GEORGIA CREDIT UNION
Affiliates
6705 Sugarloaf Parkway, Suite 200
Duluth, GA 30097
(770) 476-9625 • (800) 768-4282 • (770) 497-9534 (Fax)

AMERICA'S CREDIT UNIONS™

May 28, 2014

Mr. Gerald Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314–3428

RE: Comments on Proposed Rule: PCA - Risk-Based Capital; RIN 3133-AD77

Dear Mr. Poliquin,

The Georgia Credit Union League (GCUL) appreciates the opportunity to comment on the National Credit Union Administration's (NCUA) proposal regarding risk-based capital requirements. As a matter of background, GCUL is the state trade association and one member of the network of state leagues that make up the Credit Union National Association (CUNA). GCUL represents the interests of the 138 Georgia credit unions that have over 1.9 million members. This letter reflects the views of our Regulatory Response Committee, which has been appointed by the GCUL Board to provide input into proposed regulations such as this.

GCUL supports NCUA's authority to ensure the safety and soundness of both individual credit unions and the credit union system. In that effort, NCUA must ensure that credit unions maintain capital ratios and asset levels that provide for a stable insurance fund and a healthy financial structure for the credit union system. The recent financial crisis illustrated the costs of excessive leverage and poorly understood risk exposures. We appreciate NCUA for creating a draft proposal so that the credit union system could engage in productive dialogue, but we do question the need for this proposal since the current Prompt Corrective Action (PCA) provisions allow for risk based net worth calculations today.

While GCUL supports a strong credit union system, which includes supporting additional capital for credit unions with riskier balance sheets, we do have several concerns about the Risk-Based Capital proposal regarding the potential adverse impact this proposal will have on the credit union industry nationwide; as well as in Georgia. We also have concerns about the new risk weightings of certain credit union activities, and the proposed effective date for implementing any changes.

Impact in Georgia

Under the current regulations Georgia credit unions over $40 million in assets, as a whole, have $795 million in additional capital above the existing well capitalized seven percent threshold. The proposed rule would reduce that number to $716 million, a net change of almost $79 million. In Georgia, based on the December 2013 call report, at least three credit unions will be immediately impacted by this rule and will need to evaluate possible operational and member service adjustments.

In general, financial Institutions exist to assume underwriting, operations, liquidity and interest rate risk to generate return on investment for stockholders and yield for savers. Borrowers depend on finance. Knowing this, it means credit unions, must assume some risk **AND** create tailored value propositions for their members…especially for people of 'modest means' and in the last few years an increasing number of small businesses. NCUA must be careful not to create the conditions for excessive risk avoidance.

This proposal, as drafted, will likely impact more Georgia credit unions in the future as their services and lending portfolios respond to member needs.. Georgia has many small credit unions that are already devoting a significant proportion of resources to meet changing regulatory requirements. Small credit unions in Georgia continue to merge at an alarming rate. Implementing this proposal will force Georgia credit unions with less than $50 million in assets to consider whether growth is financially feasible due to the significant cost and restrictions placed on credit unions over the $50 million threshold. We are concerned that the proposal will lead to more credit unions evaluating whether merging with another credit union is a more viable option or whether it is preferable to review other charter options.

During the great recession, most credit unions maintained a well-capitalized position. At the end of the fourth quarter, Georgia credit unions had an aggregated net worth of 11.6 percent and had delinquency and net charge off levels of .81 percent and .61 percent, respectively. Credit unions in Georgia are conscientious about properly weighting the risks of their balance sheet under the existing regulations and ensuring adequate capital. <u>The risk weightings and additional capital requirements in this proposal will not serve to increase the protection to the credit union system but instead restrict growth and impact member services.</u>

One major concern with the proposal, as drafted, is that credit union boards and field examiners will embrace perspectives that amplify the 'extra' capital set-asides… thereby causing management to seek safety in the 'sanctuary zones' of asset allocations…a recipe for competitive mediocrity.

Lack of Justification for the Proposed Risk Weights

GCUL is concerned about the risk weighting categories as proposed. Due to the lack of justification in the proposal, the risk weights appear to be excessive and arbitrary. Many of the risk weights do not accurately reflect risk and the weightings do not account for the individual management strength of the credit unions and the areas in which credit unions and/or investments have a history of proven success. It seems that the proposal "rewards" credit unions that stick to basic consumer lending. Increasingly, members need mortgage-secured and business-purpose loans, which are heavily penalized.

Credit unions are trying to increase the member business loan cap to allow for future growth and sustainability of the credit union system and to provide a meaningful opportunity for small businesses to access credit. The risk weightings associated with member business loans will undermine those efforts and restrict small business loan growth in Georgia communities.

For some risk categories, the weighting is the same for all loans or investments in that area… that weighting leads us to believe that the categories are over generalized. One example is where the proposal includes both unsecured and secure loans… secure loans carry less risk and should be assigned a lower risk than unsecured loans.

There is a strong disincentive for investments in CUSOs, despite the fact that most CUSO activities diversify risk and provide for improved efficiencies for credit unions. In the proposal, all CUSO investments are treated the same regardless of the type of CUSO or the financial strength of the CUSO. CUSO investments should not be discouraged by capital weightings, as they are already limited to 1% of assets, an exceptionally conservative level. It is possible that credit unions will look to divest their interests in CUSO's, or severely curtail their ownership if high capital charges are applied. We are concerned that this feature will reduce opportunities for credit union growth and may reduce services offered to credit union members.

The proposed risk weights for long-term investments does not take into account applicable credit or asset liability management practices. It only bluntly discourages long term assets. As mentioned in the proposal, changes to the risk-based capital requirements are intended to address credit risk, interest rate risk, concentration risk, liquidity risk, operational risk and market risk. A risk weighting system based entirely on the initial life of an investment or a loan cannot accomplish these objectives. NCUA's current regulations provide sufficient regulatory guidance for supporting in-field assessment of risk.

In many areas, the risk weighting is more punitive than that for community banks or under BASEL III standards. Off balance sheet servicing portfolios should not be exposed to bank-like capital treatment without NCUA demonstrating potential risk exposure.

Additionally, GCUL encourages the NCUA to reconsider the exclusion of the one percent deposit each credit union makes to the National Credit Union Share Insurance Fund (NCUSIF) in the risk-based capital ratio calculation. Excluding the deposit inappropriately lowers a credit union's risk-based capital position. A credit union's deposit in the NCUSIF is an asset under GAAP. Most importantly, it is an asset of significant value to a credit union as it represents the presence of federal deposit insurance and should be included in a risk-based capital ratio calculation.

Individual Determination of Additional Capital

Under the proposal, NCUA has the authority on a case-by-case basis to increase the amount of capital a credit union is required to maintain. That is being interpreted that even if a credit union is in compliance with the rules, NCUA could require more capital. This authority is troubling, especially considering how the credit union system weathered the financial crisis. We would submit that NCUA already has tools to help manage credit union safety and soundness concerns through DOR and Cease and Desist enforcement and this additional power is not needed.

Consistency with Banks

NCUA states that it intends to make the credit union risk-based capital measure more consistent with the measures used for banks. If Congress intended credit unions to be subject to the same requirements as the banks, we believe they would have said so when H.R. 1151 was passed in 1998. In fact, in most loan categories, credit unions have significantly lower delinquencies and loss experience.

NCUA's approach of trying to bring consistency between the bank PCA and credit union PCA fails to take into account the unique aspects of credit unions, including the credit union system's inability to raise supplemental capital. Credit unions exist to improve the well-being of their members. To the extent that RBC rules disadvantage credit unions relative to bank RBC rules, credit unions could have trouble meeting the service needs of their members.

Effective Date

The proposed risk-based capital requirements are a significant departure from existing practice. The reluctance of NCUA to extend the comment period is difficult to understand, since the implications of an RBC proposal are not easy to project into a credit union's future. While most credit unions 'clear' the 10.5% well-capitalized threshold today many need time to contemplate how RBC rules would affect their operations five or ten years into the future.

Credit unions do not have the same ability as other financial institutions to raise capital. Under this proposal, several Georgia credit unions will be faced with the challenge of reducing certain products, increasing interest rates, and/or reducing dividends in order to quickly achieve the new capital requirements. An 18-month implementation period could require Georgia credit unions to make drastic cuts to member services - or increase fees and loan rates - than would otherwise be necessary with a longer implementation period. In addition, the 18-month implementation timetable stands in stark contrast to the 9-year implementation plan for banks to comply with Basel III. Circumstances do not appear to warrant rapid embracement of an RBC proposal for credit unions

Summary

Georgia credit unions have a commitment to their continued success and sustainability. Credit unions across the state have already invested significant resources to establish a strategic direction. Any change to the current prompt corrective action requirements would require the credit union to spend additional time and resources to adjust their strategic plans. GCUL is requesting additional time for credit unions to reconvene their management teams and Boards of Directors to determine necessary adjustments to their model as well as additional time to implement changes and build any additional required capital in a manner that mitigates the impact on members.

GCUL encourages NCUA to reconsider the proposed rule to account for the responsible management of Georgia credit unions to assess risks based on their individual situation.

If the RBC rules should be employed, they should be focused around 'adequately capitalized' levels…ie: 8%. There should be no 'well-capitalized' risk-based capital threshold. The credit union leverage ratio should be emphasized and the examination process should focus on tailored risk assessments built around an individual credit union's circumstances. In addition, asset risk weightings should not 'escalate' with greater concentrations because NCUA already has the ability to lean against concentration in the exam process.

Credit unions have built substantial capital 'cushions' (above minimum requirements)…the RBC proposal could lead to a long period of unnecessary capital building if credit unions attempt to build the same cushion 'above' RBC thresholds. It would require that over $7 billion be withdrawn from new service investment in the foreseeable future:

- Higher capital thresholds (ie: 10.5% RBC) could lead to slower growth potential, a competitive disadvantage and a significant member value issue.
- The (statutory) limitations for paid-in forms of capital already create some competitive disadvantage. The inability to count supplementary capital in RBC calculations would be difficult to understand.

GCUL asks that the NCUA consider the needs of Georgia communities and the important role the credit union system plays in our state when evaluating risk-based capital regulations. GCUL appreciates the opportunity to present comments on behalf of Georgia's credit unions. Thank you for your consideration. If you have questions about our comments, please contact either Selina Gambrell or Cindy Connelly at (770) 476-9625.

Respectfully submitted,

Cindy Connelly

Cynthia A. Connelly

Sr. VP/ Government Influence