LOS ANGELES
POLICE
FEDERAL CREDIT UNION

G. Michael Padgett
President/CEO

May 27, 2014

To: regcomments@ncua.gov

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

Subject: Comments on Proposed Rule: PCA – Risk-Based Capital

Dear Mr. Poliquin:

Los Angeles Police Federal Credit Union (LAPFCU) appreciates the opportunity to provide comments to the National Credit Union Administration (NCUA) on its proposed rule, Prompt Corrective Action – Risk-Based Capital. LAPFCU is a federally-chartered credit union located in Los Angeles, California, serving over 39,000 members with $799 million in assets.

LAPFCU supports NCUA's initiative to introduce risk-based standards into their capital calculations. We understand NCUA's intent to adopt a new risk-based capital rule for credit unions that considers "all material risks." Requiring credit unions with riskier or more complex balance sheets to maintain higher capital levels than lower-risk credit unions seems prudent. However, we believe that the proposed rule fails in a number of aspects. As a result, America's credit unions, and their members, will not materially benefit from this proposed rule. The application of risk weighting may negatively affect the business decisions of credit unions in how they currently invest and diversify their asset classes in the future. The proposed risk-based capital rule could discourage credit unions from engaging in businesses that are stable and benefit members. We also feel the proposed rule should provide greater clarity regarding the risk weighting of certain types of investments and parity with other Federal Banking Regulatory Agency standards upon which the proposed rule is based.

The following are comments that we are asking the NCUA to consider in developing the final version of the Risk-Based Capital Rule.

Investment Portfolio

Under the proposed rule, investment risk weightings for credit unions are significantly higher than for banks. U.S. Government obligations, directly and unconditionally guaranteed by the full faith and credit of the U.S. Government, are appropriately assigned a 0% risk weighting, no matter the maturity. However, there is no differentiation made regarding the credit risk of the remainder of the portfolio. Balances held at the Federal Reserve Bank and U.S. Government Agency Securities, such as Fannie Mae and Freddie Mac, are treated no differently than higher credit risk investments, despite their very low level of credit risk.

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Federal Agency Securities with virtually no credit risk, are risk weighted based on weighted average life maturity buckets. Agency securities with weighted average lives of 5 to 10 years are given risk weights of 150%, and securities with average lives greater than 10 years are given risk weights of 200%. This compares to 20% risk weighting for similar securities in the banking model.

We suggest a more rigorous calculation of the credit risk in the portfolio that allows for more levels of credit risk and more varied risk weightings. The current proposal's emphasis on the interest rate risk in the portfolio (maturity buckets) may not be appropriate without considering a more complete assessment of the interest rate risk in the total balance sheet. The proposed regulation does not consider many balance sheet characteristics that affect interest rate risk such as adjustable rate loans, liability composition, and the remaining maturities of liabilities.

Cash Held at the Federal Reserve Bank

Under the proposed rule, cash balances being held at the Federal Reserve are given a 20% risk weighting. Since the Federal Reserve has been designated as a source for emergency liquidity for the credit union industry, there appears to be little risk in holding cash balances at the Federal Reserve. Under the banking industry's Basel III, central bank reserves are deemed to be highly liquid assets during times of stress and thus carry a 0% risk weighting.

Real Estate Loans

The proposed risk weights for mortgage loans make no distinction between mortgage loans of varying maturities and repricing characteristics. For example, a 30-year fixed rate mortgage is assigned the same risk weight as a 1-year adjustable rate mortgage. The capital requirement for adjustable rate mortgages and shorter-term fixed rate mortgages should be lower to fairly take into consideration their reduced risk profiles.

Mortgage Servicing Assets

The proposed rule assigns a risk weight to mortgage servicing rights of 250%. We believe that this is excessive and would have the effect of penalizing credit unions that wish to retain a relationship with members whose mortgage loans have been sold to the secondary market. It creates less incentive to build the mortgage servicing portfolio, which can help protect a credit union's earnings in a rising rate environment.

Individual Minimum Capital Requirements

Under the proposed rule, the NCUA has the authority to require higher minimum capital requirements for individual credit unions based on additional supervisory concerns. This discretion could lead to arbitrary and uneven standards enforced by individual examiners instead of an industry-wide accepted standard. This could allow for subjective rulings effectively creating a way for amendments to the proposed rule without formal NCUA Board approval and commentary. The individual minimum capital requirements process is unacceptable and should be amended.

CUSO Investments

CUSOs were created to provide credit union members with products and services that the credit union could not provide otherwise. The proposed risk weighting of 250% for CUSO investments may cause credit unions to reconsider their current investments in CUSOs and possibly discourage future investments in new CUSO relationships that benefit credit unions and their members.

Summary

While LAPFCU supports NCUA's introduction of risk-based capital standards, we believe that several changes to the proposed rule are warranted. Strong consideration should be given to more closely aligning the risk weighting percentages for investments and loans with what the FDIC has adopted and lowering the risk weighting for CUSO investments and mortgage servicing assets. We also request that NCUA provide greater clarity surrounding the risk weights assigned to the various securities in a credit union's investment portfolio. Finally, the proposed rule's focus on identifying concentration and interest rate risks and not member needs, has the potential to override a credit union's judgment on business strategy, and leaves the credit union subject to examiner and Agency abuse by allowing for arbitrary higher minimum capital requirements.

Thank you again for the opportunity to comment on the proposed Risk Based Capital Rule and your consideration of LAPFCU's position.

Sincerely,

G. Michael Padgett
President / CEO