

May 28, 2014

To: regcomments@ncua.gov

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

RE: Comments on Proposed Rule: PCA - Risk-Based Capital

Dear Mr. Poliquin:

Communication Federal Credit Union (CFCU) appreciates the opportunity to comment on the National Credit Union Administration (NCUA) Board's proposal to revise Prompt Corrective Action related to Risk-Based Capital. CFCU serves select employee group in the states of Oklahoma and Kansas 60,000 members and \$921.6 million in assets. CFCU agrees there may be a need to modernize capital standards to identify excessive risk in credit union balance sheets. However, management feels the current Proposed Rule will have negative effects on CFCU members and discourage investments in long term strategies necessary to the survival of credit unions. CFCU is asking the NCUA to consider revising risk weightings to more reasonably assess concentration and interest rate risk and to better align the proposed risk-based well capitalized requirements to existing net worth requirements. Under the proposed risk-based capital rule, CFCU's capitalization level will increase. However, we believe the current proposed rule could result in many credit unions either reshaping their credit union's business model or considering a charter change. Neither option is beneficial to credit unions or members.

The modernization of NCUA rules defining minimum capital requirements and Prompt Corrective Action appears to be timely given the 2007-2009 recession and Basel III. We believe that any such modernization should take into consideration the unique characteristics and qualities of credit unions, the need to identify credit unions with excessive risk, and the need to create a risk-based standard that is comparable to Prompt Corrective Action systems that are employed by other Federal Banking Regulatory Agencies. There is no evidence that risk based capital requirements, utilized by the banking regulators, work any better than the net worth requirements currently imposed by the NCUA. The CUNA analysis of NCUSIF losses vs. FDIC losses from 2007 to 2013 shows the banking loss rate, with risk-based capital standards in place, was 8.5 times higher the credit union experience with a simple leverage ratio being used for capital adequacy. During this period the FDIC loss rate per \$1,000 of deposits was \$2.66 vs. the credit union loss rate of \$0.31 per \$1,000 of deposits. Banks have had risk-based capital requirements for nearly 25 years and these requirements neither prevented the latest crisis in 2007 nor stopped significant failures in the banking system.

The credit union industry came through the worst recession in history with few problems so the question needs to be asked, "Is it necessary to implement a proposal where most credit unions will see reduced buffers above being well capitalized"? Most credit union failures, including the Corporates, centered around high concentration levels that are subject to the annual examination process. As opposed to implementing risk-based capital standards that appear to unfairly measure interest rate risk and concentration risk, should the NCUA

consider better defining risk weights in combination with the need to improve examiner skills? Below are the comments that CFCU is asking the NCUA to consider in developing the final version of the Risk-Based Capital Rule.

CFCU General Comments:

1. **Several of the risk weightings under the Proposed Rule appear to be too general or excessive. Under the Proposed Rule, credit union risk weights would be higher than that of banks requiring credit unions to hold more capital than banks for the same assets. This is a major concern to CFCU as it would place credit unions at a competitive pricing disadvantage in an already highly competitive marketplace. In addition, using higher risk weights on long-term assets to deal with interest rate risk is misleading without considering liability maturities.**

#### Cash Held at the Federal Reserve

CFCU has been holding cash at the Federal Reserve as an alternative to short term investments and as a source of liquidity should there be an increase in the utilization rate on unfunded lines of credit or an outflow of non core deposits being parked in the balance sheet in this historically low rate environment. Under the Proposed Rule, cash balances being held at the Federal Reserve are given a 20% risk weighting. Given that the Federal Reserve has been designated as a source for emergency liquidity for the entire credit union industry, there appears to be little risk in holding cash balance at the Federal Reserve. Under Basel III, central bank reserves are deemed to be highly liquid assets during a time of stress and carry a 0% risk weighting. CFCU believes cash balances being held at the Federal Reserve should be given a 0% risk weighting in the final version of the Rule.

#### Investments

Under the Proposed Rule, investment risk weightings for credit unions are significantly higher than that of banks. The NCUA risk weights appear to be punitive and somewhat inconsistent when compared to banks thus putting credit unions at a disadvantage. All Treasury Securities and those Securities guaranteed by the NCUA or FDIC carry a 0% risk weight, no matter what the maturity. Other Agency backed Securities with no credit risk, such as FMNA and Freddie Mac, are risk weighted based on weighted average life time buckets. Investments with weighted average lives greater than 5 years are given punitive risk weights of 150% for 5 to 10 year average lives and 200% for average lives greater than 10 years. This compares to 20% risk weightings for similar securities in the banking model. In addition, a 30 year whole loan mortgage on CFCU's balance sheet would carry a 50% risk weighting while securitizing the same loan into a 30 year FNMA security, with enhanced liquidity, would carry a 150% risk weighting. CFCU believes the final version of the Rule should more closely mirror bank risk weightings for investments so as not to create such a competitive disadvantage. CFCU also believes there should be no risk weightings on investments greater than 100%.

#### Real Estate Loans

Under the Proposed Rule, no distinction is made on the risk weightings assigned to mortgage loans of various maturity and repricing terms. A 30 year fixed rate mortgage gets the same risk weight as a 1 year adjustable rate mortgage and a 30 year fixed rate home equity loan gets the same risk weight as a variable rate home equity line of credit. As opposed to implementing risk-based capital standards that unfairly lump all mortgage loans together

there should be more diversity in the risk weighting. Over the past 5 years, CFCU has been selling most 20 and 30 year fixed rate mortgage. As a result of holding only 15 year fixed rate mortgages, CFCU's balance sheet is well positioned for a rising rate environment. Under the Proposed Rule, there would be no difference between CFCU's capital requirement for its diverse mortgage portfolio and the capital requirements for a credit union that holds all 30 year mortgages in the balance sheet. CFCU believes that the capital requirement for shorter maturity fixed rate mortgage loans should be lowered in the final version of the Rule to fairly take into consideration the reduced risk associated with these shorter term mortgage loan products.

**2. The NCUSIF deposit should not be deducted from the risk-based capital numerator.**

The National Credit Union Share Insurance Fund 1% deposit is being ignored in the risk-based capital calculation. The NCUSIF deposit is a valid asset that can be refunded for various reasons including conversion to a bank or savings institution charter, a credit union electing private insurance instead of NUCA or voluntary liquidation. In addition, the deposit can specifically be attributable to a failed credit union providing an additional buffer against NCUSIF losses in addition to the failed credit union's capital. If a credit union did convert to a bank charter the NCUSIF deposit would immediately be included in the risk based capital numerator. CFCU recommends not deducting the NCUSIF deposit from the risk-based capital numerator.

**3. CFCU has concerns about the examiner being able to arbitrarily decide if the credit union needs a higher capital ratio, even if the calculation indicates the credit union is well capitalized.**

The Proposed Rule gives the NCUA authority to require a higher minimum risk-based capital ratio for individual credit unions based on NCUA examiner expertise. This discretion could lead to unfair and inconsistent interpretation and application of the Rule and will lead to mistrust between credit unions and the NCUA. CFCU strongly recommends the elimination of individual minimum capital ratios from the final version of the Rule.

**4. Consideration should be given to increasing the 1.25% allowance limit for adding to the numerator should FASB adopt the Current Expected Credit Loss model.**

FASB's proposed new standard on the allowance will most likely increase normal reserves by an estimated 30% to 100% at some credit unions. CFCU believes that more of this required allowance should count towards capital should the higher standard be adopted in the near future.

**5. Consideration should be given to permit federally insured credit unions to offer supplementary capital.**

Credit unions remain the only financial institutions that do not have access to sources of capital beyond retained earnings. If higher capital standards are to be imposed on the credit union industry under the Proposed Rule, affording credit unions the ability to raise supplementary capital the counts towards net worth requirements seems to be an appropriate policy consideration.

In summary CFCU feels the current Proposed Risk Based Capital Rule may be too general in assigning risk weightings, focuses on a regulator's model designed to identify concentration and interest rate and not member needs, has the potential to override the Board's and Management's judgments on business strategy and risk and leaves the credit union subject to examiner and Agency abuse by allowing for arbitrary higher minimum capital limits. The Proposed Rule, in its current form, will most likely reduce the risks to the NCUSIF but at a significant cost to credit unions and their members through reduced returns and higher-cost residential and member business loans. In addition it will place credit unions at a competitive disadvantage as it would require far more capital than what is required for banks, especially when considering a credit union's inability to raise supplemental capital. CFCU feels that with modifications to the Proposed Rule based on objective criteria, the final version of the Risk-Based Capital Rule could in fact be a significant improvement over current Risk Based Net Worth.

Thank you for the opportunity to comment on the Proposed Rule and for listening to CFCU's concerns. Please feel free to contact me with any questions or comments regarding CFCU's comments on the Proposed Rule.

Sincerely,

Connie Cofer  
Senior Vice President of Finance/Chief Financial Officer