SECURITY SERVICE
FEDERAL CREDIT UNION

April 16, 2015

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

Subject: Comments on Proposed Rule: Risk-Based Capital

Dear Mr. Poliquin:

Security Service Federal Credit Union (SSFCU) has reviewed the subject proposed rule, and respectfully offers our comments for the agency's consideration. As we indicated previously, NCUA's focus on assuring Capital Adequacy in individual credit unions and the credit union system as a whole is appropriate and commendable; and we agree that an improved risk-based capital regime is necessary for the safety and soundness of the credit union movement, as well as to assure a strong and healthy National Credit Union Insurance Fund (NCUSIF).

Clearly, NCUA has diligently reviewed and considered our and other constituents' comments, as the revised proposed rule incorporates significant and meaningful changes to the initial proposed rule; however, certain parts of the rule continue to lack sufficient supporting rationale and/or unnecessarily place credit unions at competitive disadvantages to banks. Consequently, we do support the revised proposed rule, but offer and discuss areas where we respectfully request alternative regulatory approaches.

Secondary Capital

Considering the rigorous capital adequacy scheme of the proposed Risk-Based Capital rule and its potential impact on the credit union business model, balance sheet structures, and growth; it is imperative that the NCUA move quickly to achieve secondary capital authority for credit unions. Credit unions steadfastly support such action, as we have for many years, and we respectfully ask the NCUA to make secondary capital authority an agency priority for 2015 and beyond.

Section-By-Section Analysis

First Lien Residential Mortgage Loan Risk Weights – We do not believe that sufficient quantitative support or other rationale exists for the proposed rule's risk weighting scheme for first lien residential mortgage loans. While we recognize that mortgage lending contributed to the failure of 27 credit unions between January 1, 2008, and June 30, 2011 (as noted in the Federal Register), we do not agree that this number is material or even significant, given the large number of federally insured credit unions that engage in mortgage lending activities. Considering the residential real estate meltdown experienced in most of the United States, having only 27 failures caused in whole or in part by residential real estate lending activities is a testament to movement-wide strong loan underwriting and loss mitigation.

Security Service FCU underwrites all first lien residential mortgage loans to secondary market standards, which require a loan-to-value ratio (LTV) of 80% or less, or a requirement for private mortgage insurance. Unless NCUA's post-mortem analyses and material loss reports suggest that loan underwriting in the 27 credit unions was safe, sound, and otherwise consistent with secondary market standards, we do not believe NCUA can draw accurate conclusions about concentration risks in credit unions system-wide.

The proposed rule creates a competitive disadvantage for credit unions when compared to bank capital adequacy requirements, as the FDIC rule weights all first lien mortgages at 50%. NCUA's rule contains a two-tier scheme where only concentrations below 35% of credit union assets are assigned the 50% risk weight, and concentrations of 35% and greater are weighted 75%. Thus, credit union capital requirements are higher than banks where sufficient distinction between the lending activities of the two types of financial institutions simply does not exist.

Instead of the two-tiered weighting approach proposed in the rule, we respectfully suggest that the FDIC 50% single-tier risk weight on all first lien residential real estate loans is more reasonable, equitable, and appropriate.

Alternatively, if, after reconsidering this matter, NCUA decides to retain the two-tiered approach, we respectfully suggest the second-tier concentration threshold be increased from 35% to 50%, thus representing a more reasonable and material asset concentration.

Junior Lien Real Estate Loans – Similar to our comments regarding first lien mortgages, we do not agree with the risk weights for junior lien real estate loans, as sufficient support does not exist for the two-tier risk weighting scheme nor for the 20% second-tier threshold proposed (should NCUA retain the two-tiered approach).

Additionally, this one-size-fits-all approach fails to take into account home equity lending activities where LTV's are appropriately limited at origination. This is especially relevant in Texas-based credit unions, where a total LTV (inclusive of first lien balances) exceeding 80% on home equity loans is prohibited by state law.

Consequently, on junior lien loans that had total LTV's of 80% or less at origination, the risks related to dramatic and sustained swings in real estate values and elevated defaults are significantly mitigated, regardless of whether or not a first lien loan balance exists. Simply stated, this practice is front-end built-in loss protection that causes collateral exposures to equal those of first lien mortgages, and as such, does not deserve a risk weight that differs from the first lien weighting approach. Thus, we respectfully suggest revisions to the proposed rule that appropriately recognize sound home equity lending practices described above, more specifically to treat the resulting home equity loan with the same risk weights as first mortgage loans in situations where a prudent total LTV is considered at underwriting.

When compared to the capital requirements for banks, the proposed rule again creates a competitive disadvantage, as the bank rule weights all junior liens at 100%. NCUA's rule weights junior lien loan concentrations below 20% of assets at 100%, but all junior lien balances at or exceeding 20% of assets at 150%. Thus, credit union capital requirements are higher than banks where sufficient distinction between the lending activities of the two types of financial institutions does not exist.

Instead of the two-tiered weighting approach proposed in the rule, we respectfully suggest that the FDIC 100% single-tier risk weight on all junior lien residential real estate loans is more reasonable, equitable, and appropriate.

Alternatively, if, after reconsidering this matter, NCUA decides to retain the two-tiered approach, we respectfully suggest the second-tier concentration threshold be increased from 20% to 50%, thus representing a more reasonable and material asset concentration.

Credit Union Service Organization Risk Weight – Given the essential role of CUSO's in the operation of credit unions, revisions made to the second proposed rule that ease the capital requirements related to CUSO investments are appropriate. While some differences exist between the credit union rule and the bank rule, the simplicity of the credit rule is arguably a reasonable tradeoff that facilitates comparability to the bank rule; however, with one exception.

The bank rule considers the concentration of similar investments by defining a threshold below which the risk weight is 100%. Referred to in the bank rule as "non-significant" investments, total bank investments in CUSO equivalents that are 10% or less of total capital are weighted 100%. In the same fashion as the proposed rule's approach to risk weighting other asset classes to consider concentrations, and in a manner consistent with the FDIC's recognition of "non-significant" concentrations of such investments, we respectfully suggest revisions to the proposed rule to add "non-significant" investment treatment, so that only total investments in non-consolidated CUSO's exceeding 10% of total capital would be subject to any tiered risk weighting scheme.

Conclusion

We agree that an improved risk-based capital regime is necessary for the safety and soundness of the credit union movement, as well as to assure the strength and stability of the NCUSIF; and we recognize and appreciate the NCUA's efforts to assure an effective risk based capital rule that appropriately reflects material risk exposures while avoiding unnecessary regulatory impacts on credit unions.

Compared to banks, significant competitive disadvantages would be imposed by the proposed rule, negatively impacting mortgage lending and CUSO investments that often facilitate the overall delivery of valuable products and services to members. Furthermore, the lack of secondary capital authority continues to cause natural person credit unions to rely exclusively on retained earnings to meet capital adequacy requirements, thus significantly limiting growth of individual credit unions and the movement as a whole.

Security Service Federal Credit Union supports NCUA's efforts to improve the risk-based capital regime for credit unions, and appreciates the agency's efforts to work with credit unions to assure the safety and soundness of the credit union system through reasonable and thoughtful regulation, while maintaining the value of the credit union charter. If you have any questions or would like to discuss any aspect of the proposed rule, please contact Executive Vice President, Chief Risk Officer Howard Baker; or me at your convenience.

Sincerely,

JIM LAFFOON
President & CEO

cc: Dan Berger, President & CEO
National Association of Federal Credit Unions

Jim Nussle, President & CEO
Credit Union National Association

Dick Ensweiler, CEO
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