

# State Employees' Credit Union



Accounting Department

April 22, 2015

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

Re: Comments on Proposed Rulemaking—Risk Based Capital—Second Proposal

Dear Mr. Poliquin,

We appreciate the opportunity to provide comments on the National Credit Union Administration's Notice of Proposed Rulemaking governing Risk Based Capital as re-proposed on January 27, 2015. State Employees' Credit Union (SECU) has provided consumer financial services to North Carolina state employees and teachers and their families since 1937. Services are provided to nearly 2 million members through 254 branches, 1,100 ATMs, 24/7 Contact Centers, a voice response service and an interactive website.

## **General Comments**

We recognize and appreciate that many adjustments were made to improve the initial Risk Based Capital proposal. However, we believe the new proposal is seriously flawed and if implemented as proposed will place credit unions at a significant competitive disadvantage with banks and other financial service providers in the marketplace which have lower capital requirements for certain assets.

The higher capital requirements for credit unions will put credit unions in a non-competitive position. The additional burdens imposed by higher capital requirements for credit unions will erode the future viability of credits unions which operate in highly competitive and changing environments. This competitive disadvantage will be borne by our members in the form of higher interest rates on loans, lower interest rates on deposits and higher fees for services. Fewer credit unions will be able to survive going forward if they are subject to higher capital requirements than others in the financial services industry because of unique and onerous regulation, however well intended it may be.

Additionally, we have substantial concerns about whether the NCUA has the legal authority to impose a two tier capital regime on credit unions. This same concern is evidenced by the disagreement on this point between sitting members of the NCUA Board. What happens if courts later agree that such authority does not exist? Why not implement the banking agencies risk based capital regime to eliminate this looming issue before it becomes a focus of litigation or legislation?

We again recommend that a complete complement of tools be provided for all of our nation's credit unions to more prudently manage capital by providing access for all credit unions to supplemental or alternative capital as an integral part of the risk based capital proposal. The risk based capital convention is incomplete without this important additional capital/risk management tool. Supplemental capital has been in use in low income and corporate credit unions for many years. The concept is not new to our industry. In addition, the Federal Reserve Bank is a proponent of banks utilizing such capital instruments in order to bring market discipline to the management of financial institutions while enhancing their safety and soundness. Our nation's credit unions deserve no less. The time to add this component is now while this regulatory capital proposal is under development.

In summary, we recommend that adjustments be made to this proposed regulation to ensure that the final rule is comparable to Banking agency risk based capital rules in order to allow credit unions to be competitive. We recommend that the use of a supplemental or alternative capital structure be added to the risk based capital convention in order to provide an additional capital tool to enhance the safety and soundness of all credit unions.

### **Other Recommendations and Comments**

More specifically we make the following recommendations for specific areas of the proposal:

**Residential Real Estate Loans**--eliminate the concentration risk thresholds requiring higher capital retention (75%) on residential real estate loans at the greater than 35% of assets level. Keep the risk weight at 50% for such loans.

The additional capital requirement makes no sense. For example, loans put on the books after reaching the 35% level could be originated at a 25% to 50% loan-to-value which present little to no risk of loss but would still require a much higher capital level. We recommend that the proposal mirror the banking agencies capital regime in which all such loans stay at a 50% risk weighting for capital retention purposes.

Concentration of long term, fixed rate loans can and should be monitored through Call Reports and the examination process. The additional capital requirement as proposed will put credit unions in a compromised and un-competitive position, serve members poorly and potentially reduce the population of credit unions which otherwise might survive and thrive.

**Junior Lien Real Estate Loans**—eliminate the concentration risk thresholds requiring higher capital retention (150%) on junior lien real estate loans greater than 20% of assets. Keep the risk weight at 100%. Again, this additional capital surcharge makes no sense and is not based on the riskiness of additional loans. The impact of such a scheme however puts credit unions at a disadvantage in the marketplace.

Concentration risk of long term, junior lien real estate loans can and should be monitored through Call Reports and the examination process. Underwriting criteria, loan policies, loan-to-value, debt-to-income, collection practices and many other factors impact the determination of the risk position of such loans and the evaluation of the capital required to prudently manage a portfolio of such assets.

**Commercial (Member Business Loans)**—eliminate the concentration risk thresholds requiring higher retention (150%) of capital for commercial loans greater than 50% of assets. Keep the risk weight at 100%. Again, this capital surcharge makes no sense and is not based on analysis of the riskiness of such individual loans. The impact of such a scheme however puts credit unions at a disadvantage in the marketplace by requiring a capital surcharge on the loans beyond the threshold. Other considerations must be taken into account to effectively assess the riskiness of any individual loans as noted previously.

**National Credit Union Share Insurance Fund (NCUSIF) subtraction from Capital**—eliminate the deduction to the numerator of the risk-based capital ratio calculation for the NCUSIF deposit. Total capital of credit unions should not be reduced by the amount of the NCUSIF deposit.

As mentioned in our May 27, 2014 response to the initial RBC proposal these funds are assets of the credit union and should be treated no differently than funds deposited with any other federal government agency. If the NCUA is anticipating that the funds may not be available to return to credit unions in the future, then a more fair solution is to assign a risk-weight to the NCUSIF deposit. The risk weight could be the same as assigned to the investment in a Federal Home Loan Bank investment (20%). In the event of actual insolvency of the NCUSIF the asset should be accounted for in accordance with GAAP under the Other Than Temporary Impairment accounting requirements, which would be the same treatment applied to investments/deposits with other federal agencies. It is punitive to erase capital by this artifice which represents a double capital surcharge for this refundable asset.

### **Conclusion**

The initial Risk Based Capital proposal was modified substantially and those adjustments were appreciated and necessary. However, the Second Proposal as it is written continues to fall short in many respects. **We do not support the proposed rule as it is currently written.**

The concentration risk thresholds, punitive risk weights and adjustments to capital included in the current proposal will put our nations' credit unions at a competitive disadvantage going forward and will damage the industry if implemented as proposed. The omission of access to supplemental or alternative capital as a means of enhancing safety and soundness is a huge mistake during the consideration of putting in place a new capital regime which credit unions will operate under for years to come. We again recommend adding this critical tool to the capital management options for all credit unions.

Your serious consideration of all of the comments on the proposal will serve to improve the final rule. We again thank you for the opportunity to comment on the second Risk Based Capital proposal.

Sincerely,

Michael J. Lord  
Chief Financial Officer  
State Employees' Credit Union  
Raleigh, North Carolina