CommunityAmerica
CREDIT UNION
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MAY16'14 PM 2:21 BOARD

May 12, 2014

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

Re: Comments on Proposed Rule: Prompt Corrective Action – Risk Based Capital

Dear Mr. Poliquin:

CommunityAmerica Credit Union (CACU) appreciates the opportunity to comment on the National Credit Union Administration (NCUA) Board's proposed risk based capital rule. CACU has used risk based capital methodologies internally for a number of years and is, in general, supportive of modernizing NCUA rules defining minimum capital requirements and Prompt Corrective Action as long as the risk based capital standard (1) is comparable to Prompt Corrective Action rules that are employed by other Federal Banking Regulators; (2) reflects the specific characteristics and features of credit unions; (3) consistently identifies credit unions with unwarranted or disproportionate risk; (4) does not arbitrarily or unfairly place credit unions at a competitive disadvantage to other financial institutions; and (5) does not inhibit or limit future business strategies essential to the survival of the credit union industry.

In reviewing the proposed rule for Risk Based Capital, we feel there are substantive shortcomings that are likely to compromise one or more of the criteria outlined above. We believe the proposed rule would be detrimental to CACU's ability to offer competitive products and services required to meet the needs of members and would limit the flexibility needed to implement current and future business strategies. Our discussion of concerns follows regarding the proposed rule that we request the NCUA take into consideration during the rule making process.

1. Risk Weightings

One of the stated objectives of the NCUA in proposing the updated rule is to comply with the Federal Credit Union Act wherein a Risk Based Net Worth Requirement (RBNW) must be formulated for credit unions defined as "complex" and the RBNW must "take account of any material risks against which the net worth ratio required for [a federally] insured credit union to be adequately capitalized [(6 percent net worth ratio)] may not provide adequate protection." The NCUA has further defined "material risks" as credit risk, interest rate risk, concentration risk, liquidity risk, operational risk, and market risk.

CACU believes there is no single risk weighting system capable of aggregating and accommodating such a diverse array of risks and, as a result, the risk weightings as defined in the proposed rules are both inconsistent and incomplete. The risk weightings attempt to apply concentration risk to First Mortgage Loans, Other Real Estate Loans, and Member Business Loans but ignore concentrations in Consumer Loans and Student Loans. Similarly, interest rate risk is implied in First Mortgage Loans and Securities Guaranteed by U.S. Government Sponsored Agencies but is absent in Consumer Loans and Debt Unconditionally Guaranteed by the U.S. Government. In addition, when addressing interest rate risk, any risk weighting system that completely ignores risk mitigation strategies associated with the liability side of the balance sheet is incomplete. It is unclear which of the various types of risk are intended to be incorporated into each of the risk weightings and which are not.

It is also unclear how the NCUA derived the risk weightings and what analytics were applied. Do they reflect the experience of credit unions and is that the reason they diverge substantially from Basel III as applied to banks? Do they incorporate risks that are absent from risk weightings in Basel III? Although loss rates and liquidity risk may vary between credit unions and banks, it would seem that risk concentrations, interest rate risk, and market risk would be experienced equally. We would respectfully request that the NCUA share the analytics employed and risk factors incorporated in each of the risk weighting categories.

2. CUSO Investment Risk Weighting

CACU has been and continues to be actively engaged with CUSOs in areas such as mortgage origination and servicing, credit card servicing, and indirect auto lending. Those activities have contributed substantially to the profitability of the credit union through both revenue generation and reduced operating expenses. Since loans to and investments in CUSOs are already subject to regulatory limits AND since the maximum loss is limited to the amount of investment it would seem reasonable that the risk weighting of CUSO investments would be 100%. By penalizing CUSO investments, the proposed rule is likely to jeopardize collaboration among credit unions focusing on revenue enhancement and expense reduction opportunities.

3. Individual Minimum Capital Requirements

The proposed rule gives examiners the authority to require a higher minimum risk-based capital ratio for individual credit unions based upon examiner experience. That authority will likely lead to inconsistent and unfair application based upon differing levels of experience and interpretation among examiners. CACU recommends strongly that individual minimum capital ratios be excluded from the final rule OR that the process and procedure for imposition of such requirements is strictly controlled and monitored for consistency in accordance with strict, well-defined standards.

4. Phase-in Period

Credit unions currently have only one source of capital — retained earnings. The NCUA has already acknowledged that a number of credit unions will fall below well or adequately capitalized as a result of the proposed rule. For those credit unions that would be subject to capital replenishment requirements, the proposed phase-in period of twelve to eighteen months appears arbitrarily short especially in light of the inability to raise additional capital other than through retained earnings.

5. Capital Cushions

What is less well understood is the impact on capital cushions maintained by a large number of credit unions that would not experience such a capital ratio shortfall on a technical basis.

CACU policy currently dictates a capital ratio floor of eight (8) percent and, in addition, maintains an additional two (2) percent cushion such that our capital ratio target is ten (10) percent. Although, CACU is very unlikely to fall below well or adequately capitalized based upon the proposed rule, erosion of our current capital cushion would require management to take action to rebuild the cushion having the same impact as if the credit union had fallen below well or adequately capitalized levels. This would require either shrinking assets or limiting asset growth until the capital cushion has been rebuilt and would certainly interfere with the planned execution of our current business strategy.

6. Impact on Future Business Strategies

Based upon the proposed rule, credit unions would in most cases be required to hold more capital than banks holding the same assets. That requirement would put credit unions at a distinct competitive disadvantage relative to banks. CACU recommends that the risk ratings in the proposed rule be altered to mirror Basel III so that credit unions and banks operate on a level playing field. In addition, this would greatly simplify risk weights by removing the inconsistencies among and incomplete implementation of "material risks". Other risks, such as concentration risk, are currently managed through examination and could continue on that basis.

The phase-in period should be substantially lengthened to allow for measured replenishment of required capital and managed capital cushions absent alternative sources of capital. This would reduce the need for affected credit unions to shrink assets or limit asset growth in order to meet capital requirements.

CUSO investments should be risk weighted at 100% to encourage, rather than discourage, collaboration among credit unions focused on enhanced sources of revenue and reduced operating expense. Such collaboration provides the credit union industry essential flexibility in meeting the needs of members profitably.

Individual minimum capital requirements should either be abandoned or strictly controlled according to well-documented standards and procedures to avoid inconsistent application by examiners with differing levels of experience and interpretations of risk.

We appreciate the opportunity to comment on the proposed rule and for listening to the concerns of CommunityAmerica Credit Union. Please feel free to contact me with any questions of comments regarding our response.

Sincerely,

Dennis E. Pierce
Chief Executive Officer
CommunityAmerica Credit Union
Chairman
Credit Union National Association