From: Jim Minge
To: _Regulatory Comments
Cc: Pamela Stephens; Suzanne Yashewski (syashewski@cornerstoneleague.coop); Larry Skinner
Subject: Comments on Proposed Rule; Risk-Based Capital
Date: Monday, May 19, 2014 2:57:51 PM
Attachments: image002.emz
image003.png
image004.png
image005.png

May 15, 2014

Via Email to regcomments@ncua.gov

Mr. Gerard Poliquin
Secretary to the NCUA Board
1775 Duke Street
Alexandria, VA 22314

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

Dear Mr. Poliquin,

On behalf of the 70,000+ members of Texas Trust Credit union, thank you for allowing me to comment on the proposed rule amending part 702 of NCUA regulations and implementing new Risk Based Capital (RBC) requirements.

Parity with Basel

Overall, we appreciate the thoughtfulness and balance of the proposed regulation. However, for quite some time, we have been reviewing our capital requirements as if we were subjected to the Basel standards adopted for our bank brethren. We were quite disturbed when we noted that the new requirements proposed by the NCUA would put us at a competitive disadvantage by requiring more than 50 basis points of additional capital. This is based on our analysis of our March 31, 2014 balance sheet using the NCUA calculator and the credit risk adjusted Basel requirements. Certainly given the differences in performance of Banks and Credit Unions through the Great Recession, and the relative difficulty Credit Unions face in raising capital, the proposed rule would target at least parity with the banking regulations.

It would appear that the largest contributor to this lack of parity is the interest rate risk provisions included in the proposed NCUA rule but not similarly included in Basel. We believe pursuing proper interest rate risk management is a critical part of our business. However we strongly believe that this goal is best accomplished through more stringent asset liability management regulations (as recently adopted) and not as part of the RBC requirements. We would suggest that the NCUA focus this proposal more on Credit Risk as is the case in the Basel regulations. Additional capital requirements for longer term assets or other categories of assets will ultimately hurt the ability for credit unions to remain competitive and pose additional management challenges.

Examiner Discretion

The provision to allow for the assignment of a higher (not lower) RBC limit for individual credit unions based on examiner judgment needs to be revised. As a CEO, it is critical to have some certainty in the number you are targeting. Many of us are fairly conservative and enjoy a cushion above that number to allow for unexpected growth. However, if you do not have certainty regarding what the requirements will be, the tendency may be to increase that cushion "just in case". This of course has the side effect of limiting growth and keeping more capital on the sidelines. In the market today, credit unions need to grow and prosper or slowly work their way to obsolescence. Any regulation that impedes this ability to grow needs to be looked at very closely. Certainly the NCUA has other arrows in their quiver to deal with those that may be posing undue risk to the share insurance fund. A provision such as the one proposed punishes the good along with the bad and should not be included.

Punitive Capital Requirements for Certain Asset Backed Investments

The 1250% RBC risk waiting for complex asset backed securities needs to be more specific and less subjective. Some investments from our collective history, such as Centrex, did not turn out well for everyone involved. This fact certainly demonstrates the need for some provision allowing the agency to require extra capital for high risk assets. However, as written this could include assets such as agency issued securities. I applaud the intent of this line item but certainly, it should be used only for non-agency guaranteed asset backed securities.

Additionally, I believe the weighting as proposed, could force credit unions to divest of assets at fire sale prices to avoid the impact of this asset on their RBC level. Also, the ability to determine when a credit union cannot demonstrate understanding of the investment in question would appear to be up to the sole discretion of the examiner. With a rule that adds complexity to the management of our balance sheet and makes it increasingly difficult for us to plan, any discretionary items have the impact of limiting our growth and creativity. To address these issues, I would suggest a risk weighting no more than double the next highest or 500% on this class of assets.

CUSO Investments

Investments in CUSO's are rated higher than delinquent loans. CUSO's are very important to the cooperative spirit of Credit

Unions and are a major strategic advantage over the banking community. There are many long lived, very successful CUSO's that help credit unions cooperate to provide better products and services to their membership. I would suggest the NCUA revisit this one size fits all requirement. Certainly the performance of the CUSO should be taken into account under the risk weighting rules. Start-up entities engaged in more high risk operations should not be included in the same category as long term CUSO's showing a history of profitable operations. We would suggest a maximum 100% risk weighting for CUSO that have operated profitably for more than 2 years with a higher risk weighting applied to those not yet profitable.

Credit Risk on Loan Pools

Certainly there are different risk levels within a homogenous portfolio of consumer loans. Just as an example, under the proposed rule, a portfolio of buy-here-pay-here car loans carries the same risk weighting as one composed entirely of A+ paper. You may argue that the additional risk for this portfolio will be accounted for by an increase in the Allowance for Loan and Lease Losses. However, as demonstrated in the Great Recession, factors that could not be reasonably estimated can cause higher than normal credit losses and have significant impacts on the capital necessary to weather the storm. If your balance sheet is made up of assets with higher credit risk, there ought to be a requirement to carry extra capital just as there should be some benefit for a demonstrated commitment to limit this risk on a credit unions balance sheet. I would suggest that the NCUA review the proposal and recognize that loans secured by vehicles to borrowers with clean credit carry a much lower risk weighting than unsecured loans to the same individual and an even lower rating than loans to individuals with lower credit scores.

Investment Weights

It seems counter intuitive to me that Treasury securities, SBA Pools or GNMA instruments, regardless of their maturity, carry a zero risk weighting while a well-managed moderate duration portfolio of agency backed securities is at 75-150%. If I understand the proposal correctly, we could buy 10 year Treasuries or 15 year SBA bonds and they would be 0% risk weighted. On the other hand a portfolio of agency guaranteed CMO's with a 3-6 year duration would be 75%-150% risk weighted. I believe if the proposal remains as is, many credit unions may consider reaching for higher yielding treasury, SBA or GNMA instruments with long durations in an effort to balance the need for earnings and risk-based capital requirements.

Hopefully the board will consider regulations, such as those outlined in Basel where risk weightings for investments are based simply on credit risk and not maturity.

Results of Non-Compliance

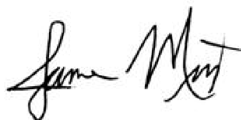
If a credit union falls below the required 10.5% RBC requirement but their capital remains above the 7% well capitalized threshold, the sole requirement should be the submission of a capital restoration plan which would seek to bring the RBC above 10.5% in a reasonable timeframe.

Effective Date

I would respectfully request that credit unions be given at least 36 months to prepare for the implementation of the RBC rule. The process of making changes to a credit union balance sheet is one that cannot be accomplished overnight. If changes are necessary as a result of the regulation, a longer implementation period would be very helpful.

I appreciate the opportunity to provide comments on this very important regulation.

Sincerely,



Jim Minge

President/CEO