From:	Michael Woods
To:	_Regulatory Comments
Subject:	Northern FCU - Comment Letter to NCUA re: RBC 2nd proposal.
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CREDIT UNION

April 16, 2015

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

Risk-Based Capital, 80 FR 4340-01

Dear Mr. Poliquin:

As the Chairman of the Board of Directors and as the CEO of Northern FCU, Watertown, NY, we are writing this letter in response to NCUA's second Risk-Based Capital (RBC2) proposal. These past 15 months have seen the Credit Union industry waste time and resources that should be spent serving our members, defending the principles of the Cooperative nature of this industry in response to the RBC proposal. This industry weathered the destruction of lives caused by the Great Recession. Indeed, we maintain our belief that the proposal is a solution in search of a problem. We believe that the RBC rule will increase cost to members, expand the right of the NCUA to interfere in the governance of credit unions through Prompt Corrective Action, and threaten the financial stability of the industry in the long term.

In fact, we do not believe that the NCUA has the legal authority to adopt these proposed regulations. Even within your own Board, there is serious doubt expressed as to your attempt to implement a two-tiered RBNW framework. As noted by several commentators and by your own Board member, this proposal is contrary to the NCUA's past interpretation of its powers. The plain language of the statue contradicts the NCUA's interpretation. Both the definition as written and the numerous letters you have received from lawmakers in both houses of Congress, who actually debated and passed the current RBNW regulations and clearly delineates its intent, should tell you that you are overreaching. We maintain that the RBC proposal is illegal and will be subject to redress through the Court system should you persist. The NCUA should look at the statistics and study performed and shared about failed Credit Unions that show that their proposed solution (RBC) would not have detected nor prevented these failures. The NCUA should address and settle all of these concerns prior to the issuance of a new and final RBC regulation.

In this revised proposal, NCUA has decided not to address interest rate risk within the RBC framework. As a result, many of the most objectionable aspects of its RBC framework have been removed. Nevertheless, NCUA is planning on coupling whatever RBC rules it adopts with additional IRR guidance. We do not believe there needs to be a new rule on interest rate risk. The FFIEC 2010 Advisory on Interest Rate Risk Management, to which the NCUA was a signatory, provides sound practices for interest risk management. The FFIEC Advisory, along with subsequent regulatory responses to questions regarding the Advisory, provide all financial institutions with sufficient guidance on managing interest rate risk. It also provides regulators with sufficient guidance for examining interest risk management. You cannot assess interest rate risk through the Call Report. Any attempt to do so will create additional regulatory burden and cost and will fail.

FFIEC Advisory calls for a dynamic modeling measuring a range of outcomes legitimately reviewed. Anything that would be attempted through the Call Report would be single point in time measure and therefore wrong.

We recommend the NCUA follow the FFIEC guidance and address interest rate risk through the exam process. The NCUA does not follow its own guidance as promulgated through FFIEC. Nowhere in the FFIEC guidance are there requirements for "instant and permanent" rate shock testing. Yet, this unrealistic rate environment is the benchmark that NCUA examiners require us to measure and orient our Policy around. We ask that the NCUA evaluate itself and follow its own rules with respect to interest rate risk examination. There is no need for anything new; there is strong need for the NCUA to get in line with the other Financial Institution regulators, all signatory to the FFIEC Advisory. In addition, examiners need adequate training so that they can assess a credit union's IRR in a fair and legitimate manor

In the preamble accompanying this proposal, NCUA claims that it needs "broader provisions" to mandate that individual credit unions "maintain capital commensurate with the level in nature of the risk to which a credit union is exposed." This language is entirely too broad, since it implies that individual examiners could impose individualized capital requirements for even well-capitalized credit unions. So long as credit unions comply with codified regulatory requirements and continue to demonstrate that they appropriately manage their institutions, regulators should not be able to substitute their judgments for that of the credit union's management. This is particularly true when the issues are as important as how best to allocate credit union assets.

If NCUA continues to insist that it has the power to impose credit union specific buffers, then the final rule should provide guidance explaining the criteria that will be used in determining which credit unions will be subject to increased buffer requirements and guidance as to how impacted credit unions can demonstrate that enhanced buffers are no longer required.

An alternative approach to assessing the riskiness of a credit union's capital allocation should be used. Instead of emphasizing numeric targets, credit unions should be empowered to decide if the risks they are taking are appropriate or require additional capital. Credit unions would have this flexibility if they utilize scenario-based stress testing. This option would encourage credit unions to consider a broad range of possible outcomes. NCUA has the authority to question a credit union's allocation decisions but it should not base these decisions on a simplistic line-in-the-sand approach that encourages credit unions to strive to adhere to regulatory targets without any regard for the quality of a credit union's decision making process.

While we still maintain that the RBC proposal as written is not legal or warranted, in addition to our recommendations above, we offer the following list of items that we believe still need to be addressed with respect to RBC.

1. Off Balance Sheet – We believe that the Overdraft Privilege (Courtesy Pay) liability should not be included as an Off Balance Sheet risk requiring capital support. While we enumerate a theoretical limit for each member who has opted into the program, as the industry knows, and the NCUA should know, utilization is really among a very small numbers of members. We routinely have an insignificant amount of outstanding draws, typically about 1.00% on average monthly. The amount we are required to capitalize is over $12,600,000. The Credit Conversion factor requires us to capitalize nearly $1.26 million and resulting in additional $126,000+ in Capital. The draws are short term in nature, and are totally at the Credit Union's discretion. We have the option to not honor any items at any time. The relevant factors are that the ODP limits have low utilization, and they are variable "limits" that are reset daily. These should be excluded from the Off Balance Sheet Capital Requirement.

2. We are pleased that the NCUA has reduced the Risk Capital category for FHLB advances from 100% to 20% which is in line with other financial regulators. Given this change, it should only follow that the NCUA should allow FHLB advances to be used as Contingency Liquidity in our Contingent Liquidity Plans.

3. We do not agree with your move of unsecured consumer loan risk weights up to 100%. We should be at parity with Banks. This move specifically is harmful to smaller Credit Unions where there will naturally be a higher concentration of these loans due to their smaller total asset size. Sound credit and loan policy and proper ALLL methodology, and pricing policy, all mitigate the additional credit risk associated with these types of loans. There is no need for this risk weighting to be any different than it is for Banks.

4. We believe that the RBC2 still double counts risk through its risk weighting schemes. Bank regulations do not impose concentration limits on mortgages. Banks can carry higher levels of mortgage assets as long as they have the capital to cover them in stress testing. Credit Unions should have the same right without imposition of concentration limits through the risk weighting categories. We ask the NCUA to reduce the risk weighting factor for 1st mortgages > 35% of Assets, and all Junior Lien mortgages to comparable weights allowed for banks. The original and revised RBC proposals unnecessarily put credit unions at a competitive disadvantage to banks.

We support NCUA's decision to raise the complex credit union threshold to $100 million. However, asset size alone does not make a credit union complex. Instead, a credit union should only be considered complex if it has at least $100 million in assets and engages in a combination of the following activities listed in the preamble to this proposal: member business loans, indirect loans, real estate loans, non-federally guaranteed student loans, investments with maturities greater than five years (where the investments are greater than one percent of total assets), non-agency mortgage-backed securities, non-mortgage-related securities with embedded options, collateralized mortgage obligations/real estate mortgage investment conduits, commercial mortgage-related securities, repurchase transactions, and derivatives.

NCUA's RBC framework remains a work in progress. Right now, credit unions still don't know the answer to crucial questions such as how will IRR is assessed? Will credit unions be given the flexibility they need to allocate resources in the way that best reflects the needs of their members? And, will examiners be given the training they need to judge a credit union's allocation decisions? No RBC framework should be finalized until NCUA answers these critical questions.

Sincerely,

Daniel St. Hilaire, CEO *Gary Rowe, CPA, Chairman*

Daniel St. Hilaire, President/CEO
Northern FCU

Gary Rowe, CPA, Chairman of Board
Northern FCU

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