Unitus
COMMUNITY CREDIT UNION

May 22, 2014

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

Re: *Notice of Proposed Rulemaking*
(Part 702 Risk Based Capital, RIN: 3133-AD77)

Dear Mr. Poliquin:

We appreciate the opportunity to comment on NCUA's Proposed Rule Part 702 Prompt Corrective Action - Risk Based Capital.

Unitus Community Credit Union (Credit Union) is a state-chartered, community credit union headquartered in Portland, Oregon with $933.3 million in assets and serves 84,640 members. As of December 31, 2013 our Credit Union had a net worth ratio of 9.00% and a risk based capital ratio of 12.07% making us "Well-Capitalized."

Risk based capital is a sound concept. Credit union operations, products and activities that create higher risk exposure warrant higher capital reserves. Accordingly we understand and agree with the need for NCUA to adopt reasonable changes to the current prompt corrective action (PCA) rules with updated risk based capital measurements. However, we encourage NCUA to consider changes to the Proposed Rule to identify the unique risk associated with each credit unions' operations and reasonably balance the need for higher levels of capital for higher risk exposures.

We respectfully submit the following comments (Specific & General) to NCUA to assist NCUA in modifying the proposed rule in a manner that reduces unnecessary regulatory burdens while maintaining the essential requirements for a modern risk based capital structure.

Specific Comments on Proposed Rule By Section

Risk Based Capital Ratio Measures - 702.104

We believe the Proposed Rule contains a number of risk weights that are arbitrary and do not reasonably address risk and will result in a significant burden for credit unions. We encourage NCUA to modify the Rule to reduce these burdens, as follows:

1. Federal Reserve Bank Deposits. Sec. 702.104 (c)(2)(ii) (Category 2). The Proposed Rule classifies credit union deposits in Federal Reserve Banks the same as deposits in commercial banks and other financial institutions - Category 2 assets with a 20% risk rating on such deposits. The risk related to credit union deposits in a Federal Reserve Bank are clearly distinguishable from and lower than deposits in commercial banks and other financial

institutions. We believe the 20% risk weighting is unnecessary. Due to the lack of risk, deposits in Federal Reserve Banks should be clarified or reclassified as Category 1 assets with a zero percent risk weight.

2. Real Estate Mortgage Loans. Sec. 702.104 (c)(2)(v), (vi) and (vii) (Category 5, 6, 7). Under the Proposed Rule, real estate secured loans are risk rated: Category 5 – 100%, Category 6 – 125% or Category 7 – 150% based solely on concentration. NCUA's proposed classifications are arbitrary and do not effectively measure risk of real estate loans. Real estate secured loans cannot be risk rated solely on concentration. The proposed categories ignore more relevant risk factors, such as borrower creditworthiness, collateral, lien position, term, and interest rates of different loan products. In addition, NCUA's proposed risk weights are higher, not comparable to, the same real estate secured risk weights of banks. These excessive risk weights for credit unions real estate secured loans place credit unions at a competitive disadvantage and will ultimately result in higher costs to consumers borrowing from a credit union. We urge NCUA to revise the risk categories for real estate secured loans to be comparable to banks and to reflect risk factors other than solely concentration risk.

3. Investments. Sec. 702.104 (c)(2)(vii) and (viii) (Category 7, 8). The Proposed Rule places investment assets in Categories 7 and 8, (150%/200%) using only investment maturity or duration-based tier weights. Investments have a wide range of risk depending on multiple risk factors beyond duration. However, the Proposed Rule ignores many of these more relevant factors. We believe NCUA should revise the investments risk weight classification based upon additional factors, such as the issuer of the investment, rather than solely by the duration of the investment.

4. MBLs. Sec. 702.104 (c)(2)(v), (vii) and (ix) (Category 5, 7, 9) Under the Proposed Rule, member business loans (MBLs) are risk rated from 100% to 200% depending on the concentration of MBLs in the credit union. NCUA's proposed Categories 5, 7, and 9 classifications: (i) do not reflect the true risk of the MBLs, and (ii) place an unfair burden on credit unions making low risk MBLs. MBLs cannot be risk rated solely on concentration. The proposed categories ignore the range of actual risks inherent in different MBL products, such as collateral, term, interest rates, etc.

The risk weighting for MBLs are not comparable to the same risk weighting for banks and places community credit unions at a competitive disadvantage with community banks. The credit union making a small business loan will apply the same underwriting and undertake the same risk as a bank, but due to higher capital reserve for such loans, cannot competitively price such loans.

5. CUSOs. Sec. 702.104 (c)(2)(ix) (Category 9). The Proposed Rule imposes a 250% risk rating on a credit union's investment in a CUSO. While there are many examples of CUSOs successfully serving their credit union owners, we acknowledge that some credit unions have incurred sizeable losses from riskier CUSO operations. Not all CUSO activities are risky but the Proposed Rule treats all CUSOs the same and provides no distinction

based on the risk of the activities. We believe the 250% risk weighting is excessive and unfairly penalizes non-complex CUSO activities.

We believe the 250% risk weighting should be lowered and allocated based on a two tiered weighting of: 150% and 100%, based on the risk nature of a credit union's CUSO activities. In addition strengthening the existing risk mitigation provisions in NCUA's CUSO Rule (NCUA Part 712) will be far more effective in reducing CUSO risks and losses than a high, arbitrary reserve level.

a. *Revised Risk Weighting for Complex CUSO Activities.* To address safety and soundness concerns of CUSOs, NCUA recently amended Part 712 to establish a national registry and reporting requirements for CUSO activities. Recognizing that not all CUSOs involve the same complexity or risk, NCUA established a two tier reporting structure for non-complex and complex CUSO activities. That reporting structure provides an effective method to similarly distinguish the risk capital measure for CUSO activities. Complex CUSOs present a higher risk, for which a 150% risk weighting would be appropriate. CUSOs that are not complex present far less risk, for which a 100% risk weighting is sufficient.

b. *Risk Mitigation in Part 712.* Credit unions are currently subject to numerous requirements designed to limit their liability for CUSO operations. Credit unions are subject to statutory and regulatory limits in the amount they may invest in their CUSO operations under 712.1 or applicable state law. CUSOs must be structured as limited liability entities. Over the years, NCUA has continuously revised Part 712 to add risk mitigation requirements including: (i) required written legal advice prior to a credit union's investment or a recapitalization of a CUSO, and (ii) requiring credit unions to take measures to ensure corporate separateness to limit liability. Also NCUA has extended these requirements beyond federal credit unions to all federally insured credit unions. Rather than impose inflated risk capital requirements on credit unions, NCUA would be far more effective in reducing CUSO risks and losses by strengthening or diligently enforcing the risk mitigation provisions in Part 712.

Individual Minimum Capital Requirements 702.105

In the Proposed Rule, NCUA provides for establishing individual minimum capital requirements (IMCRs) for a credit union that varies from the risk based capital requirements that would otherwise apply, based upon a series of 10 risk determinations. We recognize the need for NCUA to tailor minimum capital requirements for elevated risk conditions. However, we believe the standards for such determinations by NCUA under 702.015(c) are far too subjective and the Proposed Rule contains no checks or reasonable controls on NCUAs plenary authority to use IMCRs in an inappropriate or abusive manner. We encourage NCUA to add fair and reasonable preconditions for IMCR determinations including: authority limited to Regional Directors and not field examiners; prior notice requirements; documentation requirements for factual findings and clear rationale supporting a determination; and a reasonable appeal process for credit unions to challenge unfair or abusive IMCR determinations.

General Comments on Proposed Rule

Credit Union Risk Based Capital Not Comparable to Banks

NCUA's modernization of its risk based capital rules is necessary and appropriate in light of the Basel III standards established by the Basel Committee on Banking Supervision in "A Global Regulatory Framework for More Resilient Banking and Banking Systems." December 2010, June 2011. However, the NCUA's risk based capital rules need to be consistent with Basel III standards and comparable to the standards for banks less than $15 billion in assets. Throughout the Proposed Rule, NCUA has proposed risk weighting that differs significantly from the Basel standards without explanation or supporting information. Many of these differences arise from NCUA's inordinate focus on concentration risk. For example, the risk weights for residential mortgages, non-delinquent first mortgage loans, other real estate, MBLs, GSA significantly exceeds Basel standards and comparable requirements for banks. The lack of comparable risk based capital standards between credit unions and banks is not just a competitive imbalance; the inconsistency distorts the very framework sought by the Basel III Standards. We urge NCUA to carefully compare the risk weights between credit unions and banks and modify the rule to reach consistency.

Extended Implementation Period

Banks have been provided a period of over 29 months from the time the banking agencies issued their initial notice of proposed rule making in August 2012 to the January 1, 2015 effective date of the Regulatory Capital Interim Final Rules by the FDIC, OCC and FRB. NCUA's Proposed Rule provides for an 18 month transition implementation period following the effective date. We believe this period is unreasonably short and will result in forced, unplanned actions that may weaken, not strengthen credit union balance sheets and overall risk. Furthermore, credit unions have very limited ability to increase capital in which to avoid slipping in their capital classification. We urge NCUA to treat credit unions similarly and provide a reasonable implementation period of at least 29 months so each credit union can effectively manage the unique issues of their transition.

Supplmental Capital

NCUA stated that its primary mission for the Risk Based Capital Rule "is to ensure the safety and soundness of federally insured credit unions." NCUA also stated: "Capital helps ensure individual credit unions can continue to serve as credit intermediaries even during time of stress, thereby promoting the safety and soundness of the US credit union system." Further NCUA safety and soundness enhancements, without supplemental capital, is counterproductive and strangling the US credit union system. There are 6,763 federally insured credit unions that are shrinking rapidly because of capital constraints. NCUA has not provided any proposal for supplemental capital applicable tp credit unions other than a small group of low-income credit unions and the Proposed Rule is void of any supplemental capital initiatives necessary to truly ensure the long term safety and soundness of credit unions. We strongly urge

NCUA to take effective actions consistent with their primary mission, by exercising their authority to provide supplemental capital opportunities.

The risk based capital requirements must be reasonable and relatively uniform for the financial institutions industry. The consequences of unreasonable risk capital are significantly adverse to credit unions and their members. Unreasonable risk weights (i) discourage good lending making less credit available to good consumers, (ii) increase the cost of lending with higher rates and fees, and (iii) creates further margin compression for many credit unions.

In total, it is estimated that if implemented as proposed, the regulation would force credit unions to hold nearly $7.6 billion in additional capital. Today, credit unions have more than enough pressure to maintain current margins due to the significant competitive and market pressures on capital. For Unitus, we would see our capital shrink by approximately. $1.9M. The sum of these consequences will result in more harm to credit unions and an unfair penalty on credit union members.

Thank you for the opportunity to comment on this proposal. We appreciate the importance of these issues and the chance to contribute during this rule making process.

Sincerely,

Patricia E. Smith

Patricia E. Smith

President/CEO

TO: Gerald Poliquin, Secretary of the Board
FAX: (703) 518-6319
Phone:

From: Kris VanBeek, President/CEO
Pages: 3
Date: May 28, 2014

Re: Kris VanBeek – Comments on Proposed Rule: PCA – Risk-Based Capital

Mr. Poliquin:

Please find the attached letter with my comments on the Proposed Rule: PCA – Risk Based Capital. If you have any questions and or concerns I may be reached at (914) 881-1100 or via email at kvanbeek@usalliance.org.

Thank You
Kris VanBeek