April 23, 2015

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

Re: National Credit Union Administration Risk-Based Capital

Dear Ladies and Gentlemen:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the National Credit Union Administration (NCUA) proposal, *Risk-Based Capital*. ICBA is encouraged by the NCUA's second proposal on regulatory capital for credit unions and appreciates the recognition made by the NCUA that a credit union regulatory capital framework should shift toward a model implemented by the federal banking regulators for all banks in the United States. The community bank regulatory capital requirements imposed under Basel III are not optimal and should be amended to reflect the high quality nature of community bank lending across the nation. ICBA continues to recommend changes to the Basel III framework as it is applied to community banks and is currently working with bank regulators to improve the model. However, ICBA believes that credit union regulatory capital requirements should be no less strenuous than the regulatory capital requirements of community banks in the United States.

NCUA should adopt the Basel III model already adopted by prudential banking regulators and currently being incorporated into the capital frameworks of community banks of all sizes and charter types. Credit unions should be required to face the same capital requirements as banks regardless of asset size or membership base. Without comparable capital requirements for credit unions and community banks, credit unions will be undercapitalized relative to community banks. This

[1] The Independent Community Bankers of America®, the nation's voice for more than 6,000 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.

With 52,000 locations nationwide, community banks employ 700,000 Americans, hold $3.6 trillion in assets, $2.9 trillion in deposits, and $2.4 trillion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

undercapitalization risk, along with the inability of credit unions to raise capital when needed, increase the bailout risk faced by the American taxpayer.

The Proposal

The NCUA originally proposed amending credit union regulatory capital requirements to make them more comparable to bank capital regulations. With the adoption of Basel III by community banks, credit union minimum net worth requirements and outdated risk-based capital requirements quickly became insufficient thereby driving the need to enhance the capital framework to ensure that capital levels are appropriate considering the financial strain faced by credit unions during the recent financial crisis. The original proposal introduced a new risk-based capital measure that was more closely aligned with the risk-based capital requirements for banks in order to increase comparability among all types of federally insured financial institutions. Risk weights on first lien residential real estate loans would have been effectively decreased while risk weights on second lien residential real estate loans, consumer loans, and member business loans would have been effectively increased. The original proposal called for a minimum total risk-based capital ratio level for applicable complex credit unions of 10.5% to be considered well capitalized and 8.0% to be considered adequately capitalized. The minimum asset level for defining complex credit unions, or those that would be subject to risk-based capital requirements was set at $50 million under the original proposal.

Under this revised second proposal, the minimum asset level for defining complex credit unions that would be subject to risk-based capital requirements has doubled to $100 million. Additionally, the phase-in period for applying the proposed NCUA capital requirements would extend to January 1, 2019. In a dramatic shift away from Basel III, NCUA is proposing to allow the inclusion of the allowance for loan and lease losses in its entirety in regulatory capital without the cap currently required for community banks under Basel III of 1.25% of assets. Certain risk weights have been modified to attempt to capture the impact of concentration risk on credit union capital. The end result is a tiered risk weight system based on asset class concentration for those credit unions subject to risk-based capital requirements. NCUA has dropped 50 basis points from the well-capitalized level for risk-based capital ratios by reducing the minimum total risk-based capital ratio level for applicable credit unions to 10.0%.

ICBA's Comments

ICBA is encouraged by the NCUA's attempt to better align the minimum regulatory capital requirements for credit unions with those faced by the nation's community banks, who operate at a great disadvantage to credit unions because they are required to pay federal income taxes on earnings, which for many banks is also the foundation for building elevated levels of high quality loss-absorbing capital. Because credit unions can retain more earnings than community banks, they should have little or no difficulty in maintaining very high levels of tier 1 capital. However, the NCUA has not fully adopted Basel III for credit unions. In fact, the proposal provides many opportunities for credit unions of all sizes to avoid holding the regulatory capital needed to weather the next

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economic storm as suggested in the Basel III capital framework. With increased risk to the U.S. taxpayer, as well as risks to its members and employees, credit unions should be holding regulatory capital well in excess of the regulatory minimums that community banks are subjected to. The ability to avoid paying federal income taxes on earnings makes achieving elevated levels of high-quality capital much easier than for other financial institutions that are subject to federal income taxation, resulting in an uneven competitive playing field between community banks and credit unions.

ICBA notes that the NCUA has decided not to subject credit unions to the capital conservation buffer, which for community banks effectively places a minimum threshold on common equity of 7.0% and total regulatory capital of 10.5% when calculating minimum risk-based capital. Once community banks fall below these thresholds, they are severely restricted from paying distributions to shareholders and certain executive bonuses. Additionally, NCUA has reduced the level required for complex credit unions to be considered well capitalized from 10.5% to 10.0% for risk-based capital. Complex credit unions can be considered adequately capitalized at 8.0%. One must wonder how an institution such as a credit union, with its ability to avoid the payment of U.S. income taxes on income and retain all earnings, could be allowed to pose an elevated risk to the financial system and the U.S. taxpayer while managing the same risk profile as a community bank that is subject to taxation and is much better capitalized. As the asset size of the country's largest credit unions has grown rapidly, these institutions are in danger of presenting new risks to the financial system in the United States that will be extremely difficult to mitigate by these institutions and regulatory authorities in the next financial crisis without elevated levels of high quality minimum regulatory capital requirements.

In addition to these troubling developments, ICBA is surprised to learn that NCUA is proposing that credit unions below $100 million in total assets will not be considered complex under this new capital framework, up from the current level of $50 million. As a result, these credit unions will not be subject to the minimum risk-based capital ratio levels required for credit unions above this amount. Again, with credit unions exiting an extreme financial crisis where many of these institutions failed due to lack of high-quality capital and elevated risk profiles, the NCUA should be focusing its attention on raising the minimum regulatory capital levels for all credit unions. The domestic financial system and the U.S. taxpayer should not be subjected to increased risk from credit unions.

In order for the nation's credit unions to operate at a safe level of credit risk and to level the competitive landscape between credit unions and community banks, the NCUA should adopt the Basel III regulatory capital model already adopted by prudential banking regulators for community banks. At a minimum, all credit unions should be subject to the risk-based capital requirements proposed for complex credit unions and the proposed threshold for total capital should be raised to 10.5%. This level will bring credit unions on par with community banks. Additionally, ICBA recommends that the NCUA institute a capital surcharge of 5% to be applied to credit unions when they exceed total consolidated assets of $10 billion. These large credit unions, with their limited ability to

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react to depleted capital levels in times of economic uncertainty, should be subjected to increased scrutiny and additional capital reserves once they reach the $10 billion ceiling.

ICBA appreciates the opportunity to comment on this proposal. If you have any questions or would like additional information, please do not hesitate to contact me at james.kendrick@icba.org or (202) 659-8111.

Sincerely,

/s/

James Kendrick
Vice President, Accounting & Capital Policy