Robert M. Fisher, *Chairman*
Brad M. Bolton, *Chairman-Elect*
Russell L. Laffitte, *Vice Chairman*
Gregory S. Deckard, *Treasurer*
Tim R. Aiken, *Secretary*
Noah W. Wilcox, *Immediate Past Chairman*
Rebeca Romero Rainey, *President and CEO*

May 10, 2021

Ms. Melane Conyers-Ausbrooks
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

Re: Simplification of Risk-Based Capital Requirements

Dear Ms. Conyers-Ausbrooks:

The Independent Community Bankers of America ("ICBA")[1] appreciates the opportunity to provide comments on the National Credit Union Administration's (NCUA) advance notice of proposed rulemaking titled *Simplification of Risk-Based Capital Requirements.* In ICBA's view the proposed rule's alternative for adoption of a credit union leverage ratio in lieu of risk-based capital requirements is a practical approach that deserves further discussion and study but only when such an alternative is adopted in a very stringent manner identical to the current framework imposed on community banks and only when the other option is full adoption of the provisions of the Basel III capital framework as it is currently adopted by community banks. Of the two alternatives, the minimum risk threshold approach with static buffers would be the easiest to comply with since it appears to closely resemble the current credit union net worth capital standard.

Background: The advance notice of proposed rulemaking seeks to provide two alternatives to the adoption of risk-based capital requirements by complex credit unions set to become effective on January 1, 2022. Under the risk-based capital requirement framework, credit unions with total assets greater than $500 million would be subject to tailored capital requirements depending

[1] The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. With more than 52,000 locations nationwide, community banks constitute 99 percent of all banks, employ more than 760,000 Americans and are the only physical banking presence in one in five U.S. counties. Holding more than $4.9 trillion in assets, $3.9 trillion in deposits, and $3.4 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at www.icba.org.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

on the type and quantity of assets held by the institution. Assets deemed to be of greater risk would carry a heavier risk weight requiring more capital to be held by the credit union to protect against unexpected losses. With the introduction of these two alternatives, the NCUA is attempting to address concerns by stakeholders that capital requirements should be tailored to the risks of credit unions and should avoid unnecessary regulatory burden.

Alternative one introduces a risk-based leverage ratio (RBLR) for complex credit unions. The RBLR establishes a minimum risk threshold for all complex credit unions to be considered well capitalized equal to seven percent, with additional required buffers when a credit union triggers additional risk thresholds and when a credit union triggers the maximum risk thresholds. Risk thresholds would be categorized based on the NCUA's 2015 final rule on current capital adequacy regulations that introduced the risk-based capital ratio and would include such items as noncurrent loans, commercial loan concentrations, junior lien concentrations, and other investment activities with perceived heightened risk like mortgage servicing rights. This alternative essentially establishes three tiers of minimum leverage requirements for complex credit unions based on risk in order to be considered well capitalized. Tier one, a minimum threshold tier, would prescribe a seven percent net worth ratio with no additional buffers. Tier 2 would prescribe a seven percent net worth ratio plus buffer "A" for those credit unions whose risk profile is elevated enough to trigger the need for more capital. Tier 3 would prescribe a seven percent net worth ratio plus buffer "B" for those credit unions whose risk profile is elevated enough to trigger the maximum risk threshold.

Alternative two introduces a complex credit union leverage ratio (CCULR), which is essentially designed to mimic the existing community bank leverage ratio (CBLR) that is eligible for qualifying community banking organizations. If the NCUA were to adopt this alternative, the agency would need to establish a minimum nine percent ratio equal to tier 1 capital divided by total consolidated assets if the ratio were to be comparable to the CBLR.

ICBA Comments: ICBA appreciates the credit union industry's complaint that increased regulation impairs the ability of community financial services organizations to efficiently serve their communities. ICBA supports a tiered regulatory capital system for determining sufficient amounts of capital in order to achieve an adequate balance of proper supervision with sufficient freedom to provide financial services to the customer so that community banks continue to thrive. But the current advanced notice of proposed rulemaking presents many challenges,

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

concerns, questions, and confusion considering the state of regulatory capital rulemakings put forth by the NCUA.

Most baffling to community bankers is the fact that risk-based capital requirements have yet to be implemented for credit unions yet the NCUA is already proposing alternatives to simplify regulatory capital requirements. While community banks of all sizes and complexities have been forced to comply with the risk-based provisions of the Basel III capital framework, NCUA appears to be already rejecting its previously passed final rules on risk-based capital requirements even though such provisions already exempt the smallest credit unions that would have the most difficulty obtaining the resources needed to apply a risk-based capital standard. What difficulties and challenges has the NCUA observed in a risk-based capital requirement for complex credit unions? Has the NCUA consulted with the other prudential banking regulators to learn how similar sized community banks comply with risk-based capital under Basel III? Why does the NCUA believe that risk-based capital is appropriate for community banks but alternatives should be considered for federally-insured credit unions before the capital rule takes effect?

The proposed RBLR approach is a very simplistic concept that appears to be very similar to the net worth ratio that credit unions currently follow. The RBLR is a single unilateral threshold ratio that credit unions must target as a mandatory requirement with prescribed additional buffers under certain concentration risk factors. The RBLR is indeed a simple alternative as the NCUA is looking to produce in this advance notice of proposed rulemaking and one that we believe the industry would favor. However, an open question remains about when a buffer “A” trigger has occurred for additional risk thresholds and when a buffer “B” trigger has occurred for maximum risk thresholds. And how does the regulator know that the “B” trigger contains a sufficient buffer needed to avoid risk of insolvency? More details about buffer triggers would need to be explored to determine if buffer “A” and buffer “B” are sufficient to protect the share insurance fund.

Provided that the NCUA is willing to accept a current leverage ratio that is the same that is applied to community banks, the proposed CCULR approach would generally require the most capital for complex credit unions and would be the closest to being comparable to community bank capital requirements. The proposal does not definitively state that a nine percent CCULR would be the minimal accepted level but such a ratio should not fall below a level comparable to that of the CBLR if the NCUA seeks to maintain healthy, well-capitalized credit unions.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

Additionally, because the CBLR only applies to community banks with total consolidated assets under $10 billion, the same requirement should be applied to credit unions under a CCULR approach. And of course as we have consistently stated to the NCUA the default approach for a credit union capital standards framework should always be a Basel III approach that is no less stringent than the capital standards that are currently applied to community banks regardless of size.

The advance notice appropriately raises the question of how subordinated debt issued by complex credit unions would be treated under these alternative capital approaches and other NCUA rulemakings. ICBA believes that capital instruments that do not meet all of the criteria to qualify as tier 1 capital as defined by the community banking regulators should not be permitted to be included as qualifying capital when calculating credit union capital standards. For example, a small community bank with a generic risk profile that chooses to issue subordinated debt would generally be required to classify that debt as tier 2 capital. Tier 2 capital, while eligible for inclusion in the bank's total risk-based and total capital leverage ratios, cannot be included in the bank's all important common equity tier 1 capital and additional tier 1 capital calculations used to calculate essential capitalization ratios including the CBLR.

Contrast this with a complex credit union with total assets exceeding $100 billion that could be eligible to include subordinated debt in a simplified RBLR or CCULR calculation. If subordinated debt were to be included in those calculations, the larger credit union with greater ability to influence systemic risk would appear to be better capitalized than the small community bank with a much higher quality concentration of loss-absorbing capital.

In summary, ICBA believes that the NCUA must at least attempt to hold credit unions to a risk-based capital standard under a robust regulatory framework before advocating for short cuts to achieving sound supervisory practices when addressing credit union safety and soundness. Additionally, putting forth the CCULR as an alternative based on the CBLR without first requiring full Basel III compliance is a counterproductive approach. Why even pursue risk-based capital standards for credit unions if they will be followed by simplistic alternatives that are as ineffective as the current net worth ratio?

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

ICBA appreciates the opportunity to comment on this proposed rule and request for comment. If you have any questions or would like additional information, please do not hesitate to contact me at (202) 821-4364 or james.kendrick@icba.org.

Sincerely,

/s/

James Kendrick
First Vice President, Accounting and Capital Policy