OnPoint
COMMUNITY CREDIT UNION

MAY19'14 PM 2:04 BOARD

May 13, 2014

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

Re: *Notice of Proposed Rulemaking*
Prompt Corrective Action – Risk-Based Capital
NCUA Rules & Regs Part 702

Dear Mr. Poliquin:

We appreciate the opportunity to comment on NCUA's proposed rules related to Prompt Corrective Action – Risk Based Capital. This rule will likely have a significant impact on the strategies of credit unions nationwide, including OnPoint.

OnPoint Community Credit Union (Credit Union) is a state-chartered Credit Union headquartered in Portland, Oregon and serves more than 265,000 members. The Credit Union is classified as "well-capitalized," both under current Prompt Corrective Action (PCA) standards, and according to the estimated Risk-Based Capital calculation provided by NCUA's calculator. We pride ourselves on operating as a safe and sound financial institution and appreciate NCUA's proposed rule that is intended to encourage safe and sound behaviors across the credit union industry.

We agree with a risk-based approach to evaluating capital requirements, and respectfully submit the following comments to NCUA to assist NCUA in modifying the proposed rule in a manner that more accurately reflects the risk embedded in the organizations, provides fairness and consistency, and relieves regulatory burden where possible.

1. **Line-level Asset Risk Ratings.**

   In the proposed rule it appears that the NCUA assigns risk weightings to various types of assets based on a combination of credit risk, interest rate risk, liquidity risk and concentration risk. Combining these risks into one measure can result in contradictory classifications. We believe the following line items risk characteristics earn them a different risk weighting than has been proposed by NCUA.

   a. <u>Deposits at the Federal Reserve</u>. NCUA has proposed a 20% risk weight be applied to credit union deposits held at the Federal Reserve. In the proposed rule, US Government obligations unconditionally guaranteed by the full faith and credit of the US Government are assigned a 0% risk weighting, reflecting their complete safety and

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soundness. Accordingly, we respectfully propose that the risk weighting on this asset be moved to the 0% risk weighting category. Deposits held at the Federal Reserve are risk-free assets, characterized by no credit risk and unlimited liquidity. In addition, this treatment is comparable to the treatment of this asset in bank risk-based capital ratios. Assigning a 0% risk weighting to this asset would require that it be listed separately on the quarterly NCUA 5300 Call Report, a minor change that would impose minimal regulatory burden on credit unions.

b. <u>Investments with Weighted Average Life of 5 to 10 Years and with Weighted Average Life of 10+ Years.</u> The majority of mortgage-backed securities (MBS) fall into these categories. These securities provide a safe, liquid vehicle in which to invest excess funds when credit union shares exceed credit union loans. The proposed risk weightings for these categories are 150% and 200%, respectively. We respectfully propose that the risk weightings be reduced on these asset classes. Consider the following series of events as an illustration of why a lower risk weighting is appropriate:

- A credit union with mortgage loans less than 25% of assets lends to its member, in the form of a mortgage loan. The risk weighting assigned to the mortgage loan is 50%.

  - ✓ **<u>Risk Implications:</u>** The mortgage carries credit risk, interest rate risk, and liquidity risk.

- The credit union then sells the mortgage loan to a Government-Sponsored Enterprise (GSE), i.e. Fannie Mae or Freddie Mac, in the secondary market, and receives cash for the sale.

  - ✓ **<u>Risk Implications:</u>** Liquidity increases, interest rate risk decreases, credit risk decreases.

- To deploy excess cash and earn a reasonable return, the credit union purchases a mortgage-backed security from those same GSEs, with the same duration and interest rate risk profile as the loans they sold.

  - ✓ **<u>Risk Implications:</u>** Interest rate risk increases back to the level it was when the originated mortgage was made.

The net effect of this series of transactions is that the credit union has reduced liquidity risk and credit risk, with interest rate risk remaining the same. However, with the NCUA's proposed risk weightings, the credit union would be penalized with a risk weighting of 150% or higher despite having reduced their overall risk. Therefore, we recommend that a GSE mortgage-backed security be assigned no greater risk weighting than its underlying loans.

If NCUA adopts the proposed Risk-Based Capital rule without adjusting the risk weightings on the above asset types, the result will be inflated capital requirements that discourage credit unions from managing their risks appropriately, which appears to negate the spirit and intent of the risk-based capital rule.

2. Discretionary Adjustment of CAMEL Ratings

NCUA's proposed rule allows for Individual Minimum Capital Requirements (section 702.105). While we feel it is reasonable to allow for some discretionary adjustment of CAMEL ratings based on examiners' assessments of factors that may not be fully represented in the Risk-Based Capital calculation, we believe it's important that objective guidelines be put in place to ensure fair and consistent application of such discretionary authority. Current PCA requirements refer to 12 CFR 747.2003 for reclassification of a credit union's net worth category. This guidance provides direction on the content and format of the communication, and specifies that the adjustment is only to the next lower net worth category. A regulation providing similar parameters and guidance for examiners when imposing Individual Minimum Capital Requirements should be put in place.

3. Regulatory Burden

While we do not object to NCUA imposing a Risk-Based Capital requirement on credit unions, we propose that NCUA determine which currently-existing regulations may no longer be needed due to this change and eliminate them. Possible areas of overlap include guidance on concentration, liquidity and interest rate risk.

Thank you for the opportunity to comment on the Risk-Based Capital proposal. We appreciate the importance of these issues in maintaining safe and sound operations while limiting regulatory burdens on credit unions, and appreciate the chance to contribute during this rule-making process.

Sincerely,

Rob Stuart
President/CEO

Jim Hunt
SVP/CFO

c: Northwest Credit Union Association
State of Oregon, Department of Consumer and Business Services