CAP COM
Federal Credit Union
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May 27, 2014

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

Via Email to: regcomment@ncua.gov

Re: Proposed Rule: Prompt Corrective Action – Risk Based Capital (RBC)

Dear Mr. Poliquin,

On behalf of the Board of Directors and the management team at Cap Com Federal Credit Union (Cap Com), we would like to thank the National Credit Union Administration (NCUA) for providing us the opportunity to comment on the above referenced rule for risk-based capital.

Cap Com is headquartered in Albany, New York with assets of $1.1 Billion as of March 31, 2014 serving 110,000 members. We are considered well-capitalized by current standards established by the NCUA with a net worth ratio of 10.81% and would continue to be considered well-capitalized under the proposed regulations.

In theory, we agree that financial institutions should maintain an appropriate level of capital that supports its long term strategies, balance sheet composition and risk profile while also protecting the integrity of their respective insurance funds. The banking industry has regulated capital through risk ratings. It is appropriate for credit unions to comply with regulatory parameters to protect the National Credit Union Insurance Fund (NCUSIF). However, we do not believe that the "one size fits all" approach to the proposed rule would adequately and uniformly identify, assess and measure risks inherent to each and every credit union.

We offer for consideration the follow comments relative to areas in the proposed rule that are, in our opinion, detrimental to Cap Com and/or to the industry as a whole.

Albany | Brunswick | Clifton Park | Cohoes | Colonie | Glenmont | Glens Falls | Latham | Niskayuna | North Greenbush

Proposed Adjustments to RBC

The capital included in the calculation is proposed to be adjusted for: (1) NCUSIF deposits; and (2) goodwill and intangible assets. Cap Com has been involved in mergers in the past and has carried goodwill and intangible assets associated with those mergers on its balance sheet in accordance with generally accepted accounting principles. This adjustment to capital puts Cap Com at a distinct disadvantage. It also creates a significant disincentive for credit unions to consider mergers at a time when consolidation within the industry is expected to increase. The NCUA must acknowledge that the majority of mergers will actually minimize and mitigate some of the risk to the industry as a whole as weaker credit unions are absorbed into larger and more sophisticated credit unions.

Risk Weights for On-Balance Sheet Assets

In general, we believe that the application of risk weights to on-balance sheet asset classifications is arbitrary and inconsistent. The proposed rule falls short of truly identifying the risk, or lack of risk, associated with our Credit Union's overall risk profile. The NCUA has not provided its rationale or logic in assessing risk-weights to on-balance sheet assets. We believe that the NCUA should disclose the methodology deployed and studies used in establishing risk weights for on-balance sheet assets.

In our opinion, we have noted several areas in the risk weighting of on-balance sheet assets that should be addressed and corrected.

- Cash and cash equivalents are considered Category 2 assets and assessed a 20% risk weight. If assets are held at the Federal Reserve, should these not be considered Category 1 assets?
- Investments:
    - The NCUA has incorporated a maturity component (interest rate risk) as the primary factor in determining the ultimate risk weight. The credit worthiness of the security issuer should be considered in addition to the maturity in order to appropriately assess the overall risk. From the NCUA's perspective as an insurer, it would seem logical that it would be more inclined to consider the credit worthiness of the issuer rather than an arbitrary weighted-average life schedule to gauge the ultimate return of principal, especially when the NCUA is proposing to reserve its right to apply higher capital requirements for individual credit unions that have higher levels of interest rate risk.
    - The proposed rule does not consider the various levels of credit risk within a credit union's investment portfolio versus the lending portfolio. While the primary factor of risk weights in the investment portfolio is maturity (interest rate risk), it appears the greater factor on the lending portfolios is credit risk. There should be consistent application of risk ratings in measuring the overall risk exposure of the credit union.
    - Debt obligations issued by United States Government Sponsored Enterprises (GSE) are considered Category 3 assets and assessed a risk weight of 50%. These assets are measured by maturity and weighted-average lives of the obligations. The proposed rule is inconsistent in the application of risk weights

in that residential mortgage loans guaranteed by the federal government through FHA or VA as well as loans guaranteed by SBA are considered Category 2 assets. Both of these asset classifications are backed by the U.S. Government.

- Varying loan types in the Member Business Loan (MBL) portfolios are uniformly treated in the proposed rule as maintaining the same level of risk regardless of its purpose or collateral. The overall diversification of the MBL portfolio is not considered in the proposed rule. NCUA has taken a tiered approach towards assessing the risk in the MBL portfolio. Any MBL less than or equal to 15% of total assets would be assigned a 100% risk weight while MBL's greater than 15% of assets would be assigned 150% risk weighting. Not only is this risk weight arbitrary in nature, it also over-complicates what should be a straight forward calculation. Credit unions with specialized lending will be dramatically impacted by the proposed rule as it places little to no emphasis on the management of the portfolio and historical performance. The proposed rules will ultimately discourage credit unions from originating these loans.
- Credit Union Service Organizations (CUSO's):
    - Under the proposed rule, investments in CUSO's would be considered Category 9 assets and risk weighted 250%. We believe this arbitrary assessment is excessive especially when compared to other proposed risk ratings.
    - Cap Com has diversified its investments in CUSO's amongst four entities providing products and services in: (1) residential mortgage origination and servicing; (2) investment and insurance services; (3) residential and commercial real estate title insurance; and (4) car buying services. As of March 31, 2014, Cap Com FCU has invested a total of $4.8 million in these CUSO's and has recorded retained earnings of $8.8 million. Nearly two-thirds of member equity in these CUSO's is comprised of current and prior year profits. It is our opinion that these combined investments in CUSO operations do not pose a risk of 250% of our investment.
    - Cap Com's strategic development of CUSO operations was deployed through organic growth as well as acquisition. The recent acquisitions resulted in both goodwill and intangibles being recorded. Under the proposed rule, Cap Com would be required to not only reduce the capital by the amount of goodwill and intangibles recorded but it would also be required to risk-weight these assets at 250%.
    - It is our belief that the NCUA's proposed rule will have far reaching implications on the corporate structure of credit unions and thus change business models and potentially cause impairment to existing goodwill and intangible assets.

<u>Liability Composition</u>

In general, the NCUA fails to address liability management in the proposed rule. Liability management plays a key role in the level of risk (i.e. interest rate risk and liquidity risk) of a credit union. The proposed rule penalizes credit unions that are proactive in managing their liability structure to help mitigate interest rate and liquidity risk. By ignoring the liability structure, this proposed rule implies that the cost of funds is not an important component in managing interest rate risk.

Individual Minimum Capital Requirements (IMCR)
The proposed rule provides the NCUA with the authority and ability to establish higher minimum risk-based capital standards for individual credit unions in any case where the circumstances indicate that a higher risk-based capital requirement is appropriate. It is our opinion that the application of IMCR is arbitrary and subjective. The application and interpretation of regulations by NCUA examiners is inconsistent. To place the requirements of IMCR on a specific examination team is not considered reasonable or prudent. We recommend that this element of the proposed rule be eliminated.

Public Accessibility to RBC Calculator
We agree that a RBC calculator is a valuable and important tool to assess risk of a given credit union. However, we believe that its use by the general public in assessing the financial health of a specific credit union is misguided. The complexity of this proposed rule is significant and accordingly has generated a sufficient level of response from the credit union industry. To think that member or potential member can appropriately measure and interpret the resulting RBC ratio of a specific credit union is not considered reasonable. We recommend that the RBC ratio be appropriately disclosed to the public as part of the required quarterly reporting criteria. Members and potential members can assess the risk associated with a specific credit union using as much information as possible in coming to their respective conclusion.

Implementation Period
The NCUA has proposed an implementation period of 18 months to comply with the new rules. This is considered to be far too short a period and almost certainly ensures many credit unions will not be able to comply with the ruling. If the ruling passes as it currently stands, credit unions will be required to supplement capital and change their business models to engage in businesses which have a lower risk rating (as defined by the NCUA) in order to maintain their current capital position. As a point of reference, banking institutions regulated by the Federal Deposit Insurance Corporate (FDIC) in general have far greater resources and existing familiarity with risk-based capital regulations. These institutions have a longer period to comply with the requirements set forth in the new BASEL III. We believe more time is needed to fully implement proposed changes after the rule takes effect.

Supplemental Capital
The introduction of a risk-based capital system requires more options for all credit unions to raise supplemental capital. We encourage the NCUA to accelerate the efforts to implement supplemental capital options for all credit unions, in conjunction with the risk-based capital rule implementation, providing an important tool for those credit unions that will no longer be well capitalized as a result of this rule and for others that need strategic options to assist them in managing to the new risk-based capital standards.

Conclusion

While Cap Com supports NCUA's effort to monitor industry risk through risk-based capital standards, we believe that the aforementioned areas of concern warrant change to the proposed rule. We respectfully request that the NCUA provide the rationale to the methodology used in assigning risk weights to investment and loan classifications as well as considering the liability structure of credit unions and its impact on their risk-based capital. We ask that additional analysis and review be performed as it relates to CUSO risk weighting. Finally, credit unions should be provided more time to comply with the rule after it takes effect.

We appreciate the opportunity to provide comments and for your consideration of Cap Com's position on this proposed rule.

Very truly yours,

Paula A. Stopera
President / CEO

Edward Gilligan
Chairman, Board of Directors

David J. Jurczynski
EVP / CFO