qualifies as capital for purposes of any of the minimum capital ratios, is excluded from liabilities for purposes of this calculation. The NEV ratio is calculated by dividing NEV by the fair value of assets.

*Net interest margin security* means a security collateralized by residual interests in collateralized mortgage obligations, residual interests in real estate mortgage investment conduits, or residual interests in other asset-backed securities.

*Net risk-weighted assets* means risk-weighted assets less Central Liquidity Facility (CLF) stock subscriptions, CLF loans guaranteed by the NCUSIF, and member reverse repurchase transactions. For its own account, a corporate credit union's payables under reverse repurchase agreements and receivables under repurchase agreements may be netted out if the GAAP conditions for offsetting are met. Also, any amounts deducted from core capital in calculating adjusted core capital are also deducted from net risk-weighted assets.

*Nonperpetual capital* means funds contributed by members or nonmembers that: are term certificates with an original minimum term of five years or that have an indefinite term (*i.e.*, no maturity) with a minimum withdrawal notice of five years; are available to cover losses that exceed retained earnings and perpetual contributed capital; are not insured by the NCUSIF or other share or deposit insurers; and cannot be pledged against borrowings. In the event the corporate is liquidated, the holders of nonperpetual capital accounts (NCAs) will claim equally. These claims will be subordinate to all other claims (including NCUSIF claims), except that any claims by the holders of perpetual contributed capital (PCC) will be subordinate to the claims of holders of NCAs.

*Obligor* means the primary party obligated to repay an investment, *e.g.*, the

issuer of a security, such as a Qualified Special Purpose Entity (QSPE) trust; the taker of a deposit; or the borrower of funds in a federal funds transaction. Obligor does not include an originator of receivables underlying an asset-backed security, the servicer of such receivables, or an insurer of an investment.

*Official* means any director or committee member.

*Pair-off transaction* means a security purchase transaction that is closed out or sold at, or prior to, the settlement or expiration date.

*Perpetual contributed capital* (PCC) means accounts or other interests of a corporate credit union that: are perpetual, non-cumulative dividend accounts; are available to cover losses that exceed retained earnings; are not insured by the NCUSIF or other share or deposit insurers; and cannot be pledged against borrowings. In the event the corporate is liquidated, any claims made by the holders of perpetual contributed capital will be subordinate to all other claims (including NCUSIF claims).

*Private label security* means a security that is not issued or guaranteed by the U.S. government, its agencies, or its government-sponsored enterprises (GSEs).

*Quoted market price* means a recent sales price or a price based on current bid and asked quotations.

*Repurchase transaction* means a transaction in which a corporate credit union agrees to purchase a security from a counterparty and to resell the same or any identical security to that counterparty at a specified future date and at a specified price.

*Residential mortgage-backed security* (RMBS) means a mortgage-backed security collateralized primarily by mortgage loans on residential properties.

*Residential properties* means houses, condominiums, cooperative units, and manufactured homes. This definition does not include boats or motor homes, even if used as a primary residence, or timeshare properties.

*Residual interest* means the ownership interest in remainder cash flows from a

## § 704.2

## 12 CFR Ch. VII (1–1–13 Edition)

CMO or ABS transaction after payments due bondholders and trust administrative expenses have been satisfied.

*Retained earnings* means retained earnings as defined under Generally Accepted Accounting Principles (GAAP).

*Risk-weighted assets* means a corporate credit union's risk-weighted assets as calculated in accordance with Appendix C of this part.

*Section 107(8) institution* means an institution described in Section 107(8) of the Federal Credit Union Act (12 U.S.C. 1757(8)).

*Securities lending* means lending a security to a counterparty, either directly or through an agent, and accepting collateral in return.

*Securitization* means the pooling and repackaging by a special purpose entity of assets or other credit exposures that can be sold to investors. Securitization includes transactions that create stratified credit risk positions whose performance is dependent upon an underlying pool of credit exposures, including loans and commitments.

*Senior executive officer* means a chief executive officer, any assistant chief executive officer (*e.g.*, any assistant president, any vice president or any assistant treasurer/manager), and the chief financial officer (controller). This term also includes employees of any entity hired to perform the functions described above.

*Settlement date* means the date originally agreed to by a corporate credit union and a counterparty for settlement of the purchase or sale of a security.

*Short sale* means the sale of a security not owned by the seller.

*Small business related security* means a security that is rated in 1 of the 4 highest rating categories by at least one nationally recognized statistical rating organization, and represents an interest in one or more promissory notes or leases of personal property evidencing the obligation of a small business concern and originated by an insured depository institution, insured credit union, insurance company, or similar institution which is supervised and examined by a Federal or State author-

ity, or a finance company or leasing company. This definition does not include Small Business Administration securities permissible under §107(7) of the Act.

*State* means any one of the several states of the United States of America, the District of Columbia, Puerto Rico, and the territories and possessions of the United States.

*Stripped mortgage-backed security* means a security that represents either the principal-only or interest-only portion of the cash flows of an underlying pool of mortgages.

*Subordinated security* means a security that, at the time of purchase, has a junior claim on the underlying collateral or assets to other securities in the same issuance. If a security is junior only to money market fund eligible securities in the same issuance, the former security is not subordinated for purposes of this definition.

*Supplementary Capital* means the sum of the following items:

(1) Nonperpetual capital accounts, as amortized under §704.3(b)(3);

(2) Allowance for loan and lease losses calculated under GAAP to a maximum of 1.25 percent of risk-weighted assets; and

(3) Forty-five percent of unrealized gains on available-for-sale equity securities with readily determinable fair values. Unrealized gains are unrealized holding gains, net of unrealized holding losses, calculated as the amount, if any, by which fair value exceeds historical cost. The NCUA may disallow such inclusion in the calculation of supplementary capital if the NCUA determines that the securities are not prudently valued.

*Supervisory committee* means, for federally chartered corporate credit unions, the supervisory committee as defined in Section 111(b) of the Federal Credit Union Act, 12 U.S.C. 1761(b). For state chartered corporate credit unions, the term supervisory committee refers to the audit committee, or similar committee, designated by state statute or regulation.

*Tier 1 capital* means adjusted core capital. *Tier 1 risk-based capital ratio* means the ratio of Tier 1 capital to the moving monthly average net risk-weighted assets.



**National Credit Union Administration**

**§ 704.2**

*Tier 2 capital* means supplementary capital plus any perpetual contributed capital deducted from adjusted core capital.

*Total assets* means the sum of all a corporate credit union's assets as calculated under GAAP.

*Total capital* means the sum of a corporate credit union's adjusted core capital and its supplementary capital, less the corporate credit union's equity investments not otherwise deducted when calculating adjusted core capital.

*Total risk-based capital ratio* means the ratio of total capital to moving monthly average net risk-weighted assets.

*Trade date* means the date a corporate credit union originally agrees, whether orally or in writing, to enter into the purchase or sale of a security.

*Trigger* means an event in a securitization that will redirect cashflows if predefined thresholds are breached. Examples of triggers are delinquency and cumulative loss triggers.

*Weighted average life* means the weighted-average time to the return of a dollar of principal, calculated by multiplying each portion of principal received by the time at which it is expected to be received (based on a reasonable and supportable estimate of that time) and then summing and dividing by the total amount of principal. The calculation of weighted average life for interest only securities means the weighted-average time to the return of a dollar of interest, calculated by multiplying each portion of interest received by the time at which it is expected to be received (based on a reasonable and supportable estimate of that time) and then summing and dividing by the total amount of interest to be received.

*When-issued trading* means the buying and selling of securities in the period between the announcement of an offering and the issuance and payment date of the securities.

[75 FR 64829, Oct. 20, 2010, as amended at 76 FR 23867, Apr. 29, 2011; 76 FR 79533, Dec. 22, 2011]

EFFECTIVE DATE NOTE: At 77 FR 74110, Dec. 13, 2012, § 704.2 was amended by revising the definitions of *Asset-backed commercial paper program* and *Eligible ABCP liquidity facility*; adding a definition of *Investment grade* and

*Minimal amount of credit risk*; removing the definition of *Nationally Recognized Statistical Rating Organization*; and revising the definition of *Small business related security*, effective June 11, 2013. For the convenience of the user, the added and revised text is set forth as follows:

**§ 704.2 Definitions.**

\* \* \* \* \*

*Asset-backed commercial paper program (ABCP program)* means a program that primarily issues commercial paper and that is backed by assets or other exposures held in a bankruptcy-remote special purpose entity. The term *sponsor of an ABCP program* means a corporate credit union that:

- (1) Establishes an ABCP program;
- (2) Approves the sellers permitted to participate in an ABCP program;
- (3) Approves the asset pools to be purchased by an ABCP program; or
- (4) Administers the ABCP program by monitoring the assets, arranging for debt placement, compiling monthly reports, or ensuring compliance with the program documents and with the program's credit and investment policy.

\* \* \* \* \*

*Eligible ABCP liquidity facility* means a legally binding commitment to provide liquidity support to asset-backed commercial paper by lending to, or purchasing assets from any structure, program or conduit in the event that funds are required to repay maturing asset-backed commercial paper and that meets the following criteria:

- (1)(i) At the time of the draw, the liquidity facility must be subject to an asset quality test that precludes funding against assets that are 90 days or more past due or in default; and
- (ii) The facility can be used to fund only those assets or exposures that the corporate credit union has reasonably concluded, based on a documented analysis, are at least investment grade; or
- (2) If the assets that are funded under the liquidity facility do not meet the criteria described in paragraph (1) of this definition, the assets must be guaranteed, conditionally or unconditionally, by the United States Government, its agencies, or the central government of an Organization for Economic Cooperation and Development (OECD) country.

\* \* \* \* \*

*Investment grade* means the issuer of the security has an adequate capacity to meet the financial commitments under the security

§ 704.3

12 CFR Ch. VII (1–1–13 Edition)

for the projected life of the asset or exposure, even under adverse economic conditions. An issuer has an adequate capacity to meet financial commitments if the risk of default by the obligor is low and the full and timely repayment of principal and interest on the security is expected. A corporate credit union may consider any or all of the following factors, to the extent appropriate, with respect to the credit risk of a security: Credit spreads; securities-related research; internal or external credit risk assessments; default statistics; inclusion on an index; priorities and enhancements; price, yield, and/or volume; and asset class-specific factors. This list of factors is not meant to be exhaustive or mutually exclusive.

\* \* \* \* \*

*Minimal amount of credit risk* means the amount of credit risk when the issuer of a security has a very strong capacity to meet all financial commitments under the security for the projected life of the asset or exposure, even under adverse economic conditions. An issuer has a very strong capacity to meet all financial commitments if the risk of default by the obligor is very low, and the full and timely repayment of principal and interest on the security is expected. A corporate credit union may consider any or all of the following factors, to the extent appropriate, with respect to the credit risk of a security: Credit spreads; securities-related research; internal or external credit risk assessments; default statistics; inclusion on an index; priorities and enhancements; price, yield, and/or volume; asset class-specific factors. This list of factors is not meant to be exhaustive or mutually exclusive.

\* \* \* \* \*

*Small business related security* means a security that represents an interest in one or more promissory notes or leases of personal property evidencing the obligation of a small business concern and originated by an insured depository institution, insured credit union, insurance company, or similar institution which is supervised and examined by a Federal or State authority, or a finance company or leasing company. This definition does not include Small Business Administration securities permissible under section 107(7) of the Act.

\* \* \* \* \*

§ 704.3 Corporate credit union capital.

(a) *Capital requirements.* (1) A corporate credit union must maintain at all times:

- (i) A leverage ratio of 4.0 percent or greater;
- (ii) A Tier 1 risk-based capital ratio of 4.0 percent or greater; and
- (iii) A total risk-based capital ratio of 8.0 percent or greater.

(2) To ensure it meets its capital requirements, a corporate credit union must develop and ensure implementation of written short- and long-term capital goals, objectives, and strategies which provide for the building of capital consistent with regulatory requirements, the maintenance of sufficient capital to support the risk exposures that may arise from current and projected activities, and the periodic review and reassessment of the capital position of the corporate credit union.

(3) Beginning with the first call report submitted on or after October 21, 2013, a corporate credit union must calculate and report to NCUA the ratio of its retained earnings to its moving daily average net assets. If this ratio is less than 0.45 percent, the corporate credit union must, within 30 days, submit a retained earnings accumulation plan to the NCUA for NCUA’s approval. The plan must contain a detailed explanation of how the corporate credit union will accumulate earnings sufficient to meet all its future minimum leverage ratio requirements, including specific semiannual milestones for accumulating retained earnings. In the case of a state-chartered corporate credit union, the NCUA will consult with the appropriate state supervisory authority (SSA) before making a determination to approve or disapprove the plan, and will provide the SSA a copy of the completed plan. If the corporate credit union fails to submit a plan acceptable to NCUA, or fails to comply with any element of a plan approved by NCUA, the corporate will immediately be classified as significantly undercapitalized or, if already significantly undercapitalized, as critically undercapitalized for purposes of prompt corrective actions. The corporate credit union will be subject to all the associated actions under § 704.4.

(b) *Requirements for nonperpetual capital accounts (NCAs)*—(1) *Form.* NCA funds may be in the form of a term certificate or a no-maturity notice account.