Corporate System Resolution
NCUA Corporate Rule
Frequently Asked Questions (FAQs)

1. What does this FAQ cover?

This document covers the newly revised corporate regulation (NCUA Rules and Regulations Part 704) and focuses primarily on the recapitalization of corporate credit unions.

2. What are the most significant revisions related to new corporate capital requirements and how will these revisions be phased in over time?

New capital requirements will become effective sometime in October 2011; thus, corporate credit unions will have a transition period in which to raise new capital .

In October 2011, new minimum risk based capital ratios and an interim leverage ratio will become effective. For most corporates, risk based capital ratios will not dictate immediate capital needs. However, most corporates will likely need to raise additional capital to meet the interim leverage ratio.

The new regulation requires corporate credit unions to obtain a minimum 4% interim leverage ratio by October 2011, which can be comprised of any form of capital: retained earnings, perpetual contributed capital, or nonperpetual capital (similar to membership capital accounts). It is expected that many corporates will have to solicit and obtain capital from their members as October 2011 approaches to meet this new regulatory standard.

The next significant date is October of 2013, when regulations require a minimum 45 basis points of retained earnings *in conjunction with* total tier one capital (retained earnings and permanent contributed capital) of at least 4%. Some corporates may request that their members exchange a portion of nonperpetual capital for perpetual capital.

In 2016, after six years, corporates must have 1% retained earnings. After ten years, in2020, regulations require 2% retained earnings

3. Can a corporate credit union require a credit union member to contribute capital as a condition of maintaining membership and continuing services?

Yes. Revisions to the corporate rule removed the ban on conditioning membership, services, or prices for services on the purchase of paid in capital (renamed perpetual capital accounts in the new regulation). As such, corporate credit unions will have the ability under the new regulation to require a member to contribute capital or resign its membership. There are minimum notice periods, however, before the corporate can take adverse action against a member in this regard.

4. Can a corporate credit union give new contributed capital priority over existing capital accounts if there are more losses to absorb at the corporate?

Yes, at the corporate's discretion. However, this decision must be made by no later than 90 days following the promulgation of the final rule which will be approximately the end of 2010.

5. What about those corporate credit unions that may still be carrying legacy assets on their balance sheets but are not part of the NCUA securitization plan? Will these corporates be able to grow retained earnings while absorbing potential credit losses on their legacy assets?

For those corporate credit unions not conserved by NCUA on September 24, 2010, and hold legacy assets on their balance sheets, conservative estimates indicate that future credit losses will not fully erode the corporate's existing capital base**.** Generally, these legacy assets will cause the corporate to be in violation of one or more provisions of NCUA's revised corporate rule. As such, NCUA will want affected corporates to develop an appropriate course of action as soon as possible so as to come into compliance with the corporate rule and minimize the potential for future losses.

If the corporate decides an alternative approach to selling the legacy assets is sound and supportable, the corporate will need to submit an investment action plan to NCUA for approval. NCUA will consider approval of an action plan that includes retention of these legacy assets while they amortize if, for example, the corporate can document that the expected future credit losses on these assets are significantly less than the losses the corporate would take if the investments were sold at current market prices. NCUA also recognizes that future other than temporary impairment (OTTI) losses on these legacy assets may impair retained earnings growth. In those cases, NCUA will consider extensions of the period for achieving required levels of retained earnings on a case-by-case basis, but only to the extent of documented losses flowing from legacy assets identified in an approved action plan.

6. Can a natural person credit union member move/withdraw capital accounts deposited in a corporate credit union if the member disagrees with the actions of their corporate?

No, capital must be available to absorb losses at a corporate. These accounts cannot be moved without the permission of both the corporate and NCUA.

7. Can a corporate solicit capital by announcing a target level of capital, and then return solicited capital if the solicitation drive does not reach the announced level?

Yes, corporates are allowed to do this provided the corporate makes their intentions known to both the members and NCUA.

8. Can a corporate charge an annual membership fee to build retained earnings directly?

A federally chartered credit union, including a corporate, cannot under current rules charge a membership fee to existing members. NCUA is considering a further rule change that would permit corporates to charge their members reasonable one-time or periodic membership fees, so as to provide corporates another tool to grow their retained earnings. NCUA may issue a proposal on corporate membership fees as early as November 2010.

9. What happens to member credit unions' existing membership capital accounts (MCAs) if they don't convert them to the new nonperpetual capital accounts (NCAs)?

The new rule will generally permit the corporate credit union to utilize these funds to absorb losses and, to the extent they are available, return unused amounts to the member. Specifically, on the one year anniversary of the final rule, any MCA adjustable balance notice accounts must be put on notice by the corporate and returned three years later, and any term accounts will not be renewed and will be returned at maturity. The corporate can count an amortizing portion of the unconverted MCAs toward its new capital requirements until returned to the member. The amount of the account that can be considered as capital will be reduced by a constant monthly amortization that ensures the capital is fully amortized one year before the date of maturity or, for notice accounts, one year before the end of the notice period.

10. Can corporate credit unions generate sufficient earnings to meet the retained earnings minimum requirements under the investment restrictions of the new rule?

NCUA believes corporate credit unions can generate sufficient earnings under the new rule if operations are properly structured. The final corporate rule **modifies some of** the investment limitations put forth in the original proposal. One result of this modification is that corporates will be able to invest at longer weighted average lives.

While the new rule prohibits several types of securities, including private label residential mortgage backed securities, collateralized debt obligations, net interest margin securities, and subordinated securities which caused recent losses in the corporate system, there are many other types of investments from which corporates can choose. These include federal agency mortgage backed securities, corporate bonds, various asset backed securities, U.S. Treasuries, and municipal bonds.