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

Dear Mr. Poliquin:

This letter is in regards to the risk-based capital ("RBC") proposal of January 23, 2014 which is intended to improve credit union's capital position, allow for sound, long-term decisions by boards and management, and continue to allow credit unions to achieve their mission of helping members meet their financial goals.

We agree with the principal of a risk-based capital system. Common sense dictates those businesses engaging in activities entailing more risk should hold more capital. What we cannot agree with is an arbitrary and poorly designed system putting credit unions at a competitive disadvantage which has the potential to lead credit unions' management into poor credit allocation decisions, and ultimately, risks the ability for credit unions to serve their members.

Here are our suggested changes to the proposal:

Concentration Risk Weights: General

We believe concentration limits should be appropriately managed by boards and management, not through the RBC framework. Boards and management are responsible for determining risk tolerance levels for individual institutions and have the best knowledge of their markets and capabilities of their organizations to manage concentration risks. A system designed to increase the risk-adjusted capital cost of certain asset classes will lead to an overinvestment in other asset classes, driving down returns, and leading to reduced profitability and capital formation. The NCUA and state regulators already have sufficient resources to examine, supervise, and enforce concentration limits at the institution level for those businesses that are not adequately managing concentrations.

We believe the NCUA has confused correlation with causation in attempting to reduce industry-wide risk. For example, simply because two credit unions fail and they both had larger than average mortgage portfolios does not mean their mortgage portfolios *caused* them to fail. There are likely dozens of reasons *causing* their failure. Attempting to reduce concentration risk through the RBC will only create other unintended risks. It should be clear this type of system would be ineffective; the NCUA is the only Federal Banking Regulatory Agency to propose linking RBC and asset concentrations.

Concentration Limits: Mortgage Loans and Mortgage Servicing Rights

The current RBC proposal increases the risk-weightings on mortgage loans as the concentration level increases above 25% of assets. Going above this arbitrary level means a credit union will have to charge the unlucky member a higher interest rate to ensure its returns on capital are sufficient or it can charge the same rate and see its returns decline. Notice our bank competitors do not have to make this decision to charge their customers higher rates for no difference in the risk level of the applicant. We suggest a single risk-weight component of 50% for all performing mortgage loans.

We believe the 250% risk weighting is arbitrary and unsupported for mortgage servicing assets. These assets are evaluated at least annually for fair value so the NCUA has sufficient knowledge of their value. Additionally, MSR's serve as a hedge against interest rate increases and retaining the servicing enhances the member-credit union engagement. We suggest a consistent risk weight as the other Federal Banking Regulators.

Concentration Limits: Business Loans and Unfunded Commitments

As with mortgage loans, risk-weightings are substantially higher as concentrations increase. In fact, at just 25% of assets, the risk-weightings are *twice as high* for credit unions as for banks. While our business loans are currently limited to 12.25% of assets, as we serve more small business members and gain more experience, we would naturally like to request a waiver of the 12.25% limit. However, even though our experience and capacity may be superior to competitors, our cost of capital will be substantially higher for those members above the arbitrary 15% level. This higher capital cost would have to be figured into our decision to grow and serve new members or simply invest in lower return assets.

The capital treatment for unfunded commitments also reduces the ability of credit unions to appropriately serve business members. Operating lines of credit are an important source of funding for businesses and revenue for credit unions. Having to allocate capital at the 75% credit conversion factor and 100% risk weight will limit the amount of operating lines available or require higher fees, which will prompt business members to leave credit unions for other financial institutions, some of which may not be the best partner for them.

We suggest a single risk-weight component of 100% for all performing business loans and equivalent credit conversion and risk weightings as banks for unfunded commitments.

Concentration Limits: Investments and Deposits at the Federal Reserve

We fail to understand how the NCUA can propose a risk-weighting system so vastly different than the other Federal Banking Regulators for investments. The proposed methodology is simply a duplicative way to attempt to reduce interest rate risk. The NCUA already has sufficient regulatory authority through its interest rate risk regulations. The 1250% risk weighting for asset-backed investments or those an NCUA examiner *believes* a credit union does not understand, is unsupported by any rationale related to credit risk. We suggest investments be assigned the same risk weightings as the other Federal Banking Regulators have assigned.

I can only assume the 20% risk-weighting for deposits at the Federal Reserve was an oversight. I cannot believe the NUCA would assign anything other than a 0% weighting to those deposits.

Treatment of the Allowance for Loan Losses ("ALL")

The RBC limits the ALL deduction to 1.25% of risk-weighted assets. However, the entire amount of the ALL is available for losses, not just a portion of it. In fact, banks are able to deduct the total amount of ALL from their risk-weighted assets. There is no reason why credit unions should be adversely treated. Limiting the benefit of the ALL will tend to reduce total reserves over time since credit unions would, in effect, be penalized for holding any amounts greater than 1.25% of risk assets. Allowing a 100% deduction today will eliminate the need for any future concerns should the FASB adopt the new loan loss model.

Individual Minimum Capital Requirements ("IMCRs")

We are not, in principal, opposed to IMCRs since banks successfully operate with these requirements. However, the NCUA must acknowledge banks have considerably more flexibility in managing their capital structure than credit unions; banks can sell additional stock to raise capital while credit unions cannot. It must also be recognized allowing individual examiners to set IMCRs subjects the entire examination process to arbitrary and subjective judgments. Our reading of the proposal leaves wide latitude for imposing IMCRs and these additional capital requirements could set back a credit union for years to come. Open-ended capital requirements are a sure way to reduce the incentive for boards and management to provide the necessary capital for individuals, businesses, and our communities.

We believe the IMCR rationale must be better defined before the RBC proposal is adopted. Additionally as a suggestion, we believe institutions classified as "Well Capitalized" with Capital, Asset Quality, and Management ratings of at least a "2" or better should not be subject to IMCRs. Institutions where Capital, Asset Quality and Management are all rated a "3" could be afforded a safe harbor period of two to three calendar quarters prior to the imposition of any IMCR. We would further suggest a proscribed base IMCR increase (e.g. 50bps) with additional stepped increases if the board and management fail to correct identified deficiencies. These safeguards would still allow the NCUA to impose IMCRs, but would also give credit unions more certainty as to their capital requirements.

The NCUA already has vast powers to control credit unions. A well thought out IMCR policy is more important than rushing to get "something" done.

Implementation

We believe a three to four year transition period is much more reasonable than 18 months. Credit Union staff are already under considerable pressures to comply with the vast new regulatory burden being imposed. Forcing them to understand and take action on what could be significant changes in their business models or balance sheets serves no one's interests.

<u>Summary</u>

All financial institutions are operating in a world of declining margins, increased regulatory burdens, new competitors, and changing risks. If the credit union industry is to prosper, we need to recruit and retain the best people. The current RBC proposal is an attempt to move credit unions back to the world of the 1950s and 1960s: highly controlled with little prospects for innovation, risk taking, and forward thinking. Those industries cannot attract highly motivated people to run the businesses nor attract new members. Adoption of the RBC proposal in its current form will force many boards and management into discussions about charter conversions as the best way to protect our institutions and our members.

Thank you for allowing us an opportunity to comment on the RBC proposal. We welcome your questions or comments.

Best regards,

Russell E. Rosendal
President and Chief
Executive Officer