March 30, 2015

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

RE: Comments on Proposed Rule: Risk-Based Capital; RIN 3133-AD77

Dear Gerald Poliquin,

Heritage Community Credit Union has Total Assets of $200MM and serves more than 13,000 Members in the Greater Sacramento Region. I appreciate the opportunity to provide comments to the National Credit Union Administration (NCUA) on its proposed amendments to the Risk Based Capital Rule (RBC2).

While appreciative for the revised proposal compared to the first, RBC2 is an overreach by NCUA and a solution to a problem that doesn't exist. I hear time and again that Credit Unions didn't cause the financial crisis, yet an ever-growing regulatory burden seems to punish credit unions that for the most part managed their balance sheets appropriately while also helping members during the recession. The market has removed the the non-viable credit unions.

One large problem with RBC2 is that it splits credit unions into two classes. While beneficial in number to smaller credit unions, this will cause a dangerous division in our industry based on the $100 Million Asset threshold. This plays into the banking lobby's hands of trying to split the credit union system by first only taxing the largest credit unions. As a collaborative system it is important that credit unions work together and remain unified under the same set of rules. If a small credit union has excessive risks to their capital, and therefore poses an elevated risk to the insurance fund, I want them held to the same standards that my Credit Union is held to.

I agree that the current RBNW methodology is outdated and does not accurately reflect the risk levels in individual credit unions. However, the regulatory net worth level is 7 percent. If that level is deemed inadequate, the NCUA should work with the credit union system to lobby Congress to weigh in on the issue and pass legislation to arrive at the appropriate net worth level. I think it's a mistake for the NCUA to bypass Congress with the RBC2 proposal.

Based on NCUA's own data, the number of credit union failures and losses to the insurance fund were reasonable, and lower than banks through the financial crisis. I believe this demonstrates that RBC2 is not even needed. While minor adjustments and lessons learned can certainly be adopted, dramatically altering credit union balance sheets and risk structures just isn't necessary. The proposal is a solution in search of a problem. Credit Unions exist for the benefit of members. If adopted, the impact to members will be excessive and disproportional compared to the benefits to the insurance fund. This will also force credit unions to pull back lending opportunities to low income communities for fear of carrying delinquent loans at elevated risk weightings. This seems to run contrary to other NCUA initiatives.

While the number of credit unions is continuing to decrease the largest (Greater than $1 Billion in Assets) continue to grow the fastest. As a result the credit union system is developing excessive concentration risk. More at-risk-assets and members are in large credit unions. If the credit union charter is not competitive and advantageous, large credit unions will begin to convert to banks. If only a handful of the largest credit unions were to leave the system, the entire credit union system, including the share insurance fund would become unsustainable. It is clear that RBC2 is one of two large events, the other being taxation, that could force these large credit unions to convert to a bank charter. While they would then be subject to risk based capital requirements of banks, they would have a more advantageous charter, such as the ability to raise supplemental sources of capital, not be subject to restrictive field of membership constraints, and more. While the revised proposal lessens this probability, it will increase from current levels. Some of the largest credit unions will leave the system, which increases the risk to the share insurance fund. I believe this risk trumps any lowering of risk RBC2 may provide.

CUSOs are an important tool for credit unions that allow for innovation and scale that individual credit unions often can't create alone. Investments in CUSOs are also an important part of a diverse earnings strategy that limits concentration risk from fewer product lines. Diversifying credit union assets to CUSOs creates less concentration risk to the individual credit union and the share insurance fund. I believe that the 150% risk weight for investments in CUSO's is still excessive and will limit the Credit Union System's future investment. While NCUA may view this as lowering risks related to CUSO, the added concentration risk for individual credit unions will increase as they try to force higher earnings within the credit union exclusively. We don’t believe a risk weighting greater than 100% is justified.

If NCUA ultimately adopts RBC2, the loophole for requiring even more capital of credit union needs to be eliminated. If RBC2 is designed to ensure adequate capital, then let the requirement stand on its own merits. Capital adequacy planning that individual credit unions do should not be subject to examination and supervision. Many credit unions use complex modeling scenarios which are built with overly conservative assumptions to start with, then compounded with worst- case event risks. This type of risk management oversight should be promoted in the credit union system. Models with worst-case scenarios are not realistic. This model output should not be used to force higher capital requirements. If RBC is adopted we believe no additional capital requirements should be possible.

I highlight concentration risk once again as a concern with RBC2. In today's market, car loans can appear more favorable compared to real estate based loans. However, given the dramatic increase in car lending for credit unions, the unordinary residual values present in the market today, and the high concentration of car loans for the credit union system, it is inevitable that when residual values fall, credit losses from car loans will spike. This is to say, that no matter what risk weighting you assign various assets, market conditions will change. It is not practical for the NCUA to change the risk weights frequently. In addition, doing so would require credit unions to catch up to the latest risk weights which in impractical and inefficient. I believe the lower risk rating of one asset class compared to another will force credit unions to take on excessive concentrations of lower risk weighted assets. This will actually increase concentration risk compared to a diverse balance sheet. Therefore, RBC2 is not needed and will likely cause more risk, not less for the system as a whole.

The risk weights as structured, will force credit unions to pull back on lending. We are chartered to provide lending services for our members thus contributing to economic growth in our communities. RBC2 is punitive and discourages lending. I believe more credit unions will become investment clubs instead of lenders of choice, which is detrimental to our movement, our members, and our communities.

If a credit union can obtain Supplemental Capital, their ability to take risk includes all capital not just that acquired through retained earnings. Investors are disclosed the fact that the investment is not insured. The investment is therefore, at risk of loss. If supplemental capital can't be included it defeats a major reasons for credit unions to have it in the first place. The NCUA has not articulated a compelling reason for excluding supplemental capital.

Natural person credit unions performed well compared to banks, given the once-in-generations financial crisis our country experienced. Lessons can be learned in the aftermath. However, RBC2 is not necessary and creates additional risks to collaborative credit union system. I do not believe RBC2 should be adopted as a final rule. However, if RBC2 is adopted, we believe its adverse impacts on credit unions and members can be further mitigated before a final rule is approved. Thank you for the opportunity to comment on this proposed rule and for considering our views on risk based capital.

Sincerely,

Ed Turk
President/CEO
Heritage Community CU

cc: CUNA, CCUL