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September 20, 2006

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

RE: RIN 3064-AD09

Dear Sir:

We are writing to comment on the proposed regulations on FDIC assessments (RIN 3064-AD09), 71 *Federal Register* 41910, July 24, 2006. We have represented many of the credit unions that have converted to FDIC-insured institutions and we continue to advise credit unions that are either in the process of such conversions or exploring the possibility of changing their charters and deposit insurance.

We believe that the FDIC should modify two aspects of the proposed regulations affecting former credit unions that recently converted to FDIC insurance and credit unions that may consider such a change. First, FDIC-insured institutions that are former credit unions should not automatically be considered "new institutions" such that they must pay the highest rate for Risk Category I institutions until they have been chartered as a bank or thrift for seven years. Second, until the OTS (or FDIC) conducts a formal examination of a former credit union in which CAMELS ratings are assigned, they should be assigned to Supervisory Group A and should be presumed to have CAMELS ratings not less favorable than 2 for each individual component.

I. Former Credit Unions Are Not "New Institutions."

The proposed regulations provide in §327.9(d)(7) that "A new institution is a bank or thrift that has been chartered for at least seven years as of the last day of the quarter for which it is being assessed. All new institutions shall be assessed the Risk Category I maximum rate for that quarter." But former credit unions insured by the FDIC are not new; they are long-standing institutions that undergo a change of charter and deposit insurer.

Former credit unions are unlike other newly chartered banks and thrifts. Prior to conversion, they are "operating non-insured institutions," that is, operating institutions not insured by the FDIC. Unlike a true *de novo* bank or thrift, converting credit unions have long histories of successful operations under a credit union charter, during which they were regulated and examined by another federal deposit insurer, the National Credit Union Administration, and if chartered by a state, by a state regulator. Prior to approving a credit union's application, the FDIC and the OTS (or other chartering authority) conduct an in-depth entrance examination of the credit union, which provides ample opportunity to evaluate the credit union's operations and condition. Former credit unions generally operate under stable management that has a successful track record with the institution, which is well-established in its market.

As part of its application for a new charter and FDIC insurance, a credit union must submit a three-year business plan and the OTS (or in a few cases, other chartering authority) and the FDIC exercise the opportunity to review the plan in detail and where they deem appropriate, require changes. Following conversion, the former credit union must follow the business plan for three years, reporting quarterly on its performance relative to the plan, and obtain prior approval for a material change from the OTS or FDIC. Typically, a former credit union does not undertake major changes in its lines of business or activities following conversion except in some cases to increase its emphasis on home loans, which carry a lower risk-weight than the types of loans commonly emphasized by credit unions (such as auto loans and personal loans). Former credit unions typically grow at a measured pace, in accordance with their business plans, unlike true *de novo* institutions, which are subject to more volatility as they work to establish themselves in their markets.

The FDIC imposes a requirement for 8% Tier 1 capital for three years on all true *de novo* institutions, but it recognizes the lower risk profile presented by operating non-insured institutions by not imposing that policy on former credit unions. The assessment regulations should follow the same principle, and not treat former credit unions as "new institutions" subject to the requirement to pay the highest Risk Category I rate for seven years.

II. Until the First Formal Examination Following Conversion, A Former Credit Union Should Be Assigned to Supervisory Group A.

The proposed regulations (§327.9(c)) call for assigning each institution to a Supervisory Group, based on supervisory evaluations from the primary federal regulator (OTS or FDIC generally), including results of examination findings as well as other information which that regulator or the FDIC deems relevant. While the proposed regulations do not explicitly link the Supervisory Group assignment to composite CAMELS ratings, the preamble makes it clear that in addition to capital, for practical purposes composite CAMELS ratings will be a major if not the only determinant of the Supervisory Group assignment for most institutions,[1] given the burden

[1] "Risk Category I would contain all well-capitalized institutions in Supervisory Group A (generally those with CAMELS composite ratings of 1 or 2); *i.e.*, those institutions that would be placed in the current 1A category. New Risk Category II would

that would be entailed in soliciting information on individual institutions quarterly for assessment purposes.

Recently converted credit unions may not have CAMELS ratings available. A former credit union does not undergo its first formal examination until about year after conversion, and it may take several months for the examination report to be finalized and CAMELS ratings issued. Thus, the most recently converted former credit unions have no CAMELS ratings from the OTS or FDIC. Former federal credit unions will have had CAMELS ratings from the NCUA. State-chartered credit unions typically receive a written examination report only from the state regulator (even though NCUA examiners may have participated in the examination) and those reports may or may not assign CAMELS ratings.

All former credit unions that become insured by the FDIC will have undergone an entrance examination by the FDIC and in most cases the OTS. CAMELS ratings are not assigned in these examinations, nor is a written report of examination issued to the institution (feedback is mainly oral). However, we believe that no credit union would receive approval for a new charter or FDIC insurance if it displayed more than a few, minor weaknesses. Therefore, we believe it is appropriate for the regulations to specify the assignment of former credit unions to Supervisory Group A until they undergo their first formal examination by the OTS or another federal banking regulator in which CAMELS ratings are assigned following conversion to an FDIC-insured institution.

III. Until the First Formal Examination Following Conversion, A Former Credit Union Should Be Deemed to Have CAMELS Ratings Not Less Favorable Than 2.

Within Risk Category I, under the proposed regulations for institutions with less than $10 billion in assets,[2] each institution would be assessed at a rate ranging between a minimum and a maximum number of basis points (currently, a range of two to four basis points is proposed). The precise rate for an individual institution resulting from the formula in the proposed regulations will vary in accordance with specified financial ratios and the institution's weighted average CAMELS component ratings. As discussed above, recently converted institutions will not have available CAMELS ratings assigned by the OTS or other federal banking regulators, but the FDIC would not have approved the application for insurance if it had important concerns. Therefore, we believe that until CAMELS ratings are first assigned by the OTS or another federal banking regulator after a former credit union obtains FDIC insurance, it should be deemed to have CAMELS ratings not less favorable than 2 for each component, and, to accurately reflect the

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contain all institutions in Supervisory Groups A and B (generally those with CAMELS composite ratings of 1, 2 or 3), except those in Risk Category I and undercapitalized institutions. Category III would contain all undercapitalized institutions in Supervisory Groups A and B, and institutions in Supervisory Group C (generally those with CAMELS composite ratings of 4 or 5) that are not undercapitalized." 71 *Federal Register* at 41912 (footnotes omitted).

[2] Since no former credit union insured by the FDIC approaches $10 billion in assets, we do not discuss the large institution pricing method.

lower risk to the insurance fund, where an institution is particularly strong in an individual component, such as capital, as shown in its entrance examination or quarterly reporting, the FDIC should deem the rating to be a 1 for that component.

We believe that the changes we propose above would result in fair treatment of former credit unions insured by the FDIC without adding risk to the deposit insurance fund.

Yours truly,

Silver, Freedman & Taff, L.L.P.

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