Frequently Asked Questions about
NCUA's Risk-Based Capital Final Rule
October 2015

This document is intended to provide a high-level summary of frequently asked questions about the final rule on risk-based capital.[1]

Q1. How can I quickly learn about key provisions of the final rule?

In addition to this document, NCUA has created two summary documents to help stakeholders understand the final rule. They include:

- The document titled *Risk-Based Capital Ratio: Risk Weights at a Glance* compares the risk weights in NCUA's final rule and the FDIC's rule.

- The document titled *Risk-Based Capital Final Rule Compared to 2015 Revised Proposal* highlights notable differences between the revised proposed rule and the final rule.

NCUA has also revised the *Risk-Based Capital Ratio Estimator* to reflect the changes in the final rule. This spreadsheet tool allows a credit union to input its data to determine its risk-based capital ratio under the final rule.

NCUA has posted these documents and the estimator, along with the preamble and the final rule, in the *Risk-Based Capital Resource Center* available online at www.ncua.gov.

NCUA will post slides from a webinar about the risk-based capital final rule and a closed-captioned version of the webinar on the resource center once available.

Q2. What are the most significant changes NCUA made in the final rule?

The most significant changes include:

- Reducing the effective risk weight for equity investments in credit union service organizations (CUSOs), perpetual contributed capital at corporate credit unions, and certain other higher-risk equity investments to 100 percent if the total equity exposure is less than 10 percent of the sum of the credit union's capital elements of the risk-based capital ratio numerator. NCUA estimates 95 percent of credit unions with such investments will receive the lower risk weight.

- Reducing the risk weight to zero percent for share-secured loans where the shares securing the loan are on deposit at the credit union.

[1] This Q&A is not comprehensive in scope. The text of the final rule includes more comprehensive details.

- Reducing the risk weight to 100 percent for certain charitable donation accounts.

- Adding descriptions of the gross-up approach and look-through approaches to effectively lower the risk weights for certain investment funds and life insurance.

- Assigning principal-only, mortgage-backed security STRIPS a risk weight based on the underlying collateral.

Q3. When will the final rule go into effect?

The final rule will become effective on January 1, 2019. The implementation date generally aligns with full implementation of the risk-based capital requirements for banks. The implementation period of more than three years provides ample time for both covered credit unions and NCUA to prepare.

Q4. Why did NCUA have to update the risk-based capital measure now?

Many factors contributed to NCUA's need to update the risk-based capital measure, including:

- The statutory requirement for Prompt Corrective Action regulations, including a risk-based standard for complex credit unions, that are "comparable" and "equivalent in rigor" to those for the banks, which were updated in 2013.

- Agreements reached by the Basel Committee on Banking Supervision in *Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems* intending to improve the quality and quantity of banking organizations' capital.[2]

- The need to address recommendations and concerns with the implementation of Prompt Corrective Action and credit union capital adequacy contained in reports issued by the U.S. Government Accountability Office and NCUA's Inspector General.

- The need to address lessons learned from credit union failures during the Great Recession which provided compelling evidence that the existing risk-based capital requirement, which had not changed since 2002, was not sufficiently recognizing risks contributing to credit union failures.

[2] The Basel Committee on Banking Supervision published *Basel III* in December 2010 and revised it in June 2011. The group is a committee of banking supervisory authorities, which was established by the central bank governors of the G-10 countries in 1974. Documents issued by the committee are available at www.bis.org.

Q5. What should my credit union do between now and the effective date of the rule?

The final rule applies to complex credit unions, which are credit unions with $100 million or more in assets. Complex credit unions and any other credit unions projected to exceed $100 million in assets by 2019 should:

- Become familiar with the requirements of the rule and the calculation of the risk-based capital ratio.
- Consider how any projected changes to business operations and acquisition activities would impact the risk-based capital ratio.
- Evaluate your credit union's process for assessing overall capital adequacy.
- Review any future related communications issued by NCUA, such as guidance to examiners or related Letters to Credit Unions.

NCUA plans to update the Call Report by early 2018 to automatically calculate each credit union's risk-based capital ratio. In the meantime, your credit union may want to use the NCUA-provided estimator, or a similar tool, to calculate your credit union's risk-based capital ratio for information purposes. The estimator is available in the *Risk-Based Capital Resource Center* found on NCUA's website.

Q6. What will NCUA need to do between now and the January 1, 2019, effective date of the final rule?

During 2016 through 2018, NCUA will be performing the following tasks:

- Revise the Call Report to include the data items necessary to compute the risk-based capital ratio.
- Update the Automated Integrated Regulatory Examination System (AIRES) to use the new data items and include work papers specific to the risk-based capital ratio.
- Modify risk reporting systems to use the new data items to enhance off-site monitoring.
- Issue examiner guidance on the rule.
- Perform examiner training on the rule and the related examination and supervision tools.
- Provide education opportunities to credit unions on the rule.

Q7. How would credit unions be affected today if the final rule were applied now?

The 76 percent of federally insured credit unions with less than $100 million in assets are exempt from the final rule on risk-based capital.

The 24 percent of federally insured credit unions with more than $100 million in assets would be subject to the minimum risk-based capital requirements, but only 1 percent of these credit unions (as of December 31, 2014) would experience any change in their capital category.

Under the final rule, NCUA estimates that only 15 of these 1,489 complex credit unions would be downgraded from well-capitalized to adequately capitalized, and one credit union would be downgraded to undercapitalized.

All Federally Insured Credit Unions Greater Than $100 Million in Assets

Asset Range	Total Number Units	Downgraded from Well-Capitalized to Adequately Capitalized (% of Units)	Downgraded from Well-Capitalized to Undercapitalized (% of Units)
$100 million to $200 million	563	9 (1.6%)	0 (0.0%)
$200 million to $250 million	139	2 (1.4%)	0 (0.0%)
$250 million to $1 billion	560	1 (0.2%)	0 (0.0%)
Over $1 billion	227	3 (1.3%)	1 (0.4%)
Total	**1,489**	**15 (1.0%)**	**1 (0.07%)**

Q8. What is the effect of the revised proposal on existing credit union capital buffer levels?

Comments on the original and revised proposed rules included concerns about the impact on the current capital margins, or buffers, above the 7 percent net worth leverage ratio maintained by credit unions.

As demonstrated in the table below, the number of covered credit unions operating with a 500-basis-point margin above the proposed 10 percent risk-based ratio is two-and-a-half times greater than the number of covered credit unions operating 500 basis points above the 7 percent net worth leverage ratio.

Capital Buffers for Credit Unions with More than $100 Million in Assets

Well-Capitalized Level	Less than 0 basis points above	0 to 200 basis points above	200 to 350 basis points above	350 to 500 basis points above	More than 500 basis points above
Net Worth Ratio (7 percent)	14	297	449	334	395
Final Risk-Based Capital Ratio (10 percent)	23	107	140	194	1,025

Only credit unions with higher percentages of total risk assets to total assets would experience a moderate decline in the buffer they currently have over the 7 percent net worth ratio.

Q9. Why is it necessary to change NCUA's Call Report system? What is the scope and expected timing of such changes?

Commenters on the original proposal and a credit union practitioners' group both encouraged the collection and use of more detailed Call Report data. The NCUA Board agreed. This data will allow for a more precise and better calibrated risk-based capital ratio. More granular data will also enhance NCUA's off-site supervision capabilities.

As done in the past, NCUA will provide credit unions with prior notification of significant changes to the Call Report.[3] Credit unions will then have an opportunity to comment on these changes. Credit unions can expect changes to the Call Report to occur by the end of 2017. This will allow for review of the data required before the final rule's January 1, 2019, effective date.

The following is a sample of some Call Report accounts that will need to be reported differently or added to the report to accommodate the changes adopted in the final rule:

- Non-current loans
- Commercial loans
- Share-secured loans
- Government loan guarantees
- Investments
- Goodwill
- Other intangible assets
- Off-balance sheet exposures.

In revising the Call Report, NCUA will seek to minimize reporting burdens, wherever possible.

Q10. Will credit unions be authorized to raise supplemental capital for purposes of risk-based net worth?

Yes. The NCUA Board plans in a separate proposed rule to address comments supporting additional forms of supplemental capital. As the risk-based capital final rule does not take effect until January 1, 2019, there is ample time for the NCUA Board to finalize a new rule to allow supplemental capital to be counted in the risk-based capital numerator before the effective date.

[3] For example, see NCUA Letter to Credit Unions No. 12-CU-12, October 2012, Changes Planned for Upcoming Call Reports.