July 26, 2019

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

Re: Delay of Effective Date of the Risk-Based Capital Rules, RIN 3133-AF01, 84 Fed. Reg. 30,048 (June 26, 2019)

Dear Mr. Poliquin:

Better Markets[1] appreciates the opportunity to comment on the notice of proposed rulemaking captioned above ("Proposal" or "Release"),[2] issued by the National Credit Union Administration Board ("NCUA" or "Board"), that would further delay the effective date of enhanced risk-based capital standards for credit unions, which were originally finalized in 2015 ("Final Rule").[3] If approved, the Proposal would constitute the second delay of the effective date. As originally finalized, the capital rules would not have gone into effect until January 1, 2019, more than three years after the rule was finalized. Nevertheless, on October 29, 2018, less than three months before the original effective date, the NCUA finalized a year-long delay of the effective date to January 1, 2020 ("2018 Delay").[4] Now, the NCUA, less than a year after finalizing the 2018 Delay, is proposing to delay the effective date yet again, this time for another **two full years, to January 1, 2022.**

The proposed delay is misguided, contrary to statutory requirements, arbitrary and capricious, and it should be withdrawn. It is dangerous regulatory policy, as it would postpone the implementation of important capital requirements designed to help maintain the financial stability of the largest credit unions; it conflicts with Congress' mandate that credit unions be subject to

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[1] Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system, one that protects and promotes Americans' jobs, savings, retirements, and more.

[2] 84 Fed. Reg. 30,048 (June 26, 2019).

[3] Risk-Based Capital, 80 Fed. Reg. 66,626 (Oct. 29, 2015).

[4] Risk-Based Capital, 83 Fed. Reg. 55,467 (Nov. 6, 2018).

robust oversight that keeps pace with bank supervision; and it lacks any credible, empirically-supported basis.

As purported justification for further delay, the NCUA cites three tangential issues—asset securitization, subordinated debt, and the community bank leverage ratio option for commercial banks, created by the Economic Growth, Regulatory Relief and Consumer Protection Act ("S. 2155"), signed into law on May 24, 2018.[5] However, the NCUA does not explain why consideration of these tangential issues warrants a wholesale delay of the effective date of the capital rule. Nor does it explain why these issues necessitate a further delay when all of them had arisen at the time the Board issued the 2018 Delay. The NCUA also claims that credit unions need additional time for implementation. This assertion is implausible on its face, since only the largest credit unions face compliance obligations under the Final Rule and since those credit unions will have had well over **four years** to prepare for the new rules. However, beyond vague and conclusory statements, the NCUA does not substantiate this purported need for an extension. Nor does the NCUA explain its change in position from less than a year ago, when it avowed that a one-year delay of the original effective date was more than sufficient.

If the proposed delay is finalized, the NCUA will not only be violating the law, including basic requirements for rational rulemaking under the Administrative Procedure Act, but also recklessly and needlessly exposing credit unions to heightened instability, in turn threatening the well-being of their members, the share insurance fund ("SIF") and the financial system as a whole. The current, long-standing economic expansion will inevitably end and bring with it a period of financial stress, very possibly before the proposed delayed compliance date in 2022. If it does, and if the current capital standards, which the NCUA has previously characterized as inadequate, are still in place, then more credit unions will fail, more credit union members will lose access to credit, and the share insurance fund ("SIF") will be further depleted.

For all of these reasons, the Proposal is arbitrary and capricious and contrary to law. Accordingly, it is vulnerable to legal challenge in court.

COMMENTS

I. Delaying the Final Rule Will Imperil the Survivability of Credit Unions and Threaten Members' Access to Credit and Other Critical Financial Services.

A. Credit unions are an important provider of financial services.

Credit unions serve a vital role in the American financial system. They are broadly similar to commercial banks in that they "accept deposits, make loans and provide a wide array of other financial services." [6] However, they differ from commercial banks in crucial ways. Whereas

[5] Pub. L. No. 115-174 (2018).
[6] https://www.mycreditunion.gov/about-credit-unions/credit-union-different-than-a-bank-text-only

commercial banks are for-profit institutions owned by shareholders, credit unions are non-profit banks owned by their members.[7] Moreover, credit unions serve specific communities, i.e. their "field of membership," which may be, for example, people from a certain geographic location or employees of a specific company.[8]

Because credit unions cater to specific communities, they often meet unique financial needs in those communities, which may not be well-served by commercial banks. For members of those communities, particularly communities that are underserved or poorly served by for-profit commercial banks, credit unions are often a crucial provider of financial services. If members of credit unions are unable to access these financial services—either because their credit union has failed or because their credit union is restricting its lending and other activities due to financial constraints—they may not be able to access those services and they may have to turn to more costly and less convenient service providers or even predatory firms.

B. As the NCUA has recognized, improving the currently inadequate capital standards is crucial for credit unions and their members.

The same characteristics noted above that make credit unions important and unique financial services providers can lead to increased risk. Limited fields of membership mean credit unions may have less ability to diversify risk and may see higher risk concentrations in particular types of customers, assets, or industries.[9] Thus, robust capital requirements are particularly important for credit unions. As the NCUA noted in 2015, higher "levels of capital can reduce the probability of a systemic crisis, allow credit unions to continue to serve as credit providers during times of stress without government intervention, and produce benefits that outweigh the associated costs."[10]

The 2007-2009 crisis revealed that the current capital and net worth regime for credit unions is inadequate. While credit unions fared better than commercial banks during the crisis (a low bar to be sure), credit unions "also experienced elevated losses and the need for government intervention" during the crisis, including significant injections of liquidity, government guarantees, and government loans.[11] Credit union failures resulted in costs of at least $728 million to the SIF.[12] Credit unions also took bailouts from programs such as the Community Development Capital Initiative[13] and the Temporary Corporate Credit Union Stabilization Fund.[14] And, absent

[7] *Id.*
[8] *Id.*
[9] *See* W. Scott Frame, Gordon V. Karels & Christine McClatchey, *The Effect of Common Bond Membership Expansion on Credit Union Risk*, 37 FIN. REV. 613, 617 (noting that restrictions on credit union membership "tend to create significant portfolio concentration risks").
[10] Final Rule at 66,629.
[11] Final Rule at 66,630.
[12] Final Rule at 66,630.
[13] https://www.treasury.gov/press-center/press-releases/Pages/tg885.aspx.
[14] https://www.ncua.gov/support-services/corporate-system-resolution/stabilization-fund-history.

these and other extraordinary measures, "the NCUA estimates as many **as 2,500 consumer credit unions would have failed** at additional cost to the Share Insurance Fund."[15]

By delaying the Final Rule, the NCUA unnecessarily risks a repeat of these scenarios. Indeed, the Congressional Budget Office has estimated that, if the Final Rule is further delayed, the NCUA will be expected to spend $26 million to resolve failed credit unions from 2020-2022.[16] Essentially, delaying the Final Rule materially increases the risk of credit union instability, threatening their safety and soundness, the wellbeing of their members, the funds in the SIF, and, ultimately, the financial system as a whole.[17]

II. Delaying the Final Rule Conflicts with Congressional Mandates that NCUA Capital Rules Adequately Address Risks and Harmonize with the Framework for Commercial Banks.

Further delaying the effective date of the Final Rule would conflict with longstanding Congressional intent, reflected in mandates for robust federal oversight of credit unions dating back to the Federal Credit Union Act of 1934.[18] Congress has specifically directed the NCUA, in implementing capital standards, to ensure that those standards are sufficiently robust to adequately address risks to credit unions.[19] Yet as the NCUA recognized when it issued the Final Rule, the current capital framework for credit unions "is ineffective and has not been materially updated since 2002."[20] Allowing that ineffective set of regulations to linger in place for two more years, in addition to the long period of delay that has already transpired since adoption of the Final Rule in 2015, plainly conflicts with this Congressional directive.

In addition, the Federal Credit Union Act, as amended, requires that the NCUA establish a prompt corrective action ("PCA") capital framework, and it further requires that this framework be consistent with the PCA framework applicable to commercial banks.[21] As the NCUA noted in the Final Rule, the PCA framework for commercial banks has been substantially revised. Here again, additional delay of the Final Rule, which is necessary not only to adequately address risks faced by credit unions but also to ensure that the PCA framework for credit unions is consistent

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15 Final Rule at 66,630 (emphasis added).

16 https://www.cbo.gov/system/files/115th-congress-2017-2018/costestimate/hr4464.pdf.

17 While credit unions, on average, are smaller than commercial banks, and have a smaller footprint than commercial banks, they still are significant parts of the financial system, collectively holding over $1.5 **trillion** in assets. https://www.ncua.gov/files/publications/analysis/industry-at-a-glance-march-2019.pdf. Consequently, widespread trouble at credit unions could certainly imperil the financial system as a whole, or specific segments of the financial system—particularly if credit unions continue to have weaker capital standards than other financial institutions such as commercial banks.

18 Pub. L. No. 73-467.

19 Final Rule at 66,640-41.

20 Final Rule 66,629.

21 12 U.S.C. § 1790d(b)(1)(A)(ii).

with the framework applicable to commercial banks, would directly contravene congressional intent.

III. There Is No Credible Basis for the Proposal.

Basic administrative law requires that an agency "articulate[] a satisfactory explanation for its action including a rational connection between the facts found and the choice made."[22] This is not necessarily intended to be a particularly high bar—a "court is not to substitute its judgment for that of the agency"[23] and should "uphold a decision of less than ideal clarity if the agency's path may reasonably be discerned"[24]—but the Proposal fails to come close to clearing it.

Instead of "less than ideal clarity" that still allows its path to "reasonably be discerned," the Board does not even attempt to adequately support the purported justifications for the proposed delay, nor does it make any actual attempt to rationally relate these justifications to the proposed delay. The Proposal is inadequate.

Taking up a mere three pages in the Federal Register, the Proposal offers no credible basis for the proposed delay of the Final Rule. The omission of a properly supported justification or rationale for a rule proposal is always significant under the Administrative Procedure Act, but it is especially striking when the stakes are so high: It is clear that further delay imperils the safety and soundness of credit unions, threatens to inflict substantial hardship on their members, and conflicts with congressional intent.

The NCUA briefly cites three issues, tangentially related to capital, in support of further delay in the Final Rule:

- **Asset Securitization:** The NCUA claims that, because credit unions have authority to issue and sell securities, "capital standards should properly account for any asset securitization conducted by federally insured credit unions."

- **Subordinated Debt:** The NCUA claims that it needs additional time to explore allowing some forms of subordinated debt to count as capital for purposes of the risk-based capital requirements.

- **Community Bank Leverage Ratio:** The NCUA claims that it needs additional time to analyze the proposed community bank leverage ratio framework issued by banking regulators for commercial banks pursuant to S. 2155.[25]

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22 *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).
23 *Id.* at 514.
24 *Bowman Transp., Inc. v. Arkansas–Best Freight System, Inc.,* 419 U.S. 281, 286 (1974).
25 Release at 30,049.

Even assuming that these issues warrant study for another two years, in none of these cases does the NCUA explain **why** a delay of the effective date of the Final Rule until January 1, 2022 is necessary or appropriate. In particular, the NCUA does not explain why it cannot allow the Final Rule to go into effect as currently scheduled on January 1, 2020, while considering those issues and then, as it may deem necessary or appropriate, later amend the Final Rule. Moreover, the NCUA's citation of these issues as justification for the proposed delay rings hollow considering that **each of these issues had already arisen as of October 2018, when the NCUA finalized the 2018 Delay less than a year ago.**[26] The NCUA offers no explanation as to why these issues suddenly warrant an additional two-year delay on top of the one-year delay it recently finalized. This raises a strong inference of pretext—as the Supreme Court has recently noted, "[r]easoned decision making under the Administrative Procedure Act calls for an explanation for agency action," and when what an agency provides is "more of a distraction" in the form of pretext, the agency's action is invalid.[27]

The NCUA's other justification for the proposed delay—that credit unions and the NCUA need more time for implementation—fares no better. The NCUA provides no evidence whatsoever showing that credit unions or the NCUA needs more time to adjust to the Final Rule. Nor does the NCUA explain its sudden and drastic change in course. In 2018, it concluded that "a one-year delay is sufficient" given that "covered credit unions and the NCUA have had more than three years to prepare for its final implementation" and that the resulting four-year total implementation period "should be more than sufficient to allow credit unions to incorporate" the changes in the Final Rule.[28] Yet it now asserts that a doubling of the 2018 extension is necessary, all without accounting for such a dramatic change in position.

Indeed, this failure to explain its departure from its previous position that an additional one-year delay was "more than sufficient" is also fatal to the Proposal. The law clearly provides that when an agency departs from a prior position, it must "display awareness that it *is* changing position" and "must show that there are good reasons for the new policy."[29] Moreover, when a "new policy rests upon factual findings that contradict those which underlay [an agency's] prior policy," the agency must "provide a more detailed justification than what would suffice for a new policy created on a blank slate."[30] This is because, when changing policies, "a reasoned explanation is needed for disregarding facts and circumstances that underlay or were engendered by the prior policy."[31] Less than one year ago, considering all of the same factors that it now claims warrants an additional two-year delay of the effective date of the Final Rule to January 1, 2022, the NCUA deemed delaying the effective date by just a year to January 1, 2020 "more than

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[26] While it is true that the banking agencies had not yet proposed a community bank leverage ratio rule in October 2018, S. 2155, which was passed in May 2018, mandated such a rule.

[27] Dep't of Commerce v. New York, 139 S. Ct. 2551, 2576 (2019).

[28] 2018 Delay at 55,469.

[29] *F.C.C. v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009) (emphasis in original).

[30] *Id.*

[31] *Id.*

sufficient." The agency's change in course, without an adequate justification, renders the Proposal fatally flawed.

CONCLUSION

In summary, the Proposal on its face lacks a sufficiently detailed and persuasive justification for such a significant change in the effective date of the Final Rule, particularly since the delay would imperil the safety and soundness of credit unions, threaten the financial well-being of credit union members, and directly conflict with congressional intent. The Proposal should be withdrawn and the Final Rule allowed to take effect on January 1, 2020.

We hope these comments are helpful as you evaluate the Proposal.

Sincerely,

Dennis M. Kelleher
President & CEO

Stephen W. Hall
Legal Director and Securities Specialist

Jason R. Grimes
Senior Counsel

Better Markets, Inc.
Suite 1080
1825 K Street, N.W.
Washington, D.C. 20006
(202) 618-6464

dkelleher@bettermarkets.com
shall@bettermarkets.com
jgrimes@bettermarkets.com

www.bettermarkets.com