Patelco

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BANK on TRUST.

Filed via regcomments@ncua.gov

April 20, 2015

Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428
Re: NCUA's Risk Based Capital Proposal, RIN 3133-AD77

Dear Mr. Poliquin:

Patelco Credit Union appreciates the opportunity to provide comments to the National Credit Union Administration (NCUA) on its proposed rule, Prompt Corrective Action - Risk-Based Capital.

Like most credit unions, Patelco was founded to serve the financial interests of employees of a particular organization – in our case the **Pa**cific **Te**lephone and **Te**legraph **Co**mpany (now part of AT&T). The year was 1936, and Patelco's initial assets totaled a mere $500. We have expanded our field of membership to serve the employees of over 1,000 large and small businesses and communities in Northern California. With assets now totaling more than $4 billion and 287,000 members we are among the largest credit unions in the nation today. Patelco currently maintains a capital (net worth) level of over 12% of total assets, a buffer of 5% above the "well capitalized" level. While under the proposed rule, our risk-based capital level would be 23%, a buffer of 13% against the RBC rule of 10%; this is only good for a point in time and may not support the future needs of the Patelco membership.

The effect of the proposal:

According to the analysis performed by the NCUA, only 2 percent of federally insured credit unions would be affected, and based on 12/31/14 data, 19 credit unions would have their PCA category drop below the "well capitalized" level. It would appear that the current capital rules are sufficient for safety and soundness. Enacting additional complex capital rules will only add administrative burdens with no compensating benefits. More importantly, the proposal provides barriers to the credit union business model and could inhibit credit unions from fulfilling their mission to serve the needs of their members. While we can appreciate that some credit unions have failed, the cost of the failures has been immaterial on the insurance fund and in the case of the corporate credit union collapse, rules have since been implemented to address the structural risk.

Given this, we believe that amending the capital requirements through the RBC2 proposed rules is imprudent and unnecessary to furthering safety and soundness and harmful to the credit union industry. However, if the NCUA intends to proceed, we offer the following comments regarding the NCUA's RBC2 proposal.

Among the weaknesses of the RBC2 proposal is:

- The proposal adds an additional layer of risk buffer on top of the existing net worth ratio that is used for NCUA's Prompt Corrective Action (PCA) requirements. This added buffer will require Complex credit unions to maintain much higher capital reserves than have previously been required regardless of portfolio composition. The NCUA originally proposed all credit unions with $50 million or more in assets be defined as "Complex." In response to the criticisms received, the NCUA raised this to $100 million. This is still an arbitrary limit with no justification. Larger does not necessarily mean riskier. In fact, larger institutions are more likely to have the resources to build better controls than small institutions.

  The Credit Union Act addresses this by requiring the NCUA to consider the risk content of a credit union's individual portfolio before adding any additional reserve requirements in addition to the PCA net worth ratio. Drawing an arbitrary cutoff does not appear to meet this legal standard. Larger banks are required to perform stress testing to gauge their capital needs, which considers their individual portfolio composition.

  The NCUA points to the 192 credit unions that failed in the last ten years despite an average 12.1% net worth ratio as justification for this added layer. However, the NCUSIF has never been significantly drained by economic downturns. In the 2009 crash, the NCUA had to extend $26 billion, which was less than 5% of the NCUSIF.

- The risk weight for CUSOs appears to be punitive in nature treating all CUSOs the same regardless of business lines, their financial position, or their ownership structure. Despite a few CUSO failures, many CUSOs remain viable and provide creative and innovative solutions for credit union members as well as efficiencies among the credit union movement. Since the proposed rules require additional capital for these types of investments, credit unions such as Patelco may have to cancel or delay the development of innovative solutions or products which are beneficial to members but can only be offered through a CUSO.

- Banks, that up until recently had a very similar capital rules as proposed by the NCUA's RBC2 rule, can go to the open market to raise capital. Credit unions are not allowed to raise capital except from retained earnings, a very dissimilar approach to the banking model. The 4 years the NCUA has given credit unions to comply with the RBC2 rules will not be enough time, especially for those credit unions adversely impacted by this proposal to gather the needed capital through retained earnings. As a result, credit unions may need to radically change their business model to focus on net income rather than the financial welfare of their members. Without parity with the bank system regarding supplemental capital, the inability to raise capital through sources other than earnings disadvantages credit unions in the marketplace and may ultimately force fee increases, reduced benefits to members, etc. to build the required capital. This is not in the members' best interests nor does it align with the founding credit union principles and charter.

- It would appear that the NCUA did not consider other NCUA rules in place, such as investment powers and PCA rules, which are more conservative than those in the banking system and create a "less-risk" environment for credit unions in general, as compared to the banking system. For a specific example: The Credit Union Act requires the NCUA to consider risks for which being Adequately Capitalized may not provide enough protection. The proposed rule would require an additional risk buffer that brings Complex credit unions up to the Well-Capitalized level. This will require on average 10% more capital be raised and set aside. Implementing a higher standard for risk-based capital that places an additional capital burden on credit union is not commensurate with the level of risk in the industry, nor is it necessary as stated earlier.

- For some specific categories, the proposed increases do not stand up to comparison with the FDIC requirements for banks. For example, for residential mortgages, banks are allowed to use a 50% weight regardless of the proportion of those loans to the bank's overall portfolio; complex credit unions will only get the 50% weight for residential mortgages if such loans make up 35% or less of the portfolio. If such loans make up more than 35% of the portfolio, then the portion exceeding 35% will be given a 75% weight.

- The rules proposed in RBC2 are not a complete set of rules expected to be implemented to address the overall financial risk landscape. Other related rules to be proposed in the future may also have a negative impact to the industry and further compound the effects of RBC2. Adding or changing rules via a piecemeal approach will create significant uncertainty, confusion, and inefficiencies in the credit union industry.

In summary, credit unions with over $100 million in assets will be categorized as Complex regardless of their portfolio composition or balance sheet concentration risk. Asset size does not equal balance sheet complexity. Given this, credit unions of $100 million or more will be required to weigh assets significantly higher than comparable banks, which will require them to set aside higher amounts of capital, which they cannot raise in the open market like their peer banks. Again, 4 years to raise capital through retained earnings is insufficient time to be effective without having to potentially harm their members.

There continues to be many concerns with this proposal and the dramatic adverse effect it would have on credit unions; thus, we believe that the need for any rule change should be re-evaluated and at the very least, some of the rule should be reconsidered based on comments provided.

Thank you for the opportunity to comment on this proposed rule and for considering our views on risk based capital requirements.

Sincerely,

Erin Mendez

Erin Mendez
President, Chief Executive Officer
Patelco Credit Union