May 22, 2014

The Honorable Debbie Matz, Chairman
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Chairman Matz:

As an ex-state bank examiner, I applaud the NCUA for using a risk based capital approach to regulating credit unions. The approach seems fair, consistent, and transparent. I think a majority of credit unions believe that riskier balance sheets need to carry more capital to be deemed well-capitalized. The problem that I have with the proposed regulation is with the weightings of the assets and the respective capital needed. This will be most pronounced in the investment portfolios of credit unions. A bank with $100 million in total assets and $5 million in investment securities maturing in five to ten years is only required to keep $105,000 in risk based capital. A credit union with the same balance sheet composition will have to keep $787,500 in capital or 7.5 times as much as its bank counterpart. It gets even worse for investments with maturities greater than 10 years. Credit unions will have to keep 10 times as much in capital to be considered well-capitalized.

My employer is a CUSO focused on providing our member credit unions with business loan underwriting and other loan portfolio services. The proposed risk based rules will negatively impact credit unions that invest in or loan money to CUSOs. Existing CUSO investments will be hit with a six percent charge on their investment, so a credit union with a $50,000 investment in a CUSO will be assessed a capital charge of $3,000. Credit unions will probably still use the services of CUSOs, but they will want a greater return on their investment (at least six percent more).

Access to business loans is greatly needed right now in our economy, especially small business loans in rural communities. The decision to grow a business loan portfolio is made more difficult under the proposed risk based rules. For example, a $60,000,000 credit union currently has a business loan portfolio of $8,000,000 on its books or 13% of its assets. Under the proposed risk based rules, capital of $480,000 ($8,000,000 X .06) will be needed to carry this portfolio. If the credit union grows its business loan portfolio to $10,000,000 it will have to keep $800,000 in capital because business loans now make up 16% of the balance sheet. This change in capital requirements seems punitive. Furthermore, the risk based rules are not accessing the true risk of the credit union's business loan portfolio. Compare two credit unions with the exact same size of business loan portfolios. Credit union A has 25 loans totaling $8,000,000 in a well-diversified portfolio of real estate loans and C&I loans. Credit union B has 4 business loans totaling $8,000,000. Two of the four loans are to companies secured only by inventory, receivables and equipment. Which of the two portfolios are riskier? Under the proposed risk based rules, they appear equal.

In a limited capital system created by free enterprise, business entities should maximize their return on capital. By placing higher capital requirements on relatively risk free assets, credit unions will be forced into a strange balance sheet dilemma with uneasy results. Credit unions will sell off their longer maturity bonds. This cash will be kept in fed funds or very short term investments which will reduce the yields on their portfolios. In order to maintain profit goals, efficiencies would have to be gained and that usually means cutting jobs at credit unions. Another bad scenario would be that credit unions loosen their lending standards and make more loans in an attempt to get higher yielding assets on the books to make up for the loss of income from the longer dated bonds. A credit bubble could soon develop and history proves credit bubbles always pop with bad consequences.

Risk weights should not be significantly higher than requirements of FDIC insured banks. It appears that interest rate risk is a concern for the NCUA and the proposed risk based capital rules are being implemented to help control this risk. I suggest that interest rate risk should be managed properly through the examination process and not directly through regulation. Credit unions that have excessive interest rate risk should be reprimanded through the examination process. Many credit unions have very capable management that are currently managing their interest rate risk by match funding strategies (seeking long term funding for long term assets), using swaps, options, or other interest rate risk hedging products.

Please don't take away the creative nature of well-run credit unions with overly burdensome risk based requirements. The NCUA should pride itself in not being heavy handed when it comes to writing regulations. The credit union industry has enjoyed success over the last decade while many banks have gone out of business and deemed the decade a depression like era. The success and survival of credit unions might be the result of an industry not burdened as heavily as its banking competitors.

Sincerely,

Ben Bigger

Ben Bigger
Vice President/Loan Review Manager
BAFS, LLC.