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Mr. Gerard Poliquin, Secretary of the Board
National Credit Union Administration
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Subject: Prompt Corrective Action Risk-Based Capital (RBC2)

I am writing on behalf of Credit Union of America (CUA), which serves the communities in and around Wichita, Kansas and Great Bend, Kansas. We have more than 55,700 members and $623 million in assets. CUA appreciates the opportunity to provide comments to the National Credit Union Administration (NCUA) on its proposed rule, Prompt Corrective Action - Risk-Based Capital (RBC2).

Summary and General Comments

Though improved over NCUA's RBC1 proposal, this RBC2 proposal remains dysfunctional as a proposed regulation in search of meaningful justification. Banking has been subject to risk-based capital, yet that did little to avoid the financial and banking crisis of 2008 to 2013, so the validity of risk-based capital seems like a concept we've all agreed to pretend will make the financial system "safer." Back-testing reveals that RBC2 is likely to be ineffective, there is doubt that the NCUA has legal authority to set a risk-based standard to defining "well capitalized," and a number of proposed risk weightings remain inappropriately high. This proposal would have substantial adverse impact on an industry that has shown responsible constraint and commendable risk management.

No Demonstrated Necessity for this Proposal

The NCUA has founded this proposed regulation to emulate the FDIC, yet the FDIC has pulled back from a complex RBC model to a simpler approach, in part

because the complex model proved ineffective at identifying or mitigating bank risk during the 2008-2013 financial crisis. In her letter to the Governmental Accountability Office in December 2011, NCUA Chairman Matz reported on how well consumer credit unions had performed during the financial crisis. Further, FDIC Vice Chairman Thomas Hoenig argues strongly that the risk-based capital model is “fundamentally flawed” which during the 2008 banking crisis “protected no one: not the banks, not the public and certainly not the FDIC.” The NCUA has remained focused on hoisting a discredited complex RBC model on a credit union industry which has historically exhibited far less risk than the banking industry. This threatens to impose substantive compliance costs for credit unions dealing with complex regulatory reporting and in some cases creating competitive disadvantage, with the merest probable benefit to effective risk management. Back-testing analysis performed by CUNA, applying the proposed RBC2 standards to credit unions that failed during the 2008 crisis, found that out of 26 CUs with over $80 million in assets (prior to the crisis), only three would have met the RBC2 criteria for being undercapitalized and subject to PCA plans. If credit unions are to be saddled with a complex new capital regulation, it is appropriate to do a little back-testing to determine how effective it would have been in detecting credit unions that failed. Back-testing reveals that this proposed regulation is incapable of achieving the purported results. Unless we are in the business of regulation for regulations’ sake, such an ineffective regulation should not be imposed.

A comparative review of bank versus credit union insurance fund losses and reserve levels, beginning with the double-digit inflation crisis in 1990, reveals that credit unions have experienced only a small fraction of the volatility of the banking insurance fund. Average annual losses per $1,000 of insured deposits over that span from 1990 to 2012 were $0.18 for the NCUSIF, while for the FDIC losses were five time higher, at $0.93. This calls into question the need for a complicated risk-based capital rule for credit unions.

Defining Complex CUs by Asset Size is Too Simple and Inappropriate

NCUA proposes the simple variable of asset size for defining credit unions as “complex,” though RBC2 would boost the asset threshold to $100 million. This is too low of a threshold, as many credit unions at this asset level are not particularly complex from the perspective of balance sheet and product structures or operational complexity. In fact, the primary certain complexity is that of regulatory compliance. The Federal Credit Union Act outlines that NCUA is expected to define complex credit unions on the basis of their

portfolios of assets and liabilities, so the proposed definition seems non-compliant with both the FCU Act as well as with Congressional directives which did not anticipate PCA rules to be based simply on asset size. Prompted by the NCUA Complexity Index described in RBC1, we suggest that a more appropriate level for categorizing a credit union as complex should begin at $500 million plus a Complexity Index of 17 or greater. This would take into account criteria related to balance sheet and operational complexity, minimizing the number of CUs affected while covering the credit unions with the largest portion of shares insured by the NCUSIF. Any asset level selected in a final rule should also be indexed to a general measure of inflation.

NCUA Lacks Authority to Impose Higher Requirements for "Well-Capitalized"

We believe this portion of the proposal is extra-legal and goes beyond the NCUA's legal authority. The FCU Act establishes that NCUA is co link risk-based capital requirements to the adequacy of net worth only the adequately-capitalized classification. Hence, the proposed requirements to higher risk-based requirements for a "well-capitalized" classification go beyond the authority granted in the FCU Act. The former chairman of the Senate Banking Committee, commenting on that portion of the FCU Act, has written that "If we had intended there should also be a separate risk-based requirement to be well capitalized (in addition to the 7% net worth ratio), we would have said so." It is revealing that the NCUA discards this type of clarification about Congressional intent, and continues to pursue extra-legal authorities and regulations.

Numerous Risk Weightings Remain Unnecessarily High

Despite some improvements in RBC2 over RBC1, there are a number of proposed risk weightings meriting disagreement.

1. Several proposed risk weightings affecting real estate loans are inappropriate because they create a competitive disadvantage by imposing higher risk weights on credit unions than for banks. The proposed risk weighting of 75% for first lien residential mortgage loans exceeding 35% of assets is unnecessarily high, relative to banks who are only subject to a 50% risk weighting. Similarly, current real estate loans exceeding 20% of assets would be disadvantaged by a higher risk weight than for banks. There is no support for NCUA's embedded assertion that these types of loans exhibit increasing credit risk as a

credit union builds a larger portfolio, and the risk weights should be no higher than for banks.

The proposal would result in reducing our ability to provide mortgage financing for members in our communities and intentionally put us at a competitive disadvantage in relation to a bank making the same loan. Our credit union has been ranked 5th in market share for new mortgages in our community. Our long-term loss ratio on mortgage lending has been 0.052%, even during the worst of the 2008-2013 economic downturn. This solidly demonstrates our ability to effectively underwrite these types of loans even as their proportion and balances have grown.

2. The risk weighting as high as 150% for commercial loans exceeding 50% of assets is significantly higher than for bank commercial loans, where lower risk weightings of 100% can apply. There is no basis to suggest that these loans create greater risk of loss if they appear on a credit union balance sheet rather than a bank balance sheet, and should be no higher than for banks.

3. CUA believes the proposed 300% risk weighting for publicly traded equity investments is excessively high, and serves as an unnecessary limitation affecting investments for employee benefit funding. CUA has had equity-based investments for purposes of employee benefit funding since 2000. Based on our observation and experience with fluctuation in the value of these assets, even during the financial turmoil of the 2008 to 2012 period, a weighting in the range of 100% to 150% for these types of assets would be more appropriate.

4. Credit Union of America is a participant in the FHLB Mortgage Partnership Finance (MPF) Program. We have a concern with the way in which RBC2 defines the MPF Program, because the wording of RBC2 appears to create different risk classifications for the credit enhancement (CE) obligation, depending on whether a credit union services the MPF loans or sells the loans with servicing released. In reality, the CE obligation is unaffected by the retention versus sale of servicing. The definition of the MPF Program should be modified by deleting the reference to "servicing."

5. CUA does not support the risk weight for unconsolidated credit union service organizations (CUSO) investments, which remains too high and should be no higher than the 100% risk weight proposed for CUSO loans.

Call Report Information Concerns

NCUA noted in the RBC2 proposal that additional data will be needed on the Call Report, quickly dismissing this burden as "easily… handled as part of the normal and routine maintenance of a credit union's data reporting system." We have concerns that the NCUA no longer recognizes nor appreciates the complexity and time requirements of compiling this data and making a constant stream of revisions to data and reporting systems. I have reviewed FDIC call report documents, and found that they utilize various optional schedules for collection of data that is less likely to apply to all banks. NCUA could follow a similar approach to ease data collection. Further, I have found that NCUA Call Report instructions are often poorly written, leading to confusion and multiple interpretations and inconsistencies by both CUs and examiners. I would urge the NCUA to spend time clarifying and improving definitions and instructions, and also addressing omissions, before plunging ahead to add yet more complexity.

Imposition of Comprehensive Capital, Written Strategies, and Subjective Requirement for Capital in Excess of Well-Capitalized

We remain concerned with the subjective latitude retained by NCUA to dictate that even a credit union that is well-capitalized needs more capital. Every "complex" credit union would be required to prepare a capital adequacy plan and accumulate capital on top of the 7% net worth and the 10% RBC2 requirements. These plans, risk assessments, and amounts of additional capital must be updated on a recurring basis, and would be subject to the widely-varying interpretations of every examiner who evaluates the plan, the risk assessments, and the amounts of additional capital required. This introduces a perpetual subjective element, wherein a credit union can never be sure its plan will be deemed compliant from one examiner to the next. NCUA apparently does not believe that well-capitalized means well-capitalized. On top of doubtful authority for NCUA to impose higher capital requirements for being well-capitalized, we object to the proposed authority to subjectively determine that well-capitalized is not, in fact, well-capitalized enough.

We believe the layered-on capital adequacy provisions of the RBC2 proposal should be eliminated.

Implication of a Separate Interest Rate Risk Rule

As a result of deleting interest rate risk (IRR) provisions from the RBC1 proposal, NCUA has solicited input about an additional potential future IRR rule, likely founded on measures of net economic value. We strongly disagree that NCUA needs to layer a new and separate IRR regulation on top of the numerous NCUA rules and letters which already address IRR risk and management. Existing NCUA rules already require written programs and policies for IRR measurement, monitoring, and consideration of IRR in decision-making. NCUA should be capable of identifying CUs with exceptional levels of IRR during the supervisory exam process. Rather than burdening all CUs with a new complex one-size-fits-all IRR regulation, NCUA and the industry they regulate would be better served if NCUA focuses on the outliers of IRR. Bank regulators don't impose a one-size-fits-all quantified IRR rule, but rely on the supervisory process to identify banks that justify more-detailed IRR assessment. There is little evidence that another layered IRR regulation will somehow achieve capacity to manage IRR better than during the interest rate increase during the 2004 to 2006 period, a period where no natural-person CU has been reported to have failed due to excessive IRR exposure.

NCUA's Proposed Implementation Time Line

We believe the proposed time line is too short, and that implementation should be delayed until 2021. Credit unions cannot instantly raise additional capital that may be required under RBC2, and will need that additional time to increase earnings in ways that respect the nature of a cooperative member-owned organization. This timing would also synchronize with NCUA's termination of the corporate stabilization fund. The massive and exaggerated stabilization assessments of that program took billions of dollars of capital out of credit unions, so it is appropriate to delay RBC2 implementation until a time when credit unions should receive refunds, helping increase capital levels imposed by RBC2.

Conclusion

Thank you for the opportunity to comment on this proposed rule, and for considering our views on risk based capital requirements. If you have questions or want to request clarification regarding our comments, please feel free to contact me at 316-265-3272 ext. 140 or via email to PaulM@cuofamerica.com.

Sincerely,

Paul Meissner
Senior Vice President-Finance/Chief Financial Officer