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May 27, 2014

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

RE: Proposed Rule – Prompt Corrective Action - Risk Based Capital (RIN 3133-AD77)

Dear Mr. Poliquin,

We appreciate the opportunity to comment on this very important proposed regulation and hope the NCUA Board and Agency Leadership is sincere about listening and reacting to credit union concerns voiced through these comment letters.

Five Star Credit Union (Five Star) is a State-Chartered Federally Insured community based financial institution with over $250 million in assets and over 25,000 members. Five Star has been a low income designated credit union since 2004 and a Community Development Financial Institution since 2010. We currently serve a diverse membership base in mostly low income rural communities located in Southeast Alabama and South Georgia. In order to properly serve our membership, grow and prosper, Five Star has to be flexible and find opportunities where and when they present themselves. We believe several areas of the proposed rule will severely impact service to our members and our ability to grow by requiring or encouraging us to limit certain products and services we offer due to capital concerns, and by increasing the cost of these services to our members. As a member-owned financial institution, we act as an intermediary between borrowers and savers. Borrowers expect us to have cash to lend to them at fair and competitive rates and savers expect a reasonable return for their money and a safe place to put it. As facilitators in this process, we earn a return for our ability to attract both savers and borrowers and for assuming the risks inherent (interest rate, credit, liquidity, operational, market, concentration, strategic, compliance & reputation) in both transactions.

We fully believe a credit union's capital reserves should reflect the level of risk dictated by their individual balance sheets and that are required to appropriately serve its respective membership; however, we feel the proposed regulation does not allow adequate room for each credit union to serve the uniqueness of its individual membership base. We are in favor of revisions to the agency's current risk-based net worth (RBNW) requirements and we fully support the NCUA's efforts to address perceived weaknesses in its current format. We also acknowledge the challenges in developing regulations to fairly and accurately reflect perceived risks across the credit union industry as a whole. Below are the primary concerns Five Star has with the proposed rule and each will be addressed in separate sections.

- Using a single capital regulatory process as a way to measure and mitigate several areas of risk
- Proposed risk weight categories and associated risk weights
- The general requirement that all credit unions should fit in a 'one size fits all' capital structure
- Deducting Goodwill from the capital used to calculate the new ratio
- Limiting ALLL to 1.25% of risk-based assets
- Risk weighting unfunded MBL commitments
- Individual Minimum Capital Requirements
- Requiring compliance within 18 months

Using a single capital regulatory process as a way to measure and mitigate several areas of risk

The NCUA set forth several goals for the proposed rule. Specifically, goal number two was that "the requirement should address credit risk, interest rate risk, concentration risk, liquidity risk, operational risk and market risk." We understand that the Federal Credit Union Act (FCUA) requires NCUA to "design the risk-based net worth requirement to take account of any material risks against which the net worth ratio required for an insured credit union to be adequately capitalized may not provide adequate protection." We do not feel the FCUA should be interpreted to include all of the risks the agency is trying to capture in this rule. Not only is this inconsistent with the comparable Basel III guidelines for community banks, the rule as written oversimplifies control for certain risks at the expense of others. Proposed risk weight categories as written (which we discuss in greater detail under our "Proposed Risk-Weight Categories" paragraph), may create an opportunity (or "risk-based incentive") for credit unions to reduce interest rate risk and concentration risk, but may increase credit risk for those institutions that choose to focus on a more risky product (such as unsecured loans), simply because that product has a more favorable risk-based treatment. We believe attempting to mitigate several areas of risk using a single regulatory capital process cannot appropriately and adequately provide protection from these varied risks. *We recommend limiting regulation regarding credit union capital to exclusively reflecting the inherent risk to an institutions capital base in consideration of the actual risk that exists within each asset category and not attempting to control all or other risks associated with operating a complex financial institution in one regulation.*

Proposed Risk-Weight Categories and Associated Risk-Weights

For the purposes of this comment letter we will limit our comments in this section to non-investment assets. We feel the proposed rule attempts to determine risk exposure through the expansion of risk-weight allocations by concentrations. Rather than assign standard risk-weights based on risk of loss in a particular loan type as in Basel III, the proposed rule expands the current agency practice of assigning risk-weights based on specific concentration parameters of each loan type. As an example, other real estate loans have been separated from first mortgage loans and assigned individual concentration parameters ranging from 100% to 150%. Member business loans, which are already limited by regulation, are assigned new and increased concentration parameters ranging from 100% to 200%. In contrast to these categories, consumer loans, which could easily have a higher risk profile than either secured real estate loans or member business loans do not receive a "risk-weight penalty" due to concentration, but instead receive a standard risk-weight of just 75% regardless of concentration level. All of the non-investment risk categories, with the exception of delinquent consumer loans, have the same or significantly greater weights than the risk weights under Basel III. There has been no clear explanation provided as to how these risk-weights were derived or why some of them are so different from the corresponding risk-weights under Basel III. In addition to the generally higher weightings (which cause credit unions to accumulate higher capital levels than our community bank competitors), the various risk-weight assignments in the proposal may create "risk-weight incentives" for credit unions to take on certain types of risks, regardless of whether or not those risk are appropriate for the specific credit union. The risk-weight parameters as written have a bias towards consumer lending whether or not that loan is unsecured or secured. To give an example as written, an unsecured non-delinquent consumer loan would receive a risk-weight of 75%, which is lower than either a secured member business loan (100%) or a secured other real estate loan (also 100%). Furthermore, if either the secured member business loan or secured other real estate loan exceeds 25% of total assets, their risk-weights increase to 150% and 200% respectively. Additionally, regardless of the lending opportunities that may be available in an individual credit union's market, every credit union will be able to make unlimited unsecured consumer loans without "risk-weighted penalties" that are present in other loan categories without regards to the quality of the individual loan categories' portfolio. We feel credit unions should not be regulated towards loan products that are not conducive to the service of their membership by a regulatory capital process. Each credit union, based on the needs of their individual membership, market and existing staff expertise, should be able to choose and deliver the products demanded by their membership provided they have sufficient reserves reflecting their product choices and the risks associated with those choices. *We recommend that the agency adopt risk-weight guidelines that are more consistent with the risk-weight guidelines established in Basel III and eliminate all concentration limits.*

The general requirement that all credit unions should fit in a 'one size fits all' capital structure

Requiring that all credit unions fit in to a 'one size fits all' capital requirement regardless of the individual credit union's member needs may have unintended damaging consequences to the growth and strength of the industry as a whole. For example, requiring the same capital requirements for a credit union in South Alabama as a credit union in Alaska is as illogical as requiring those two credit unions to have the same disaster recovery plan. We can plan and prepare for an Alaskan blizzard in South Alabama with all the proper supplies and rations (i.e. Capital), but in reality the risks inherent in Alaska are very different from those in South Alabama. A credit union should be able to offer the products and services that best serve their members, and not try to force member needs into products defined as less risky by a regulation. Requiring members to adapt to us instead of us adapting to our members will have a detrimental effect on FSCU and may negatively affect our industry. The NCUA should be mindful of not instilling an industry culture of excessive risk-avoidance as it may create a recipe of greater industry mediocrity.

Deducting Goodwill from the capital used to calculate the new ratio

Deducting Goodwill from the capital allowed for use in the new requirement may hinder the growth of the industry, reduce the ability for credit unions to serve member needs, and pose additional risk to the NCUSIF. The credit union industry has experienced success and growth through mergers (some strategic and others necessary due to regulatory actions) over the past few years which has placed goodwill on the balance sheet of credit unions across the country. The industry is projected to continue this consolidation trend for the foreseeable future. If the regulation proceeds as proposed the questions should be asked, what happens to the credit unions that would have been merged? And what happens to the members that were being served by those credit unions? We believe credit unions seeking merger partners in the future will be faced with two options: voluntary or involuntary liquidation. Reducing capital by the amount of goodwill will significantly reduce the number of mergers that take place, and force members being served by these credit unions in to higher rates and fees at other alternative financial institutions. The credit unions that are forced into involuntary liquidation will pose greater risk and potential loss to the NCUSIF. *We recommend NCUA reduce the Goodwill risk rating from 100% to 25% in the final regulation which would still allow for a reasonable level of risk to be recognized.*

Limiting ALLL to 1.25% of risk-based assets

Reducing and limiting the amount of loan loss reserves that can be included as capital is completely inconsistent with its purpose. The Allowance for Loan and Lease Losses (ALLL) is created to absorb losses present in the loan portfolio, and by reducing and limiting (from 1.50% to 1.25% of total risk-weighted assets) the amount to be used for regulatory capital will understate a credit unions true ability to address the amount of risk on its balance sheet. If a credit union anticipates future losses due to circumstances outside its control (i.e. a recession, mass layoff at a large employer) and funds its ALLL in excess of 1.25% of total risk-weighted assets to meet its needs, it will be punished for its conservative and prudent business decision. In the event a credit union had to be liquidated the entire balance in the ALLL would be available to reduce the impact to the NCUSIF; however, the credit union's benefits are capped while it is a going concern. The proposed rule states that lowering the percentage provides an incentive for granting quality loans and recording losses in a timely manner. We feel this could further push credit unions away from lending to members with higher risk profiles which in many ways goes against one of the reasons credit unions were established. *We recommend the NCUA allow 100% of a credit union's ALLL to be counted in the capital equation used for the Risk Based Capital calculation.*

Risk weighting unfunded MBL commitments

The risk weightings and concentration thresholds proposed for Member Business Loans (MBLs) are limiting and burdensome to Five Star's (and the industry's) ability to adequately serve our members business credit needs. The regulations does not take into account the individual credits unions' business lending expertise or the demand in the respective credit unions market. We believe the new regulation will result in higher fees and interest rates to members and lead to fewer members being served. We also believe adding unfunded commitments on business loans as part of the calculation will add unnecessary obstacles for credit unions to serve their members. We foresee credit unions having to limit the available credit for member businesses to grow and will either drive those members to find other financial institutions to meet their needs or require the members to continuously come back and request additional borrowings which will increase the cost for those members in either situation. *We recommend the NCUA remove unfunded commitments from the capital requirement*.

Individual Minimum Capital Requirements

The ambiguous and subjective language allowing NCUA to require higher minimum capital requirements is concerning. The proposed regulation states the NCUA can require higher capital requirements when a credit union has failed to properly plan for, or execute, necessary retained earnings growth. Under this proposed language NCUA could require increased capital of a well or adequately capitalized credit union suffering from a year of negative earnings due to unforeseeable events. The proposed language allows enough room for NCUA to require higher capital of any credit union at any time regardless of its capital structure and member needs. This language will now add another level of uncertainty that credit unions have to manage and plan for in their strategic goals, and that other level uncertainty is the risk tolerance of the entire NCUA staff and board. How will a credit union that effectively manages its liquidity and cash flows to meet its members and business needs also manage the same liquidity and cash flows for a risk adverse examiner who see value in maintaining a higher level of liquidity? *We recommend the Agency take more time to develop a better set of objective requirements that could lead to higher capital requirements for a credit union given a particular set of circumstances and feel this portion of the regulation as written is unnecessary given the existing latitudes already in place through the agency's current enforcement processes and recommend that it be removed.*

Requiring compliance within 18 months

Requiring compliance with in an 18 month period will not allow the industry enough time to properly evaluate the full ramifications of the regulations and adequately change its balance sheet structure. Although there are a limited number of credit unions immediately effected by the regulation we believe other credit unions (FSCU included) may have to shift strategic goals to position ourselves in a new direction, and implementing those new goals will be daunting. With credit unions only avenue to increase capital being through retained earnings it will take longer than 18 months for a credit union to take appropriate steps to increase earnings to a sustainable level ensuring their ability to maintain capital levels necessary to serve their member's needs under any new requirements. We believe a compliance time frame equivalent to the Corporate Credit Union's requirement of 36 months would allow credit unions adequate time to shift their strategic goals and earning capabilities to meet the new regulation. Banks were given up to nine years to comply with Basel III, we do not feel 36 months (or longer) would put the NCUSIF at a greater risk than it is at now.

We greatly appreciate the opportunity to submit our thoughts on the proposed Risk Based Capital Requirement. We respect the responsibility of the NCUA and its role in ensuring the safety soundness of the industry, and we ask that the success of the credit union industry during the roughest economic time since the Great Depression not be forgotten or easily dismissed.

Sincerely,

J. Wallace Johnson	*Robert A. Steensma*	*Tyler Beck*
J. Wallace Johnson	Robert A. Steensma	Tyler Beck
Board Chairman	President/Chief Executive Officer	Vice President/Chief Financial Officer