

September 05, 2018

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-Supplemental Rule

Dear Mr. Gerald Poliquin,

I am writing on behalf of the California and Nevada Credit Union Leagues (Leagues), one of the largest state trade associations for credit unions in the United States, representing the interests of more than 260 credit unions and their approximately 10.7 million members.

The Leagues welcome the opportunity to provide comments to the National Credit Union Administration (NCUA) on their proposal to: (1) delay the effective date of the NCUA's October 29, 2015 final rule regarding risk-based capital (RBC 2015 Final Rule) for one year, moving the effective date from January 1, 2019 to January 1, 2020, and (2) amend the definition of a "complex" credit union for risk-based capital (RBC) purposes by increasing the threshold level for coverage from \$100 million to \$500 million.

The Leagues urge the NCUA Board to withdraw the RBC rule. While the RBC 2015 Final Rule is vastly improved over the original proposed rule, we continue to believe that an RBC rule is unnecessary given the solid performance of natural person credit unions and the National Credit Union Share Insurance Fund (NCUSIF) during the recent financial crisis. Further, we agree with Chairman McWatters' analysis at the time the rule was promulgated that the NCUA does not have the legal authority to implement a two-tier RBC system [\[1\]](#). For these reasons we continue to oppose the rule and recommend it be withdrawn.

Absent a full withdrawal of the RBC 2015 Final Rule, the Leagues generally support the current supplemental proposal, and we offer the following comments and recommendations that would better tailor the rule and provide further regulatory relief to credit unions.

### **Definition of Complex**

Under the RBC 2015 Final Rule, the NCUA determined that credit unions exceeding the \$100 million asset-size threshold had portfolios of assets and liabilities that were complex based on the products and services in which such credit unions engaged. The NCUA has further analyzed the impact of the NCUA's RBC requirements and the portfolios of assets and liabilities of credit unions to identify potential ways to reduce regulatory burden on credit unions.

As a result, the Board is now proposing to revise the original complexity index (revised complexity index or RCI) and to apply a new complexity ratio (CR) for analyzing the portfolios of assets and liabilities of credit unions to determine which are "complex."

### **Complexity Index**

The \$100 million asset threshold adopted in the RBC 2015 Final Rule for determining whether a credit union is complex was based on a complexity index (original complexity index or OCI). The OCI counted the number of complex products and services provided by credit unions based on several indicators. However, the OCI did not consider the volume of the complex activity engaged in by such credit unions.

The Board has proposed a revised complexity index that makes six changes to the original complexity index. The Leagues agree with each of the six proposed changes to the RCI. We also encourage the NCUA to use the delayed effective date to revisit the individual risk-weightings to ensure proper balance between an activity's true risk and its risk weight.

The Leagues note that NCUA's data show 53 percent of credit unions with assets between \$500 million and \$750 million engage in six or more complex activities; however, for credit unions with assets greater than \$1 billion, this number increases to 77 percent. This is an important distinction when determining an appropriate asset size threshold.

### Complexity Ratio

In addition to the revised complexity index, the NCUA is also proposing to use a ratio of complex assets and liabilities to total assets (complexity ratio or CR) to evaluate the extent to which credit unions are involved in complex activities.

The numerator of the CR would be the dollar value sum of the complex assets and the liabilities held by a credit union (where complex assets and liabilities are determined using the same complexity indicators as used in the RCI). The denominator of the CR would be the total assets of the credit union.

NCUA's analysis shows that the CR increases from 23 percent among credit unions with less than \$500 million in assets to 40 percent among credit unions with more than \$500 million in assets. Further, the data shows two-thirds of credit unions with more than \$500 million in total assets have a CR above 30 percent; while only 11 percent of credit unions with less than \$500 million have a CR above 30 percent.

The Leagues agree with the use of a CR as a method to consider the volume of complex activity and to set the asset size threshold more judiciously. However, the NCUA's data does not provide CR categorization at other asset levels. We recommend the NCUA consider how the CR for credit unions with \$500 million in assets compares to those with \$1 billion in assets.

We also suggest the CR can be utilized by the agency as a way to prioritize supervisory oversight of covered credit unions.

### Asset Threshold

Based on the RCI and new CR, the Board believes that \$500 million in total assets would be a more appropriate threshold level for defining a complex credit union and would reduce regulatory burden on credit unions by more closely tailoring the applicability of the NCUA's risk-based capital requirement to cover only those credit unions that, if they failed individually, could present an undue risk of loss to the NCUSIF.

The Leagues fully support increasing the threshold level. However, we suggest the NCUA review more detailed RCI and CR data and consider increasing the threshold level for RBC coverage to \$1 billion.

As of the first quarter of 2018, there were 297 credit unions (approximately 5%) with more than \$1 billion in assets. These credit unions pose a risk to the NCUSIF given that they hold over 63 percent of total assets. Also, based on the RCI, and as noted above, 77 percent of credit unions with assets greater than \$1 billion engage in six or more complex activities. Unfortunately, the NCUA did not provide CR data for asset levels greater than \$500 million. This information should be provided and considered in setting the asset size threshold.

### Continue Improvements

While the Leagues agree the asset size threshold should be raised, and we recommend it be increased to \$1 billion, we continue to believe that an asset threshold oversimplifies the complexities of the balance sheet and may cover more credit unions than Congress intended. The Leagues encourage the NCUA work to more precisely define "complex".

Congress' directive to NCUA for designing the risk-based net worth requirement was to address those risks for which the standard leverage ratio was insufficient<sup>[2]</sup> and to base its definition of "complex" credit unions "on the portfolios of assets and liabilities of credit unions."<sup>[3]</sup> It is hard to believe Congress envisioned that nearly 30 percent of credit unions would be considered complex, as would be the case with the current \$100 million asset threshold. At \$500 million, nearly 10 percent would be considered complex, and at \$1 billion, only five percent of credit unions would be considered complex. A \$1 billion complexity threshold would more closely align with the spirit of § 1790 of the Federal Credit Union Act.

## **Delay Effective Date**

The NCUA Board proposes to delay the effective date of the RBC 2015 Final Rule for one year, in part because the NCUA needs additional time to prepare for the rule's implementation. The NCUA says that "based on feedback from the credit union community and agency staff" more time is needed to make necessary adjustments to systems, processes, and procedures.

The Leagues support delaying the effective date of the RBC 2015 Final Rule; however, the Leagues recommend a two-year delay. We believe a two-year delay will provide credit unions and the agency sufficient time to implement necessary systems, processes, and procedures; will allow credit unions time to assess how a final rule on supplemental capital may be utilized for their RBC purposes; and will provide a consistent target date for covered credit unions' work efforts.

## **Implementation Complexity**

The effective date of the RBC 2015 Final Rule is January 1, 2019, providing credit unions with a little more than three years to implement. While credit unions have and will continue to work diligently to meet their deadline, the timeline does not allow sufficient implementation time. The Leagues recommend the NCUA Board provide a full five-year implementation timeframe. The credit union system is healthy and strong and the NCUA can allow more time for covered credit unions to make the strategic and operational changes necessary to prepare for RBC requirements.

## **Align with Legislative Efforts**

The Leagues would also like to note that recent legislative actions also reflect the opinion that a two-year implementation delay is necessary. We recommend aligning the effective date with the timeframe set forth in Section 701 of HR 5841, the *Foreign Investment Risk Review Modernization Act of 2018*. HR 5841 delays the effective date until January 1, 2021. Having a consistent effective date will allow covered credit unions to employ their resources appropriately and ensure their efforts are not wasted.

## **Supplemental Capital for RBC Purposes**

Under the RBC 2015 Final Rule, the Board declined to permit credit unions (other than low-income credit unions) to include other supplemental forms of capital in the RBC ratio numerator. However, the Board issued an advanced notice of proposed rulemaking in February 2017 and specifically requested comments on how supplemental capital can work for risk-based capital purposes. The Leagues support permitting all federally insured credit unions to issue supplemental capital that would count towards their risk-based net worth requirement. We strongly urge the NCUA finalize a supplemental capital rule before the effective date of the RBC rule and provide credit unions with the necessary tools to manage RBC requirements.

## **Conclusion**

The Leagues commend the NCUA Board for their efforts to establish a more appropriate and tailored threshold level for defining a complex credit union. We suggest the NCUA review more detailed RCI and CR data and consider increasing the threshold level for RBC coverage to \$1 billion. We also recommend delaying the effective date of the RBC 2015 Final Rule for two years, moving the effective date from January 1, 2019 to January 1, 2021.

Thank you for the opportunity to comment on the proposed RBC supplemental rule and for considering our views and recommendations. If you have any questions regarding our comments, please contact me.

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[1] Board Member J. Mark McWatters Statement on the Final Risk-Based Net Worth Rule; available at: <https://www.ncua.gov/newsroom/Pages/speeches/2015/october/McWatters-Statement-Final-Risk-Based-Net-Worth-Rule.aspx>

[\[2\]](#) 12 U.S.C. § 1790d(d)(2).

[\[3\]](#) 12 U.S.C. 1790d(d).

Sincerely,

Diana Dykstra  
President and CEO  
California and Nevada Credit Union Leagues

cc: CCUL