



The National Voice of the State Credit Union System

July 26, 2019

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

Re: NASCUS Comments on Proposed Rule: Risk-Based Capital – Delay of Effective Date

Dear Mr. Poliquin:

The National Association of State Credit Union Supervisors (NASCUS)¹ submits the following in response to the National Credit Union Administration's (NCUA's) request for comments on the proposed further delay of the effective date of NCUA's October 29, 2015, final rule implementing a new regulatory framework for risk-based capital.² NCUA states that the proposed delay of the effective date of the rule from January 1, 2020 to January 1, 2022 would provide credit unions more time to prepare for implementation of the rule as well as provide NCUA an opportunity for a "comprehensive and holistic" evaluation of the 2015 final risk-based capital rule.³ In particular, NCUA identifies the establishment of an alternative leverage ratio, subordinated debt rules, and securitization rules as under consideration for incorporation into the risk-based capital framework.⁴ Should NCUA approve a delay to the effective date of the 2015 risk-based capital rule, NCUA's current Prompt Corrective Action rules (PCA) would remain in effect.

Further delaying the effective date of risk-based capital rules is not without controversy. However, given the critical importance of promulgating subordinated debt rules for inclusion in the risk-based capital framework, NASCUS supports a delay in the effective date of the final rule. NASCUS also supports evaluating the merits of an alternative leverage ratio (ALR) so long as care is given to ensure an ALR provides regulatory relief rather than inadvertently creates regulatory burden. Of course, NCUA should continue to work with state regulators in evaluating and developing the appropriate framework within which to supervise credit union balance sheet risk and capital sufficiency. Finally, should the effective date of the 2015 final rule continue to be delayed, NCUA should make changes to its existing PCA rule to correct deficiencies in the existing PCA framework.

NASCUS recognizes the utility of risk-based capital requirements for enhancing safety and soundness. Ensuring that credit unions choosing to hold higher risk on their balance sheets also hold appropriate levels of corresponding capital is sound regulatory practice, consistent

¹ NASCUS is the professional association of the nation's 45 state credit union regulatory agencies that charter and supervise over 2,100 credit unions.

² 80 Fed. Reg. 66625 (October 29, 2015).

³ 84 Fed. Reg. 30048 (June 26, 2019).

⁴ Ibid at 30049.

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with the prevailing supervisory trends world-wide, and a prudent measure to mitigate potential losses to the National Credit Union Share Insurance Fund.

Delaying Effective Date of Final Risk-Based Capital Rule

NCUA has repeatedly and unequivocally assured stakeholders that final risk-based capital rule implementation would be **preceded** by supplemental capital rulemaking.⁵ NASCUS has been steadfast in our conviction that a framework for supplemental capital is essential for a credit union risk-based capital rule.⁶ We urge NCUA to work with state regulators expeditiously to promulgate a subordinated debt rule and concur that the effective date of the 2015 risk-based capital rule should be delayed until subordinated debt rules are finalized. We also note that supervisory guidance has yet to be issued to examiners and industry to assist in implementing the risk-based capital rules and uncertainty remains related to fields 22-46 on the 5300 Call Report intended to capture risk-based capital related information.⁷

While NASCUS recognizes and respects the supervisory consensus that a risk-based capital framework is a necessary element of a robust regulatory system, we must support delaying the effective date at least until the subordinated debt rules are finalized, appropriate guidance issued, and Call Report changes are published. Although this delay may result in controversy, it is necessary to remain consistent with the NCUA's well-founded commitment to include elements that are not yet complete.

⁵ See National Credit Union Administration, Final Rule; Risk-Based Capital, 80 Fed. Reg. 66626, 66660 (Oct. 29, 2015) (“the Board plans to address additional forms of supplemental capital in a separate proposed rule, with the intent to finalize a new supplemental capital rule before the effective date of this risk-based capital final rule.”);

See also NCUA Board Member Mark McWatters Statement on the Final Risk-Based Capital Net Worth Rule (Oct. 29, 2015) <https://www.ncua.gov/newsroom/Pages/speeches/2015/october/McWatters-Statement-Final-Risk-Based-Net-Worth-Rule.aspx>.

See also NCUA, *Report to the House Financial Services Committee on the Final Risk-Based Capital Rule*, November 2015. Available at <https://www.ncua.gov/regulation-supervision/Documents/RBC/final-risk-based-capital-rule-report.pdf>. (accessed August 27, 2018).

See also NCUA's *Frequently Asked Questions about NCUA's Risk-Based Capital Final Rule*, October 2015. Available at <https://www.ncua.gov/Legal/Documents/RBC/RBC-Final-Rule-FAQs.pdf>. (accessed August 27, 2018). Question #10 reads in full:

Q10. Will credit unions be authorized to raise supplemental capital for purposes of risk-based net worth? Yes. The NCUA Board plans in a separate proposed rule to address comments supporting additional forms of supplemental capital. As the risk-based capital final rule does not take effect until January 1, 2019, there is ample time for the NCUA Board to finalize a new rule to allow supplemental capital to be counted in the risk-based capital numerator before the effective date.

⁶ See NASCUS comments to NCUA September 7, 2018, available at <https://nascus.org/regulatory-resources/09-07-18%20RBC%20supplement%20proposal%20comments.pdf>; and NASCUS comments to NCUA November 20, 2017, available at <https://nascus.org/regulatory-resources/11.20.17%20reg%20reform%20comments.php>; NASCUS comments to NCUA May 9, 2017, available at <https://nascus.org/regulatory-resources/05.09.17%20Comment%20alt%20capital%20anpr.php>; and NASCUS comments to NCUA, April 27, 2015, available at <https://nascus.org/RBC2%20Comment%20Letter.pdf>.

⁷ 83 Fed. Reg. 4518 (January 31, 2018). See NASCUS Comments on Proposed Call Report Modernization, available at <http://nascus.org/regulatory-resources/04.03.18%20comment%20call%20report%20profile.php>.

In addition, NASCUS recognizes that for some credit unions the regulatory certainty of implementation on January 1, 2020 is preferable to the “Sword of Damocles” nature of ever-present risk-based capital rules that never take effect yet are never repealed. Since 2015, “covered credit” unions have, in theory, managed their balance sheets with an eye toward the effective date of the risk-based capital rule. As we approach the four-year mark of suspended implementation, it seems reasonable that the NCUA should formally announce that the NCUA does not plan to allow the present risk-based capital rules to become effective in their current, unrevised form. To provide greater certainty with respect to the risk that the 2015 risk-based capital rule might nevertheless take effect, the NCUA Board has authority also to rescind the 2015 rule, and to announce that it will be replaced with a new rule in which the flaws of the 2015 are remedied and the NCUA is prepared to move forward with implementation.

Alternative Leverage Ratio

NASCUS supports evaluating the establishment of an alternative leverage ratio akin to what has been proposed by banking regulators.⁸ As we recommended to NCUA in 2018, NCUA should consider whether it would be appropriate, from both a supervisory perspective and a credit union operational perspective, to create an alternative leverage ratio for complex credit unions (sometimes referred to as an “off-ramp”).

As NCUA considers whether to create an “off ramp” for complex credit unions, we urge the agency to be mindful of the following:

- Use of an alternative leverage ratio should be limited to qualifying credit unions. Clear eligibility requirements should be established to ensure that use of the alternative leverage ratio is appropriate for the particular credit union.
- Qualifying credit unions should be allowed the operational flexibility to choose, at any time, to meet the alternative threshold or comply with the risk-based requirements.
- If a credit union has chosen the alternative leverage ratio, and subsequently falls below that threshold, the regulation should require the credit union to begin reporting under the risk-based rules to determine whether PCA applies. Applying PCA to a credit union that falls below the alternative leverage ratio, but whose balance sheet when risk weighted complies with the final risk-based capital rule would be to contort intended regulatory relief into a regulatory burden.⁹

Consulting and Cooperating with State Regulators

State regulators have experience with risk-based capital regulation and supervision in state-chartered commercial banks. Congress recognized this expertise when it directed NCUA to

⁸ See 84 Fed. Reg. 3062 (Feb. 8, 2019).

⁹ See *Proposed Community Bank Leverage Ratio Would Provide Reg Burens Not Relief*, James Cooper, CSBS online (February 15, 2019). Available at <https://www.csbs.org/proposed-community-bank-leverage-ratio-would-provide-reg-burden-not-relief>.

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consult and work cooperatively with state regulators when implementing the PCA framework of Part 702.¹⁰ NCUA should continue to collaborate with state regulators to develop subordinated debt rules, fine tune the risk weightings of the 2015 risk-based capital rule, and evaluate whether an alternative leverage ratio would be beneficial to the credit union system.

Amending the Existing PCA Rules

Prior to 2015, various shortcomings in NCUA's existing PCA rules had been identified. Some of those deficiencies were resolved by the passage of the 2015 final Risk-Based Capital rule. However, should the NCUA Board finalize a further delay in the 2015 risk-based capital rule, the existing PCA rules would remain in effect.¹¹ In that case, NCUA should make necessary adjustments to the existing PCA rules to remedy the shortcomings for the interim period before the effective date of the 2015 rules. For example, the existing PCA rule's treatment of loans sold with recourse fail to distinguish between loan transfers that qualify for true sale accounting pursuant to Generally Accepted Accounting Principles as well as transfers of loans with recourse partially guaranteed by a government entity.

At a minimum, NCUA could adopt the 2015 final rule's asset threshold to provide relief to credit unions under \$500 million in assets from the ongoing current PCA risk-based capital rules. However, we note that even such a remedy would inappropriately leave the remaining covered credit unions exposed to previously acknowledged flaws in the existing PCA treatments of some recourse loans. In light of the proposed further delay, these issues must be addressed.

NASCUS appreciates the opportunity to submit comments on the NCUA Board's proposal to further delay the effective date of the 2015 final risk-based capital rule. We would be happy to discuss our comments and recommendations in more detail at NCUA's convenience.

Sincerely,

- signature redacted for electronic publication -

Brian Knight
Executive Vice President & General Counsel

¹⁰ 12 U.S.C. §1790(l).

¹¹ 84 Fed. Reg. 30048 (June 26, 2019).