Finger Lakes federal credit union | People You Know. Service You Trust.
www.flfcu.org

May 21, 2014

regcomments@ncua.gov

RIN: 3133-AD77

TO: National Credit Union Administration

On behalf of the Finger Lakes Federal Credit Union Board, Management, and Staff, we want to express our appreciation for the opportunity to provide constructive input regarding NCUA's proposed risk-based capital plan. The Credit Union industry needs risk-based capital regulations that insure the safety of the industry and the NCUSIF, while providing credit unions an open framework to grow and be successful. The keys to that success are as varied as the credit unions themselves and the environmental conditions they face. Each credit union has developed management talent and operations to allow them to best serve their members and to effectively manage risk. Their individual approach to risk management may be dependent on their size and position in the marketplace. Historically, the two areas of risk that have seriously threatened the viability of financial institutions are Interest Rate Risk (poor Asset Liability Management) and Credit Risk. The two are often different as could be shown by the thrift crisis of the early 1980s versus the credit issues of the late 2000s. The NCUA's Risk Based Capital Proposal is an attempt to use one set of rules to regulate these two diverse risks that clearly deserve individual attention. Most of the credit unions affected by this proposal treat them as separate risks and have developed standards and measurements to manage the risk and opportunity presented by each.

INTEREST RATE RISK AND ASSET/LIABILITY MANAGEMENT:

Asset Liability Management has grown into a core responsibility of credit unions, one that no longer is a process meant to satisfy regulatory requirements, but one that drives funding and investment decisions to manage interest rate risk. The semi-annual and quarterly ALM reviews by smaller credit unions and almost daily reviews of larger ones, are bringing thoughtful intelligent responses in the management of difficult to predict interest rate environments. Those that responded on a timely basis to this new low rate environment have retained their profitability while others are finding it very challenging. The attached Peer Group Analysis review is one indicator of how longer term investing, a decision born from good ALM practices, has aided profitability. There is a strong correlation between both the larger asset size organizations and the higher net amount of long term assets they have with a greater return on assets for 2012 and 2013. This is a direct result of improved interest rate risk management

MAIN OFFICE
27 Seneca Street, PO Box 433 • Geneva, NY 14456-0433
Ph: (315) 781.1334 • Fax: (315) 781.2385
Loan Line: (315) 781.2945

OVID BRANCH (WILLARD)
7116 County Road 132 • Ovid, NY 14521
Ph: (607) 869.5315 • Fax: (607) 869.3260

PHELPS BRANCH
1394 Route 96, PO Box 96 • Phelps, NY 14532
Ph: (315) 548.2100 • Fax: (315) 548.2323

through ALM reviews, that determined that there are sufficient long term liabilities on their balance sheets to support investing in longer term assets.

The current risk based capital calculation and the current proposal are indifferent to good ALM practices in that they only measure interest rate risk on the assets of a credit union to the exclusion of the liability side. Requiring a 200% risk weighting for a 10 year agency MBS regardless of how it is funded, leaves one questioning the perceived value by the NCUA of sound interest rate risk management practices. The NCUA is rightly concerned with interest rate risk to credit unions when rates go up 500 basis points (whose timing is still questionable). This argument stems mostly from an antiquated understanding of Non-Maturity Deposits (Share Drafts, Regular Shares, and Money Market Accounts). The average lives and interest rate sensitivity of these liabilities are being actively measured by many credit unions and good risk determinations are being made. As a result most are finding that they are still Asset Sensitive and would welcome higher interest rates. The current fear is the possibility of falling rates.

This is all being said because interest rate risk (Asset Liability Management) needs to be separated from the process used to determine the risk weights of individual asset categories. The framework created in the process of assigning risk weights to assets masks the inability of the NCUA to properly address the Non-Maturity Deposits issue. Longer maturity assets are not bad if there are longer term maturity liabilities to fund them! The proposed Risk Based Capital Regulation should focus on assigning proper risk weights to assets based on their risk of loss due to credit quality not interest rate risk. Asset Liability Management and Interest Rate Risk Management need to play an independent role, as outlined by the NCUA in its regulatory framework to be effective in protecting the industry and the NCUSIF.

RISK WEIGHTING OF ASSETS:

We would now like to turn what should be the real objective of the proposed regulation, that of finding the proper risk weights for assets and what should be included as capital. The second part is easier to address in that we believe that the NCUA has the formula for inclusion in capital pretty much correct. They have appropriately identified those items that serve as a buffer to absorb losses before requiring the NCUSIF to make members whole for their insured deposits in adverse situations. The process of risk weighting assets is more challenging, and the setting of adequate or well capitalized level ratios and the prompt corrective actions attentive to them presents even greater challenges. The objective is to be fair to all credit unions so that those that manage well are not harmed by poor regulation or poor performers.

The first weighting of concern is for 1 to 4 family first mortgages. We are not sure if the NCUA is concerned more with interest rate risk or concentration risk for these assets. Interest rate risk should be addressed through ALM and as for concentration risk, 70% of all consumer debt is in mortgages as reported by the Federal Reserve Bank of New York, as of December 31, 2013 (chart is attached). As many credit unions have primarily consumer assets, targeting a limit of 25% or 35% of assets through risk based capital requirements seems inconsistent with asset availability. The appropriate risk weighting should be 50% for all mortgages, equal to that for community banks.

The next weighting is for Home Equity loans. The loss ratio for these loans, as shown in the attached Peer Analysis, is generally less than or close to the losses for other secured consumer loans. They should be at the 50% level, the same as mortgage products to be consistent with community banks. Mortgages and Home Equity loans make up 75% of all consumer lending, again a deep market that should not be limited for credit unions because of concentration concerns.

The next weighting of concern is investments with a weighted average life of greater than 1 year. The higher weighting of these assets is an asset liability management issue and they should all be at the 20% level, again consistent with community banks.

The NCUA should reconsider the high risk-weighting it has given to corporate perpetual capital provided by credit unions. The perpetual capital investment made was both an investment in Corporate Credit Union services and an investment in the Credit Union system. Credit unions should not be penalized for investing in their industry.

THE RISK BASED CAPITAL RATIO REQUIREMENT:

The most serious concern of all is the Risk Based Net Worth Requirement level itself. In a recent Filene Research Institute report on "Credit Union Capital Adequacy", they said that merits of a Basel III-type regime should be carefully considered when applied to US Credit Unions. The concern was the possibility of being disadvantaged against community banks. Carrying the concept one step further, does the proposed level for domestically operating credit unions need to be as high as foreign banks and those operating on an international basis. From a somewhat biased viewpoint, we would consider similar assets in the United States to be of higher quality than in most if not all of the other regions of the world. This is often the case when we see a flight to quality when there are disruptions or economic issues in other countries.

There have also been some discussions on why the large spread between the Adequately Capitalized Level and the Well Capitalized Level. With some exceptions, credit unions strive to be well capitalized. They want to survive a difficult operating environment and emerge healthy in its aftermath. Given the challenges of the past six years, we would say that the capital requirements at the beginning of that period would suffice as a standard for this proposal. An adequately capitalized level of 7.00% and a well capitalized level of 8.50% would seem to be more in order than the proposed levels. If these levels were to be adopted, then it may be appropriate for the NCUA to have the authority to require higher capital levels for individual credit unions under certain circumstances. The NCUA needs to have management latitude to perform their regulatory responsibilities and the opportunity to work with organizations that may require additional oversight. The process should require review and approval at the senior management levels of the NCUA to insure consistent application of any additional requirements.

FINGER LAKES FCU:

The protection of Finger Lakes Federal Credit Union's capital and operational opportunities is important to our Board and Management Team. When we do our strategic planning we want to see the NCUA and the regulatory environment not as a threat to our business, but as the protector of the industry. That means insuring the safety and soundness of credit unions without unreasonably constraining their ability to grow, be profitable, and service membership. Natural Person and Corporate Credit Unions, on a whole, are now operating in a very safe and sound manner. We are asking the NCUA to reconsider its Risk Based Capital Proposal to align it more appropriately with other regulators and with existing regulations.

Lastly, we want to be able to expand our facilities, products, and services to better serve our members and potential new members. We have sound risk practices and are constantly working on our Strategic Plan with a three year time horizon. Our commitment is to always be well capitalized and to have an above average return on assets for our peer group. We depend on our ALM process to guide our investment in all asset acquisitions. All was well until we modeled our plans against the new proposal. If enacted as is, we would likely have to delay or eliminate some of our objectives and redirect some investments to maintain a well capitalized status. This is due to weaknesses in the proposal and is inconsistent with the strengths and aspirations of Finger Lakes Federal Credit Union.

Again we appreciate the opportunity to comment,

Finger Lakes Federal Credit Union

Jerry W. Zehr

Please direct communications on this letter to:

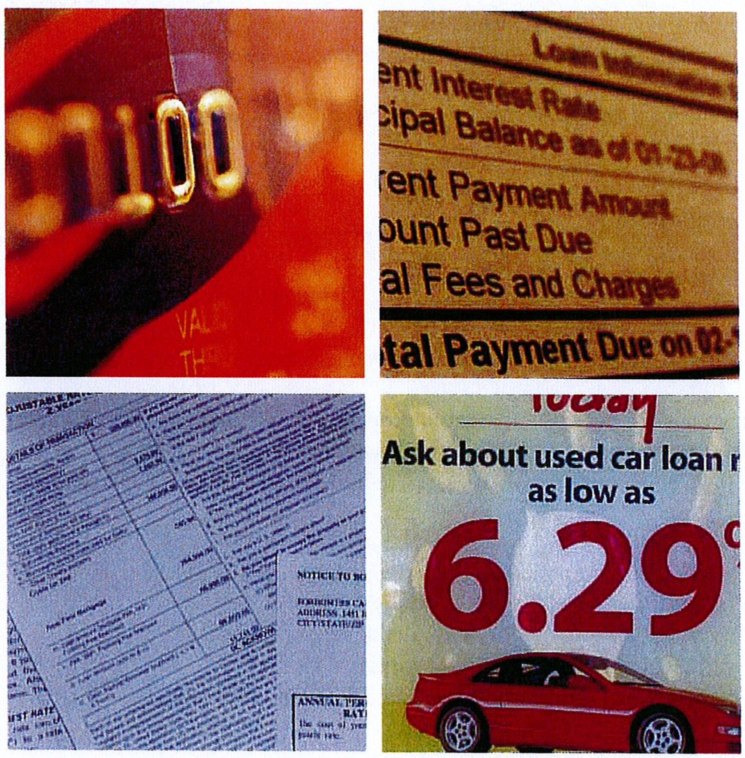
Jerry W. Zehr, Senior Vice President/Chief Financial Officer

315-781-1334 ext. 144

jzehr@flfcu.org

QUARTERLY REPORT ON
HOUSEHOLD DEBT AND CREDIT

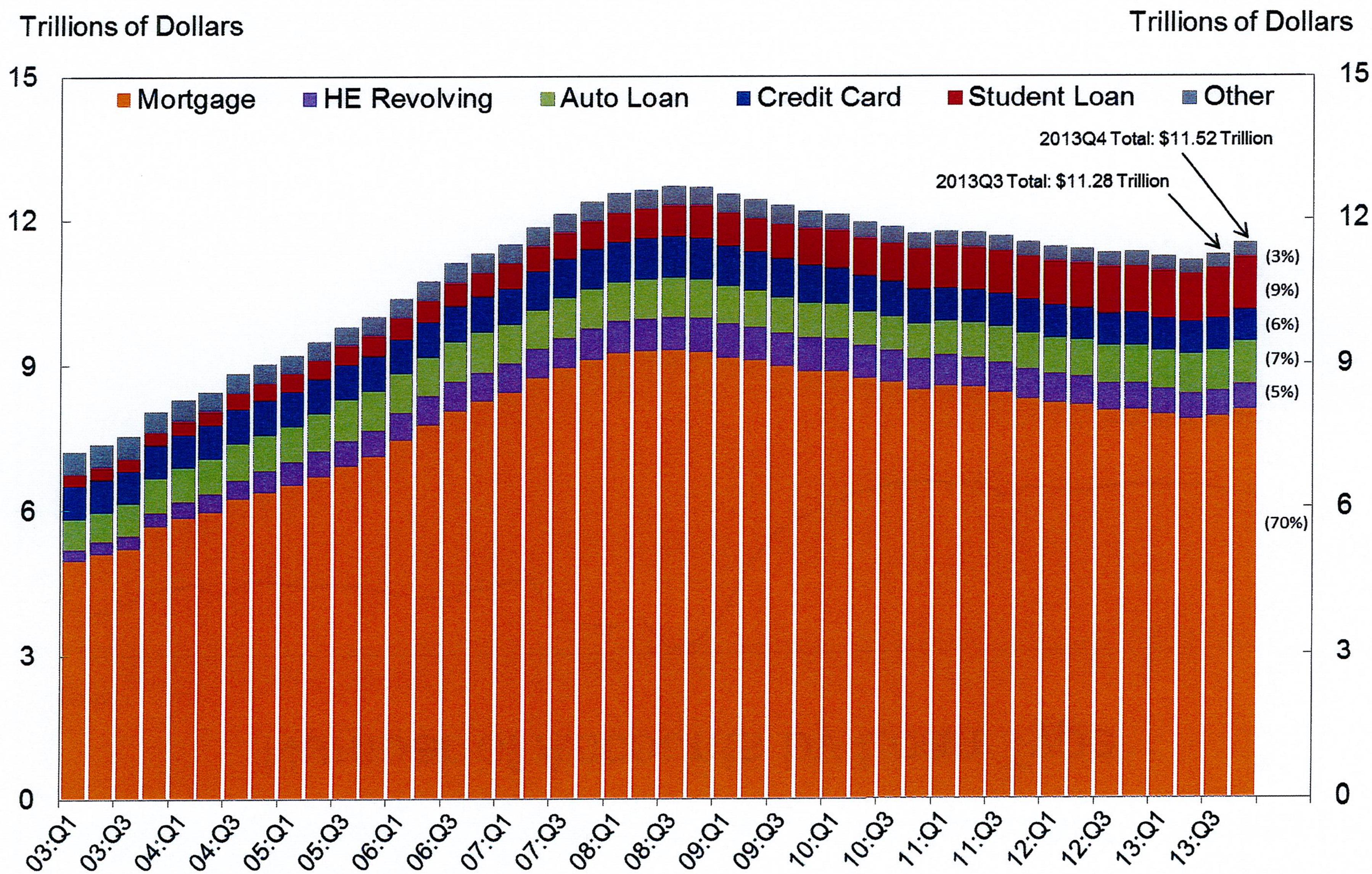
February 2014



FEDERAL RESERVE BANK OF NEW YORK

RESEARCH AND STATISTICS GROUP · MICROECONOMIC STUDIES

Total Debt Balance and its Composition



Source: FRBNY Consumer Credit Panel/Equifax

PEER GROUP ANALYSIS FROM NCUA CALL REPORT DATA

ALL INSURED CREDIT UNIONS

YEAR-END 2013 FPR REPORTS

PEER GROUP ASSETS	**NET LONG**	NET WORTH	**RETURN ON ASSETS**		LOAN LOSS RATIOS FOR 2013						LOSSES TO AVE. LOANS	
					CREDIT	VEHICLE	FIRST	OTHER	INDIRECT	BUSINESS		
IN $000,000	**TERM ASSETS**	12/31/2013	**2012**	**2013**	CARDS	LOANS	MORTGAGES	REAL ESTATE	LOANS	LOANS	**2013**	**2012**
LESS THAN 2	**4.45%**	17.60%	**-0.62%**	**-1.37%**	0.17%	0.33%	0.00%	2.91%	0.00%	0.00%	0.82%	0.84%
2 TO 10	**11.31%**	14.44%	**0.02%**	**-0.07%**	1.57%	0.34%	0.16%	0.29%	0.89%	0.10%	0.64%	0.63%
10 TO 50	**23.76%**	12.21%	**0.27%**	**0.21%**	1.41%	0.36%	0.21%	0.39%	0.71%	0.52%	0.51%	0.58%
50 TO 100	**31.17%**	11.21%	**0.56%**	**0.48%**	1.48%	0.44%	0.20%	0.35%	0.66%	0.37%	0.51%	0.59%
100 TO 500	**36.55%**	10.78%	**0.67%**	**0.59%**	1.65%	0.48%	0.23%	0.45%	0.69%	0.50%	0.53%	0.65%
GREATER THAN 500	**37.20%**	10.59%	**1.09%**	**0.99%**	2.06%	0.47%	0.21%	0.61%	0.56%	0.42%	0.58%	0.78%
ALL INSURED CUS	**35.86%**	10.78%	**0.93%**	**0.85%**	1.94%	0.46%	0.22%	0.55%	0.60%	0.43%	0.57%	0.73%