MCUL
MICHIGAN CREDIT UNION LEAGUE

July 25, 2005

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

RE: Michigan Credit Union League's Comments on Proposed Rule 713, Fidelity Bonds

Dear Ms. Rupp,

The Michigan Credit Union League (MCUL) appreciates the opportunity to provide comments to the National Credit Union Administration (NCUA) concerning the NCUA's proposed rule 713 on fidelity bonds. The MCUL is a trade association representing over 90% of state and federally chartered credit unions in the state of Michigan. This comment letter was drafted in consultation with the MCUL Government Affairs Committee, which is comprised of Michigan credit union staff and officials.

MCUL supports the NCUA's efforts to modernize the agency's fidelity bond rules for federal credit unions (FCUs) and federally insured state-chartered credit unions (FISCUs). We believe the proposed changes to the fidelity bond coverage to increase maximum deductibles for select credit unions, and increase bond coverage for other credit unions in certain asset thresholds are positive for the credit union industry. We do, however, have some suggestions as to the standards use to determine eligibility for increased deductibles, which are outlined below.

<u>Summary of Comments</u>

- MCUL believes that the increase in deductibles is appropriate to offset some of the additional costs of increasing fidelity bond limits, however we believe the proposed standards of allowing credit unions who only qualify under the RegFlex guidelines, in particular the capital standards, may be too restrictive. We think a more appropriate standard may be to use the capital standards in NCUA's Prompt Corrective Action (PCA) regulation.
- We believe the proposed increase in fidelity bond coverage requirements, considering the financial environment and the increase in large asset size credit unions, is appropriate.
- There are no additional situations that we have identified where we anticipate the purchase of additional fidelity bond coverage would be necessary. In addition, we are not aware of credit unions that currently use Credit Union Blanket Bond Standard Form 23 of the Surety Association of America, however we do not preclude its use and therefore do not have an opinion on whether it should be rescinded.

Discussion

Fidelity Bond Adjustment for RegFlex Credit Unions.
MCUL supports the increase in deductibles for credit unions. We believe that most of the large credit unions impacted by this change have the financial ability to absorb some of the increased risk that higher deductibles bring. In addition, we believe that an increase in deductible limits will help offset some of the premium increase that would accompany the proposed requirement to increase fidelity bond coverage for these credit unions.

While agreeing with the proposal to increase fidelity bond deductibles, the MCUL believes that the qualifying factors for the increase in deductible limits are too restrictive. MCUL believes that the net worth specifications under RegFlex of 9% are too restrictive and may encourage large credit unions to maintain capital reserves far beyond what they need to maintain safety and soundness. The effect of maintaining an unnecessarily high net worth would prevent credit unions from offering programs and services to better meet the needs of their members.

MCUL believes a better standard in qualifying for increased deductible limits would be to use Prompt Corrective Action (PCA) guidelines. The capital standards established by PCA are less restrictive than those under RegFlex guidelines and are deemed to be reasonable for safety and soundness standards. These guidelines are a more reasonable approach to ensuring safety and soundness, while not unduly restricting the ability for credit unions to continue to offer their members important services.

Increase in Fidelity Bond Coverage Requirements. MCUL believes that these changes are reasonable considering the economic changes since the $5 million maximum coverage requirement was implemented in 1977. Since 1999, the number of federally insured credit unions with assets greater than $500 million has doubled and the assets held by these credit unions have increased by over 240%, now representing almost half of all assets held by all federally insured credit unions. We believe that an increase in bond amounts is reasonable in the face of the economic trends, especially when paired with an increase in deductible amounts.

MCUL also believes that the increase in bond coverage for small credit unions from a minimum of $100,000 to a minimum of $250,000 is reasonable considering the increase in losses from smaller credit unions through fraud, which in some cases has produced losses that exceeded their assets. In addition, according to NCUA projections, it does not appear that an increase in fidelity bond coverage would pose an excess hardship on small credit unions. Based on the NCUA Board's estimation, the cost of increasing bond coverage from $100,000 to $250,000 would be nominal, averaging $100 to $200 per year. Finally, it is the Board's estimation that the majority of smaller credit unions already have bonds of at $250,000, up to as high as $1 million.

No Additional Scenarios for Increasing Bond Amounts Anticipated. The current rule states that an FCU/FISCU should purchase additional coverage when circumstances warrant, such as cash on hand or cash in transit. Comment was requested regarding whether there may be additional situations in which credit unions may want to consider in determining whether to raise their bond coverage above the required amounts. At this point the MCUL does not have any additional situations in which it would recommend increasing bond amounts.

The proposal also notes that Credit Union Blanket Bond Standard Form 23 of the Surety Association of America has not been changed since 1950 and is no longer used by many credit unions. Comment was requested regarding whether to rescind the form. While the MCUL is not aware of any of our member credit unions who currently use the form, we have not done an extensive enough inquiry to know for sure. Thus at this time we cannot advise whether to rescind or maintain the bond form.

We appreciate the opportunity to comment.

Sincerely,

Matthew Beard
Regulatory Specialist
Michigan Credit Union League

cc: Credit Union National Association, Inc.