Pawtucket Credit Union

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VIA EMAIL

May 27, 2014

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

Dear Mr. Poliquin:

Pawtucket Credit Union (PCU) is a State Chartered Credit Union located in Pawtucket, Rhode Island (Region1). PCU has fifteen (15) branches that service 82,000 members in Rhode Island and Massachusetts with $1.20 billion in deposits, $1.39 billion in loans and $1.59 billion in assets. PCU is considered "well capitalized" with net worth of 9.42% compared to a RBNW requirement of 7.28% at March 31, 2014. This letter is in response to the proposed amendments to NCUA's Prompt Corrective Action regulations as they relate to Risk-Based Capital rules.

Risk Weightings

Many Credit Unions in the north eastern part of the United States are mortgage lenders. Our membership has looked to PCU over the years as a source of financing for purchasing and remodeling their homes. In 2008 and 2009, at the beginning of the "Great Recession" that is now mostly behind us, the Credit Unions and community banks in our market were the lenders that continued to meet the needs of mortgage borrowers as the National lenders abandoned the Rhode Island market for over two years. PCU wrote $247 million and $305 million in mortgages in 2008 and 2009, respectively, while managing liquidity, interest rate risk and balance sheet growth by selling $170 million of that production.

Because PCU is a mortgage lender, the proposed risk weightings that increase to 75% for mortgage holdings over 25% and up to 35% of assets and 100% of mortgage holdings in excess of 35% of assets will adversely affect PCU's capital level. In addition, the tier weightings for investments with maturities over 1 year will adversely impact PCU in spite of the nature of those investments being primarily Federal Home Loan Bank, Federal National Mortgage Association, Government National Mortgage Association, Federal Home Loan Mortgage Corporation and Federal Farm Credit paper with little or no credit risk.

The BASEL III risk weightings for the banks remain constant, regardless of mortgage and investment portfolio size. If the proper policies and procedures are in place for lending and investments, loan underwriting standards are prudent, and an appropriate and rigorous ALM process is in place, the level of risk assigned by the proposed rules to the next dollar in the loan portfolio that exceeds 25% of assets or the securities maturing after 1 year appears inordinately high. Management is concerned that these risk weightings, particularly their impact on the calculation of risk-based capital levels, will impair PCU's ability to deliver the lending products desired by our membership in the future.

Additional Capital under the Proposed Rules

While we can appreciate that under both the current Prompt Corrective Action rules and proposed Risk-Based Capital rules PCU is "Well Capitalized", our concern is that under the proposed rules, the 214 basis point margin of net worth to the RBNW Requirement becomes 161 basis points from the 10.5% required to be well capitalized to the risk-based capital ratio of 12.11% calculated under the proposed rules (based on March 31, 2014 call report numbers).

In order to maintain this margin at the same level, PCU would need an additional $6.4 million of capital without any asset growth. Without access to the capital markets and with the low rate environment we continue to experience, it is not possible to increase net income without more earning assets that have to be funded by deposits or wholesale funding that will by necessity increase the denominator of the risk-based capital calculation under the proposed rules.

Impact on Our Ability to Compete and Members
Many credit unions, like PCU, kept lending channels open in some of the most difficult years since the 1930s. As proposed, the higher capital levels required for credit unions to remain well capitalized, compared to community banks, will put credit unions at a competitive disadvantage. Increasing capital on a base of earning assets will require higher rates on loans and/or lower rates paid on deposits. For lenders like PCU, managing asset categories to maintain capital levels going forward could also result in altering product offerings that would disadvantage credit union membership.

Need for and Timing of Changes to Capital Levels
The financial services industry has come through some of the most difficult years (2009-2011) since the Depression. The credit unions that made it through have not only paid for losses due the failure of natural person credit unions but also the failures of the Corporate Credit Unions. NCUA examinations of natural person credit unions have become more stringent over the last half dozen years keying in on areas such as asset/liability and interest rate risk processes and monitoring, liquidity, policies and procedures, loan underwriting and the calculation of the provision for and allowance for loan losses. These exams should provide insight into the management practices of credit unions. From the time the economy began its downturn (late 2008/2009), PCU has never had a year with negative earnings and capital has exceeded 9% at each year end; the equity ratio has increased since the end of 2010 while total assets have also increased. The credit unions that have survived learned how to generate net income and maintain equity in a truly adverse business and interest rate environment. As the economy and business climate improves, is an increase in equity levels necessary to ensure the financial well-being of credit unions?

The Management of PCU appreciates that the NCUA has provided the ability to comment on the proposed risk-based capital rules and your consideration of the comments above in deciding upon the actions to be taken with regard to the proposed rules.

Sincerely yours,

Karl A. Kozak
President / Chief Executive Officer

George J. Charette
Executive Vice President/Chief Financial Officer