EXCEL
Federal Credit Union

May 5, 2014

MAY 08'14 PM 12:57 BOARD

Mr. Gerard Poliquin
Secretary to the NCUA Board
1775 Duke Street
Alexandria, VA 22314

RE: Risk Based Capital Rule Comment

Mr. Poliquin:

NCUA has asked for comments to the proposed Risk Based Capital Rule. In reviewing the proposed rule, the abundance of mailings and e-mails from our league, and the proposed letters from other credit unions' management, it should not be a surprise that Excel Federal Credit Union's management has issues with the proposed risk weighting for:

- CUSO's
- Investments
- Non-delinquent first mortgages
- Mortgage servicing assets
- Member business loans
- Corporate credit union paid in capital
- Individual minimum capital requirement
- Implementation period

CUSO's:

Credit union service organizations (CUSO's) are an integral part of our operations. We own the majority certificates of two LLC's designed to originate and service residential and commercial mortgages. Since their inception, each CUSO has provided a return of investment over 200%. These CUSO's have not been a hindrance to our capital position, but in actuality enhanced our capital through their respective net income. The proposed rule sets a risk weight of 250 percent on investments in and 100 percent in loans to CUSO's. The rule ignores the issue of profitable CUSO's. Also, there is no clear reasoning given for the disparity between the higher risk rating of an investment in and a loan to the CUSO. The risk weighting should be the same 100 percent for both investments in and loans to CUSO's.

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Investments:
The proposed rule risk weights investments based on their respective maturities regardless of the investment structure. We, like the majority of credit unions, utilize our ALM policy guidelines to earn the best interest rates for both short and long term investments while managing interest rate risk. The proposed rule does not take into account the type of the investment, i.e. certificate versus federal agency; nor does the rule factor in potential interest rate exposure offsets such as variable rate investments. Permissible credit union investments are less volatile than those permitted for commercial banks, yet their risk matrix is simpler than the one proposed by NCUA. NCUA should design a risk weight matrix that mirrors the FDIC and would assign a single risk weight to regardless of maturity. Also, the categories should be fewer and the risk weighting less punitive. For example, the FDIC assigns a 20 percent risk weight for investments with maturities less than five years.

Non-delinquent first mortgages:
The proposed rule would apply risk weights to the non-delinquent first mortgages a credit union owns. The proposed rule does not take into account a credit union's geographic or economic environment regarding loan demand; nor does the proposed rule acknowledge the credit union's control of concentration risk in its ALM policy and by its management. The proposed rule ignores any prudent underwriting practices and would penalize credit unions for a concentration of loans that are not inherently risky. Additionally, the proposed rule may have the unintended consequence of denial of credit to qualified members; thereby, creating a denial of service to a credit union's membership. Why not use the BASEL III weight of 50 percent of all first mortgages or adopt a structure increasing the range of asset concentration, i.e. less than 30 percent of assets would be risk weighted at 50 percent?

Mortgage servicing assets:
The proposed rule sets a 250 percent risk weight for mortgage servicing assets. Last year, NCUA finalized a loan participation rule intended to assist credit union management and NCUA manage the potential concentration risk in loan participations. The finalized rule is working and a higher risk weight would be counterproductive to the credit unions wishing to mitigate loan and liquidity risk through loan participations. The proposed rule should be amended and decrease the risk weight below 250 percent (to 150 percent) and even more so if the loan was sold without recourse but continues to be serviced by the credit union.

Member business loans:
The proposed rule creates a risk weighting matrix for every member business loan (MBL) at 100 percent up to a total of 15 percent of a credit union's assets; 150 percent of the loan from 15 to 25 percent; 200 percent of the loan for greater than 25 percent concentration of a credit union's assets. The risk weighting of the proposed rule ignores variable rate terms of a MBL; loan participation of the MBL to mitigate credit and concentration risk; a credit union's history of MBL loan losses or the MBL portfolio's performance. Credit unions with proven minimal losses within their MBL portfolio and effective underwriting standards as evidenced by past NCUA exams should be accorded lower risk weighting of their MBL portfolio. In the 10 years our credit union has been engaged in business lending, our highest dollar loss was $50,000 on a total MBL portfolio of almost $8 million. Despite this minimal loss history

and an eight percent of total assets ratio, our entire MBL portfolio would be risk weighted at 100 percent. As it is, the proposed rule is influencing a credit aversion to granting or considering member business loans at a time when qualified credit union members are seeking them. Member business loans are a growth and income earning opportunity for credit unions and should be viewed as such. Risk weighting should address specific MBL types and apply reasonable risk weights, but also make concessions for portfolio performance and MBL structure.

Corporate credit union paid in capital:

The proposed risk weighting for corporate credit union paid in capital discourages credit unions' investing in their corporate credit unions. Over the past five years, NCUA mandated several regulatory edicts to corporate credit unions; not the least of which has been higher capital requirements, stricter investment limits, concentration risk prohibitions, and changes in governance. These regulatory changes and the risks they eliminated should be represented by a lower risk weight. The proposed risk weight does not reflect the actual investment risk. This proposed rule would serve as a disincentive for credit unions to invest in and support their corporate credit unions. Corporate credit unions through self-imposed mergers (Georgia Central and Southwest Corporate) and new regulatory requirements are more stable now than in years past. The risk weighting should reflect this.

Individual minimum capital requirement:

The individual minimum capital requirement in the proposed rule should be removed. This portion of the proposed rule is entirely subjective and would allow NCUA through the examination process to increase a credit union's risk based capital requirement regardless of the actual risk based capital ratio of the credit union. This one piece of the proposed rule totally undermines its entirety. A pre-defined calculation allows a credit union the ability to manage its assets within the prescribed limits. The appeals process to a subjective increase in a credit union's risk based capital lacks any independence since the appeal must be filed with the same NCUA Board that made the judgment in the first place. An independent appeals process where the final decision is not given by the NCUA Board that made the decision in the first place would be preferable and entirely fairer to the credit union.

Implementation period:

The 18 month implementation period for the proposed rule seems too short to accomplish the widespread changes it means to introduce. It would take considerable time and planning by credit union management to prepare for the new risk based capital requirements. Credit unions need ample time to build up capital reserves since most cannot raise supplemental capital. It would take at least three years for credit union management to research, develop and plan the fundamental changes to their loan structure, investment portfolio and future product offerings.

While Excel Federal Credit Union is considered "well capitalized" based on NCUA's current risk based capital calculation simulator (16.56%), our future growth, profitability and survival would be impeded by passage of this proposed rule in its current form. The risk weights put the credit union industry at a severe disadvantage in comparison to banking counterparts.

The proposed rule revises the risk weights for many of NCUA's current asset classifications and requires higher minimum levels of capital for credit unions with perceived riskier portfolios. Credit unions' capital is built on accumulation of previous years' earnings; however, a bank can issue additional shares of stock to create a capital influx. The proposed rule's risk weighting approach would cripple a credit union's ability to thrive and service its membership since the only ways to increase capital would be to increase fees to the membership or decrease assets by "running off" deposits. Either way threatens a credit union's viability.

All of this – capital and associated risks can be mitigated through effective management planning, and oversight through policies that clearly define the risk limits within the specific credit union based on the specific geographical economic market. Effective internal loan policies establish credit risk guidelines; ALM policies establish interest rate risk guidelines; effective management controls concentration risk. These policies and management are "examined" annually for reasonableness and compliance. The proposed rule is not an effective tool to manage interest rate, credit or concentration risk and cannot be used as a substitute for competent management and effective policies and competent regulatory supervision.

Sincerely,

Ian Kijanski
CFO
Excel Federal Credit Union