To Whom It May Concern:

The proposal to assess a 250% weighting factor to Mortgage Servicing Rights (MSRs) under the current Risk-Based Capital proposal is a perfect example of the NCUA contradicting its own guidance.

The NCUA has made it clear that it wants credit unions to carefully manage interest rate risk. For most credit unions, that means that there is little room on their Balance Sheets to hold 30-year fixed rate assets. To comply with the NCUA's mandate on managing interest rate risk, most credit unions need to sell most of their 30-year fixed rate mortgage originations to third parties, often Fannie Mae, Freddie Mac, or Ginnie Mae. The sale of a mortgage loan to a third party automatically creates an MSR asset. The only way that a credit union can manage the member relationship after such a sale, on what is usually the most significant transaction any of its members have with it, is to hold that MSR asset on its Balance Sheet and continue to service that loan. The NCUA has stated that providing that type of high-level service is exactly the type of relationship credit unions should be maintaining with their membership.

So with this new RBC proposal, the NCUA is effectively saying that it wants credit unions to sell the most significant member relationships that it has in order to manage interest rate risk, but that it is going to penalize severely any credit union that tries to provide services to those members after the sale. If a credit union wants to avoid that severe penalty, under this RBC proposal, it must sell its member relationship simultaneously with the sale of its loan, and turn that member relationship over to Wells Fargo or JPMChase or Ocwen and let them take care of that member's needs for the next thirty years instead of the credit union. In other words, "we want you to create MSRs, but we plan to penalize you if you try to retain them on your Balance Sheet."

The risks of owning this asset do not warrant anything close to a 250% risk weighting. MSRs have only two significant risks associated with them – prepayment risk and operational/reputation risk – both of which are relatively easily mitigated. Prepayment risk can be mitigated by maintaining a viable origination pipeline. Operational/reputation risk can be mitigated by maintaining a good system of internal controls.

To explain how an origination pipeline hedges the risk of MSR prepayments, consider that the most popular hedge against the interest rate risk inherent in a residential mortgage pipeline is the **sale** of MBS TBAs. One very viable hedge against the prepayment risk inherent in MSRs is the **purchase** of MBS TBAs. Maintaining a viable origination function will serve as an automatic, built-in hedge against the prepayment risk of MSRs. Anytime an institution is experiencing rapid prepayments in its MSR asset, such as during a refinance boom, it should simultaneously be experiencing huge revenue increases in its mortgage origination business that will more than offset any MSR losses from prepayment. Virtually every credit union that maintains MSRs on its books has a viable origination function to counterbalance the prepayment risk.

It is also not a realistic concern that a credit union would overstate the value of its MSR asset, because under Generally Accepted Accounting Principles, MSR assets have to be marked to market periodically, so even if MSRs were overvalued initially, they would have to be written down to fair market value at their first mark, and that is the level at which they would be carried on the credit union's books from that day forward.

Another important factor to consider is that MSRs provide a reliable source of significant fee revenue for many credit unions, and such revenues are generated from fees that are paid by investors, not by members, so for that reason MSRs are a particularly good source of fee revenue for credit unions. A reliable source of fee revenues clearly enhances the safety and soundness of any financial institution.

In short, this proposed risk weighting is ultimately harmful to the credit union industry by discouraging the sale of long-term fixed rate assets and by impairing the value of this important non-interest revenue stream.

Thank you for providing me the opportunity to provide feedback on this very important issue.

Sincerely,

Richard J. Mullen
SVP, Chief Lending Officer
Coastal Federal Credit Union.