CENTRAL
ONE FEDERAL CREDIT UNION

MAY21'14 PM 3:03 BOARD

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

Re: Risk Based Capital Proposal

Date: May 14, 2014

Dear Mr. Poliquin,

Thank you for the opportunity to comment on NCUA's Proposed Risk-Based Capital Rule. Central One Federal Credit Union is a $375 million credit union serving over 29,000 members in Central Massachusetts that will be adversely affected by the proposed rule, moving from "Well Capitalized to "Adequately Capitalized", due to the overly conservative logic behind this newly proposed regulation.

While the theory of assigning different capital requirements based on balance sheet structure may be prudent, the proposed rule for assigning risk weights is inconsistent and significantly distorts the measurement of a credit unions' risk level. The proposed risk weightings paint asset classifications with a broad brush without measuring the specific characteristics and true risk level of those asset classifications. The inconsistencies incent certain riskier behaviors while penalizing some behaviors with less risk. The following are specific concerns we have with the proposal:

<u>Other Real Estate</u>

Adjustable rate home equity lines of credit have been a very effective tool to mitigate interest rate risk for a rising interest rate environment. For many years, regulatory bodies have been warning financial institutions to take steps to prepare for the eventual rise in interest rates. The proposed rule will effectively neuter one of the most powerful tools we have to mitigate interest rate risk. It is puzzling that a conservatively written, home equity portfolio carries a higher risk weighting than an unsecured loan portfolio and is subject to very strict concentration risk limits. The starting risk weighting for other real estate should be lower than unsecured loans and the concentration risk penalty should start at a much higher point than 10% of assets.

<u>Investment Weights</u>

In the proposed rule, investments are the only category to carry higher risk weightings as the weighted average life increases. It does not make sense that a 30 year fixed rate mortgage carries a risk weighting of 0.50 to 1.00 depending on concentration, yet the same structure when securitized carries a risk weighting that is two to three times higher. The proposed rule penalizes a product that helps credit unions limit both credit risk and concentration risk. This rule may cause credit unions to portfolio more of their mortgages, which will effectively make credit unions incur much more interest rate risk.

NCUSIF Deposit

On the numerator side (capital), the deduction of the NCUSIF deposit from the capital base harshly penalizes credit unions for their cooperative structure. By eliminating the NCUSIF deposit from our capital, it is essentially being treated as an expense and no longer an asset of the credit union. Our NCUSIF deposit, held by the NCUA, theoretically is in the safest hands possible and should not be deducted from the capital base.

Credit Union Service Organizations (CUSOs)

CUSO's have been a great way to diversify our income sources while building capital and better servicing our membership. One of the benefits of CUSOs is that their performance isn't tied to the same external factors as the rest of the credit union, such as interest rate movements. The risk weighting of 2.50 is totally unwarranted (especially for wholly owned CUSOs) since in most situations credit unions would be able to sell or liquidate their investment in a shorter time period than the 2.50 risk weighting would imply.

Unfunded Commitments

The treatment of unfunded commitments will force credit unions to rethink the services that we provide members, particularly small businesses. Many small businesses rely on the credit union to expand their businesses and for many the unfunded portion provides a comfort level in the event they need short term funding. The reality that we have seen is a good portion of the credit line will never be used, but provides an invaluable service to our local businesses.

The 75% conversion ratio for commitments on business loans does not mirror reality for the usage rate and the rule would force many credit unions to decrease credit lines to small business owners.

Corporate Credit Union Capital

The risk weightings for investments in corporate credit unions are an unnecessary penalty against credit unions who stepped up to the plate to help stabilize the corporate credit union system when they were most in need to limit losses to the industry. With the new stricter rules implemented by the NCUA relating to corporate credit unions, the majority of the risk has been eliminated and the risk weightings for corporate credit union investments are excessive.

Short Implementation Period

If a new risk based capital rule is approved, we feel that the rule taking effect 12 to 18 months after approval is far too short of a timeframe for credit unions to comply and alter their business strategies. Years of decision making by credit unions cannot be unwound in a short time frame and a fairer approach would be for the rule to be phased in over a lengthy period of time similar to Basel III where the final capital requirement of 10.5% is not reached until 2019.

To summarize, the risk weightings do not take into account important characteristics of the balance sheet. Unfortunately a simple formula cannot accurately measure risk. Credit unions will not be managing actual risk, but managing around a flawed system.

Thank you for taking into account our concerns and that the feedback received will help lead to a more realistic and fairer measurement process.

Sincerely,

David A. L'Ecuyer
President/CEO