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April 27, 2015

Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration ("NCUA," "Administration," or "agency")
1775 Duke Street
Alexandria, VA 22314-3428
regcomments@ncua.gov

RE: RIN 3133-AD77 - Comments on Proposed Rule: PCA – Risk Based Capital II

Mr. Poliquin:

Oregon Community Credit Union ("OCCU") respectfully submits the following response to and outline of our continued concerns with the NCUA's modified proposed amendments to Part 702 of its regulations regarding Prompt Corrective Action: Risk-Based Capital ("RBC II" or "modified proposed amendments").

EXECUTIVE SUMMARY

- **Reconsider the *need* for the proposed RBC rule within the credit union industry and the *efficacy* of such a rule given the *demonstrated* and *crisis-tested* sufficiency of industry capital levels.**
- **Lower the proposed risk weights for both non-consolidated *investments in CUSOs* and *mortgage servicing assets*.**
- **Allow all forms of goodwill to be considered as capital in the RBC equation numerator without effective date limitation.**
- **Reconsider the *need* for special interest rate risk rulemaking given the *already clear guidance* and *level examination scrutiny* of this highly visible area given today's low rate and anticipated rising rate environment.**
- **Reconsider the *definition* of "complex" credit unions to include factors other *than asset size*.**
- ***Continue* to *support* the inclusion of *supplemental capital* in the proposed RBC equation numerator and champion requisite federal and state rulemaking accordingly.**
- **Reconsider the *need* for *additional capital adequacy* review during examinations that could *conflict* with the proposed RBC rule and create *inconsistent* supervisory expectations.**

RESPONSE OVERVIEW

1. We certainly appreciate the Administration's reconsideration of several key components of the RBC I proposal following the comment period and applaud the following significant modifications: (i) removal of provisions allowing for broad examiner discretion in requiring capital levels greater than those established within the proposed amendments; (ii) delay of the effective date of any final rule, allowing for a 3-year or longer implementation period necessary for credit unions to cost effectively rearrange their balance sheets to comply; (iii) reconsideration of the more restrictive factors of both the numerator and denominator in the proposed risk-based capital ratio equation; (iv) reconsideration of several asset risk-weightings; and (v) consideration of additional rulemaking allowing for credit unions to raise supplemental capital in order to meet the proposed risk-based capital thresholds and continue to experience growth and serve Members while complying with the thresholds.

   While not directly impacted, OCCU also acknowledges positive changes to the threshold for a "Well Capitalized" classification under RBC II and to the improved definition of a "complex" credit union by means of a higher asset size threshold; both are also strong improvements with respect to the industry at large.

2. The above improvements notwithstanding, OCCU continues to encourage the Administration to further consider the purpose of such a requirement. We continue to question the foundational support for such a rule:

   I. As we requested in our response to RBC I, the modified proposed amendments should also be carefully re-evaluated with respect to the *need* for such rulemaking. The current net worth (or leverage) ratio requirement has served the industry well while allowing credit unions to manage their asset bases as they see fit subject to maintaining Member reserves at 7% or more of those assets in order to be classified "Well Capitalized."

   II. We continue to stress the facts: *natural person credit unions*, such as OCCU, remained strong during the recent financial crisis. There is no evidence to support that these credit unions were undercapitalized during or following the crisis and thus we ask the Administration to consider factually whether the NCUSIF would have experienced any material reduction in losses had RBC II been in place during that crisis. If not, the efficacy of such a requirement should be carefully weighed against its costs and impacts to an otherwise well capitalized industry.

3. Should the NCUA continue its intent to implement a version of RBC, we again request consideration of a measure of flexibility in the process as opposed to a rigid matrix-driven model applied to all credit unions subject to compliance. Examples of such flexible factors might include:

   i. The existence of demonstrated asset quality, demonstrated risk management activities, positive historical performance, and other qualitative and environmental factors in the calculation of risk-based capital regardless of weight-based outcomes.

   ii. Inclusion of risk-weight *ranges* for credit unions performing favorably with respect to the above performance factors as well as those designated as "Well Capitalized" under the current net worth ratio.

   iii. Reclassification of the risk-based capital table as a *model*, much like current IRR or liquidity risk management tools, as opposed to a "hard and fast" rule requiring rigid compliance thereto.

   iv. Exemptions to the proposed amendments or, alternatively, a capital "credit" for those credit unions historically concentrated and operating in business lines subject to significant additional capital requirements, such as MBLs, but where strong historical performance is demonstrated.

   v. Application of the more restrictive risk-based capital ratios *only* for credit unions below the "Well Capitalized" level.

   vi. Delayed effective date subject to the availability of supplemental capital.

4. Mr. Poliquin, OCCU offers the above comments and recommendations following our careful review of the proposed modified amendments and their probable impact on our credit union and on our industry. Our review of the modified proposed amendments disclosed the following:

   i. While the modified proposed amendments rectify some of the concerns regarding the seemingly arbitrary assignment of certain asset weights, we continue to struggle with the notion that a "one-size-fits-all" solution can or should be applied universally to such an advantageously diverse population of credit unions without consideration of each credit union's unique strengths and characteristics.

   ii. Continued concern with respect to certain selected proposed asset weights, principally for mortgage servicing assets and investments in CUSOs.

   iii. Continued concern with the proposed treatment of goodwill as a component of the RBC calculation.

iv. Frankly, we find inclusion of an entirely separate and new risk consideration in interest rate risk surprising in the second draft of a capital risk rulemaking proposal.

v. Continued concern regarding the definition of a "complex" credit union premised entirely on asset size.

vi. Serious reservations regarding a new capital "adequacy" test in addition to the RBC requirements and metrics, potentially creating a separate and subjective second assessment of capital sufficiency during the regulatory examination process.

vii. While citing as a primary objective the desire to be consistent with "Other Federal Banking Regulatory Agencies" in initially proposing the amendments, the result of RBC II is that credit unions would still be competitively disadvantaged relative to banks in a number of asset weights.

viii. The modified proposed amendments will still have the unintended effect of weakening strong, well-managed credit unions and hurting the Members they serve.

SPECIFIC ISSUES

In considering the modified proposed amendments, we offer the following detailed observations:

1. Asset Weights

   I. While positive changes were made to the risk weights assigned to many asset categories, we continue to encourage the Administration to re-evaluate those assigned to mortgage servicing rights and investments in CUSOs.

   II. A 150% risk-weight (reduced from the originally proposed 250% and now only applied to unconsolidated investments) is assigned to investments in CUSOs with no regard to actual *per institutional* CUSO purpose (such as cost savings, or service CUSOs), profitability, or risk management activities places a still seemingly arbitrary penalty on applicable credit unions based on the supposition that all such CUSOs are risky ventures.

   III. The modified proposed amendments would still require OCCU and other current CUSO investors to re-evaluate whether the returns from those ventures can support the high risk-weighting assigned to this equity investment in the CUSO over potential benefit to the Membership.

IV. In addition, we have contemplated additional CUSO development opportunities, many in service-provision capacities to other credit unions, but would be required to offset any value-added considerations of these ventures with formulistic capital constraints on the entire asset class developed without any consideration of the relative risks of each prospective CUSO's mission or OCCU's demonstrated ability to manage those risks.

V. The modified proposed amendments did not alter the 250% risk weighting for mortgage servicing assets which we believe could discourage interest rate risk-reducing/liquidity generating loan sale strategies, negatively impacting and discouraging loan participations between credit unions, resulting in Member service reduction.

VI. With respect to risk weights in general, in some cases, the modified proposed amendments still include higher asset risk-weightings than required of banks resulting in credit unions tasked with having *higher capital* requirements relative to achieving the same capital ratio result.

VII. This places credit unions at a disadvantage relative to price-based competition, the precise and seminal argument made by the same banks against the cooperative model for nearly a hundred years.

2. Goodwill

I. While the modified proposed amendments now allow for "supervisory" goodwill as part of the capital numerator in the RBC equation; it only does so until January 2025 and all other forms of goodwill continue to be excluded.

II. While the NCUA's definition of a "supervisory" merger is liberal and might well include typical mergers of credit unions, its exclusion of other forms of goodwill could affect further business decisions due to this unfavorable treatment in the RBC calculation.

III. The January 2025 expiration for the inclusion of "supervisory" goodwill in the RBC calculation acts as a quasi and retroactive penalty for those credit unions whom participated in merger activities with troubled institutions in an effort to reduce the risk of loss to the NCUSIF during the financial crisis, often at the urging of state and federal regulators. We recommend that the Administration grandfather goodwill inclusion for those credit unions and allow that capital source to amortize or otherwise be deemed impaired and written down as required by GAAP.

IV. Beyond January 2025, outright exclusion of goodwill in the RBC calculation may serve to dissuade credit unions from assisting the regulators in acquisition of troubled institutions while proactive and welcome inclusion may have the opposite and more desirable effect.

V. Goodwill is recognized by GAAP and should be recognized in the RBC methodology; as such we recommend that all goodwill be included in the RBC calculation to the extent and duration in which GAAP recognizes it and, if not, that non-"supervisory" goodwill be phased out over a 10-year or longer period in the final rule.

3. Interest Rate Risk

I. The modified proposed amendments eliminated higher asset risk weights for longer term investments and other assets, thereby essentially eliminating interest rate risk ("IRR") from the RBC calculation; however, the Administration has solicited comments from credit unions regarding how the agency might otherwise incorporate IRR into section 702 Prompt Correct Action rules.

II. We remind the NCUA that IRR was specifically addressed in 2012 via Letter to Credit Unions ("LTCU") 12-CU-05 and 12-CU-11, Interest Risk Rate Policy and Program Requirements and Interest Rate Risk Policy and Program Frequently Asked Questions, respectively. We question the need for additional rulemaking with respect to IRR and especially caution against another "one-size fits all" model approach similar to RBC I and II.

III. Perhaps even more so than capital management, IRR management is subject to multiple analytical methodologies and subjective conclusions with respect to IRR faced by any one particular credit union and, furthermore, is based on materially dependent assumptions about macro-economic forces that make a uniform model problematic. OCCU believes the current rules, including the 2012 LTCUs and the highly scrutinized nature of the examination process in this area specifically (given a now 5+ year expectation of a rising interest rate environment) provides sufficient oversight of IRR.

IV. Should the NCUA pursue rulemaking with respect to a distinct IRR component of section 702, numerous and complicated considerations will need to be evaluated including:

a) The *method* to be used to assess IRR – net income ("NI") and net economic value ("NEV") impacts with respect to IRR are metrics predominantly used, typically depending on the size and complexity of the credit union and its balance sheet; NCUA will have to be fairly specific with respect to which metric (or both or an alternative metric) is to be used under enumerated circumstances.

b) The *assumptions* used to assess IRR – modeling IRR impacts require critical and often highly subjective assumptions input into a model in order to "shock" relevant metrics such as NI or NEV given wildly diverse interest rate movement projections. With such broad latitude in modeling inputs, any IRR rulemaking will, in order to effectuate a uniformly applied model, necessarily need to include tangible and consistent model input requirements.

c) The *time frames* used to assess IRR – current rule emphasis is placed on forward-looking analytics and credit unions apply a variety of future period assessments when analyzing IRR; future rulemaking in this area will need to include requirements with respect to the satisfactory forward-looking time frames that will be subject to any IRR thresholds.

d) The *models* used to assess IRR – credit unions presumably employ a variety of different techniques or models, including those developed in-house, and those acquired through third party vendors and service providers; future rulemaking in this area will require delineation of expectations for the use of modeling in the IRR assessment practice.

e) The *regulatory* IRR limits to be applied – perhaps the most problematic consideration when contemplating a statutory scheme for IRR management is the development of a uniform set of IRR limits or thresholds against which credit unions must consistently be assessed and rated. As noted above, unlike capital metrics, IRR metrics and results will return risk profiles quite differently depending on balance sheet construction and thus a single set of regulatory risk limits will certainly be more arbitrary than predictive of true risk.

f) Finally, the *regulatory rating scheme* for IRR – banks are subject to a CAMELS composite rating with the "S" assessing sensitivity to market risk; NCUA rulemaking in this area will require modification to the industry's long standing composite rating scheme.

4. "Complex" Credit Unions

I. While the Administration increased the asset size definition of a "complex" credit union within the modified proposed amendments, thereby removing additional smaller credit unions from the proposed rule, we still find it problematic that complexity is defined solely by asset size.

II. Surely, several larger credit unions or those with assets greater than $100 million are, via the nature of their business models and balance sheet, far less complex than others perhaps a fraction of their size. We believe the NCUA should consider "complexity" apart from asset size in an effort to subject those more complex institutions to the higher capital requirements of RBC.

III. By increasing the asset size for credit unions deemed "complex" and thus subject to the modified proposed amendments while simultaneously lowering the "Well Capitalized" RBC ratio from the initially proposed 10.5% to 10.0%, the number of credit unions ultimately subject to the rule would only be 22% while only 2% would be negatively impacted in terms of an other than Well Capitalized" status. These projections further call into the question the need for and efficacy of such a rule.

IV. "Complexity" factors to consider might include the following and should include some definition with respect to which of the below triggers a "complex" definition:

a) Deposit account types and relative concentrations thereof.

b) Range and complexity of available Member services.

c) Lending product types and relative concentrations thereof.

d) Availability of investments and other non-deposit investment products.

e) Extent to which the credit union owns or invests in CUSOs and the nature of those businesses.

5. Supplemental Capital

    I. OCCU again applauds the agency in acknowledging the stark differentiation between banks managing to risk based capital rules with their ready access to corrective supplemental capital and credit unions that generally have no access to supplemental capital apart from growth in retained earnings. We support any rulemaking that contemplates the availability and use of supplemental capital in the RBC capital calculation and offer the following recommendations:

        a) Presumably, federal and state laws will require modification in order to allow credit unions to raise supplementary capital; the NCUA can influence those initiatives and proactively allow for supplementary capital, once available, to be included in the RBC calculation.

        b) Assuming required law changes take place, consider:

            1) The types of supplementary capital that might be appropriate for the cooperative model and be included in the RBC calculation.

            2) Any supplemental capital limits or, alternatively, limits with respect to inclusion in the RBC calculation.

            3) Minimal levels of investor due diligence and suitability prior to accepting supplemental capital.

            4) Consumer protection considerations with respect to those investors.

            5) Applicable consumer/investor disclosure requirements.

6. Capital "Adequacy"

    I. The modified proposed amendments specify that "notwithstanding the requirements" of RBC II, credit unions will additionally be held to a capital "adequacy" assessment given their risk profiles to ensure adequate and commiserate capital and compliance with internally desired capital ratio thresholds, despite its RBC classification. In our view, this clouds the issue in that if a risk based capital metric does not adequately capture the sufficiency of capital levels relative to an institution's risks, why implement it?

II. This capital "adequacy" assessment process includes expectations that in order for a credit union to ensure and demonstrate this capital sufficiency and goal setting relative to its risk profile, it must document its assessment to establish its capital goals relative to its risks as well as develop a comprehensive written strategy to maintain an "appropriate level of capital."

III. Apart from RBC requirements, this proposal places additional managerial requirements on already over-burdened credit unions and could result in disparate results relative to a credit union's RBC classification; in fact, this level of proposed capital management appears to mirror, in some respects, the capital management and stress testing required of the nation's largest banks, thrifts, and credit unions.

IV. We recommend the NCUA reconsider this proposal as outside of a statutory mandate for capital adequacy as contemplated in RBC II, a credit union's internal assessment of capital adequacy relative to its risks and associated capital ratio goals should not be subject to the inconsistent scrutiny embedded in the examination process.

Mr. Poliquin, we appreciate once more the opportunity to be heard on this matter critical to our industry.

Sincerely,

Mandy Jones

Mandy Jones
Chief Executive Officer
Oregon Community Credit Union