CREDIT UNION OF TEXAS

May 23, 2014

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

Re: Proposed NCUA Risk Based Capital Rule

Dear Mr. Poliqin,

Credit Union of Texas, like many other credit unions commenting on the proposed risk-based capital rule, understands and agrees that a risk-based capital regulatory scheme may be a sensible approach to regulation in today's global economy. However, we believe the approach should be both rational and reasonable, neither of which appears to be present in the current proposal.

Credit Union of Texas supports a risk-based capital (RBC) proposal that: 1. Encompasses only credit risk in its risk weightings[1] 2. Has risk-weighted capital standards not more stringent than Basel III for community banks and appropriately and objectively assigns risk weights based on actual risk; and 3. Provides for a longer implementation timeline.

Credit Union of Texas has serious concerns with the rule as proposed.

Credit Risk is the Only Appropriate Risk Factor to Measure

Basel III is a credit-risk weighting system. NCUA, on the other hand, is intending to encompass Additional Risk into its risk weights. We urge NCUA to consider that credit risk is generally easily measured—and thereby regulated--on a macroeconomic scale. The other types of risk that NCUA is attempting to mitigate are typically much more of an individualized analysis of risk to a particular institution, and therefore much less effectively mitigated by a one-size-fits-all regulation. A one-size-fits-all approach has never worked for credit unions—not in the context of the financial services industry as a whole and not among the widely varying credit unions themselves. It is our opinion that encompassing Additional Risks in the proposed risk-weights is an attempt to substitute for effective, thorough and sometimes difficult examinations of an individual credit union, where the Additional Risks are more appropriately evaluated, managed and mitigated. We urge NCUA to consider our risk-based capital rule on a level playing field with Basel III, and only consider credit risk as the weight to measure.

[1] In addition to credit risk, NCUA attempts to also risk-weight interest rate risk, concentration risk, liquidity risk, operational risk and market risk (collectively "Additional Risks").

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Risk Weight for CUSO Investments

The NCUA proposal weights Investment in CUSO at 250%. We are aware that NCUA compares CUSO investments with equity investments (400% risk weighting) for community banks.[2] We entirely disagree that this is the correct category for such a comparison, and credit unions are not duped into believing that NCUA has done us any favors by risk weighting CUSO investments at "only" 250% when banks are "at 400%". The correct Basel comparison, investments in subsidiaries, has a risk-weight of 100%, as we understand the rule. This is the apples to apples comparison.

If NCUA believes credit union investments in CUSOs are such a substantially greater risk to the credit unions, the recent increased NCUA regulatory oversight of CUSOs is the more appropriate way to monitor that risk. CUSO risk is highly individualized, not an across-the-board risk weight that burdens all credit unions the same way. Further, there is no recognition in the proposed rule for different types of CUSOs. For example, the rule draws no distinction between a lending CUSO or a service provider CUSO, or whether it is a wholly owned CUSO; however, any one of these factors change the risk to a credit union.

A wholly-owned CUSO is consolidated into a credit union's balance sheet, and there is not a separate line-item amount for "Investments in CUSOs" on that balance sheet. At Credit Union of Texas, our wholly owned subsidiary, Credit Union Services, Inc., (CUSI) originates and holds consumer auto loans and leases. In the proposed NCUA model, the loans and leases (which make up 96% of CUSI's total assets) are risk weighted within the calculation model at 75%-150%, as appropriate. Again, this makes up a substantial amount of the total CUSI assets. The remaining assets, Cash and Other Assets, are also risk weighted as part of the Credit Union's balance sheet in the appropriate category in the model. Therefore, the *assets* owned by our CUSO are appropriately risk weighted. The amount that is left to include as "Investment in CUSOs" represents the equity of the CUSO. The equity of the CUSO is the amount that is left over after all liabilities are paid. In CUSI's case, at December 31, 2013, after all consolidating elimination entries are made, total liabilities remaining are a mere $1.2 million. *This* is the risk to the credit union, but yet the 250% risk weighting is being imposed on our equity of $42.7 million. In our opinion, this result is neither reasonable nor rational and in fact, is just wrong.

Additionally, the 250% risk weight is on the current value of the CUSO investment (which may be substantially more than the initial investment in the CUSO), and may have the unintended consequence of penalizing and discouraging growth in a CUSO. We do not believe that NCUA would impose a rule that would deliberately attempt to stifle CUSO growth; thus, we ask that NCUA review the 250% risk weight in light of that consequence and either (i) eliminate the separate and additional 250% risk weighting for a wholly owned CUSO or (ii) assign a 100% risk weighting to "Investment in CUSOs" and specify that the CUSO assets consolidated into the credit union's balance sheet are excluded from the model.

[2] According to Larry Fazio, NCUA Director of the Office of Examinations and Insurance, in the YouTube video published on the NCUA channel on April 17, 2014.

Specific Calculations for Credit Union of Texas

As an example of how these proposed changes would impact our credit union, as of December 31, 2013, we were well capitalized at 7.70%. Under the current RBC proposal, our RBC is 8.43%, or adequately capitalized. The most significant discrepancies are in two areas: Investments and Investment in CUSOs.

Investments are weighted based on weighted average life and increase from 20% for investments with a weighted average life of less than one year to 200% for weighted average lives greater than 10 years. Under Basel III, as we understand it, all investments are weighted at 20% regardless of average life. This difference in these weightings alone requires additional capital support of $108 million.

Secondly, by requiring our Investment in CUSOs, specifically CUSI which is consolidated, to be risk weighted at 250%, this increases the capital support by $74 million (compared to a risk weighting of 100%). Keep in mind that the loans and leases that are held in CUSI, due to consolidation of financial statements, already require capital support of $168 million in their respective line items. The additional assets in CUSI require $6.6 million of capital support, for a total of $174.6 million in capital support for the individual assets *plus* the $109 million requirement for the Investment in CUSO. This is $283.6 million in capital support for a profitable CUSO that has equity of $42.7 million and liabilities of $1.2 million after consolidation. This combination of double counting risk and excessive risk weighting just does not make sense.

Implementation Timeline

It is our understanding that the implementation process of Basel III has taken place over a 9 year period, while NCUA appears determined to impose this Draconian requirement as quickly as it believes is feasible.[3] NCUA, without logical justification, is proposing to impose much stiffer requirements on credit unions than the bank regulators and the FDIC have imposed on commercial banks. Credit unions will need--and they deserve--more time to digest and adjust to whatever the finally adopted version becomes. Based on the impact to our credit union, we believe three years following the final adoption makes much more sense and will give us the necessary time to evaluate and reallocate our risks if we choose to do so. It should be remembered that the credit union industry has covered its own problems during the recent financial crisis, and that NCUA's remorse over mishandling the corporate credit union debacle does not justify such a drastic timeline, when a more reasonable approach still would accomplish NCUA's goals.

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[3] NCUA's concern about timing was only regarding how long it would take the agency to amend the call report for RBC purposes, not how long it might take a credit union to reduce its risk profile by carefully adjusting its investments and portfolio in a manner that would minimize losses as much as possible. We feel that the agency's administrative duties are not paramount to a credit union's ability to prudently adjust its risk profile. *See* the YouTube video published on the NCUA channel on April 17, 2014.

Credit Union of Texas does not disagree with the concept of risk based capital. However, we urge careful review of the proposed risk weights to ensure that any such a weighting system is meaningful and adequately assess the risks to the individual credit union. Most importantly, the end result of a risk-based capital system must not have a disproportionate impact on capital that should otherwise be available to consumers. In our opinion, this proposed rule shows that NCUA is more preoccupied with protecting the Share Insurance Fund[4] than with promoting the health and welfare of the credit unions and their members. There has to be a balance of those interests where the agency can reasonably and thoughtfully do both.

Sincerely yours,

John B. Lederer
President and Chief Executive Officer
Credit Union of Texas

[4] We do not disagree with NCUA that protecting the Share Insurance Fund is a significant policy underlying the implementation of risk-based capital; we disagree that it should be the primary policy behind a risk-based capital rule.