**NCUA Risk Based Capital Proposal – Talking Points**

Given the potential impact of the NCUA’s Risk Based Capital Proposal the MCUL has prepared the following talking points in an effort to assist Michigan credit unions in drafting comment letters to the NCUA regarding this proposal.

* The NCUA proposal would layer on top of the statutory leverage ratio requirements a risk based standard that would require credit unions to hold capital at 8% of risk-based assets in order to be considered adequately capitalized, and 10.5% to be considered well-capitalized. That is in addition to the 6% and 7% leverage ratio requirements to be adequately and well-capitalized. In reviewing the Federal Credit Union Act (FCUA) this requirement appears to be outside of the current requirements. Specifically Section 216:

 *(d)* ***Risk-based net worth requirement for complex credit unions.****—*

*(1)* ***In general.****—The regulations required under subsection (b)(1) of this section shall include a risk-based net worth requirement for insured credit unions that are complex, as defined by the Board based on the portfolios of assets and liabilities of credit unions.*

*(2)* ***Standard.****—The Board shall design the risk-based net worth requirement to take account of any material risks against which the net worth ratio required for an insured credit union to be adequately capitalized may not provide adequate protection.*

*(e)* ***Earnings-retention requirement applicable to credit unions that are not well capitalized.****—*

*(1)* ***In general.****—An insured credit union that is not well capitalized shall annually set aside as net worth an amount equal to not less than 0.4 percent of its total assets.*

* **Supplemental Capital:** If your credit union will be considered less than well capitalized under the proposed rule the following point should also be addressed:

The FCUA requires the NCUA to consider the cooperative nature of credit unions in the rule making process. Currently credit unions do not have access to capital markets. NCUA should be encouraged to accelerate their efforts to implement supplemental capital options for all credit unions, in conjunction with the Risk Based Capital Rule implementation. If supplemental capital options are available credit unions who will no longer be considered well capitalized under the proposed rule would be given an important tool to assist them in managing the new risk-based capital standards.

* **Definition of “complex” credit union**: The FCUA currently considers a “complex” credit union, as defined by the Board, and is based on the portfolios of assets and liabilities of credit unions. The proposal would implement *only an asset threshold for credit unions over $50 million*. This does not meet the requirements defined under the FCUA as complex.

 *(d)* ***Risk-based net worth requirement for complex credit unions.****—*

1. ***In general.****—The regulations required under subsection (b)(1) of this section shall include a risk-based net worth requirement for insured credit unions that are complex, as defined by the Board based on the portfolios of assets and liabilities of credit unions.*
* **Examiner Subjectivity** – The proposed rule, if implemented in its current form would allow for subjectivity by a regulator to require additional risk based capital above what is proposed in the regulation. What are your thoughts on this? For example, even if a credit union is considered “well-capitalized” under the proposed rule an examiner could require additional capital. How would this impact your credit union?
* **FASB proposal and accounting for credit losses**  - If the FASB proposal were adopted it could increase many credit union’s ALLL by 50%. ALLL could not be maintained below the 1.25%
* **Low Income Credit Unions -** If your credit union has the Low Income Designation or is applying for such, the proposal could impact your efforts to assist the community members who may not be able to obtain financing or accounts elsewhere. Driving those members to lenders with substantially higher rates and fees associated. Low Income credit unions and credit unions as a whole are responsible for reserving appropriately for potential risk in the ALLL in an effort to protect member assets. How would this impact your credit unions risk based net worth ratio?
* **BASEL III and Community Banks –**The proposal indicates that the risk weightings assigned to various assets and securities under the proposal are to align credit unions with Corporate Credit Unions and BASEL III for community banks. The risk weightings in the current proposal deter greatly from those of BASEL III for example:
	+ Investment securities are risk-weighted under BASEL III based on credit risk. Under the proposed rule, investment securities would be risk-weighted by credit unions based on average weighted maturity.
	+ Residential mortgage loans and member business loans are also risk-weighted at a much higher percentage under the NCUA’s proposal than the risk weights for such assets under BASEL III. The BASEL system as applied to smaller banks is concerned almost exclusively with interest rate risk, NCUA’s proposal also takes into account concentration and interest rate risk. (See example below)

|  |
| --- |
| **Comparing Small Bank Basel and the NCUA Risk Based Capital Proposal**  |
| **Aspect**  | **Small Bank Basel Risk Weights**  | **NCUA RBC Proposed Rule Risk Weights**  |
| Residential Mortgage Loans  | 50% (regardless of concentration)  | 50% (0% - 25% of assets) 75% (25% - 35% of assets) 100% (35% and above of assets)  |
| Small Business Loans  | 100% (regardless of concentration)  | 100% (0% - 15% of assets) 150% (15% - 25% of assets) 200% (25% and above of assets)  |

* **Investment in CUSOs –** The CUSO risk rating of 250% is disproportionate as well. Would this impact your credit union’s potential future CUSO investments?
* **Timeline for implementation:** The NCUA has indicated that a timeline of 12-18 months would be used for implementation of the proposed rule, however this time line is much too short. Banks were given a much longer period of time to comply with BASEL III, providing for a transitional period out to 2019.
* **Historical perspective –** The 7% net worth requirement under the existing rule was sufficient to sustain the credit union industry through the recent financial crisis, and credit unions did not require a taxpayer bailout.