CU*ANSWERS CONCENTRATION RISK OFFERINGS 2011

COMPLETING CONCENTRATION RISK ANALYSIS ON THE CU*BASE PLATFORM

OVERVIEW

The process of completing your concentration risk analysis on the CU*BASE platform begins with an understanding of which assets you believe you must aggregate to test as a segment. A segment is defined as a pool of assets that act similarly to changes in economic conditions. The majority of the time this segmentation will solely revolve around the loan portfolio. However, in the event the credit union has asset backed securities in the investment portfolio, these investments need to be combined with the associated segment of the loan portfolio. This document is designed to assist the user in the use of the system to pull the aggregate of these segments only.

The 10-CU-03 NCUA letter to credit unions describes the considerations for developing these segments. However, it does delve deeply into the methodology used to test these segments outside of testing against credit union capital. Use caution when developing your segments as becoming too granular creates a situation where no segment on its own will exceed 100% of capital. Typical segments may include:

Real estate
Automobiles or simple collateralized
Unsecured credit including Visa
Commercial loans
Indirect loans

Any single segment listed above may have its own subset of loan types which the credit union believes will react dissimilarly to other loans in the segment, and must be evaluated on their own as they pose significant risk to capital. Overall, segment determination should be a carefully thought out and be a defendable process as in the end this segment of the process will dictate the results of your analysis.

On top of segment determination the credit union must also determine if they have any "named borrower" relationships that in themselves could be considered a concentration of risk. Generally, the credit union is required to evaluate these types of relationships as a percentage of capital. These relationships could be contained in one account base with a single TIN or potentially contain multiple account bases with differing TINs. To garner the data from the CU*BASE platform the user would use the "Member Aggregate Balance Analysis" option found on menu MNRPTD which will detail loan relationships by account base. In the event the credit union has members with multiple base accounts, the user should use the Process Member Applications menu option (MNLOAN #1), enter the account base, and select the "OL-All Open (Active) Loans For Which This Borrower Is Responsible" loan file action code. This option gives the user all loan accounts for which the member is listed as the primary account holder or co-borrower, based on member social security number.

SEGMENT AGGREGATION

Assume the credit union established that the segments listed above are those that should be evaluated for concentration risk. Where should you start to look? First it may be as simple as the balance sheet. If each one of these segments was in itself a loan category with a unique principal balance G/L, the best way to report the totals would be through the printing of a financial statement or using the "Loan/Share Trial Balance Review" option on the Management Processing/Dashboards menu (MNMGMT).

In the event that the loans are spread over multiple categories, the credit union will need to use the "Selective Loan TB/Statistics" option found on the report menu MNRPTE. Using this menu option, the user can enter ranges of purpose, security, or category codes and drill down to a very granular level to aggregate just those loans which match the criteria of the segment.

In addition to the loan aggregation data the credit union may also need to evaluate specific investments. Aggregating investments to perform analysis such as this has never been a requirement in the past, so it is likely the credit union would have to complete some reconfiguration. The recommended methodology would be to use the "Investment Type" field on the system to create the similarities and then run an Investment Trial Balance report from the Investments menu (MNINVS).

There are a number of variables necessary to produce the concentration risk test. Refer to the table below for a list of those variables, with an available column to details the results.

Variable	Location on CU*BASE	Amount/ Percentage
Loan Segment 1 dollar amount	MNRPTE Option 2	
Loan Segment 2 dollar amount	MNRPTE Option 2	
Loan Segment 3 dollar amount	MNRPTE Option 2	
Loan Segment 4 dollar amount	MNRPTE Option 2	
Investment Segment 1	MNINVS Option 23	
Investment Segment 2	MNINVS Option 23	
Investment Segment 3	MNINVS Option 23	
Historical loss ratios for segment 1 (last 3 to 5 years)	Credit union internally derived	
Historical loss ratios for segment 2 (last 3 to 5 years)	Credit union internally derived	
Historical loss ratios for segment 3 (last 3 to 5 years)	Credit union internally derived	
Historical loss ratios for segment 4 (last 3 to 5 years)	Credit union internally derived	
Economic index tied to event risk multiplier 1	Department of Labor statistics	
Economic index tied to event risk multiplier 2	State government site	
Economic index tied to event risk multiplier 3	Google	
Credit Union total capital (including ALLL)	MNGELE option 16	
Total credit union assets	MNGELE option 16	

NEXT STEPS

So now that you have all of the numbers what do you do next? Two way to approach this. For those credit unions wishing to complete this on your own you will need a testing model to evaluate your results. In the event you do not have one Audit Link has developed a model which they are happy to supply. For those that wish to have Audit Link perform the analysis for them please give Jim Vilker or Patrick Sickels a call to discuss a custom engagement.