ICBA
INDEPENDENT COMMUNITY BANKERS of AMERICA®

May 28, 2014

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

Re: Prompt Corrective Action—Risk Based Capital

Dear Ms. Murphy:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the NCUA's proposal to amend the NCUA's current prompt correction action rules for federally insured credit unions by introducing risk-based capital requirements for "complex" credit unions. Under the proposal, credit unions with more than $50,000,000 in total assets would be considered "complex" and would be subject to risk-based capital standards similar to Basel III in addition to existing net worth requirements.

As the proposed rule explains, the National Credit Union Share Insurance Fund experienced several hundred millions of dollars in losses due to failures of individual credit unions holding inadequate levels of capital relative to the levels of risk associated with their assets and operations. According to the NCUA, "examiners did warn officials at those credit unions that they needed to hold higher levels of capital to offset the risks in their portfolios, but the credit union officials ignored the examiners' recommendations."

The purpose of the proposal is to incorporate the lessons learned from those failures and better account for risks not addressed by the current net worth requirements. As Chairman Debbie Matz explained at a recent credit union conference, "the current one-size-fits-all net worth requirement of 7% is outdated and insufficient…and does not belong in the ever-growing, increasingly complex credit union industry."

[1] *The Independent Community Bankers of America®, the nation's voice for nearly 7,000 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services.*

ICBA members represent more than 24,000 locations nationwide and employ more than 300,000 Americans, ICBA members hold more than $1.2 trillion in assets, $1 trillion in deposits, and $750 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

ICBA's Comments

We commend the NCUA for incorporating risk-based capital standards into its current prompt corrective action (PCA) requirements and agree that these new requirements will enhance the ability of a credit union to cope with a capital impairment during economic downturns. **We also commend the NCUA for recognizing that the main reason the NCUSIF sustained such high losses from failed credit unions during the past five years was because of high concentrations of Member Business Loans (MBLs) at those failed institutions. This fact alone is sufficient reason for Congress not to raise the current restriction on MBLs of 12.25% of total assets and why the NCUA should be more restrictive concerning its standards for granting MBL exemptions from the 12.25% restriction.**

Since tax favored federal credit unions have such a significant competitive advantage over community banks because their net income is tax-free, ICBA believes that capital standards for both institutions should at least be comparable so that the two institutions can compete on a level playing field. **Unfortunately, the NCUA's proposed risk-based capital standard, if adopted, would not be comparable to Basel III—the capital standard recently adopted by the banking agencies to apply to banks and bank holding companies beginning in 2015--and therefore would not create a level playing field.** The proposal is not comparable to Basel III for several reasons.

First, the proposal would only subject "complex" credit unions to risk-based capital standards. This would mean that only one third, or about 2,200 federally insured credit unions, would come under the new standards. This is much different coverage than under the Basel III standards which cover all FDIC-insured financial institutions, no matter how small.

Second, although the NCUA's proposal is similar to Basel III, it varies significantly in many respects from Basel III and in ways that significantly benefit credit unions. For instance, the proposed risk weight for consumer loans made by credit unions would be set at 75% as opposed to 100% for community banks under Basel III. Consumer loans would not only include unsecured loans and lines of credit to consumers, but also unsecured credit cards loans, new vehicle loans, used vehicle loans, and leases receivable. Since credit unions vigorously compete with community banks for consumer loans particularly for new vehicle loans, the lower risk weight gives them a significant competitive advantage.

Furthermore, under the proposal, while member business loans or MBLs with concentrations of less than 15% of assets would carry a 100% risk weight, there is no higher risk weight (i.e., 150%) for high volatility commercial real estate loans as there is under Basel III. Under the proposal, credit unions that have been granted exemptions from the statutory 12.25% of total assets threshold would have higher risk weights for their MBLs, but only if the MBL concentrations at the credit union exceeded 15% of total assets. (In ICBA's opinion, NCUA waivers from the 12.25% threshold should be severely curtailed if not eliminated. This would eliminate the need for higher risk weights (i.e., 150% and 200%) for MBLs that exceeded the statutory threshold concentration of 12.25%.) In any case, the fact that credit unions can make high volatility commercial real estate loans with a 100% risk weight gives them an additional competitive advantage over community banks.

With respect to equity investments and in particular equities not publicly traded, the NCUA proposal is to risk weight CUSO equity investments at 250% and investments in corporate credit union capital at 200% whereas, under Basel III, these investments would be risk weighted at 400% for community banks. The explanation-- these investments do not warrant higher risk weights—is unconvincing given the fact that many failed credit unions had these types of investments. In any case, this is another example where the NCUA proposal and Basel III are not comparable.

Under Basel III, community banks will be subject to three risk-based capital ratios, including one that essentially allows only common equity to be included in the numerator. However, under NCUA's proposal, complex credit unions would only be subject to one risk-based capital ratio and the numerator of that capital ratio would include all sorts of capital elements including "appropriation for non-conforming investments," "secondary capital accounts," and "Section 208 assistance included in net worth." While the proposed NCUA capital ratio is roughly comparable to the total risk-based capital ratio for banks, there still is no explanation in the proposal as to why the NCUA omitted a stricter capital ratio comparable to the common-equity tier one ratio that community banks must comply with.

In short, NCUA risk-based capital proposal would only serve to perpetuate the current un-level playing field which community banks and credit unions compete in. To achieve comparability, the NCUA should extend this proposal to at least two-thirds of its regulated institutions and should increase the risk weights for consumer loans, MBLs and equity investments and implement an additional risk-based capital ratio comparable to common equity tier one ratio that would include only retained earnings. Otherwise, credit unions will not only remain tax-advantaged, but capital-advantaged.

ICBA appreciates the opportunity to comment on the NCUA's proposal to amend its current prompt correction action rules by introducing risk-based capital requirements. If you have any questions or would like additional information, please do not hesitate to contact me by email at Chris.Cole@icba.org or by phone at (202) 659-8111.

Sincerely,
/s/ Christopher Cole

Christopher Cole
Senior Vice President and Senior Regulatory Counsel