Coventry Credit Union

Operations Center
2006 Nooseneck Hill Rd.
Coventry, RI 02816

May 5, 2014

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

Re: RIN 3133-AD77; Prompt Corrective Action – Risk Based Capital

Dear Mr. Poliquin:

Thank you for the opportunity to comment on this proposed regulation, which in my opinion is well thought out and a vast improvement on the current methodology.

This letter solely addresses the proposed Risk Based Capital issue as relates to investments in USDA/SBA loans purchased in the secondary market. These investments have two components:

1) The loan principal which is 100% guaranteed in the event of default by the USDA or SBA, and thus by the full faith and credit of the U.S. Government.
2) The premium paid at purchase, which is at risk and must be written off in the event of default or early re-payment.

These investments, which are deemed permissible investments under NCUA Rules and Regulations (see OGC opinion letter attached), are not considered participation loans and are thus carried in the NCUA Call Report in the Investment Section as "Other Investments". As such, in the proposed calculation of risk based capital (per the NCUA "New Risk Based Capital Calculator"), the risk factors are assigned based solely upon the declared weighted average life (WAL) of these investments. At December 31, 2013, our Credit Union holds a $34 million USDA/SBA purchased loan portfolio, of which approximately $30 million represents loan principal, and $4 million represents the premium paid at acquisition. The preliminary Risk Based Net Worth calculation assigns a value of $27 million to this portfolio, based solely upon assigned WAL, and is included in the denominator of the calculation.

Unlike SBA and USDA loans that are either originally underwritten by the Credit Union or purchased as a loan participation, which are assigned a risk factor of 20% in the proposed rule, the USDA/SBA loans purchased in the secondary market do not have the risk that the loan guarantee could be withdrawn due to either improper loan underwriting or inadequate on-going loan monitoring. The loans purchased in the secondary market are first reviewed by the USDA/SBA prior to their being made available in the secondary market, and a certificate issued guaranteeing the loan principle and interest. As such, the principal portion of these investments carries zero risk of loss.

May 5, 2014

Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration

As a result, it is clear that the principal portion of these investments should be assigned a zero risk rating for purposes of determining risk based capital. Per page 66 of the proposed rule, a zero risk factor is assigned to "U.S. Government Obligations directly and unconditionally guaranteed by the full faith and credit of the U.S. Government ... ". This section could be interpreted to include the principal portion of the purchased loans that are fully guaranteed by the USDA or the SBA.

I would therefore recommend that this section be expanded to specifically assign the appropriate risk rating of zero on the principal portion of investment purchases of loans 100% guaranteed by the USDA or SBA.

Conversely, the premium paid to acquire these loans is at risk, and should therefore not be included or attached to the loan principal balance as discussed above. My understanding is that banks are required to carry these purchases as loans in their FDIC Call Report filings, and thus include the premium paid when assigning a capital risk rating. My further understanding is that banks assign a risk rating of 20% to the purchased loans, inclusive of both the loan principal and premium. This could be one methodology that could be utilized in assigning a risk rating to these purchased loan investment portfolios.

I would recommend that the NCUA consider adding the "Premium paid on investments in loans fully guaranteed by the USDA and SBA" to the 250% risk rating bucket, which includes mortgage servicing assets. In my opinion, the premium paid on these investments have characteristics similar to that of a mortgage servicing asset, in that if the mortgage servicing portfolio and/or the USDA/SBA purchased loan portfolio were to be sold on the secondary market, most if not all of the value assigned to these assets would be recovered.

In conclusion, the assigning of a risk rating of zero to the principal 100% guaranteed by agencies of the U.S. Government, and the assigning of a 250% factor to the premium portion of the purchased investment that has measurable risk, would provide for a more accurate measurement of the actual risk these investments pose to the Credit Union and thus, to the NCUA Insurance Fund.

Sincerely,

David L. Root
President/CEO