**Telcoe Federal Credit Union**

**Concentration Risk Policy**

**Purpose**

The purpose of this policy is to document TFCU’s philosophy on risk concentrations, establish policy authorities related to managing risk concentrations, and summarize concentration limits.

Concentration risk is defined as any single exposure or group of exposures with the potential to produce losses large enough (relative to capital, total assets, or overall risk level) to threaten a financial institution’s health or ability to maintain its core operations.

**Philosophy**

Quantifying and managing aggregate risks is the foundation for managing concentration risks. Ensuring that TFCU has sufficient capital to accommodate aggregate risks, including risks stemming from concentrations, is the most important component of an effective risk management process. Quarterly, aggregate risks to net worth are quantified including internal measurement of concentration limits, and third party measurement of risks associated with interest rate and liquidity. This dual process incorporates the entire financial structure, including balance sheet concentrations. The quarterly review is designed to be proactive so that potential changes in the balance sheet are identified and tested in advance to ensure aggregate risks do not exceed net worth available to absorb risks.

Quality underwriting at the individual loan level decreases the credit risk exposure from concentrations of loans. Low loan loss experience for TFCU, even during difficult economic times, indicates that the underwriting standards in practice have a material impact on credit quality. A key to minimizing credit exposure from a concentration or group of loans is to continue to ensure effective underwriting occurs.

The investment portfolio further constrains credit exposure by restricting investment activities to only those instruments that possess little or no credit risk; i.e., limiting private label and uninsured securities.

Interest rate risk is limited by guidelines set forth in the ALM Policy, which include simulation testing requirements and acceptable limits for NEV and NII. Assets with maturities greater than 3 years are monitored internally by pricing and maturity reports quarterly. Furthermore, a relationship to sell mortgages on the secondary market is established and will be used to limit long term mortgages and provide liquidity.

Managing risk concentrations is a dynamic process as change is constant. As member behavior, the economic environment, and TFCU’s balance sheet evolve, the concentration risk management process also needs to evolve. This evolution will require monitoring the prescribed concentration limits and balance sheet mix for trends which could require modifying limits and adjusting strategic planning as needed to ensure excess risk is not incurred.

**Responsible Parties**

The Board of Directors has ultimate responsibility for ensuring the credit union conducts operations in a safe and sound manner. The Board’s responsibility related to concentration risk management is as follows:

* Review and approve the Concentration Risk Policy, including limits, periodically
* Review and decide appropriate action for exceptions to policy that may occur
* Review the Concentration Risk Report, which will be provided by management quarterly
* Ensure that the Board adequately understands the activities engaged in by TFCU and the financial condition and trends in order to inquire about, debate, and decide on issues relevant to concentration risk.

The board delegates operational authority for monitoring concentration risks to the ALCO. It is the responsibility of ALCO to perform the following duties:

* Ensure compliance with this policy
* Review and discuss the Concentration Risk Report provided by management quarterly
* Review other ratios and information necessary to understand changes in the financial structure of TFCU
* Assess conformity to the limits of the Concentration Risk Report
* Report findings, conclusions, and recommendations to the Board.

The Concentration Risk Program is to be periodically reviewed by an internal audit function. The scope of the audit should be sufficient to validate the accuracy of the reports provided to the ALCO and Board, and also ensure conformance with this policy and other applicable policy or regulation.

**Concentration Risk Limits**

The concentration risk limits matrix identifies specific concentration limits to be measured. These limits were determined to be necessary based on potential economic risks to the balance sheet or required by regulation. In each case, the specific risk area addressed by the concentration limit is identified. All limits were scrutinized in relation to net worth to ensure undue risk is not undertaken.

Any concentration segment that is outside of an established limit must be addressed within 30 days of identification. An action plan to bring the limit back in compliance or justification requiring board approval must be adopted at the next regularly scheduled board meeting. Updates will be provided to the Board at each subsequent board meeting until the segment is back within established limits.

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| **Concentration Risk Limits** |  |  |  |  |
|  |  |  |  |  |
| Item Limited | Limit | Risk Area | Cross-Ref | Date Added/ Modified |
| **Loans** |  |  |  |  |
| Aggregate Limit per member for all loan types | 10% of unimpaired shares and surplus | Credit | Loan Policy | Apr-12 |
| Loans to Shares | 95% | Liquidity | ALM Policy | Apr-12 |
| Loans to Assets | 90% | Liquidity | ALM Policy | Apr-12 |
|  |  |  |  |  |
|  |  |  |  |  |
| **Unsecured** |  |  |  |  |
| Signature Loans | $6,000 | Credit | Loan Policy | Apr-12 |
| Vacation and Christmas | $2,000 | Credit | Loan Policy | Apr-12 |
| Mastercard | $11,000 | Credit | Loan Policy | Apr-12 |
| Total unsecured per borrower | $15,000 | Credit | Loan Policy | Apr-12 |
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|  |  |  |  |  |
| **Real Estate Loans** |  |  |  |  |
| RE loans by remaining term: |  |  |  |  |
| <=7 years | 200% NW | IRR | ALM | Apr-12 |
| >7 to 15 years | 100% NW | IRR | ALM | Apr-12 |
| > 15 years | 50% NW | IRR | ALM | Apr-12 |
|  |  |  |  |  |
| **Member Business Loans** |  |  |  |  |
| Aggregate Limit of Outstanding MBLs | 10% of NW | Credit Risk | MBL Policy | Apr-12 |
| Maximum Loan Amount to One Member or Group | 2.25% of NW | Credit Risk | MBL Policy | Apr-12 |
|  |  |  |  |  |
| **Investments** |  |  |  |  |
| WAL more than 84 months at time of purchase | 20% of portfolio | IRR | Investment Policy | Apr-12 |
| FV decline more than 17% at time of purchase | 20% of portfolio | IRR | Investment Policy | Apr-12 |
| Investments in any federal agency | 200% of NW | Credit | Investment Policy | Apr-12 |
| Investment per CUSIP | 20% of NW | Credit | Investment Policy | Apr-12 |
| FHLB Investments per issuance | 20% of NW | Credit | Investment Policy | Apr-12 |
| Mutual Fund | 10% of NW | Credit | Investment Policy | Apr-12 |
| CCU | 200% of NW | Credit | Investment Policy | Apr-12 |
| CDs and operating accounts | Max uninsured 5% of NW | Credit | Investment Policy | Apr-12 |
|  |  |  |  |  |
| **Total Real Estate Products** |  |  |  |  |
| Aggregate Balance of RE loans and RE related Investments | NTE 650%of NW |  |  | July- 12 |