assuming an immediate and sustained parallel shift in interest rates of up to and including plus 300 basis points, and shortens by 6 years or less, assuming an immediate and sustained parallel shift in interest rates of up to and including minus 300 basis points.

(iii) *Price sensitivity test.* The estimated change in the price of the CMO/REMIC is 17 percent or less, as a result of an immediate and sustained parallel shift in interest rates of up to and including plus and minus 300 basis points.

(2) The three tests contained in paragraph (e)(1) of this section shall apply at the time of purchase and on any subsequent date, based on market prices, interest rates, and estimated prepayments at the time of testing. CMOs/REMICs must be retested at least quarterly, more frequently if market or business conditions dictate.

(3) Before a federal credit union may invest in a CMO/REMIC, the board of directors must set forth, in its investment policy, the method by which the credit union will obtain the prepayment estimates necessary to conduct the tests contained in paragraph (e)(1) of this section. In its policy, the board must state whether the credit union will use either a median prepayment estimate or individual prepayment models, one of which may be the median estimate. Only one method may be selected; once selected, it is the only method that may be used when testing a CMO/REMIC. If the board elects to use individual prepayment models, it must identify specific models, with a minimum of two. If a median prepayment estimate is used, it must be obtained from an industry-recognized information provider. At purchase, the median estimate must be based on at least 5 prepayment models. At retesting, the median estimate must be based on at least 2 prepayment models. If individual prepayment models are used, estimates must be obtained from all of the prepayment models identified in the federal credit union's investment policy. One of the individual prepayment models may be the median prepayment estimate from an industry-recognized information provider. At purchase, a CMO/REMIC must pass the tests for each prepayment model used. At retesting, the CMO/REMIC must pass the tests for a majority of the prepayment models used at the time of purchase.

(f) *Corporate credit unions.* A federal credit union may purchase shares or deposits in a corporate credit union, except where the NCUA Board has provided notice that the corporate credit union is not operating in compliance with part 704 of this chapter. A federal credit union's purchase of corporate credit union capital shares, as defined in part 704 of this chapter, is limited to one percent of the investing credit union's assets.

(g) *Municipal securities.* A federal credit union may purchase and hold a municipal security only if it has been rated in one of the two highest rating categories by at least one nationally recognized statistical rating organization.

(h) *Variable rate investments.* The index of any variable rate investment must be tied to domestic interest rates and not, for example, to foreign currencies, foreign interest rates, or domestic or foreign commodity or equity prices. For purposes of this part, the U.S. dollar-denominated London Interbank Offered Rate (LIBOR) is considered a domestic interest rate.

(i) *Yankee dollars, eurodollars, and bankers' acceptances.* A federal credit union may invest in yankee dollar deposits in a Section 107(8) institution, in eurodollar deposits in a branch of a Section 107(8) institution, and in bankers' acceptances issued by a Section 107(8) institution.

§ 703.5 Prohibitions

A federal credit union is prohibited from:

(a) Purchasing or selling a standby commitment or an option contract, except as permitted under § 701.21(i) of this chapter;

(b) Purchasing or selling futures or interest rate swap contracts;

(c) Engaging in pair-off transactions, adjusted trading, when issued trading, or short sales;

(d) Purchasing stripped mortgage backed securities, residual interests in CMOs/REMICs, mortgage servicing rights, commercial mortgage related securities, or small business related securities; and

(e) Purchasing a zero coupon investment with a maturity date that is more than 10 years from the settlement date.

§ 703.6 Pledging securities.

(a) *Permissible activities.* A federal credit union may pledge securities through reverse repurchase transactions, securities loans, and collateralized borrowing, and receive in exchange cash, other securities, and/or a fee.

(b) *Limitations.* (1) A federal credit union may enter into a transaction described in paragraph (a) of this section provided that the transaction is priced to reflect accrued interest, the risk of the securities, and the terms of the transaction.

(2) Cash obtained in a transaction described in paragraph (a) of this section is subject to the borrowing limit specified in Section 107(9) of the Act.

(3) Any investment purchased with cash obtained in a transaction described in paragraph (a) of this section must be a permissible investment for federal credit unions and must mature no later than the maturity of the transaction.

(4) Any security received in a transaction described in paragraph (a) of this section must be a permissible investment for federal credit unions.

§ 703.7 Divestiture requirements.

(a) Any federal credit union in possession of an investment that fails a requirement of this part, either because it has been downgraded below a minimum rating by the same rating agency used when it was purchased or because it is a CMO/REMIC that does not meet one of the tests set forth at § 703.4(e) upon retesting, must, within 30 days of the date of the failure, provide written notice of the failure to the board of directors and the appropriate regional director, except that notification to the regional director is not required if the investment matures within 90 days.

(b) If the federal credit union does not sell the failed investment within 30 days of the date of the failure, it must provide to the regional director, within 60 days of the written notice, a written plan to hold the investment. The regional director, however, has the authority to require the written plan within a shorter timer period or require immediate divestiture if serious safety and soundness concerns are present. The plan must address:

(1) The investment's characteristics and risks;

(2) The process to obtain and adequately evaluate the investment's market pricing, cash flows, and risk;

(3) How the investment fits into the credit union's asset liability management strategy;

(4) The impact that either holding or selling the investment will have on the federal credit union's earnings, liquidity and capital in different interest rate environments; and

(5) The likelihood that the investment may again pass the requirements of this part.

(c) Except where serious safety and soundness concerns are present, the federal credit union is not required to sell the investment until it receives a written response to the plan described in paragraph (b) of this section from the regional director.