CUNA
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February 1, 2010

Jennifer J. Johnson
Secretary
Board of Governors of the
Federal Reserve System
20th St & Constitution Ave, NW
Washington, DC 20551

Re: Docket No. R-1381, Establishment of Term Deposits

Dear Ms. Johnson:

The Credit Union National Association (CUNA) appreciates the opportunity to comment on the Federal Reserve Board's (Board) proposed amendments to Regulation D, Reserve Requirements of Depository Institutions. The proposed rule would authorize the establishment of term deposits, which would be similar to interest-bearing certificates of deposit but which would be held at the Federal Reserve. By way of background, CUNA is the largest credit union trade organization in this country, representing approximately 90 percent of our nation's nearly 8,000 state and federal credit unions, which serve approximately 93 million members.

Discussion

We supported the Board's implementation of amendments to the Financial Services Regulatory Relief Act, effective October 9, 2008, to pay interest on certain deposits of eligible institutions held at Reserve Banks, such as on required reserve balances. The Act also authorizes the Board to pay interest on balances in excess of required reserve balances. In that connection, the Board is proposing to amend Regulation D to authorize the establishment of interest-bearing term deposits at Reserve Banks. The Board's stated rationale is that, "[t]erm deposits are intended to facilitate the conduct of monetary policy by providing a tool for managing the aggregate quantity of reserve balances."

Under the proposal, institutions eligible for the term deposits are those defined as "depository institutions" in section 19(b)(1)(A) of the Federal Reserve Act. This could also include credit unions.

We generally support the proposal, but we urge the Board to consider any unintended effects of the plan. We believe the authorization of term deposits may provide a favorable option for institutions to earn interest on short term investments without credit risk.

Auction Process

Under the proposed auction process, the Board would conduct regularly scheduled auctions, offering a fixed quantity of term deposits with relatively short maturities. Eligible institutions wishing to take part in the auction would indicate both the interest rate they would accept and the amount of money they would deposit at that rate. The Board seeks comment on whether it is necessary to place any limitations on the maximum amount of term deposits that an institution may hold or on the maximum portion of a single offering that an institution may win at auction.

If the auction method were adopted, we are concerned that larger participating financial institutions would dominate the process.

We encourage the Board to include in the final rule a vehicle for smaller institutions, including credit unions, to participate as a group. Such an aggregator would help ensure that all institutions would be able to participate in at least the auction stage of the process regardless of asset size or institution type.

In addition, we recommend the Board consider limiting the maximum portion of a single offering that an institution may win at auction, as well as limiting the aggregate amount of term deposits an institution may hold.

Maturity Terms

As proposed, term deposit maturities would not exceed one year and would likely range from one to six months. An institution would be permitted to hold term deposits of more than one maturity simultaneously, but would not be permitted to withdraw deposits prior to maturity. The Board seeks comment on what the appropriate maturity or maturities for term deposits should be, and whether more than one maturity should be offered.

In our view maturities should be consistent with those for similar investments, in multiple terms of 30 days each.

We also recommend the Board consider allowing early redemption of term deposits under certain circumstances that would be predetermined by the Board. Such an exception would provide flexibility for institutions that encounter unforeseen financial difficulties. However, we recommend the Board attach a reasonable penalty, the parameters of which should be addressed in the final rule, to any term deposits redeemed prior to maturity.

Discount Window

We support the proposed provision to allow participating institutions to use term deposits as collateral for borrowing from the Federal Reserve's discount window. Assuming a process would be implemented to allow smaller institutions to participate in term deposits, allowing such deposits to collateralize discount window borrowing for eligible institutions would provide an alternative means to access affordable funds.

Thank you for the opportunity to express our views on this important proposed rule. If you have questions about our letter, please do not hesitate to give Senior Vice President and Deputy General Counsel Mary Dunn or me a call at 202-508-6743.

Sincerely,

Luke Martone

Luke Martone
Regulatory Counsel