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220 Donald Lynch Blvd.
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April 24, 2015

Mr. Gerard Poliquin
Secretary to the NCUA Board
1775 Duke Street
Alexandria, VA 22314

Re: Comment letter on NCUA's revised risk-based capital rule proposal – RIN 3133-AD77

Dear Mr. Poliquin:

In my role as Senior Vice President of Marketing and Strategy at Digital Federal Credit Union, I'm writing you to share my comments on NCUA's revised risk-based capital rule proposal. I believe the rule, if implemented as proposed, will cause unnecessary harm to the ability of credit unions to serve their member/owners as they deserve to be served. I appreciate the opportunity to outline some of the issues I see and offer ideas for improvement before the rulemaking process is completed.

Unnecessary regulation

There is no clear basis for disregarding the current prompt corrective action (PCA) regulations and adopting a completely different model. There were no issues identified as part of the NCUA's most recent review of the regulation performed as part of the NCUA's rolling three-year review of regulations in 2012. This analysis was performed subsequent to the NCUA's December 19, 2011 response, included in the January 4, 2012 United States Government Accountability Office (GAO) Report to Congress (GAO-12-247)¹. This response by Chairman Matz, indicated:

"It is also worthy to note that consumer credit unions performed very well during the worst financial crisis since the Great Depression, and NCUA was highly successful overall in mitigating failures and losses for consumer credit unions. The 85 consumer credit union failures occurred over a two and a half year period during the height of the economic crisis. As noted in the report, the level of annualized failures is relatively low, only marginally higher than pre-crisis levels, and involved institutions with less than 1%

¹ <http://www.gao.gov/assets/590/587409.pdf> United States Government Accountability Office – Report GAO-12-247 – January 2012.

of total credit union assets. NCUA was effective in prioritizing our supervisory resources during the economic crisis to prevent the failure of larger credit unions that came under stress, and in mitigating losses for those that did."

In late January 2013, the NCUA's Office of General Counsel released the list of regulations being reviewed, indicating, "Regulations under review in 2013 include rules governing member business loans, fair credit reporting, privacy of consumer financial information, appraisals and share insurance. ... Additionally, NCUA will expand its review of federal credit union bylaws, which began in 2012." Based on this release, it would appear the PCA review was completed in 2012, since it was not expanded into 2013.

The NCUA suggests that the Proposed Rule was written to be more consistent with Other Federal Banking Regulatory Agencies (Other Agencies). The overall credit union industry has consistently been devoted to servicing their members differently than banks. Credit unions have proven to be an economic force in local markets and softened the effects of the recent economic downturns to its members. The overall credit union industry is not looking to be more consistent with banks and has devoted time to being a cooperative in nature.

Asset size should not define a credit union as "Complex"

The Federal Credit Union Act (FCUA) provides that the NCUA may only adopt RBNW rules for "insured credit unions that are complex, as defined by the Board based upon the portfolios of assets and liabilities of credit unions."² While the increased threshold of \$100 million represents progress, it still disregards the composition of assets and liabilities of individual credit unions. A more detailed definition of "complex" is warranted.

In addition to the above considerations, I recommend the NCUA increase the proposed asset threshold from \$100 million to \$1 billion. This threshold should be used in combination with actual operational complexity as measured by the NCUA's Complexity Index. The NCUA discussed a Complexity Index as part of the supplemental information. Thus, it is proposed that all federally-insured credit unions with assets under \$1 billion be considered non-complex, and that only those credit unions with assets above \$1 billion with a Complexity Index value of 20 or higher be required to meet risk-based capital provisions.

Requirements for Capital Adequacy are unclear

The Proposed Rule requires that "complex" credit unions "must have a process for assessing its overall capital adequacy in relation to its risk profile and a comprehensive written strategy for maintaining an appropriate level of capital" and "the nature of such capital adequacy assessments should be commensurate with the credit union's size, complexity, and risk-profile." The requirement for credit unions to have a comprehensive written strategy poses excessive

² http://www.ncua.gov/Legal/Documents/fcu_act.pdf (Page 82)

regulatory burden to credit unions (see **Significant under estimation of the regulatory burden** discussed below) and the ruling is too vague. There are no clear guidelines and/or criteria for NCUA's defined "comprehensive written strategy" for credit unions and NCUA examiners within the proposed regulation. This results in inconsistently applied requirements throughout the NCUA and its regions. Credit unions already have adequate capital adequacy policies, processes, and procedures in place. Therefore the NCUA should remove the requirement of a written strategy from the RBC rule. Furthermore, this proposed requirement appears to have a strong resemblance to the Capital Planning and Stress Testing rules issued last year for credit unions with assets of \$10 billion or more.

Significant under estimation of the regulatory burden

The Proposed Rule's Paperwork Reduction Act section estimates the additional data collection requirements for an estimated 1,455 complex credit unions to be a one-time 40-hour burden, or \$1,276 cost per credit union. The Proposed Rule does not incorporate the estimated burden for establishing a comprehensive written strategy for maintaining an appropriate level of capital and other changes to the credit union's operations other than data collection. The effects of this proposal will be a much greater burden on complex credit unions upon the implementation year and for ongoing years. The NCUA's final rule on Capital Planning and Stress Testing estimated 750 hours of paperwork burden in the initial year and 250 hours in subsequent years³.

Other than submitting a plan to the agency, it is unclear how the requirements of this proposal differ from the final rule on Capital Planning and Stress Testing. Using the cost estimate previously utilized by the NCUA, a more reasonable estimate (compared to zero) would be \$23,926 per credit union or \$34.8 million to the industry for the initial year of the final RBC rule. Additionally, there would be an ongoing annual cost of \$7,975 per credit union or \$11.6 million to the industry. Over a five year period, the cumulative cost to the industry would be approximately \$81.2 million.

Align risk-weights for Credit Unions – not for Banks

The revised RBC Rule from the original proposal has many positive changes, such as the removal of the cap for the allowance for loan losses and changes to real estate loans risk-weights. Nevertheless, here are two of the risk-weights within the proposed regulation that continue to warrant further evaluation. NCUA should not ignore the uniqueness of credit unions and how credit unions handled the effects of the recent economic downturns to their members. Credit unions are known for promoting and conducting responsible lending and managing their financial statements. The diversification and growth opportunities provided by the cooperative nature of credit unions provide a sustainable future the industry and members of credit unions.

³ <http://www.ncua.gov/Legal/Documents/Regulations/FIR20140424CapitalPlanningStressTesting.pdf> (Page 24315)

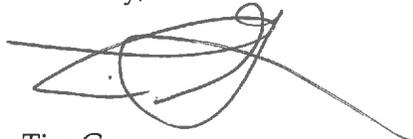
The Proposed Rule is inconsistent with Congress' direction that "design of the risk-based net worth requirement should reflect a reasoned judgment about the actual risks involved."⁴ The following outlines two risk-weight concerns under the Proposed Rule that require additional attention and reevaluation:

- **Real Estate Loans** – The Proposed Rule risk-weights the entire real estate portfolio with consideration of concentration risk of the portfolio to total assets of the credit union. The Proposed Rule does not consider the types of real estate loans within a credit union's portfolio. For example, a credit union's real estate portfolio's adjustable rate loans and/or shorter term loans, such as 10-year fixed rate loans, have far less risks than the portfolios' 30-year fixed rate loans. The Call Report currently has information disclosed at some level of detail for a credit union's real estate portfolio. Therefore, the NCUA should further segment a credit union's real estate portfolio to then risk-weight the varying risks within a credit union's real estate portfolio.
- **NCUSIF Deposit** – The credit union system capitalized its own separate, federal insurance fund, years ago. This structure and its current value should not be overlooked. The 1% deposit made by all federally-insured credit unions to the NCUSIF is an asset which should be properly included in any risk-based capital calculation. This amount is fully refundable should a credit union convert to private insurance (where allowed), or convert its structure to a bank. This balance is considered an asset in accordance with Generally Accepted Accounting Standards. The NCUSIF deposit should be included in the RBC calculation.

Thank you again for the opportunity to share my comments on the proposed risk-based capital rule. I sincerely hope NCUA will consider the changes to the regulation I've recommended so that the ability of Digital FCU and our sister credit union to serve our member/owners is not needlessly impaired.

If you have any questions about my comment letter, please contact me by email at tgarner@dcu.org or by phone at (508) 263-6856.

Sincerely,

A handwritten signature in black ink, appearing to read 'Tim Garner', with a long horizontal line extending to the right.

Tim Garner
SVP Marketing and Strategy

⁴ S. Rep. No. 193, 105th Cong., 2d Sess. 13 (1998) (S. Rep.)