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December 31, 2013

Mr. Gerard Poliquin
Secretary to the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

Re: Proposed Rule on Capital Planning and Stress Testing RIN 3133-AE27

Dear Mr. Poliquin:

The Pennsylvania Credit Union Association (PCUA) appreciates this opportunity to comment on the National Credit Union Administration's (NCUA) proposed rule on Capital Planning and Stress Testing. PCUA is a state-wide advocacy organization that represents a majority of the nearly 500 credit unions located in the Commonwealth of Pennsylvania.

PCUA consulted with its Regulatory Review Committee and State Credit Union Advisory Committee (the Committees) in order to provide comments on the proposal. The Committees consists of credit union CEOs and senior management staff. Members of the Committees also represent credit unions of all asset sizes. The comments contained in this letter reflect the input of the Committees and PCUA staff.

In summary we support a properly developed method of capital planning and stress testing. We oppose many aspects of the structure or methodology of stress testing articulated in the proposed regulation. We urge NCUA to draft and submit for comment an additional proposed rule consistent with the comments in this letter.

Capital Planning

The Committee observed that scrutiny of a credit union's capital adequacy, liquidity, asset-liability management and business plan occurs through the supervisory examination. Credit unions of any asset size are undergoing such supervision. A capital plan, complete with the identification of pending business undertakings that would have a material impact on net worth is prudent and enhances safety and soundness. Also, we appreciate that capital protects the National Credit Union Share Insurance Fund (NCUSIF). Federally insured credit unions support steps that reduce the possibility of share insurance assessments.

NCUA's stated rationale for capital planning, particularly its reliance on requirements imposed by the Board of Governors of the Federal Reserve for large bank holding companies, causes some concern. Bank holding companies, regardless of size, can engage in activities far beyond those of credit unions and, as a result, present a greater risk profile than any credit union. Further, banks and bank holding

companies can issue capital stock somewhat readily to raise capital. With that in mind, the capital planning aspects of the proposed regulation should be reworked with the structure of credit unions more in focus.

For example, proposed section 702.503(b) (1), mandatory elements of capital plan, requires a quarterly assessment of expected sources and levels of capital. The only source of credit union capital is retained earnings. Reciting the sources of earnings in a capital plan where the sources of earnings are set out in the Federal Credit Union Act or state credit union law strikes us as redundant. This section should be amended accordingly.

Section 702.502(b)(3) mandates a discussion of how the credit union will, under expected and unfavorable conditions, maintain ready access to funding meeting its obligations to creditors, counterparties and continuing to serve members. In October of this year, NCUA finalized amendments to Part 741 of its regulations addressing Liquidity and Contingency Funding. 78 Fed. Reg. 64879. A credit union that has a satisfactory liquidity plan consistent with Part 741 should be deemed to be in compliance with this aspect of capital planning.

Capital Analysis and Stress Testing

The provisions on capital analysis and stress testing warrant more discussion and ultimately some adjustments before the regulation is finalized. The peer group of credit unions with assets of \$10 billion or more have a total net worth to total assets of 9.96%.¹ Therefore, there is no dire necessity to finalize this regulation. The ultimate goal of the regulation should be to ensure safety and soundness and create a system of analysis and testing that is consistent with the structure of credit unions.

The proposed rule, as presented, creates a strong impression that NCUA seeks to eliminate risk from the balance sheets of credit unions and homogenize them. Risk mitigation enhances safety and soundness; however, a regulatory effort aimed at plotting every strategic move that a credit union might make does not advance safety and soundness. Rather, credit unions are likely to find themselves rendering fundamental business decisions to satisfy stress testing mandates as opposed to serving consumers and, correspondingly, building a balance sheet that enable a credit union to serve its members.

We strenuously oppose section 702.503(c)(2) that requires an analysis of net economic value using interest rate shocks of +/- 300 basis points and the assumption that all non-maturity shares have final maturity not exceeding two years. At a minimum, NCUA must articulate where it developed these assumptions and why they are appropriate measures of safety and soundness for federally insured credit unions.

In the supervisory context, namely in connection with interest rate risk and ALM, NCUA has emphasized net economic value (NEV) as a determinant of volatility, and, ultimately, an indicator of safety and soundness. NEV, while common, is not the only measure. Credit unions would be best served by a more holistic approach where the regulation would permit each credit union to develop its own modeling in conjunction with its ALM vendor or internal staff and set those parameters in its capital policy and processes. That would enable each credit union to develop a plan that reflects its financial state, size and complexity as required by section 702.503(b) (1).

¹ Data from Callahan's Peer2Peer Software.

The background to the proposed rule offers no support for assigning a two-year maturity to non-maturity shares. We maintain that two years is not an appropriate rate of decay. Assets will likely have a weighted average life greater than two years. Mandating a two-year maturity on non-maturity shares will essentially bid down yields and the repricing of assets and liabilities. This will have a material, adverse effect on NEV and resulting stress test capital ratio. This is especially alarming when we observe that money rates will increase at some point. It is important to build adequate flexibility into this rule, now, to ensure that it does not manufacture a capital or liquidity crisis, at least in terms of the stress-test capital ratio, when rates increase. To this end, the rule should permit more flexibility in terms of asset-liability mismatch. In addition, the rule should permit credit unions to build their own assumptions on the average remaining life of non-maturity deposits based on their direct experience and observations.

Stress Test Scenarios

The proposal states that NCUA will provide a description of the stress test scenarios by December 1 of each year. The agency's authority to develop the scenarios is overly broad. NCUA's discretion to craft the scenarios must be confined such that the scenarios are consistent with and appropriate for our structure, noting that credit unions are cooperatives. In addition, NCUA should do more than provide a description of the scenarios. The scenarios should be stated with specificity, outlining each element or measurement. Credit unions cannot build an appropriate capital plan and corresponding analysis without forewarning of the testing scenario.

NCUA Action on Capital Plans

Under proposed section 702.505, the NCUA will notify a covered credit union of the acceptance or rejection of its capital plan by June 30 of each year. The provision articulates some criteria by which NCUA may reject a capital plan. A covered credit union will have 30 days to re-submit its capital plan to NCUA. The grounds for rejecting a capital plan should be more specific, enabling a covered credit union to readily re-submit a capital plan. Section 702.505(b) (2) provides NCUA with wide latitude to reject a plan if it believes that methodologies or assumptions are not reasonable. The final rule should articulate what is reasonable. Or, more appropriately, working with credit unions and ALM vendors/consultants, the final rule could identify "best practices" in connection with methodology. One particular method need not be the result. A variety of methods routinely used in this business should be available to covered credit unions.

The mandate that a plan could be rejected if the process is unsafe or unsound or would violate any law or regulation strikes as us curious. The proposed regulation mandates the elements of a capital plan. We are at a loss to identify how a plan drawn up on the basis of the rule could be unsafe or unsound or violate a law. The phrase "any law, regulation" should be struck from the proposal as overly broad. This provision should be tailored to the Federal Credit Union Act or, in the case of a federally insured, state-chartered credit union, the appropriate state credit union statute.

Finally, in the event that a capital plan is rejected, 30 days is insufficient time to re-submit the plan. We anticipate that significant work and analysis will be involved in redesigning a capital plan. Sixty days, or, at least 30 business days, to correct and re-submit a plan would be more feasible.

Publication of Stress Tests

NCUA asked for comment on whether the results of stress tests should be made public. While stress test results of banking institutions are publicized, in light of the structure of credit unions, we do not see a

compelling rationale for making the results public. Many large banking institutions are publicly traded. The publication of stress test results can be beneficial to investors. Credit unions do not issue capital stock; therefore, the same type of disclosure provisions need not apply to credit unions. Share insurance protection and the availability of a credit union's financial statements provide adequate transparency to members. Our opinion on publicizing stress test results might moderate if a system of alternative or supplemental capital existed for federally insured credit unions.

Supplemental Capital

In light of the proposal's emphasis on capital adequacy and planning, we would point out that credit unions could improve their capital position by the creation of a system of supplemental capital. NCUA's white paper on alternative capital, published in 2010, provides a good blueprint for implementing supplemental capital. We would be happy to work with NCUA to re-energize efforts to secure statutory authority for supplemental capital.

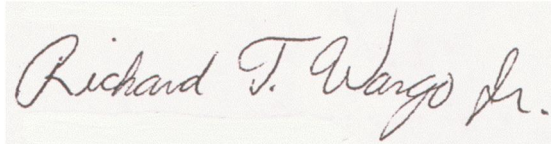
Conclusion

PCUA and its member credit unions support capital planning and the protection of NCUSIF. Many credit unions already perform stress testing of their own accord for ALM and related purposes. The stress testing contained in the current proposal would have adverse consequences on the stress test capital ratio and should be readdressed in a second notice and comment period. The publication of stress test results offers little in terms of additional transparency to credit union members.

We would be happy to discuss these comments with the NCUA Board and staff at your convenience.

Sincerely,

PENNSYLVANIA CREDIT UNION ASSOCIATION



Richard T. Wargo, Jr., Esq.
Executive Vice President/General Counsel

RTW:llb

cc: Association Board
Regulatory Review Committee
State Credit Union Advisory Committee
M. Dunn