Dover Federal
CREDIT UNION
1075 Silver Lake Blvd., Dover, DE 19904

April 24, 2015

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

RE: Comments on Capital Adequacy- Risk-Based Capital Proposed Rule

Dear Mr. Poliquin:

There is no doubt that the current capital regulations need to be updated to a system that would reflect lower capital requirements for lower-risk credit unions and higher capital requirements for higher-risk credit unions. However, I believe the revised proposal under consideration still has significant flaws which will do more harm than good to the credit union industry and ultimately the members/communities we serve. In particular, my concerns are:

- Impact on the growth opportunities of the credit union industry and communities we serve.

  There are no local community banks in Kent County Delaware. As such, many small businesses are approaching Dover Federal for their small business loan needs. If this proposal is enacted the Credit Union's ability to address this community need would be diminished leading to a stifling of economic development.

- NCUA's legal authority to prescribe a separate risk-based capital thresholds for "well capitalized" and "adequately capitalized" credit unions and to require individual credit unions to hold capital above those required by statute or rulemaking.

- NCUA's use of a $100 million asset threshold as the definition of a "complex," credit union.

  While the revised proposal has increased this limit to $100 million from the original proposal of $50 million, it still fails to address what is truly a complex credit union. Complexity should be determined by the composition of the balance sheet, not the size of the balance sheet.

- NCUA's proposed risk-based capital ratio for "well capitalized" is set at 10 percent;

  It is appreciated that NCUA revised this limit from the original proposal to create parity with the banking industry. However, banks can satisfy their total RBC using a combination of Tier 1 and Tier 2 capital. Credit unions, however, do not have ability to engage in all the available Tier 2 capital instruments. Instead, credit unions must satisfy their capital requirements with elements more similar to a bank's Tier 1 capital. While the proposed rule would allow credit unions to count ALLL towards their RBC ratios, it would not permit all credit unions to count secondary capital. Therefore, until credit unions are permitted to issue secondary capital for risk-based purposes the "well-capitalized" RBC limit needs to be adjusted to a lower threshold.

- NCUA's treatment of risk-weighted assets, such as investments in CUSOs, mortgage servicing assets, and corporate paid-in capital.

  NCUA's stated basis for this approach is to address the real estate and member business lending (MBL) concentration risk that led to credit union failures and NCUSIF losses during the recent financial crisis. In the preamble to the proposed rule, NCUA cites a 2012 GAO report that concluded credit concentration risk contributed to 27 of the 85 credit union failures between 2008 and 2011. NCUA also relies on its Office of Inspector General's conclusion that the NCUSIF suffered $25 million in losses because of failed credit unions with larger real estate concentrations. In particular, NCUA notes the failures of Cal State 9 Credit Union, Beehive Credit Union, and Ensign Federal Credit Union as examples of losses due to substantial residential real estate and equity loan concentrations.

  While the above information is factual, it is being applied out of context and distorting the overall health of the credit union industry's performance in these asset areas. Furthermore, NCUA already has the needed authority to identify high risk potential and mismanagement within individual credit unions to take the needed corrective steps without unduly burdening the industry as a whole.

- The need for NCUA to promulgate a rule allowing all credit unions access to secondary capital for risk-based purposes.

- Questionable effectiveness of RBC in the banking industry.

  During the FDIC's April 8, 2014, board meeting, the Bank Insurance Fund approved a new rule to strengthen the leverage capital requirements for the eight largest, most systematically important banking organizations. The new rule requires a 6% leverage ratio for the insured banks to be considered well-capitalized under prompt corrective action. Bank holding companies would need to have a leverage ratio of 5%. By comparison, the Basel framework requires only a 3% minimum leverage ratio for both levels of a banking organization. During the meeting, FDIC chairman Martin J. Gruenberg said the leverage approach "benefits the financial system as a whole and reduces the potential systemic risk these institutions pose." He supported the cooperative model's capital standard saying: "This is a rule of significant consequence. In my view, this final rule may be the most significant step we have taken to reduce the systemic risk posed by these large complex banking organizations."

In a more extensive statement, FDIC vice chairman Thomas M. Hoenig laid out the benefits of a leverage ratio versus the traditional risk-based approach: "The supplementary leverage ratio is a more reliable measure that is simple to calculate, understand, and enforce than the subjective risk-weighted measures, and it provides a highly useful initial assessment of a bank's balance sheet strength...Experience has shown that relying only on a risk-based capital measure serves the public poorly ... As recently as year-end 2013, reported risk-based capital ratios for the largest global banks averaged 13% while the average leverage ratio was less than 5% ... .I am confident that supervisors will rely increasingly on the leverage ratio, as the market already does, to judge a firm's capital levels, loss absorbing capacity, and balance sheet strength".

A third FDIC board member, Jeremiah O. Norton, supported the rule with the following points: "There is recent economic research to support the conclusion that the leverage ratio is a statistically significant predictor of bank default while the Basel Tier I risk-based capital ratio is not."

I urge the NCUA Board to review all of the submitted comments in order to create an improved capital regulation. This regulation should protect the credit union industry and the share insurance fund without placing arbitrary undue hardships on credit unions that will prevent the industry from providing the products and services that benefit members and communities we serve.

Sincerely,

David W. Clendaniel
President/CEO