

## **CURIA's Capital and Net Worth Reform Provisions**

The first title of H.R. 1537, the Credit Union Regulatory Improvements Act of 2007 (CURIA), would update the capital structure of credit unions to correspond more closely with current risk-based capital standards for FDIC-insured banks. Title I of the bill incorporates the revised Prompt Corrective Action (PCA) capital reform proposals developed by the National Credit Union Administration (NCUA), which oversees federally chartered credit unions and administers the National Credit Union Share Insurance Fund (NCUSIF).

### The Need for Capital Reform

The Credit Union Membership Access Act of 1998 mandated a capital and PCA system for federally insured credit unions to ensure that potential safety and soundness problems were detected and addressed at the earliest opportunity and with the least risk of potential loss to the NCUSIF. The PCA system was based on the capital and PCA system Congress imposed on bank and thrift institutions in 1991 in response to the large number of bank and thrift failures in the 1980s. Like the earlier bank PCA system, credit unions were classified into one of five capital categories, ranging from "well capitalized" to "critically undercapitalized," with a capital threshold assigned to each category expressed as a net worth ratio (net worth to total assets).

Unlike the earlier bank PCA system, however, the 1998 Act assigned each credit union category only a single leverage net worth ratio requirement, while the bank PCA system involved a three-tier system based on the type of capital and levels of asset risk. Thus, a well capitalized credit union is required to maintain a 7% net worth leverage ratio, while a comparable well capitalized bank must have a Tier 1 capital leverage ratio of 5%; a Tier 1 risk-based ratio of 6% and total risk-based capital of 10%.

In an April 2005 report, NCUA determined that the PCA system created by the 1998 Act was too inflexible and that a more risk-based approach would both foster healthy capitalization levels and permit more efficient capital management through adjustments to credit union assets and activities. More recent NCUA studies have determined that 98% of credit unions are well capitalized and, given credit unions' conservative management and limited ability to manage capital compliance, have accumulated, on average, capital in excess of 11% of total assets, well above the leverage capital requirement. If given more flexibility in managing capital, credit unions could still maintain a healthy cushion above require capital requirements, while safely returning more earning to members and expanding members services and outreach programs.

### Risk-Based Capital Provision

Title I incorporates NCUA's revised proposal to create a risk-based capital and PCA structure for federally insured credit unions. It would replace the current "one-size-fits-all" 7% leverage net worth ratio requirement with complimentary leverage and risk-based standards. A well capitalized credit union would have to maintain a leverage net worth ratio of 5.25% and a risk-based ratio of 10%. When a credit union's capital deposit with the NCUSIF (equal to 1% of insured deposits) is added, required credit union capital would equal or exceed the current capital requirements for FDIC-insured banks and thrifts. The proposal would incorporate all relevant international risk measurements applicable to BASEL I and IA financial institutions.

The PCA reform proposal would align credit union net worth requirements more closely to a credit union's actual risk profile, while providing appropriate safeguards for the National Credit Union Share Insurance Fund, the American taxpayer and the overall credit union system.