May 06, 2014

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

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

Dear Gerald Poliquin,

I am writing on behalf of VA Desert Pacific FCU, which serves employees of the Department of Veterans Affairs primarily in Southern California. We have 4,600 Members and $59m in assets. VA Desert Pacific FCU appreciates the opportunity to provide comments to the National Credit Union Administration (NCUA) on its proposed rule, Prompt Corrective Action – Risk-Based Capital.

I do not agree that this proposed rule is even necessary. It is trying to address dissimilar risks with a single cookie-cutter mathematical formula without regard to the detrimental impact on the credit union industry or the real impact of the risks it seeks to address. NCUA has tools to assess interest rate risk, liquidity risk, credit risk and concentration risk without trying to load these risks onto a one-size-fits-all computation. Comparison of the proposal to existing credit union-wide assets implies that the industry is over $7 billion undercapitalized with no evidence that this is actually true or that the resulting increase in capital, if enacted, is necessary or prudent.

General Comments:

NCUA provided a calculator for credit unions to see how the rule would affect them based on most recent call report data. According to this calculation, our credit union would continue to be 'well capitalized'. Nevertheless, we are greatly concerned that our ability to manage our balance sheet will be hampered by this rule. We have extremely fast prepayments on our loan portfolio (average life 15 months). We cannot maintain margins if we are forced to keep investments short as well. We make investment decisions based on the projected outcome in multiple scenarios (falling, flat and rising rates) seeking to place instruments that 'win' in as many scenarios as possible. This regulation penalizes any balance sheet approach not poised for rising rates. Even a simple ladder strategy would be penalized. No one knows when/if rates will rise. Japan has been in a flat rate environment for nearly 20 years! And when/if rates do rise and 'falling rates' are a more real possibility than they are now, will NCUA revise this rule to bias it against short term investments and reverse the current bias against long term investments? This bias is a significant flaw in the rule as it stands.

NCUA claims that only 199 credit unions will shift from being 'well capitalized' or 'adequately capitalized' to 'undercapitalized' under this regulation. More importantly are the hundreds of other credit unions that will shift from being 'well capitalized' to adequately' capitalized (or barely adequately capitalized). These credit unions will immediately receive pressure to increase capital (something that can only be done quickly by reducing deposits or restricting growth). These credit unions will not feel free to make the good business decisions that will serve their members, grow and expand their credit unions. They will be forced to manage to regulator demands rather than market conditions and member needs. This rule will, as a mathematical necessity, restrict growth in almost all asset categories except short term investments. I am particularly concerned for my credit union neighbors who specialize in mortgage and business lending, which may be forced to have a balance sheet that looks more like that of the "average credit union" than like the one they have managed for years and that meets the needs of their memberships.

Specific Concerns:

Risk Weightings: The risk weightings for various asset types are internally inconsistent. For example, a delinquent 1st mortgage carries a higher risk weight than a credit card loan (which has no collateral backing it), a delinquent signature loan has the same risk weighting as a 5 year agency MBS and certain real estate collateralized loans carry the same risk weight as a student loan. How can this be? Risk weightings are also inconsistent with the bank rule they claim to mirror. For example, a 10 year Treasury carries the same risk weight under proposed PCA as a junk bond does under BASEL III, a 5-year CD would is considered 7½ times more risky than the same CD under BASEL III and a mortgage loan is up to twice as risky as a security using the exact same loan as collateral!

Recommendation: make the risk weightings logical and consistent with BASEL III **IF** it is even necessary for the credit union industry to "be just like a bank". Limit risk weighting to no more than 100% when the amount that can be lost is less than or equal to the balance of the asset.

Exclusion of NCUSIF deposit: The argument is being made that since the NCUSIF deposit is being excluded from both the denominator and the numerator that it will have no effect on a credit union's capital ratios. This is false. For the average credit union, NCUSIF deposits represent .80% of total assets but almost 7.50% of capital. Excluding the NCUSIF from both assets and risk-based capital therefore will reduce the average credit union's risk-based capital ratio by 78 basis points.

Recommendation: keep the NCUSIF deposit in both the denominator and the numerator

Higher capital requirements on a case by case basis: I disagree with this provision of the rule. The increase in the proposed rule of capital requirements for almost every asset class (sometimes up to double) is sufficient without allowing another subjective layer of capital requirements. Within the rule itself is a declaration that NCUA board cannot delegate its authority in this area, so how is it appropriate (or even legal) to allow such action by a field examiner?

Recommendation: limit capital requirements to the rule itself. No subjective measures unless the rule change itself is to be eliminated.

Restriction of dividend payments: I disagree with this provision of the rule. Dividends are driven by profitability (availability of funds after payment of expenses), not by capital ratios. If a credit union is prevented from paying dividends, you might as well close the credit union, because members will withdraw their funds.

Recommendation: Since the stated purpose of this rule is not to reduce the number of credit unions, this provision, which will certainly have that effect, should be eliminated.

Implementation: Once finalized, this rule proposes that credit unions must be fully compliant with in 18 months. This is far too short a time to make such significant changes in a balance sheet and is inconsistent with the time table in place for BASEL III, which has a multi-year implementation schedule.

Recommendation: Make implementation a phased effort similar to that of BASEL III.

Mandatory conservatorship/liquidation: I disagree with this provision of the rule. Nothing should EVER be mandatory. To me, "mandatory" is an excuse for not wanting to take the time to consider less draconian measures. "Mandatory" is a way to avoid thinking, discussing and considering all the aspects of a specific case.

Recommendation: Eliminate all actions defined as "mandatory" in the rule.

In summary, this rule is unworkable in its present form. It is inconsistent with BASEL, it is internally inconsistent, it inappropriately quantifies risk and it fails to account for interest rate risk in the loan portfolio or acknowledge the risk mitigation characteristics of the liability side of the balance sheet. It should be reworked and reissued for comment or withdrawn entirely.

Thank you for the opportunity to comment on this proposed rule and for considering our views on risk-based capital requirements.

Sincerely,

Cindy Glessner
CEO
VA Desert Pacific FCU

cc: CCUL