STATE OF IOWA

TERRY BRANSTAD, GOVERNOR
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IOWA DEPARTMENT OF COMMERCE
DIVISION OF CREDIT UNIONS
JOANN JOHNSON, SUPERINTENDENT

Date: December 6, 2016

To: Iowa State Chartered Credit Unions

From: JoAnn M. Johnson, Superintendent

Re: Changes to the CAMEL Rating System Effective January 1, 2017

Addition of "S" Rating for Market Sensitivity

The Iowa Division of Credit Unions (IDCU) uses the CAMEL examination rating system which is an acronym for component ratings of Capital, Asset Quality, Management, Earnings and Liquidity. Each of the CAMEL components is evaluated separately, as well as in relationship to each other. In addition, the credit union is given an overall CAMEL composite rating. The CAMEL rating system is an examination tool to reflect the financial condition and overall operating soundness of the credit union.

Effective January 1, 2017, IDCU will begin using the CAMEL component "S" or "Sensitivity to Market Risk" rating at all examinations. The CAMELS rating system has been in place for many years. The Federal Financial Institutions Examination Council (FFIEC) adopted the Uniform Financial Institutions Rating System (UFIRS), commonly known as the CAMELS system, which is utilized in the federal banking system and with many state credit union regulators. Further background, as well as component and composite ratings definitions, can be found in the attached appendix.

Adding the "S" component or "Sensitivity to Market Risk" is being implemented to address the degree to which interest rate changes can impact a credit union's earnings or net worth. This component also focuses on a credit union's ability to measure, monitor and manage its interest rate risk exposure. The utilization of the "S" component also recognizes the increasing balance sheet complexity in Iowa credit unions and ensures improved assessment of supervisory communication regarding interest rate risk and liquidity risk.

The addition of the "S" component is not intended to add to the regulatory burden or require additional policies and procedures. The Division will continue to use the same examination procedures for examining liquidity and interest rate risks. The quality of management systems and expertise of management must be commensurate with risk exposure. The rating of the "S" component will be a combined assessment of both the level of market risk and the ability to manage market risk.

In the IDCU examination report the six CAMELS components, as well as the composite rating, will be assigned at each examination. .Since the NCUA has not yet adopted the "S" rating and made appropriate changes to the AIRES software and other reporting systems, we will use a workaround similar to other states who have adopted the "S" rating component. If the "L" and the "S" ratings are different, the lower of the two components will be input into AIRES in the "L" portion of the CAMEL rating. For example, if the "S" is rated a "3" and "L" a "2", then a "3" rating will be input into AIRES CAMEL rating under "L".

Disclosure of the CAMELS Ratings

Since 2006, the IDCU has utilized the Iowa Risk Rating System (IRRS) which focused on the financial risk areas with a primary emphasis on the management of those risk areas. The Division continued to issue an internal CAMEL rating at each examination.

IDCU's focus is on greater transparency in the examination and supervision processes. With increased focus on the CAMELS ratings for scheduling joint exams and other expansionary requests, IDCU will be disclosing the CAMELS and composite ratings at each exam beginning January I", 2017.

Examination staff will be disclosing the CAMELS and composite ratings assigned at each examination to the Board of Directors and management team. The examination process will continue to focus on the financial and operational trends and risks, with continued emphasis on the credit union's management of those risk areas. **The CAMELS and composite ratings are considered a confidential regulatory rating and should not be disclosed beyond the Board of Directors and management team.**

We hope the greater transparency of the "S" rating for market sensitivity and the full disclosure of the CAMELS and composite ratings will assist Iowa credit unions to continue to serve their members and prosper.

Please contact your Examiner in Charge or Supervisory Examiner Ann Mulcahy if you have any questions.