



May 28, 2014

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

RE: RIN 3133-AD77 Comments on Proposed Risk-Based Capital Rule

Financial Resources Federal Credit Union, formerly the Ethicon Employees Federal Credit Union and the Raritan Federal Credit Union, was formed over 75 years ago and currently provides a variety of financial products and services to almost 25,000 members with total assets over \$400 million.

The proposed rule will have a negative impact to Financial Resources, our products & services, members and community since it is discouraging mortgage, home equity and member business lending as well as longer term investments, regardless of asset quality or type. The rule includes punitive risk weights which differ from sound investment, liquidity, and asset liability management/interest rate risk practices.

The following are the main areas that are addressed in this document.

- **Risk Weighting of Assets**
- **Individual Minimum Capital Requirements (IMCR)**
- **NCUSIF Deposit**
- **Mortgage Servicing Rights**
- **Investment in Credit Union Service Organizations (CUSOs)**
- **Supplemental Capital**
- **Allowance for Loan and Lease Losses**
- **Implementation Period**



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Risk Weighting of Assets.

The proposed rule is treating the same assets (as listed in below table) at credit unions riskier than if those same assets were at community banks, requiring more capital for credit unions, thereby placing the credit union industry at a disadvantage to the banking industry. This disadvantage will translate to higher product costs (loan rates) and lower returns (dividends) to members, or both.

Asset	% of Assets or Weighted Average Life	NCUA Risk Weighting Proposed Rule	Community Bank (BASEL III) Risk Weighting
1 st Mortgage	25%-35%	75%	50%
1 st Mortgage	>35%	100%	50%
Home Equity	10%-20%	125%	100%
Home Equity	>20%	150%	100%
Business Loans	15%-25%	150%	100%
Business Loans	>25%	200%	100%
Investment	1-3 Years	50%	20% *
Investment	3-5 Years	75%	20% *
Investment	5-10 Years	150%	20% *
Investment	> 10 Years	200%	20% *

*All Agencies, GSE (Notes, MBS, CMO)

Critical information on loans and investments is not being considered. For loans, product type (fixed versus adjustable rate), term and loan quality is not considered in the proposed ruling. Loan to value (LTV), debt to income (DTI), borrower credit analysis and other underwriting criteria are also not included. For investments, only weighted average life is being considered in the proposed ruling, thereby ignoring product type, government sponsored enterprise (GSE) and investment grade.

Recommendation: Final rule to incorporate critical risk information on loans and investments (product type, quality, LTV, grade) or adopt the BASEL III/Community Bank model.

In addition, category 10 incorporates risk weight of 1,250% for an asset-backed investment for which the credit union is unable to demonstrate understanding. This category should be eliminated or risk weighting reduced to 250% with further definition for asset-backed investment.

Individual Minimum Capital Ratio (IMCR).

This gives subjective authority to examiners to override all risk weighting or leverage ratio outcomes.

Recommendation: IMCR to be removed from the final plan.



NCUSIF Deposit.

NCUSIF deposit is a valid asset since it would be refunded if a credit union converted to bank or savings institution charter or if a credit union elected private insurance.

Recommendation: NCUSIF deposit should be included (not deducted) in risk-based capital numerator.

Mortgage Servicing Rights (MSRs).

The proposed rule sets a 250% risk weight for mortgage servicing assets. An important tool in managing interest rate risk is the sale of long-term fixed rate loans into the secondary market. The 250% risk weighting however contradicts and discourages this practice. Financial Resources FCU measures MSRs using the fair value method and reports changes in fair value of servicing assets in earnings in the period in which the changes occur.

Recommendation: To reduce the risk weighting on MSRs to 100%.

Investment in Credit Union Service Organizations (CUSOs).

The proposed rule has a 250% risk weight. There is no consideration of what types of services are being provided; whether the CUSO has a history of profitability; or whether the investment amount has been fully recovered by the credit union through savings or income. Many credit unions are looking at CUSO relationships as a way to consolidate functions in an effort to provide specialized services to members, reduce operating expenses and/or offset declining income levels.

Recommendation: To remove any risk weighting above 100% for CUSO investments and loans.

Supplemental Capital.

A credit union's net worth is currently based solely on retained earnings. Allowing federal credit unions access to secondary or supplemental capital is a more constructive approach to achieving capital objectives than shrinking assets/deposits.

Recommendation: To allow healthy, well-managed consumer credit unions to issue supplemental capital that will count as net worth.

Allowance for Loan and Lease Losses (ALLL).

The proposed regulation limits the allowance for loan and lease losses (ALLL) credit in the risk-based capital ratio numerator to 1.25% of risk assets. The allowance account should be accounted for at full value in the calculation.

Recommendation: The ALLL limit should be eliminated from the final rule in order to allow full credit of the allowance account.



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Implementation Period.

The 18 month phase-in period is a very short period of time to potentially restructure our balance sheet. Meanwhile banks have over five years to fully implement BASEL III.

Recommendation: Extend the implementation period to a time period similar to what community banks have, or at a minimum, extend the period to at least five years.

The proposed risk-based capital rule overrides boards' and managers' judgments on business strategy and risk and will affect our ability to best serve our members.

Thank you for the opportunity to comment on the proposed regulation 12 CFR Parts 700, 701, 702, 703, 713, 723 and 747 for Prompt Correction Action – Risk Based Capital.

Beth V. Elbaum, CPA, MBA, PHR
Senior Vice President, Administration/CFO
Financial Resources Federal Credit Union