From:	Smith, Steve
To:	_Regulatory Comments
Subject:	Sharonview Federal Credit Union, Steve Smith, Comments on Proposed Rule - Prompt Corrective Action; Risk-Based Capital
Date:	Friday, May 16, 2014 9:59:25 AM
Attachments:	image005.png

Dear NCUA,

Thank you for the opportunity to provide comments on your Proposed Rule on Risk Based Capital (RBC). Sharonview Federal Credit Union is a federally chartered credit union with $1.1 billion in assets headquartered in Fort Mill, South Carolina. We have sixteen branches in North Carolina, South Carolina, and New Jersey and serve over 66,000 member/owners. We have a heavy concentration in real estate loans at 67% of our loan portfolio and primarily hedge interest rate risk with long-term borrowings from the Federal Home Loan Bank of Atlanta. We currently have $190 million in long-term loans outstanding with them. In addition, we have $20 million in interest rate swaps with six-year original terms maturing later this year.

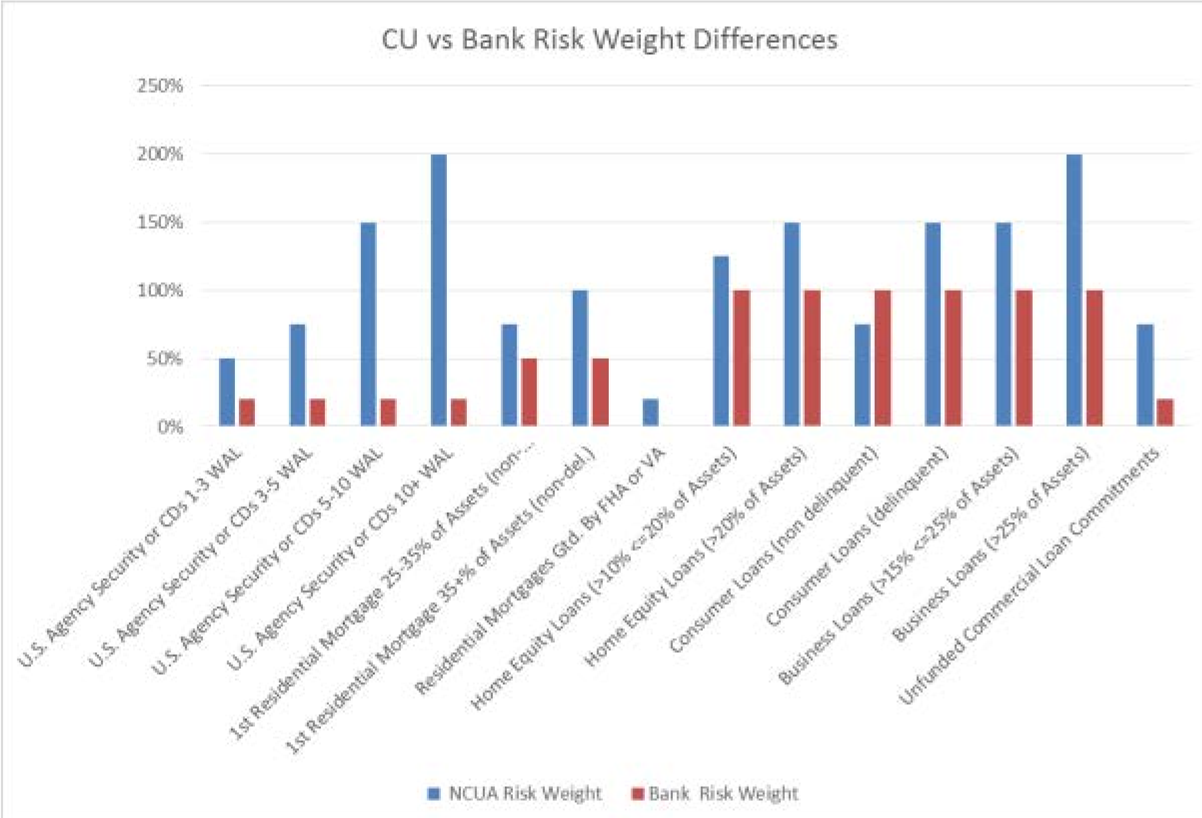
We generally support the adoption of risk based capital rules. However, it is sobering to note that banking regulators appear to favor a simple leverage ratio over subjective risk-weighted measures. In addition, risk-based capital requirements have been in place at banks for over two decades and yet their losses per assets insured from 2007-2013 were 8.8 times that of credit unions using a simple leverage ratio. Significant changes are needed in the proposed rule to avoid credit unions being burdened with a higher "capital tax" than our competitors. Changes are needed in five areas:

- Risk weightings of investments and mortgage loans
- Deduction of NCUSIF deposit from capital
- Limitation on ALLL "add-back" to risk based capital
- "Comprehensive understanding" of asset backed investments or 1,250% weighting
- Individual minimum capital ratio (IMCR) authority given to examiners: overrides all risk weighting or leverage ratio outcomes

Risk Weightings of Investments and Mortgage Loans

NCUA's proposed rule requires more capital (via higher risk weights) than banks in all but one asset class. This is illustrated in Table 1:

Table 1



The 250 percent risk-weight for investments in CUSOs is arbitrary, lacking in sufficient rationale, and doesn't reflect the actual risk of investing in CUSOs. CUSO investments should be weighted 100 percent. Corporate paid-in capital is risk weighted too high at 200 percent. Paid-in capital would be more appropriately weighted at 125 percent to recognize that the corporate credit union structure is now a less risky asset than it was during the crisis. The other regulators assign a zero percent risk weight to Federal Reserve balances while this proposal assigns a 20% weight to these balances. We keep all of our overnight investments at the Federal Reserve and find no justification whatsoever for a risk weight higher than zero percent.

NCUA is attempting to account for interest rate risk, concentration risk, and credit risk in determining these risk weights while the banks focus is on credit risk. Interest rate risk cannot be fairly assessed without looking at liabilities and off-balance sheet hedging tools like derivatives. This overly simplistic view of interest rate risk unfairly penalizes institutions like Sharonview Federal Credit Union with our relatively high concentration in real estate loans. Our interest rate risk is low due to our $190 million in long-term borrowings and other tools mitigating interest rate risk that are not considered in assigning the risk weights to these assets. We recommend some sort of credit be given to longer term liabilities or off-balance sheet derivative transactions to account for the resulting reduction in interest rate risk. If this cannot be done, we recommend adoption of mortgage loan risk weights equal to that of banks.

Deduction of NCUSIF Deposit from Capital

We recommend not deducting this deposit from both the numerator and the denominator. This is a valid asset and provides an additional buffer against NCUSIF losses on addition to our capital if a credit union fails.

Limitation on ALLL "Add-Back" to Risk Based Capital

The ALLL limit for adding to the numerator is proposed at 1.25% of risk-weighted assets. FASB's proposed new standard on ALLL will likely significantly increase normal reserves. We recommend either having no limit on the ALLL, or increasing it to 1.75% or higher.

Comprehensive Understanding of Asset Backed Investments or 1,250% Weighting

While consistency of expertise among NCUA examiners has improved, it is still not consistent enough to empower every examiner with assigning a weight of 1,250% to asset backed securities based solely on their judgment of the credit union's understanding of asset backed securities. We recommend removal of this provision or define "asset-backed investment" to a reasonable definition that excludes agency mortgage backed securities.

Individual Minimum Capital Ratio (IMCR) Authority Given to Examiners: Overrides all Risk Weighting or Leverage Ratio Outcomes

This gives NCUA the authority to require a higher minimum RBC ratio for individual credit unions based on NCUA expertise. This discretion will inevitably lead to unfair and inconsistent interpretation and application. As stated earlier, the consistency of expertise among NCUA examiners is not where it needs to be for examiners to be granted this much authority. We strongly recommend elimination of individual minimum capital ratios from the rule. At the very least, the appeals process needs to be revised and include an independent resolution.

In summary, significant changes are needed in the Proposed Rule on Risk Based Capital. The rule attempts to help regulate interest rate risk but is not effective in doing so as it completely ignores interest rate mitigating factors, such as long-term borrowings or derivatives. Ignoring these factors significantly penalizes credit unions like Sharonview who will be forced to manage to RBC that assesses interest rate risk in an overly simplistic, overly conservative, and therefore erroneous manner. While NCUA desires a RBC scheme that is similar to banks, the differences in risk weights between banks and this proposal are simply too great to be considered comparable. This would put credit unions at a competitive disadvantage and require far more capital than what is required for banks.

We thank you for providing us the opportunity to provide our comments.

Steve Smith CPA, CFP, PFS
Chief Financial Officer
P.O. Box 2070 | Fort Mill, SC 29716
704.969.6705 (P) | 704.719.2266 (F) | 800.462.4421
SHARONVIEW
FEDERAL CREDIT UNION