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• COMMUNITY •
Federal Credit Union

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April 23, 2015 - 38

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

Re: Comments on Proposed Rule: Risk-Based Capital

Dear Mr. Poliquin:

My name is Sam Scro and I am the CEO of Auburn Community Federal Credit Union located in the city of Auburn in the Finger Lakes region of the state of New York. Our credit union was founded back in January 1936 and we possess charter# 988. The credit union was granted a community charter in December 2001 allowing it to serve anyone who lives, works, worships, or attends school in Cayuga County. We currently have over 7,600 members and just over $80 million in assets.

At the direction of our Board of Directors, our credit union was one of the over 2200 credit unions that responded to the initial proposed risk-based capital rule (hereinafter referred to as RBC1) and we would like to thank NCUA for all of their hard work in redrafting and refining their efforts in rolling out the second edition of the proposed risk-based capital rule (hereinafter referred to as RBC2). Again, at the direction of our Board of Directors, we would like to thank NCUA for the opportunity to respond and comment on RBC2. Unfortunately, our position has not deviated much from our first correspondence to the agency. We believe that both RBC1 and RBC2 are solutions in search of a problem that does not exist for the vast majority of credit unions and especially for our own credit union.

Our credit union has numerous issues with RBC2 including: asset size determining the classification of a credit union as complex or not; risk weighting percentages used on loans and investments; our credit union not having access to secondary/supplemental capital to meet RBC2 requirements; the implementation period compliance dates if this proposal proceeds to begin with; the legality of a two-tiered capital system; and most importantly, the negative impact to our credit union and to our members.

The passage of RBC2 in its present form would have an ***extreme negative impact*** on our credit union. The proposed risk weighting for investments that are used for employee benefit funding set ***at 300% are very harsh and unrealistically attainable***. Our credit union has had to defend itself over the past nine months regarding an investment made in 2011 with New York Life Insurance for the purpose of funding an employee benefit deferred compensation plan. This plan was in place for over three and one half years before NCUA found fault with it by citing concentration risk concerns during our last exam. For your convenience, we have provided copies of all correspondence between the agency and our credit union regarding this investment.

We have been told by NCUA examiners through the years that our credit union is "plain vanilla". In reading through the entire document, it is apparent that if the activities (loans, investments, etc.) of a credit union fall outside the agency's "one-size fits all" parameters, then that credit union is now considered complex. In the case of our credit union, by the nature of our New York Life investment, we automatically would be considered complex and subject to all the provisions of RBC2 even though we just hit $80 million in assets at the end of March. Increasing the asset size from $50 million to $100 million is a positive change considered by the agency, however, it should be raised to $500 million before considering a credit union as complex. Before NCUA automatically classifies our credit union as complex due to our investment with New York Life and imposing the 300% risk weighting to our investment, they should consider the ***quality*** of the investment we hold with them and the ***likelihood*** of that investment going bad. To play devil's advocate, there is a greater chance that our credit union would lose our 1% NCUSIF balance due to Congress combining the FDIC and NCUA insurance funds by creating one super-regulator than there would be of New York Life Insurance Company going bankrupt. With that being said, shouldn't NCUA return our 1% NCUSIF deposit and just bill us each year when credit unions go bad? (For example, NCUA needs $100 million dollars to cover failed credit unions for the year; if there are 6400 credit unions then send each credit union a bill for $15,625 and return to us the $700,000 of our money so we can reduce our risk exposure).

In 2014, our credit union earned over $201,000. As currently proposed at a 300% risk weighting, if our credit union contributed $200,000 to undivided earnings each year, it would take us ***30 years*** just to cover the capital requirement for our New York Life investment alone! To reduce our investment to comply with the proposed rule would mean investing into lesser quality companies at a reduced yield and at a greater expense. This course of action is irresponsible and would not result in a prudent business decision being made. At the very least, a provision should be made for our credit union and others with similar ***high quality investments***, that we are exempted from complying from this rule along with all credit unions that have entered into these plans *prior* to the passage of this proposed rule. There were long-term commitments made by key employees and the credit union before these investments were consciously made and to disrupt strategic plans of the credit union and adversely and capriciously affect employees with changes that are impossible to comply with is morally wrong. ***We are strongly encouraging NCUA to revisit the risk weighting on these investments to avoid irreparable harm to the credit union and the employees who would be affected.***

To immediately have to restructure our balance sheet to comply with RBC2 would create chaos and undermine long-term strategic decisions made by our credit union. Due to our structure, we do not have the luxury of selling stock to raise capital which will be needed to comply with this proposal. As a federally chartered community credit union, we are at a further disadvantage from other credit unions with regards to seeking merger partners as the rules and regulations make it nearly impossible for us to grow by merger to achieve economy of scale and generate more income to increase capital. There currently exists a gross inequity in the ability of our credit union to grow and expand through the use of mergers that is afforded other types of credit union charters, yet we will be painted with the same brush by this proposal to the detriment of our credit union and our members. We are being told we can keep our investments and keep our loans as we currently have them and all we have to do is increase our capital. We would gladly agree to some of these changes if we had the freedom to conduct and grow our membership free of the restrictions that are afforded the other types of credit unions. To mimic the bankers battle cry but with a credit union twist, "Hey, NCUA, level the playing field for all credit unions regarding mergers and expanding our fields of membership!"- give us a fighting chance to comply. Without a major overhaul of unifying the structure of membership eligibility for all credit unions, (with uniformity across all charter types) the agency is pre-determining which credit unions will thrive, survive, or be kicked to the roadside with the passage of this rule. ***If the cart is to go before the horse on this issue, than at the very least, implementation should not go into effect until 2021 to coincide with the end of the Corporate Stabilization Fund. This would afford all credit unions with additional time to restructure their balance sheets in an orderly fashion to minimize the negative effects of RBC2.***

RBC2 risk weighting on loans is an improvement over RBC1, but we have concerns that while most are comparable to the banking systems which NCUA is mandated to come up with, this could be improved further. Case in point is share secured loans with a risk based weighting of 25% when it is at 0% for the banking industry. We have the members' money securing the loan so why would we need to set capital aside for these loans? As Yogi Berra said in an AFLAC Insurance commercial to the bewilderment of those in the ad: "...and they give you money, which is just as good as cash!?" Please explain the agency's stance on this item because we do not see the risk with share secured loans. Another area of concern is with the proposed risk weights on first lien residential mortgage loans over 35% of assets and current non-junior real estate loans over 20% of assets having higher risk weights than those in the banking industry. Roughly 48% of our loan portfolio consists of home equity loans. During our last exam, the Supervisory Examiner and Examiner both suggested they would prefer to see the credit union "get into" the first mortgage market and double our then current real estate portfolio from $9.5 million by $18-$19 million up to a total of $27-$28 million. If we did that, our real estate portfolio would represent 73% of our total loan volume (they recommended this as they felt there would be less concentration risk with real estate loans as opposed to our New York Life investment). As CEO with nearly 30 years in the industry, I cautioned the examiners that we did not want to enter the market without having established relationships with realtors, we did not want to enter the market with interest rates at historic lows, and we did not want to become the next S&L fiasco reminiscent from the

1980's when rates rose dramatically. We will not jeopardize the long-term viability of our credit union making long-term low-interest loans for the sake of making more loans. We will definitely enter this market in the future when rates have risen to acceptable levels. ***We urge NCUA to adjust the risk weights on real estate loans so they are at par or lower than those of the banking industry so as not to restrict our ability to lend to our members.***

We know the agency is tasked to come up with a system comparable to that of the banking industry. We know the agency paid to get an opinion they wanted to justify them having the authority to implement a risk-based capital requirement for a credit union to be well capitalized as opposed to adequately capitalized as a provision of the FCU Act calls for. Many politicians and credit unions, including our credit union, do not feel this is necessary nor was this the intent of the law. An examiner can determine during the course of their audit whether or not a credit union has poor underwriting standards or is making questionable investment decisions. RBC2 contains an implied Advanced Notice of Proposed Rulemaking on interest rate risk suggesting that a separate IRR rule is needed. NCUA has already adopted an IRR rule and our credit union has already developed and adopted a written policy on IRR management and a program to implement the policy as part of our ALM responsibilities. To further burden our credit union and other credit unions to devote already scarce resources for duplicative efforts is criminal. The costs of compliance are becoming unbearable and are unnecessary for those of us who did not cause the problems leading to the "Great Recession". ***We believe the 7% net worth ratio with provisions for prompt corrective action should be left intact.***

In closing, we are a credit union, not a bank. Credit unions are structurally and fundamentally different from banks. A capital-based system mirroring that of the banking industry is not something NCUA should be emulating as the banking system did not serve them as well as the credit union model performed during the recent financial crisis. As our regulator, you are entrusted to protect the insurance fund, a fund which is made up from our members' hard-earned monies. Within our own industry, credit unions operate under differing rules and restrictions. To propose a capital rule that already acknowledges and includes special carve-outs for credit unions engaged in certain types of activities is unfair by its very nature and discriminatory. The fact NCUA has had to appease politicians representing those credit unions with special circumstances to make RBC2 palatable is proof that RBC2 is a solution in search of a problem and should be put to rest. **It takes courage and conviction to be a leader rather than a follower. There is nothing wrong with NCUA stating <u>we are different and better</u> than the banking industry and it is the banking industry that should be emulating the credit union model and not the other way around. There is nothing wrong with NCUA telling the credit unions that upon further review, we don't need this rule.** ***<u>We emphatically encourage NCUA to be a leader and rescind this proposed rule.</u>***

Sincerely submitted on behalf of the Board of Directors and Management,

Sam Scro

Sam Scro, CEO