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Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

NEW HAMPSHIRE CREDIT UNION LEAGUE
COMMENTS ON PROPOSED RULEMAKING FOR PART 702

BY E-MAIL ONLY - regcomments@ncua.gov

Dear Secretary Poliquin:

On behalf of the New Hampshire Credit Union League ("League"), please accept this letter of comment relative to the proposed rulemaking by the National Credit Union Administration ("NCUA") relative to risk based net worth ("RBNW") found at 12 C.F.R. Part 702. The League is the state credit union trade association serving approximately 19 federal and state chartered credit unions that are federally-insured and cooperatively owned by 537,031 consumers as members in the state of New Hampshire, and operates as part of the Credit Union National Association ("CUNA").

The League appreciates the opportunity to provide input on such an important topic. The League believes that this is the single most consequential rule that credit unions have ever faced. The impact of the proposal is far reaching and long lasting. Even though the proposed new capital standard applies only to credit unions in excess of $50 million in assets, the League believes that every credit union is concerned as the proposal significantly impacts the management of credit unions and growth.

The League notes that the NCUA is reviewing its risk based capital rules at a time when the framework for capital changes in the financial services industry is well underway. The League is pleased that NCUA has already stated that provisions of the proposed rule are not "etched in stone" and has indicated a willingness to complement its previous rules addressing interest rate risk through the approved use of derivatives and interest rate risk policies with the proposed RBNW rule. Finally, the League believes that the NCUA welcomes and will act on suggestions for change received not only through the current public comment letter process but also by considering those received through its upcoming Listening Sessions scheduled in geographically dispersed locations across the country in the upcoming months of June and July.

1. The State of New Hampshire Credit Unions

New Hampshire credit unions, regardless of size or charter, have withstood the most challenging economic cycles since the Great Depression. From the crisis in the 1980s, 1990s, and late 2000s, to the present, credit union capital positions have remained strong and stand at the end of last year at a healthy 10.37%. Similarly, delinquency is at a manageable level of .47 %. The League suggests that New Hampshire credit unions have demonstrated the ability to learn from previous fiscal challenges as well as to manage through tough economies. Competence in capital management and the adequacy of the existing regulatory leverage ratio is evident.

The League notes that there are presently 10 credit unions in New Hampshire possessing assets in excess of $40 million, a realistic threshold to measure the impact of the proposed rule in the short term. Of these credit unions, 2 would fall from well-capitalized in the current system to adequately-capitalized in the proposed system. Furthermore, only 1 would enjoy a greater cushion above the well-capitalized threshold under the NCUA proposal. A total of 8 credit unions or 80% of our total would experience a decline in their well capitalized levels. Thus, if passed in its present form, then the League suggests that the rule will have significant unintended consequences for credit unions.

The remainder of this comment letter will further address these concerns. It should be noted that the issues raised in this comment letter were provided to the League by New Hampshire member credit unions through comments compiled from the use of an on-line survey, an educational session, a series of workshops and individual comments and discussions.

2. The Proposed Rule Lacks Necessity, is Misapplied, Contains Technical Flaws and Incorporates a One Size Fits All Approach

As a system, credit unions should not ignore the concept of risk-based net worth. It is helpful to know where the most risk is and to adopt measures in place to address it. However, the League first questions whether the proposed capital rule is even necessary in light of the fact that federally-insured credit unions' high net worth leverage ratio requirement already demands higher capital levels than similarly sized banks. The League recommends that a design of any risk-based net worth requirement by NCUA should reflect a reasoned judgment about the actual risks involved.

Moreover, the League notes that the Federal Credit Union Act ("Act") directs NCUA to devise a risk-based requirement, but the risk-based component for the well-capitalized threshold can be no higher than the component for the adequately capitalized level. Under the proposal, an adequately capitalized credit union would need to maintain a net worth ratio of 6% as required by statute and a RBC ratio of 8% of equity to risk assets. A well-capitalized credit union would need 7% as required by statute and a higher RBC ratio of 10.5%. The recent comment letter submitted to the NCUA by the former Chairman of the U.S. Banking Committee Alfonse

D'Amato who served at the time the Act was amended to include prompt corrective action provisions sheds insight into statutory intent and is worthy of review. It concludes that a separate risk based requirement for well capitalized credit unions was not contemplated.

The League also suggests that the excess capital requirement as presented does not reasonably reflect inherent balance sheet risk. It is the product of a formula that is overly simplistic and inconsistently attempts to manage concentration, credit, and interest rate risks by using one model to produce one value of overall risk. Liabilities are expressly ignored. Trying to manage a credit union to just one number that captures only half of a credit union's balance sheet engenders instability, restricts innovation and competitiveness and creates disadvantages to credit union membership.

As the system proposed only goes in one direction, the League is unable to support it. Implementation will result in essentially allowing the NCUA to manage credit union growth. The NCUA will determine how deep a credit union gets into certain loan categories. It will be able to manage investment modeling and investment in new products that a credit union may make in CUSO-driven offerings.

Finally, the proposal also dictates that if the proposed formula does not work, then the rule as presented permits the NCUA discretionary authority to determine a credit union's proper capital level. This rule would significantly diminish the responsibility of boards and management to make critical financial judgments, determine the strategic direction of the credit union, and oversee policy.

3. The Proposal Will Weaken Credit Unions' Ability to Meet Member Needs and Deliver Member Value

The challenge of excessive regulation may be more daunting than all of the challenges in the proposed rule combined. If credit unions are being regulated to the past economic crisis, one that we may never see again as noted in remarks delivered recently by Consumer Financial Protection Bureau ("CFPB") Director Richard Cordray, then prospects for helping consumers improve their financial lives today will continue to be adversely impacted.

If this proposal is approved as proposed, then all credit unions would need to have their balance sheet in one hand and the risk-based capital requirement in the other hand to determine what they can offer to their members with no flexibility to manage the credit union when the financial environment changes.

This is especially problematic because credit unions in general do not have access to supplemental capital and in order to meet these additional capital requirements, would likely have to implement some combination of the following strategies: (1) eliminate or significantly reduce existing products, (2) charge members higher fees, (3) raise loan rates and / or drop deposit rates, (4) restructure the balance sheet to sell long-term loans and investments, or (5) deliberately slow or reduce asset growth. None of these strategies benefit our members or contribute to the long term sustainability of the credit union charter.

4. The Risk Weights Do Not Account for Key Considerations and are Inconsistent

Credit unions are presented to members and the public as a more affordable alternative to banks. Credit unions may be a more affordable alternative, but certainly a far less competitive alternative under the proposed rule. Of priority concern in the Northeast under the proposal is the restrictive treatment of a staple product: mortgages. The risk weightings are overly general and do not take into account the nuances of particular portfolios. They appear to be structured to discourage credit unions to engage in common forms of lending. As a general premise, the League strongly opposes measures in the proposal for credit unions that exceed Basel III standards for small banks. Such measures should be redirected to more accurately reflect the risk to credit unions.

For example, some real estate loan portfolios are not as risky as others based on policies, loan-to-value, and other terms. NCUA examiners have constantly measured credit unions against the principle that short term and adjustable rate mortgage loans have less risk than longer term fixed rate loans. Many credit unions sell all or a majority of fixed rate product into the secondary market as repeatedly recommended by examiners. Yet the proposed rule does not reflect this concept. In fact, high risk weights under the proposal are imposed even on residential mortgages guaranteed by the federal government. An additional local adverse impact will be experienced by credit unions who utilize the Mortgage Partnership Finance Credit Enhanced Product available from the Federal Home Loan Bank as a tool to help share in the risk of loans sold. Lumping mortgages and basing the weighting on years to maturity totally discounts quality. Mitigating factors must be incorporated into the final rule.

Mortgage servicing rights are also treated unfairly under the proposal. They should incorporate any market value changes for the servicing rights.

The League also notes that New Hampshire credit unions continue to evaluate the impact of the recent QM rules promulgated by the CFPB on their mortgage lending products and member needs. The NCUA should exercise caution in its final deliberations on the mortgage risk weights to ensure that any changes in capital for credit unions does not harm access to credit for consumers in light of all recent changes to mortgage rules during this delicate transition period.

With respect to member business loans ("MBLs"), the proposal appears to regulate credit risk in a capital requirement alone. Credit unions are held to a very high regulatory standard when making a business loan. The proposed rule penalizes such lending and does not consider historical experience or portfolio performance. For credit unions whose strategic plans incorporate an increase in business loan portfolios, the proposal will have a chilling impact by slowing growth in business loans, which are already subject to a statutory cap, and ultimately a detriment to member access to capital and community economic growth.

The risk weights are applied equally for all loans or investments in some categories. The League does not support this treatment and suggests that performing secured consumer loans should not be combined with unsecured consumer loans. Without question secured loans are less risky than unsecured loans and the proposed rule should reflect this fact. The risk weights for long term investments again only capture interest rate concerns and ignore credit or asset liability management considerations. The risk weight focus on average life of an investment is also not a complete measurement.

The treatment of investments in CUSOs is also a concern. The significantly high proposed weight will hamper credit union collaboration and investment in credit union businesses that provide value to the membership and professional expertise to deliver products and services in a safe and sound manner. It does not consider the financial, managerial strength, or record of performance of a CUSO. Without change, this provision of the proposal is very likely to reduce the array of services available to members.

The weightings NCUA assigns to corporate credit unions is also concerning, especially given the revision NCUA has made to the regulation governing corporate credit unions, Part 704. Corporate credit unions have been significantly limited in how they can invest member funds, including strict concentration limits. Under the revised Part 704, corporates also must maintain additional capital. The proposed risk weighting on perpetual capital in corporates does not reflect the reduced risk that corporates have under the revised Part 704 and credit unions should not be penalized for continuing to participate in the corporate credit union network. Similar to the work NCUA has done to reduce interest rate risk through its new IRR regulation and its new derivatives regulation, NCUA did not consider the changes it has already implemented with corporates with the revision of Part 704 when assigning corporate risk weights.

The League suggests that without modification, the proposed risk weightings will encourage changes in credit union balance sheets and send a signal that growth should be based on assets with lower risk weights to minimize the compliance and regulatory burden.

5. **Discretion to Change Risk Weights and Capital Requirement is Overly Broad**

Additional authority under Section 702.105(c) of the proposal which permits the NCUA to impose higher capital requirements on individual credit unions also causes concern. The absence of parameters around this authority regardless of which level of supervision at the NCUA administers it could result in an inconsistent application of the rule. If a credit union updates its strategies, policies, products and systems to comply with the rule and maintains any corresponding level of capital, then it should have some assurance that it will not be subject to an overbroad standard that may require additional capital.

6. **Risk Based Capital Calculations on the NCUSIF and Goodwill do not Reflect Credit Union Value or Uniqueness**

The proposed rule seeks comment on whether the National Credit Union Share Insurance Fund deposit should be excluded from the risk based capital calculation. The League suggests that the treatment of the deposit as an asset reflects the voluntary capitalization of the share insurance fund by the industry, distinguishes the credit union fund from others and greatly contributes to the structural stability and strength of the fund. It is a tangible cash deposit with the NCUA beyond the reach of creditors. The elimination of the NCUSIF deposit from the proposed calculation effectively takes away a valid asset, classified under GAAP, that would be immediately returned if the credit union were voluntarily liquidated or converted to another form of charter. The proposal treats it like an expense or a write-off. Goodwill has real value, particularly in merger transactions, and is similarly viewed under the proposal. The proposed elimination has a material impact on the risk based capital ratio and will cause confusion as to its future economic value. The League does not support exclusion.

7. Credit Unions Will Be at a Disadvantage Compared to Banks

The rule, as proposed, also misses the mark in that it places credit unions at a competitive disadvantage and requires far more capital than what is required for banks. NCUA's proposed formula would require a credit union to keep an approximate 128% higher capital level, $1.8 million per $100 million of assets, than a bank with the same asset level and balance sheet composition. That is a problem because the only way credit unions can raise capital is by charging more on loans or paying less on savings, so the rule would require credit unions to offer terms on loans and deposits that are less attractive than their banking counterparts. The result is that a credit union borrower would be required to pay a higher capital tax than a bank borrower.

The League suggests that it is not reasonable to impose additional hardships such as the competitive impact as credit unions did not cause the economic meltdown and aided consumers and businesses in the wake of the recession. In contrast, banks benefited from the extremely low rate environment and have not passed those benefits back to their customers. It is appropriate to consider regulatory treatment under the proposed rule in an equivalent manner to our ethical and responsible practices.

This elevated risk rating system will also impact pending transactions within the industry. The number of credit unions willing to consider merging with other credit unions will likely be reduced, refocusing the industry to consider conversions to other types of charters whose Basel III calculation appears to be less onerous.

8. The Implementation Period is Too Short and Contributes to the Regulatory Burden

The time period for implementation is unreasonably short at 18 months given the complexity of the proposal. The League is concerned that the proposed implementation period does not permit a sufficient period to allow for industry education as well as time to plan for and execute balance sheet, operational and system accommodations and strategic adjustments. A much longer period is requested. The experience and recommendation by the FDIC in finalizing a tiered approach in terms of years and asset size has merit. Credit unions need more time to make the necessary changes to be in compliance. The proposal does not allow for an adequate transition period.

In summary, the League believes that sound regulatory policy requires a balancing of safety and soundness principles with sufficient flexibility to allow credit unions who are deeply rooted in their local economic environments to manage a plan that promotes growth for their credit union, service to members and a stable economic environment. A reasonable RBNW structure incorporating the suggestions set forth in this letter will continue the NCUA's encouragement to credit unions to help members in any manner possible.

New Hampshire credit unions have strong consensus that the proposed rule will place them at a disadvantage by requiring higher capital levels and simultaneously penalizes credit unions for certain investments as evidenced by the excessive and inconsistent risk weightings on assets such as mortgages, investments, and CUSOs. The League suggests that the proposed RBNW does not have to be so heavily weighted to interest rate risk based on the NCUA's work in recent years and most recently through the derivatives, liquidity and interest rate risk policy rules. Planning for the future, rather than regulating to the past financial cycles, is the direction that the League encourages the NCUA to consider in finalizing the proposed rule. Utilizing the examination process to foster discussion between examiners and credit unions to promote an understanding of each institution's strategic plans for assessing and mitigating risk is welcomed.

Thank you for your consideration of the views of New Hampshire credit unions. I look forward to working with you on this important proposed rule.

Sincerely,

Paul Gentile

Paul C. Gentile
President/CEO

PCG/mabc