Kentucky Credit Union League AND AFFILIATES

May 19, 2014

Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 55314-3428

Sent electronically to: regcomments@ncua.gov
Re: RIN 3133-AD77

Dear Mr. Poliquin:

On behalf of the 79 credit unions across Kentucky, I am writing to express our concerns with your recent risk-based capital proposal.

The Kentucky Credit Union League (KCUL) encourages National Credit Union Administration (NCUA) to reconsider the proposed changes to the Prompt Corrective Action Risk-Based Capital proposal. While KCUL supports efforts to ensure the credit union industry retains the necessary level of capital, the proposal does not allow Kentucky credit unions to properly evaluate their individual risk and the needed capital requirements for their individual institutions and does not provide a sufficient framework to allow credit unions enough time to replenish their capital buffer.

The proposed rule allocates risk based on the asset category rather than the strength of the credit union's management and quality of the asset. Kentucky credit unions with higher concentrations of certain lending products or longer-term investments have more sophisticated policies, procedures and experienced staff in those specific areas. The method of determining risk and capital requirements in this proposal restricts Kentucky credit unions which have the expertise to effectively deliver these services to the community and have the systems in place to properly manage and mitigate the associated risks. KCUL requests that NCUA reconsider the asset classifications to allow more flexibility in the risk weightings to incorporate additional factors particular to the credit union; specifically with real estate loans, member business loans, and longer-term investments.

The regulatory burden continues to increase for credit unions of all asset sizes, especially for real-estate lending products. Kentucky credit unions that have been able to maintain significant real-estate loan offerings to their community have done so through continued strategic planning and by dedicating substantial resources to adapt to new regulatory restrictions. Kentucky credit unions that had planned on long-term growth in certain real estate loans may not be able to execute that plan based on capital requirements. Credit unions will need to determine if it is feasible to raise the newly required capital and continue to provide certain lending products to communities within the state. Increasing risk weights based on concentration may penalize a credit union for developing an expertise in those areas and expanding these particular product offerings.

Credit unions have been working diligently to increase the member business loan cap to allow for future growth and to provide a meaningful opportunity for small businesses to access credit. The risk weightings associated with member business loans will undermine those efforts and restrict small business loan growth in Kentucky communities. The risk weightings also limit a low-income designated credit union's ability to fully utilize a necessary tool to provide loans in rural and underserved communities.

The proposed risk weights for long-term investments do not take into account applicable credit or asset liability management considerations; instead, it only captures interest rate risk concerns. A risk weighting system based entirely on the weighted average life of an investment does not allow Kentucky credit unions to take full advantage of their existing investment options to continue to serve their members. NCUA's current regulations already provide a regulatory framework which more accurately allows for credit unions to individually identify, manage and mitigate their risk exposure.

In addition to the high risk-weightings in certain areas based on concentration, KCUL is also concerned about the proposed cap of 1.25 percent of total risk weighted assets for the Allowance for Loan and Lease Losses (ALLL). NCUA has stated the amount of ALLL should be based upon management's current judgments about the credit quality of the credit union's portfolio. This judgment should be based upon all known relevant internal and external factors that could affect collectability. The Risk-Based Capital proposal reduces management's ability to account for individual credit quality factors that may potentially impact the credit union's portfolio.

The exclusion of the one percent deposit each credit union makes to the National Credit Union Share Insurance Fund (NCUSIF) in the risk-based capital ratio calculation should be reconsidered. Excluding the deposit inappropriately lowers a credit unions' risk-based capital position. Under GAAP, the credit union's NCUSIF deposit is an asset. This asset is of significant value to a credit union, as it represents the presence of federal deposit insurance and should be included in the risk-based capital ratio calculation.

If the proposed rule were to be enacted in its current form, at least one Kentucky credit union would be immediately impacted by the rule and would need to evaluate possible operational and member service adjustments. Another 22 credit unions with assets over $40 million would likely be impacted in the future as the services and investments in their models continue to grow. Twelve credit unions would see their cushions over well capitalized shrink under the proposed rule.

Credit unions are already devoting a significant proportion of their resources to meet changing regulatory requirements. And, small credit unions have been merging at an unprecedented rate. Implementing this rule as proposed will force credit unions which are currently below the $50 million in assets to consider whether growing their model is financially feasible due to the significant cost and restrictions placed on credit unions which exceed the $50 million threshold. It may also force more credit unions to consider whether merging with another credit union is a more viable option for future growth.

Credit unions in Kentucky are committed to their continued success and sustainability. These credit unions have already invested significant resources to establish their strategic direction. Changing the capital requirements would require the credit unions to spend additional time and resources to adjust these plans in accordance with the rule. An 18 month implementation period will not provide adequate time for credit unions to reconvene their management teams and Board of Directors to determine which adjustments to their model may be necessary or to build any additional capital in a manner that mitigates impact to members.

The Risk-Based Capital proposal is a significant departure from credit unions existing requirements, and credit unions do not have the same ability to raise capital that other financial institutions may have. If the proposed rule were implemented in its current state, many credit unions would be faced with the challenge of reducing product offerings or increasing interest rates and reducing dividends in order to quickly achieve the new capital requirements. A longer implementation period could reduce the need for credit unions to make more drastic cuts to member services than would otherwise be necessary.

We encourage the NCUA to reconsider the proposed Risk-Based Capital rule to account for the responsible management of Kentucky credit unions to assess risks based on their individual model. We ask that the NCUA consider the needs of Kentucky communities and the important role the credit union system plays in our state when evaluating risk-based capital regulations.

Sincerely,

Wendell Lyons
President