PYRAMID
FEDERAL CREDIT UNION
PO BOX 12100 TUCSON, AZ 85732
www.pyramidcu.com
p: 520.795.7950
f: 520.296.4147

May 28, 2014

Mr. Gerard Poliquin
Secretary, NCUA Board
1775 Duke St
Alexandria, VA 22314

Dear Mr. Poliquin,

As CEO of Pyramid FCU, I would like to comment on the new proposed Risk Based Capital standard. I feel this proposal is not in the best interests of our members. The proposal as you have published will create an undue burden on our future going forward. Pyramid FCU is a low-income, CDFI certified credit union and has been so since 2010. We are also located in Arizona which has withstood a lot of economic hardship during the last few years. Other parts of the country have been similarly impacted. I understand and agree with the NCUA Board's desire to create a requirement for a credit union's capital to be commensurate with their level of risk posed to the system. This proposal goes about it in the wrong manner. It does not address the issue of fraud in credit unions that have been examined year after year. It does not address the issue of credit unions that are concentrated in one asset type. It does not address risk poised by liabilities of credit unions nor those by credit unions with a large mark-to-market loss on investments. It does not address the issue of secondary capital which would provide a buffer to the NCUSIF, but I understand that is a matter to be discussed at a different time. It does try to micro-manage risk that all credit unions take on every day whether lending, investing or borrowing depending upon the circumstances. Your proposed rule is going to force us to explore areas of lending, investing and borrowing that we would not otherwise do. Each institution already has concentration limits and I am sure you already have "indicators" that flash warning signals when they cross a certain threshold. We already have ALCO reports detailing interest rate risk that are readily to the NCUA annually through their exam process. Why don't you use what is already out there? Just being consistent in the exam process would be very helpful and I do feel you are improving in this area over the last couple of years. Perhaps the largest risk to the system is through something the NCUA Board has recently enacted – allowing larger, complex, sophisticated credit unions to use derivatives to hedge their interest rate risk. Without the government bailout of AIG, the derivatives market would have collapsed overnight. Only chosen parties were made whole in these investments and there are many established companies no longer in existence due to the collapse of the derivatives market.

Overall, the proposal should be sent back to the drawing board and the basis for this proposal should start from scratch. Specifically, I have trouble with the following portions of the proposed rule:

PYRAMID
FEDERAL CREDIT UNION
PO BOX 12100 TUCSON, AZ 85732
www.pyramidcu.com
p: 520.795.7950
f: 520.296.4147

1. Mortgages – Credit Union mortgages traditionally outperform other secondary market mortgages. The risk weighting for all mortgages should not be higher than those of our banking counterparts (50%). In addition, the proposed rule makes no distinction based on term, rate or loan to value. All of these items are important when measuring risk in the mortgage portfolio and should receive consideration in the new rule. Many of our mortgage loans are 60% LTV or less. Why should we be penalized for making another 60% LTV mortgage? Interest rate risk measurements are already in place and manage that risk a lot better than a random percentage which is what we have here.

2. Member Business Loans – I am not certain whether or not credit union member business loans outperform "Bank" business loans. However, again, the percentages are not applied equally across the Board as treated by others in the financial service arena. If you feel a credit union with 25% of assets in Business Lending is too much, then pass a rule to that effect. No amount of capital can make up for bad lending. You have your exam processes, use it to measure your risk.

3. Investments – Where did these measures come from? Government agencies that are 100% guaranteed by the Federal Government have a requirement that is up to 10 times what is required of the banking industry. Again, each "complex" credit union should be managing their interest rate risk and each of these reports are already available to the examination staff. Why is there a need to rate these riskier? There is interest rate risk, but there is an implied government backed guaranty that helps alleviate risk. In Arizona, we have been through one of the worst times for real estate values and we have not lost one cent in our government backed agency and MBS securities. Five years ago, we should have been investing longer term and would be reaping the rewards of that today. Use the Interest Rate Risk reports and don't try to micromanage this segment. There is a good time to be longer term in your investments (when rates are falling) and there is a time to have shorter investment terms (when rates are rising). Don't take away our flexibility in managing our assets. Not sure why you risk rate overnight deposits at the FED at 20%. If they are unable to meet their obligations, we are all pretty much in trouble. You should change this to reflect reality.

4. Ability to require higher capital based upon somebody's findings (examiner, supervisor, NCUA Board, etc.). This portion really irks me to no end. Since the downturn, we have had our capital component downgraded due to – a) being located in Arizona; b) because we think your losses will be higher and we don't want to look bad if you get in trouble, c) because if I don't, my

PYRAMID
FEDERAL CREDIT UNION

PO BOX 12100 TUCSON, AZ 85732
www.pyramidcu.com
p: 520.795.7950
f: 520.296.4147

Supervisor will be upset, or my favorite, d) don't worry everyone is being downgraded. Our capital has always been around 10%. There are countless credit unions that were required by the NCUA "special examination teams" to overfund their allowance account and lower their capital. These same credit unions in Arizona have recovered millions of dollars in unnecessary ALLL funding to bolster their capital back to where it was before the great depression. Our examiner (supervisor, NCUA Board) has no business dictating what should be an accounting function. The ability to require more capital from a credit union is essentially a death sentence to them without the ability to address it through a secondary capital mechanism.

5. NCUSIF deduction – Why is this even in here? This is the fundamental core of our credit union movement, and it is totally discounted in the rule. This needs to be changed.

6. Delinquent loan treatment – Credit Unions have always been at a disadvantage when comparing delinquent loans to banks. We count ours as delinquent at 60 days and the banks count theirs as delinquent at 90 days. Credit Union losses are lower than the banks losses. If you are going to compare them, then put them on equal footing and either lower the requirement or increase the reportable delinquency definition to 90 days.

7. Only counting up to 1.25% of the Allowance for Loan Loss Account – Again, during the economic downturn in Arizona, there were credit unions that had more in their Allowance for Loan Loss Account than they had in capital. I feel you should count all of the funds in the Allowance for Loan Loss account because most of that overfunding ends back up in the income statement. Just look at what happened in Arizona.

In many measures, the new proposed Risk Based Capital Rule is more of a punishment for things that have already happened. This rule forces credit unions to take on more risk in order to make more income to satisfy the increased capital needs. As we approach the 35% threshold for mortgages, should we begin looking to make more business loans which we know very little about? There are times when having more risk on your balance sheet may be beneficial. This rule punishes you for that. We could meet all of the minimum measures in this new proposal and present significantly more risk to the insurance fund than we ever have.

I should add in closing that Pyramid FCU, like many other credit unions will have higher measures of capital across the board. It will however, force us to begin to look to new sources for income because we will no longer be able to count on traditional loans (mortgages, autos, unsecured) to meet our needs.

PYRAMID
FEDERAL CREDIT UNION
PO BOX 12100 TUCSON, AZ 85732
www.pyramidcu.com
p: 520.795.7950
f: 520.296.4147

I hope that the NCUA Board will withdraw this proposal and come back with one that will be better for our members and their capital. After all, that is who our capital belongs to.

Thank you for allowing me to submit my comments. Feel free to contact me with any questions or if you need any further assistance.

Ray Lancaster
CEO
Pyramid FCU
520 721-5099