BOARD ACTION MEMORANDUM

TO: NCUA Board

DATE: July 12, 2012

FROM: Director, Office of Examination and Insurance

SUBJ: 2012 Stabilization Fund Assessment & Request for TCCUSF to borrow from U.S. Treasury

ACTION ITEM: Approve the following to fund the payment of obligations of the Temporary Corporate Credit Union Stabilization Fund (TCCUSF) due and payable in 2012:

- 2012 TCCUSF assessment of 0.095 percent (9.5 basis points) of each federally insured credit union's insured shares as of June 30, 2012, for an estimated total of $790.53 million[1] according to §217(d)(1) of the FCU Act.
- Authorization for the Executive Director to borrow up to $2.5 billion from the U.S. Treasury for the TCCUSF.

ACTION DATE: July 24, 2012

OTHER OFFICES CONSULTED: Office of the Chief Financial Officer, Office of General Counsel, Office of Corporate Credit Unions, Asset Management and Assistance Center, and Office of Chief Economist.

VIEWS OF OTHER OFFICES CONSULTED: Concurred.

SUBMITTED TO THE INSPECTOR GENERAL FOR REVIEW: Yes.

BUDGET IMPACT, IF ANY: TCCUSF receipt of approximately $790.53 million recognized as income and available to fund repayment of corporate credit union stabilization fund liabilities. Borrowing will reduce the available $6 billion borrowing authority, established under P.L. 111-22 Helping Familes Save Their Homes Act of 2009, by the amount borrowed until repaid. Borrowing costs will be funded by current cash balances and future cash inflows.

RESPONSIBLE STAFF MEMBERS: Larry Fazio, Director of Examination and Insurance; Mary Ann Woodson, Chief Financial Officer

SUMMARY: Staff recommends the following:

- NCUA Board approve an assessment of 0.095 percent (9.5 basis points) of insured shares, totaling approximately $790.53 million.

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[1] Estimated based on insured shares as of March 31, 2012. The actual assessment will be billed based upon insured shares as of June 30, 2012.

- NCUA Board approve authorization for the Executive Director to borrow up to $2.5 billion from the U.S. Treasury for the TCCUSF.

The funds generated by the assessment, along with borrowed funds from the Treasury, will be used to pay obligations due and payable in 2012, primarily the principal and interest on maturing Medium Term Notes (MTNs) issued by corporate credit unions and guaranteed by the TCCUSF. The timing and amount of the borrowing is consistent with original cash needs and uses envisioned under the Corporate System Resolution Program, including an appropriate contingency amount.

Per Special Activities Delegation 30 to the Executive Director, Board authorization is required prior to borrowing funds from U.S. Treasury. The delegation reads (emphasis added):

> Authority to take all actions necessary to administer the Temporary Corporate Credit Union Stabilization Fund, with authority to redelegate, including but not limited to, authority to pay all administrative expenses, <u>to borrow from the Secretary of the Treasury from time to time with prior authorization from the Board</u>, to repay advances made to the Stabilization Fund, to invest Stabilization Fund assets, and to transmit certification of expenditures to the appropriate Congressional committees. June 18, 2009 Open Board Meeting.

These actions are consistent with the purpose of the enabling legislation.

Background

In November 2011, NCUA provided an estimate of 8 to 11 basis points of insured shares for the 2012 TCCUSF assessment for credit union budgeting purposes. The majority of this estimate was based on the projected near term net cash flow needs of $2.66 billion in total for 2012.

<u>TCCUSF – Funding Needs and Loss Estimates</u>
Based on May 31, 2012, data[2], NCUA projects $2.66 billion in net cash obligations due and payable through December 2012, illustrated in Table 1 on the following page.

[2] Data includes transfer from the NCUSIF of $278 million in March 2012 and a repayment of US Treasury borrowings of $300 million in April 2012.

Table 1

Net Cash Needs – to December 2012	$ Billions
Uses of Funds – to December 2012	
Corporate medium term note guarantee – due 10/19/12	2.02
Corporate medium term note guarantee – due 11/2/12	1.51
Other obligations	0.12
Total projected uses of funds	**3.65**
Sources of Funds – to December 2012	
Cash available from AMEs	0.71
Monetization of other corporate assets	0.28
Total projected sources of funds	**0.99**
Net obligations to be funded	**2.66**
Less: Treasury borrowing	1.87
Total Pre-2013 Projected Cash Needs	**0.79**
Projected Total 2012 Stabilization Assessment – 03/31/2012 insured shares[2]	**9.5 basis points**

Outstanding borrowings total $3.2 billion as of May 31, 2012. The projected amount of borrowing of $1.87 billion from the United States Treasury will bring the total to $5.1 billion and falls within NCUA's current borrowing authority of $6 billion.

With the 2012 assessment, federally-insured credit unions will have paid a total of $4.08 billion of the total projected Corporate System Resolution Program expenses, as follows:

- $337.4 million in 2009
- $999.6 million in 2010
- $1.956 billion in 2011
- $790.5 million in 2012[3]

NCUA uses the firm BlackRock to conduct quarterly modeling of losses and cash flows on the legacy assets of the corporates securitized in the NCUA Guaranteed Notes (NGNs). Based on BlackRock's modeling, actual performance and updated projections in monetizing the other assets in the asset management estates, the total projected costs for the Corporate System Resolution Program as of December 31, 2011, range from $6.0 billion to $9.3 billion.

[3] Estimated based on insured shares as of March 31, 2012. The actual assessment will be billed based upon insured shares as of June 30, 2012.

As reflected in Table 2, by deducting the $4.08 billion already assessed, inclusive of the 2012 assessment, **the projected remaining assessments over the life of the TCCUSF are between $1.9 billion and $5.2 billion.**

Table 2

TCCUSF	Previous Estimate (Q2 2011)	Current Estimate (Q4 2011)
Range of Total Projected Assessments	$5.2B to $9.5B	$6.0B to $9.3B
Less 2009,2010, and 2011 Assessments	-$3.3B	-$3.3B
=Range of Post 2011 Remaining Projected Assessments	$1.9B to $6.2B	$2.7B to $6.0B
Less 2012 Assessment		-$0.8B
=Range of Post 2012 Remaining Projected Assessments		$1.9B to $5.2B

Impact of Assessment

The March 31, 2012, call report data discloses continued improvement in the operating results of federally-insured credit unions. Credit unions reported a relatively strong return on average assets (ROA) of 0.89 percent, excluding accruals some reported for the projected 2012 NCUSIF premium and TCCUSF assessment.[4] The proposed 9.5 basis point assessment reduces annualized aggregate ROA for the industry by 8 basis points.[5] However, profitability does vary across asset sizes, with smaller institutions having lower ROA levels, albeit higher net worth levels as noted in Table 3 below.[6]

Table 3

FICU Assets	< $10M	$10M- $100M	> $100M	All
ROA (adj.)	0.07%	0.44%	0.96%	0.89%
Projected ROA after Assessment	-0.01%	0.36%	0.88%	0.81%
No. Projected to be unprofitable from assessment	123	179	33	335
Current Net Worth Ratio	14.37%	11.20%	9.81%	10.01%

The assessment reduces the aggregate net worth ratio from 10.01 percent to 9.96 percent, with an average 6 basis point decline.

[4] Under GAAP, credit unions should not accrue for NCUSIF premiums or TCCUSF assessments. In addition, the current staff outlook indicates a NCUSIF premium in 2012 is not likely necessary.

[5] In 2011, the TCCUSF assessment of 25 basis points reduced the return on average assets (ROA) by 20 basis points and resulted in negative earnings in 586 of the 7,094 (8.3%) reporting credit unions. There was no NCUSIF premium in 2011.

[6] The impact of the assessment on corporate credit unions is less significant due to the lower percentage of insured shares. The assessment for all corporate credit unions is only 0.0040 percent of corporate credit union assets.

Additional information on the impact of the assessment using annualized March 31, 2012, data is as follows:

- 335 (6.25%) out of the 5,358 FICUs reporting positive net income at March 31, 2012, may experience negative core income for 2012 solely due to the TCCUSF assessment.[7] Core net income excludes any current accrual for potential NCUA assessments,[8] gain on sale of investments and fixed assets, non-operating gains, and merger-related gains.
- 46 (0.69%) of the 6,627 FICUs reporting net worth greater than 7 percent as of March 31, 2012 may experience a decline in net worth to less than 7 percent from the assessment, subjecting them to the earnings retention requirement of Prompt Corrective Action (PCA).
- 15 FICUs (0.23%) may experience a decline in net worth to below 6 percent, requiring them to prepare a net worth restoration plan.
- 1 FICU (0.02%) with a net worth ratio over 2 percent may experience a decline to less than 2 percent resulting from the assessment.

Given the fixed near term cash needs of the TCCUSF, the relatively strong financial performance of the industry in the past year, no anticipated need for an NCUSIF premium in 2012, and continued economic uncertainty looking forward into 2013, staff recommends the NCUA Board approve a 2012 TCCUSF assessment of 9.5 basis points. A 9.5 basis point assessment is projected to total $790.53 million.

<u>Recording the Assessment</u>
The Office of the Chief Financial Officer will prepare the TCCUSF assessment invoices and distribute them to all federally insured credit unions with the assessments due by October 9, 2012. Since NCUA Board approval of this assessment establishes the liability, credit unions should expense the assessment in August and report the entire expense on the September 30, 2012 call report.

RECOMMENDED ACTION: Approve the following to fund the payment of obligations of the Temporary Corporate Credit Union Stabilization Fund (TCCUSF) due and payable in 2012:

- TCCUSF assessment of 0.095 percent (9.5 basis points) of each federally insured credit union's insured shares as of June 30, 2012, for an estimated total of $790.53 million, according to §217(d)(1) of the FCU Act.
- Authorization for the Executive Director to borrow up to $2.5 billion from the U.S. Treasury for the TCCUSF.

[7] Generally accepted accounting principles require credit unions to expense the assessment when approved by the NCUA Board (the third quarter of 2012). The immediate impact of the assessment on net income as of March 31, 2012, results in approximately 1,493 FICUs recording negative net income after the assessment for the period. The negative impact of the assessment declines with each subsequent quarter.
[8] As of March 31, 2012, credit unions accrued $93.6 million in TCCUSF assessment expenses and $28.4 million in NCUSIF premium expenses in anticipation of future assessments and premiums.