CHARTWAY
FEDERAL CREDIT UNION

April 30, 2014

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

Dear Mr. Poliquin

On behalf of the board and membership of Chartway Federal Credit Union, we appreciate the opportunity to respond to the proposed Prompt Corrective Action Risk-Based Capital ruling. We are in agreement that having a Risk-Based Capital regulation in place that benefits both credit unions and the NCUSIF is necessary; and we applaud the NCUA's efforts to ensure that those balanced protections are in place for our industry.

We also appreciate the NCUA's willingness to allow credit unions across the country to submit comment letters in response to the current proposal, with an intention to ensure that credit unions and the NCUSIF do actually benefit. We trust that the letters will be used to directly influence the final ruling. Our feedback, and that of other credit unions, provides the opportunity to move forward with a cooperative spirit and shared understanding of how the ruling should read.

We clearly understand the importance of the safeguards that the proposed RBC ruling should provide. We also can attest to the need to address concerns related to credit union failures; however, we believe these protections are overshadowed by the financial impact on credit unions and the burden it places on serving our members.

Overall, we believe the proposed ruling does not create the regulatory capital framework that fits the credit union industry. It appears that the regulation as proposed has adopted a Basel-style approach without taking into account the unique differences between banks and credit unions. Our structure and our losses are significantly different from banks, which needs to be integrated into the final regulation.

Chartway is a case study on how our relationship with the NCUA would be impacted by the ruling. Over the past 5 years, Chartway acquired three distressed (under-capitalized) credit unions. Working closely with the NCUA, we collaboratively negotiated a mutually beneficial resolution, thereby saving the credit unions and reducing the financial burden on the NCUSIF. However, the proposed ruling redefines Goodwill and escalates the required capital levels, which would have eliminated any possibility of these acquisitions occurring if this regulation had been in effect.

Additionally, we are concerned that the regulation as proposed does not take into consideration the outcome this ruling would have on capital buffers. In our perspective, the ruling is too punitive for growing credit unions - especially when combined with the fragile nature of the economy and the credit union industry. When the Net Worth and RBC ratios are applied within the proposed weight changes, it simply creates excessive financial hardship for those credit unions with more than $50 million in assets.

It is clear that most credit unions are better off today than they were following their capital level low-points following the 2008 economic crisis. Most have recovered to a point whereby growth and survival have become a reality. Further, we believe the time is right to encourage growth within the industry, and are concerned that the current proposal stifles this opportunity, leading to lasting negative impacts on the future of credit unions and their members.

As such, we have addressed four areas of "Proposed Concerns" as outlined in the following sections. As believers that identifying challenges is not constructive without solutions, we provide an accumulating list of 22 recommendations throughout each of these sections. We trust that the NCUA will take each into consideration as we work together to develop a ruling that will improve our industry, our competitiveness and our soundness for the future.

1. Rationale of the Current Proposal

We fully believe that any regulation should have a very clear rationale – inclusive of transparent and understood Objectives, along with the supporting regulatory detail. At the highest level, it is our view that there is no clear Statement of Objective in this proposal. Current PCA regulatory Objectives, as enacted by Congress in 1998; and implemented by NCUA in 2000, were formed with the following considerations:

1. Credit unions do not issue Capital
2. Credit unions solely rely on Net Income / Retained Earnings for Net Worth
3. Credit union Boards are made up of Volunteers

Under the current proposal, however, it appears that regulatory Objectives may be to:

1. Establish a risk-weighting system that is more indicative of the potential risks within credit unions
2. Help credit unions absorb losses
3. Establish a safer, more resilient, and more stable credit union system

We believe the Objectives need to be more clearly defined, address the true drivers of risk that lead to the recent causes of credit union failures and serve as the foundational principles for the details within the regulation.

Further, there is a lack of alignment in the stated Purpose of section 216 of the Federal Credit Union Act and the potential reality of the proposal, if implemented. That stated Purpose is "to resolve the problems of federally insured credit unions at the least possible long-term loss to the NCUSIF", however the Purpose appears to be inconsistent with the elements of the proposal. First, there is a much greater degree of consistency with the risk-based capital measures that the NCUA employs for corporate credit unions and that the FDIC employs with banks, as opposed to the unique nature and structure of natural person credit unions. Secondly, we know that there were three primary reasons that natural person credit unions failed during the recent economic crisis: Fraud, Member Business Lending and Construction Lending. While these reasons could be fairly defined as the "problems" addressed in the stated Purpose, the broadly outlined detail of the current proposal is more suggestive of failures driven by a much more vast number of business elements, many of which are seemingly unrelated to the crisis.

There is also a question of fairness and transparency with respect to the independent setting of required capital levels beyond the standardized levels of the proposal. A credit union could be fully compliant with the stated requirements through the execution of a comprehensive strategy, and subsequently be re-directed by the NCUA to a capital level not aligned with the strategy, with the success of a given strategy having no bearing.

Just as the NCUA has re-aligned their Examination Focus / Intentions to reflect current times, we offer the following as recommended re-aligned Regulation Objectives:

Regulation Objectives Recommendation

1. *Position the credit union industry for Survival (Growth)*
2. *Provide credit unions with access to alternative forms of Capital*
3. *Establish an overall framework of Safety & Soundness for credit unions*
4. *Mitigate risks experienced in failed credit unions*
5. *Ensure credit unions are equipped to compete in consumer financial services*

Regardless of the Objectives, stated Purpose, formation of the detailed elements and independent capital level determinations, we believe the losses in the NCUSIF will actually grow if this proposal is implemented as currently designed. As discussed later in this letter, the constraints on Goodwill will be a direct deterrent to the acquisition of Distressed credit unions; and thus increase exposure to the NCUSIF. This directly contradicts the logically defined Purpose.

2. Credit Union Strategy

No matter what a credit union's specific strategy may be, we believe that growth is a central requirement for ultimate success. At its core, the credit union industry is framed around providing competitive products and services to members and future members; and in order to maintain that competitive position, a level of scale from growth is fundamental. The more economical a product can be delivered, the better the pricing that can be passed on to the member – and, as such, economies of scale are a paramount for the necessary cost structure and ultimate competitiveness. Remaining competitive is an absolute requirement for survival against the likes of banks of all sizes with seemingly endless investable capital levels.

With respect to Chartway, our strategy is to grow our business on two fronts – Organically and through Mergers & Acquisitions. There are three straight forward facets of our Organic front. First, we intend to be a price-leader in volume-based products lines. In doing so, while we will offer the full slate of consumer products, we see ourselves as becoming more specialized in very focused product categories that align with our volume-based orientation. Secondly, our franchise has to be accessible to current and future members. Demographics are shifting towards the digital or virtual channels on a daily basis, but clearly, having a branch channel contingent as an access or delivery point remains a strategic requirement. Lastly, with volume-based activities serving as a driving force of our business model, we continue to pursue CUSO collaborative opportunities when they offer increased scale potential.

Our Merger & Acquisition front covers two primary arenas – Distressed credit unions and Healthy credit unions. Growth through the acquisition of Distressed credit unions is a win on a number of levels, and we have executed three such transactions to date. Our legacy members visibly benefit by having increased delivery access and less visibly through increased operating scale. The members of the acquired credit unions benefit with a continuation of the valued, and often long-standing, relationship they have had with their credit unions. And, of course, the industry benefits through reduced losses to the NCUSIF. Mergers with Healthy credit unions provide much of the same operating benefit, obviously without any impact to the NCUSIF.

Clearly, the current proposal constrains our ability to grow both Organically and through Mergers & Acquisitions. Organically, all three of our key facets are stifled. The combination of the need for increased margins and a loss of half of our ALM capabilities decrease our competitive pricing position immediately. The risk-weights on Fixed Assets also hinder the required investment for growth. A 100 percent risk-weight on investments to further develop our franchise through our branch channel, or to develop and implement more efficient and user-centric sales and service technologies does not appear to be aligned with the true risk. We have not experienced, nor witnessed, investments on these fronts bringing about undue risks to the credit union industry. With the proposed risk-rates, our investments in channel development and technology growth will greatly slow, if not terminate, for the foreseeable future. And, somewhat contrary to our industry's collaborative basis, utilizing CUSOs is much less attractive due to their associated risk-weights. This is problematic both from the perspective of discouraging efficient business models, but also appears contrary to the partnering culture of the credit union industry.

Just as important to us, our Merger & Acquisition front is challenged at a minimum, and potentially eliminated altogether. Goodwill, the value of future benefit that is derived from the acquisitions, is an absolute must in acquisitions of Distressed credit unions. Without Goodwill, we simply cannot afford to grow through this arm of our strategy, nor continue in the win-win relationship with the NCUA to decrease costs to the NCUSIF. We believe other credit unions will be in that exact same situation, creating additional exposure to the NCUSIF. To date, Goodwill has resulted in a savings to the National Credit Union Share Insurance Fund (NCUSIF) of approximately $900mm industry-wide. Further, we believe that the market exposure is actually $1.3B, or 12% of the (NCUSIF) fund. The inability for Chartway or others to acquire Distressed credit unions will pointedly impact the credit union industry in a negative direction, contradicting NCUA's PCA Purpose.

Similarly, the Goodwill impact from the proposal is a disincentive to acquire Healthy credit unions. While our focus to date has been on the Distressed arena, and supporting the livelihood of the industry in that manner, we also fully recognize our need to grow through mergers and acquisitions of Healthy credit unions – and the proposal clearly stifles our ability to act.

Simply said, many capabilities that we currently enjoy to strategically manage our business will be removed – directly reducing our growth. As such, as more overarching Strategy Enabler recommendations, that are supported by detailed elements recommendations later in this letter, we offer the following:

Strategic Enabler Recommendation

6. *We believe that Organically competing based on Price in volume-based products across multiple channels should be encouraged by the regulation*

7. *We believe that growth through Mergers & Acquisitions, benefiting the acquiring credit union, merged credit union and the NCUSIF, should be encouraged by the regulation*

3. Elements of Proposed Risk-Based Capital Ratio

Net Worth (the RBC numerator)

The reasoning in adding and subtracting certain balance sheet items from the Net Worth (the numerator) in the RBC calculation to reflect a measure of equity available to cover losses in the event of liquidation is understood; however, in the case of Goodwill (a full reduction), the Allowance for Loan Loss (a capped addition) and Credit Reserve Valuation Allowance (ignored completely) in the determination of the amounts adjusting Net Worth as proposed should be reconsidered.

a. Goodwill

As stated in the Federal Register, Goodwill (as an intangible assets) contains a high level of uncertainty in a credit union's ability to realize value from these assets and we agree, however, if the value associated with that Goodwill asset can be determined through proper testing, then a level of certainty would exist and could be utilized to offset potential losses in the event of liquidation. To effectively establish "certainty" and value to the Goodwill asset, the following should be considered prior to finalizing the RBC ruling.

Currently an annual, independent and qualified testing of the Impairment of Goodwill must be performed in strict accordance with the Statement of Standards for Valuation Services ("SSVS") of the American Institute of Certified Public Accountants. The purpose of this independent test is to determine if the current market value of the entity as represented by the Goodwill asset is less than, equal to or greater than the stated book value as reflected on the Balance Sheet of the credit union.

Upon completion of a qualified Test of Goodwill Impairment, the results are to be treated and recorded by the credit union in accordance with GAAP as follows:

- If the tested value of Goodwill reported is less than book, the Goodwill asset must be written down through the Income Statement thereby reducing both the GAAP and RBC Net Worth position. This essentially achieves the objective of the proposal with a required adjustment reducing the Net Worth of a credit union by an amount equal to the value of the asset that would be available in the event of liquidation.

- If the tested value of Goodwill reported is greater than or exceeds book value, no adjustment per GAAP is made to Net Worth, thereby maintaining an even more conservative Goodwill position related to Net Worth for RBC purposes. It should be noted that the RBC proposal totally ignores this position.

This independent Test of Goodwill Impairment and correlating entry recorded in accordance with GAAP would therefore both justify the value of Goodwill represented on the Balance Sheet and bring a high level of certainty in achieving the objective of the RBC proposal (without the need to reduce Goodwill in the Risk Based Net Worth calculation).

Accordingly, it is our recommendation that the proposed RBC ruling not require a reduction of Goodwill from Net Worth if a credit union engages a qualified and independent firm to perform a Test of Goodwill Impairment on an annual basis and records any reduction in value to the asset in accordance with GAAP. We understand the conservative regulatory approach in protecting the NCUSIF with the treatment of goodwill in the manner proposed but believe that a weighting of

100 percent is excessive and further, that value and certainty is accomplished with proper testing of Goodwill.

In consideration of the above recommendation and with value and certainty established, if NCUA required a “cushion” in the amount of Goodwill available to cover losses in the event of liquidation, at a minimum, any amount of reported Goodwill value over book as reported in the Test of Goodwill Impairment should be applied in reducing the amount deducted from the RBC Net Worth position. Again, this is a more conservative approach in the treatment of Goodwill and would still result in a reduction to Net Worth associated with Goodwill. If this compromise was accepted, the reduction to Net Worth for CFCU recorded Goodwill would still be significant at $37mm (at 53 percent) however less than the proposed $71m (at 100 percent).

Additionally, it should also be understood that the treatment of Goodwill as currently proposed is in direct conflict with the stated purpose of section 216 of the Federal Credit Union Act “to resolve the problems of (federally) insured credit unions *at the least possible long term loss to the NCUSIF*.” Collectively credit unions have Goodwill associated intangibles recorded on their balance sheets totaling approximately $900mm as compiled from the NCUA 5300 reports for period ending December 31, 2013. Based on GAAP for mergers and acquisitions, Goodwill recorded on the balance sheet of the surviving / acquiring credit union is created as the balance sheet of the acquired credit union is marked to fair value at the date of acquisition. Subsequently, if Goodwill exists and in accordance with GAAP, any cash assistance provided from Share Insurance Fund (NCUSIF) to the surviving credit union will offset or reduce (dollar for dollar) the amount of Goodwill booked by the surviving / acquiring entity.

Considering a credit union currently adheres to the proper accounting treatment per GAAP along with required testing of Goodwill impairment as summarized above, the proposed Risk Based Capital rule in the treatment of Goodwill if implemented would have actually *cost the NCUSIF fund an additional $900mm* by incenting credit unions to either avoid the acquisition of distressed credit unions all together or require additional cash assistance from the NCUSIF in order to maintain their Risk Based Capital position as currently proposed.

Goodwill Recommendation

8. *It is recommended that the RBC Net Worth calculation not require a reduction of Goodwill recorded on the books of the credit union from Net Worth if the independent Test of Goodwill reports no impairment.*

9. *In consideration of recommendation (8) above, if Goodwill is to be a reduction of Net Worth as proposed, at a minimum, the recorded book balance of Goodwill reducing Net Worth in the RBC calculation should be adjusted by any amount of reported Goodwill value over book as reported in the independent Test of Goodwill Impairment.*

b. Allowance Loan Loss (ALLL)

The Federal Register / RBC proposal states that because the ALLL is available to cover expected levels of loan losses, the proposed numerator would include the ALLL (an addition to Net Worth) but it would be limited to 125 percent of total risk-weighted assets. It continues in stating that the limit established would provide an incentive for granting quality loans and recording losses in a timely manner. Finally, it states that the limit would not result in a disincentive to fully fund the ALLL above the 125 percent ceiling since complex credit unions are bound by GAAP in maintaining the ALLL.

The imposition of a 125 percent ceiling as described in the proposal appears both arbitrary and contradictory since the adequacy position of the ALLL in accordance with GAAP is validated annually as a part of the independent CPA Opinion Audit (required of all complex credit unions) and further reviewed within the NCUA examination process. Secondly, and again in accordance with GAAP, any ALLL position that is reflecting a material over or under funded position must be adjusted through the Income Statement and would therefore be reflected properly in the RBC Net Worth position in a timely manner. Lastly, if a credit union is "bound" to GAAP in maintaining the ALLL position as referred to in the proposal, the ALLL position would accurately reflect the impact related to both the level of credit quality in lending (in both the quantitative and qualitative factors of the ALLL analysis) and the timeliness in charging off loans as part of the adequacy analysis and position.

Accordingly, no limitation or ceiling to the ALLL should be arbitrarily imposed in calculating the RBC Net Worth position.

Allowance for Loan Loss Recommendation

10. It is recommended that no limitation or ceiling be placed on the Allowance for Loan and Lease Losses where a credit union receives on an annual basis an independent CPA Opinion Audit and operates in accordance with GAAP requirements.

c. Valuation Allowance

In addition to the annual Test of Goodwill Impairment, our credit union engages a qualified and independent third party to perform a periodic assessment of the adequacy of the Credit Reserve Valuation Allowance associated with acquired loans in accordance with the Statement of Standards for Valuation Services ("SSVS") of the American Institute of Certified Public Accountants.

This credit valuation allowance and associated credit balances are recorded on the credit union books in a manner similar to the ALLL except that the loans related to this adequacy analysis (performed independently) would correlate separately to those loans acquired in a merger or acquisition and in accordance with GAAP, are not a part of the Allowance for Loan Loss adequacy analysis or position (discussed in "b" above). It should also be noted that the credit reserve valuation balances and position are also reviewed for adequacy as a part of the CFCU CPA Opinion Audit with over or under funded positions adjustments reported and recorded as required. Additionally, NCUA reviews the same as a part of the credit union annual examination.

Notably, these significant credit balances have been ignored and may be "hidden" as NCUA instructs credit unions to net the acquired loan valuation allowance or credit balance against the acquired loan balances in reporting these loans for the NCUA 5300. This is obviously different than the instructions required for the reporting of the Allowance for Loan Loss associated with those loans not acquired in a merger. The impact to the RBC calculation for Net Worth is therefore inconsistent as the ALLL is treated as an addition to Net Worth (the numerator) while the Valuation Allowance associated with acquired loans is netted to the loan balance affecting only the calculation of the Risk Based Assets (the denominator). Inconsistent as well is the manner in which delinquencies associated with the loans with correlating valuation credits are reported and weighted in the proposed Risk Based Asset calculation.

Accordingly, the Credit Reserve Valuation Allowance or loan credits associated with loans acquired in a merger or acquisition should be treated in the same manner as the Allowance for Loan and Lease Losses. That is, as an addition to the Net Worth (numerator) in the RBC calculation with loan balances and delinquents reported consistently in the Risk Based Asset calculation.

Credit Reserve Valuation Allowance Recommendation

11. *The regulation as proposed has ignored the Credit Reserve Valuation Allowance in the RBC calculation (numeration) and therefore it is recommended that the recorded credit valuation balances be treated as an increase to Net Worth in a manner similar to the Allowance for Loan and Lease Loss.*

Risk Based Assets (the RBC denominator)

The proposal states that risk categories and risk weights would be assigned to each specifically defined balance sheet asset. In developing the risk weights, the proposed design or basis of the regulation considered the Basel accords, material loss reviews prepared by the NCUA Inspector General and GAO comments in their review of the financial services industry's implementation of PCA.

The proposal further states that because the Federal Credit Union Act requires the risk based measure to include all "material risks" that was interpreted to include credit risk, concentration risk, market risk, interest rate risk, operational risk and liquidity risk.

To incorporate all the above described risk measurements collectively into a "one size fits all" risk based asset calculation is truly a formidable task and can result in measurement criteria that is not indicative of a credit unions actual risk position. This is especially evident in the areas of risk that are closely aligned with an effective Asset Liability Management Program where a credit union mitigates Interest Rate Risk (IRR) by employing ALM strategies and associated risk measurements that extend across the entire balance sheet (as required by NCUA) versus selected segments of the balance sheet as reflected in the RBC proposal. Consider Part 741 of the NCUA Rules and Regulations defining Interest Rate Risk and components of measurement as related to the "vulnerability of a credit union's financial condition to adverse movement in market interest rates" as follows:

Net Economic Value (NEV)	The difference between market value of assets minus the market value of liabilities

Earnings (NII and NI)	By altering interest-sensitive income and expenses (e.g., loans income and share dividends)
Economic Value / Liquidity	Affect the credit union's assets and liabilities because the present value of future cash flows and, in some cases, the cash flow themselves may change when interest rates change

In each of the NCUA defined risk measurements with the exception of credit quality and operational risk, both sides of the balance sheet are incorporated as reflected above. In the proper measurement of risk, a credit union cannot separate assets from liabilities in determining and establishing strategies that provide for the needs of the member with service, product and competitive positioning, while at the same time, in alignment with the mitigation of each associated risk outlined in the proposal. This is a critical flaw in the current RBC proposal that simply imposes risk weightings across each asset-only category without regard to the true balance sheet position of a credit union. Essentially this will replace effective asset liability management based on member needs with puzzle-like input to a risk adverse regulatory grid. By substituting good risk management with such an approach as proposed will not only adversely impact member service but expect the accumulation of Net Worth to actually slow as earnings are negatively impacted with disadvantages in both competitive positioning and the reduced interest spread benefit that would typically be derived from effective well managed financial intermediation (ALM) strategies.

Asset Liability Recommendation

12. It is recommended that the RBC regulation consider and incorporate proper Asset Liability Management risk related benchmarks / thresholds as currently applied throughout the industry thereby utilizing the entire balance sheet position of a credit union as opposed to the one-size fits all "Asset Only" as currently proposed.

Balance Sheet Assets

a. Investments — The Federal Register / proposal associated with Investments states its objective as providing a fair measure of the interest rate risk and liquidity risk associated with longer term investments.

It is agreed that proper alignment of investment maturities must be correlated with Interest Rate Risk and Liquidity exposure as noted in the proposal, however the risk level of the credit union must be considered in determining the associated risk weightings as assigned. As example, our credit union reflects a low risk rating (utilizing NCUA benchmarks) in each category of Interest Rate Risk measurement and as well in Liquidity. With $38m in GSE (low credit risk) five year maturities with low overall IRR risk and no current need to liquidate, why would a 150 percent risk weight rating be assigned versus 20 percent as would be assigned in the Basel approach? We understand the potential risk related to NEV, NII, NI and liquidity as market rates fluctuate but the impact in this case is minimal. It seems the proposal incorrectly assumes that all credit unions are positioned as "high risk" in the categories of Interest Rate Risk and Liquidity and utilizes that same logic in the proposed assignment of investment maturity risk weightings.

Accordingly, it is recommended that the RBC weighting associated with Investment maturities be aligned with the Basel weights of 20 percent in each maturity bucket. NCUA should address in the examination / supervisory process those select credit unions that choose to operate in a high risk IRR or liquidity position versus penalizing the majority of credit unions effectively managing that risk.

Investments Recommendation

13. *It is recommended that the weightings associated with credit union investments follow and align with the current Basel weightings for each maturity bucket.*

b. Non-Guaranteed Mortgage Loans

With Construction Lending being one of the three primary reasons for credit union failures, we appreciate the interest in having commensurate risk-weightings for certain segments of Mortgage Lending. The segmentation rules for non-guaranteed Mortgage Lending in the Federal Register / proposal, however, do not appear aligned to the inherent risk levels. Currently, the segmentation criteria consist of the percentage of real estate assets of a credit union's total assets, and real estate loan delinquency. The equity or Loan-to-Value Ratio is not utilized in the criteria, and we believe that it provides a more attributable level of true risk rather than the percentage of real estate assets to total assets. Non-delinquent Mortgages with Loan-to-Value Ratios of 80% or less, regardless of a credit union's real estate concentration are likely more appropriately assigned the 50 percent risk-weight that is now proposed for the credit unions with the lowest real estate concentration. Logically, from there, it would flow that non-delinquent Mortgages with Loan-to-Value Ratios above 80% would have an incrementally greater risk-weight; and any delinquent Mortgage would be assigned a risk-weight of 25 percentage points above its non-delinquent Loan-to-Value based assignment. This would maintain the intent of 100 percent risk-weights for the delinquent high Loan-to-Value Mortgage loans, but also provide lower risk-weights for current Mortgage Loans that are satisfactorily collateralized.

Non-Guaranteed Mortgage Loans Recommendation

14. *Risk-weightings should be based on Loan-to-Value and Current Delinquency*

15. *Non-delinquent Mortgages with Loan-to-Value Ratios of 80% or less should have a 50 percent risk-weight*

16. *Non-delinquent Mortgages with Loan-to-Value Rations above 80% should have a 75 percent risk-weight*

17. *Delinquent Mortgages should have an incremental 25 percentage point risk-weight from their base*

c. Other Loans

For all other Consumer Loans (i.e., excluding MBLs), the 75 percent risk-weight for non-delinquent loans is acceptable, however, delinquent loans being assigned a 150 percent risk-weight does not appear aligned with the cause of credit union failures. While a delinquent unsecured or automobile loan implies more risk than that of non-delinquent credit cards, we don't view the risk as 2x when underwritten through sound lending practices.

Other Loans Recommendation

18. *Delinquent Consumer Loans should have a 100 percent risk-weight*

d. Fixed Assets

The Federal Register provides no significant supporting information or basis for the 100 percent risk weighting assigned to Land and Building (net of depreciation) in the RBC calculation. This unfairly assumes that the entire asset or associated recorded book balance is considered at risk and accordingly, in a credit union liquidation or merger that no value is to be derived from these related assets. Further, in considering that the credit union is an ongoing entity, the 100 percent weighting essentially requires that for every $1.00 dollar invested in growth and efficiency, an additional $10.5 cents must be set aside thereby penalizing those credit unions that employ such efficiency or expansion in their overall positioning strategies.

In the credit unions acquired by CFCU and due diligence performed in bidding on many credit unions in a position of failure, losses of such magnitude associated with Land and Building used for credit union purposes was neither experienced nor observed. At a minimum consider the worst case property value losses experienced during the most recent recession at twenty five to thirty five percent. It is understood that losses associated with certain foreclosed (REO's) properties were considerable as a credit union may have engaged in member construction lending or loaned to members for speculative property purchases. Losses associated with those properties and practices should not be confused or co-mingled with risk weighting on properties that are utilized for credit union purposes.

Fixed Assets Recommendation

19. *It is recommended that risk weightings associated with Land and Building utilized for credit union purposes be reduced from 100 percent to 25 percent.*

<u>4. Implementation</u>

The RBC proposal is the most significant ruling that credit unions will face this year and likely for years to come. Nevertheless, the time period to review the provisions, develop clear and concise plans for the future, and execute them by the deadline is extremely concerning. The current proposal suggests an 18 month implementation timeframe, approximately 70% shorter than that which banks had for implementation.

Furthermore, when considering that banks have the ability to recruit capital from means beyond earnings, providing credit unions such a shorter implementation period than banks begs even a more serious question of fairness. If credit unions were provided with access to Supplemental Capital, an implementation timeframe equitable to that of banks is understandable – certainly not shorter. Without Supplemental Capital, a longer implementation timeframe will be necessary. Without these extended timeframes to allow a fully planned and reasonable process to incorporate the new regulation into each credit union's business model, the magnitude of business disruption and risk to the future of the industry is very concerning. While the particular issue does not directly impact Chartway, the Federal Reserve determination this week that banks will need 2 years beyond the already-planned 5 years to divest Collateralized Loan Obligations that fall under the Volcker rule is indicative of the challenges that may not even be realized until implementation commences. Simply stated, credit unions will need far more time than the currently proposed 18 months to accurately build a PCA – Risk-Based Capital program that meets all of the ruling requirements. The current timeframe does not appear logical or fair when compared to what the banks are currently going through.

Moreover, an extended deadline would help to ensure credit unions' comments and recommendations regarding the proposal can be careful considered without pressures on the NCUA. This will ensure the ruling is well prepared and written prior to putting it into effect.

While banks were given years to address and respond to Basel iii, credit unions currently do not have that luxury. We ask that NCUA consider significantly extending the implementation deadline to allow credit unions to provide sound, long-term solutions that meet our shared objectives.

Implementation Recommendation

20. *If coupled with the use of Supplemental Capital, credit unions should have at least 5 years for implementation – at least matching that of banks*

21. *Without the use of Supplemental Capital, credit unions should have at least 8 years for implementation – compensating for few capital accumulation tools than banks*

Supplemental Capital

The ability for credit unions to survive in today's highly competitive market and ever expanding financial services arena without the ability to raise supplemental capital can no longer be ignored or delayed and now coupled with the impact of the RBC regulation as proposed *must* be accelerated in order initiate the process well in advance of the RBC implementation date.

The many facets of the supplemental capital debate have reigned for so many years (and documented in the NCUA 2010 White Paper) over questions / issues related to the preservation of the cooperative mutual model, the obvious need for investor safeguards, opening the door to taxation or what agency is to regulate this capital. Then shift this ongoing debate to questions regarding the most effective supplemental capital model to utilize considering Voluntary Patronage Capital versus Mandatory Membership Capital versus Subordinated Debt. The debate must now be brought to closure as the credit union industry as a whole has been placed in a position of risk and failure without the regulatory or legislative resolve that is required in addressing this problem.

The performance and ability of credit unions to maintain capital levels solely from earnings both historically and during the worst of economic times has allowed the issue of supplemental capital to remain in a state of avoidance. However, in today's marketplace, the need for supplemental capital is critical with credit unions at an obvious disadvantage as the only provider of financial services that cannot raise capital. Consider:

- The inability of credit unions to provide members a "safe haven" in times of economic turbulence as the growth rate in deposits may exceed earnings and dilute the capital position of a credit union.

- The ability of both traditional and non-traditional competitors to bring to their customers new and innovative products / services in a timely manner while credit unions delay such member opportunities until earnings catch up to the investment in "capital" required.

- The disadvantage to members in the inability of credit unions to price competitively, as again, earnings must precede or offset any short-term impact to capital whether related to pricing, economic or other external factors. Without question this results in higher priced loans, lower priced deposits, increased fees or worse, unnecessary risk taking to achieve yield through investment activities.

- The dis-service to the community in the inability of credit unions to contribute in either economic growth or recovery efforts as product offerings, capital investment opportunities or providing competitive services to members or groups is stymied during a time of need. This is especially evident with the flat yield curve environment experienced over the past years of ongoing economic recovery where credit union spreads are narrow thereby preventing growth and services to our members.

The list goes on but essentially a credit union cannot effectively serve its members, invest in the community, promote new or organic growth or maintain a fair and equitable competitive position in the marketplace when severely constrained by a system that does not allow capital growth or preservation except though earnings.

Supplemental Capital Recommendation

22. *It is recommended that the ability to raise supplemental capital that qualifies as GAAP Net Worth (the numerator in the RBC calculation) be legislated, and available to all credit unions in a period of no less than five years in advance of the Risk Based Capital implementation date.*

In summary, we strongly support the necessity of a Risk-Based Capital regulation that benefits both credit unions and the NCUSIF; and we realize that it will take numerous iterations to reach a final version. It is our position that the RBC ruling would be better crafted if the NCUA takes into consideration the impact it will have on the credit union industry – specifically, on the potential harm it will have, as currently proposed, on credit unions' growth, their members and ultimately their survival.

Overall, we believe that the ultimate intent of the capital regulation should properly serve credit unions, their members and the NCUSIF – ensuring growth, while protecting against the drivers of recent credit union failures. It is for that reason that we have taken the opportunity to provide our recommendations throughout this letter that we believe supports that intent. Those 22 recommendations are collectively summarized as follows:

Regulation Objective Recommendation

1. *Position the credit union industry for Survival (Growth)*

2. *Provide credit unions with access to alternative forms of Capital*

3. *Establish an overall framework of Safety & Soundness for credit unions*

4. *Mitigate risks experienced in failed credit unions*

5. *Ensure credit unions are equipped to compete in consumer financial services*

Strategic Enabler Recommendation

6. *We believe that Organically competing based on Price in volume-based products across multiple channels should be encouraged by the regulation*

7. *We believe that growth through Mergers & Acquisitions, benefiting the acquiring credit union, merged credit union and the NCUSIF, should be encouraged by the regulation*

Goodwill Recommendation

8. *It is recommended that the RBC Net Worth calculation not require a reduction of Goodwill recorded on the books of the credit union from Net Worth if the independent Test of Goodwill reports no impairment.*

9. *In consideration of recommendation (8) above, if Goodwill is to be a reduction of Net Worth as proposed, at a minimum, the recorded book balance of Goodwill reducing Net Worth in the RBC calculation should be adjusted by any amount of reported Goodwill value over book as reported in the independent Test of Goodwill Impairment.*

Allowance for Loan Loss Recommendation

10. *It is recommended that no limitation or ceiling be placed on the Allowance for Loan and Lease Losses where a credit union receives on an annual basis an independent CPA Opinion Audit and operates in accordance with GAAP requirements.*

Valuation Allowance Recommendation

11. *The regulation as proposed has ignored the Credit Reserve Valuation Allowance in the RBC calculation (numerator) and therefore it is recommended that the recorded credit valuation balances be treated as an increase to Net Worth in a manner similar to the Allowance for Loan and Lease Loss.*

Asset Liability

12. *It is recommended that the RBC regulation consider and incorporate appropriate Asset Liability Management risk related benchmarks / thresholds as currently applied throughout the industry thereby utilizing the entire balance sheet position of a credit union as opposed to the one-size fits all "Asset Only" as currently proposed.*

Investment Recommendation

13. *It is recommended that the weightings associated with credit union investments follow and align with the current Basel weightings for each maturity bucket.*

Non-Guaranteed Mortgage Loans Recommendation

14. *Risk-weightings should be based on Loan-to-Value and Current Delinquency*

15. *Non-delinquent Mortgages with Loan-to-Value Ratios of 80% or less should have a 50 percent risk-weight*

16. *Non-delinquent Mortgages with Loan-to-Value Rations above 80% should have a 75 percent risk-weight*

17. *Delinquent Mortgages should have an incremental 25 percentage point risk-weight from their base*

Other Loans Recommendation

18. *Delinquent Consumer Loans should have a 100 percent risk-weight*

Fixed Assets Recommendation

19. *It is recommended that risk weightings associated with Land and Building utilized for credit union purposes be reduced from 100 percent to 25 percent.*

Implementation Recommendation

20. *If coupled with the use of Supplemental Capital, credit unions should have at least 5 years for implementation – at least matching that of banks*

21. *Without the use of Supplemental Capital, credit unions should have at least 8 years for implementation – compensating for few capital accumulation tools than banks*

Supplemental Capital Recommendation

22. *It is recommended that the ability to raise supplemental capital that qualifies as GAAP Net Worth (the numerator in the RBC calculation) be legislated, and available to all credit unions in a period of no less than five years in advance of the Risk Based Capital implementation date.*

As part of our ongoing assessment of the proposal, my team and I had the opportunity to review the NCUA Board Chairman's video regarding Risk Based Capital that was released on April 17th. Overall, while we certainly agree with the intention of having a framework in place that ensures that credit unions hold capital at levels commensurate with the risk in their portfolios, it is our view that the drivers of the 102 credit unions that failed during the crisis are not adequately addressed with the proposal. In turn, undue capital requirements are being placed upon credit unions with portfolios very different from what brought about the failures. Additionally, the $750mm that the video notes as costs to the NCUSIF from the failures would be more than doubled under the current proposal through Goodwill limitations. Thirdly, we agree with various industry estimates that the number of impacted credit unions may far exceed NCUA's estimate of 200 noted in the video knowing that the true impact may be inclusive of both capitalization level downgrades and, more frequently, but just as important, buffer reductions. For all of those reasons, we believe much more work is necessary to form a final regulation that benefits both credit unions and the NCUSIF.

To that point, we remain willing and available to provide assistance in drafting a ruling that more closely meets our industry's needs and the overall economic situation. Working together with credit unions, either within a special forum or committee to improve the process, we stand prepared to partner with the NCUA for the development of a collaborative and rational solution.

We thank you for the opportunity to offer our perspectives on this proposed regulation that will have such lasting effects on the credit union industry, and trust the door is open for consideration of our recommendations.

Sincerely,

Ronald L. Burniske

Ronald L. Burniske
President & CEO