NCUA LETTER TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22314

DATE: **June 2009** **LETTER NO: 09-CU-14**

TO: **Federally Insured Credit Unions**

SUBJ: **Corporate Stabilization Fund Implementation**

Dear Board of Directors:

Acting under new authority granted by Congress, the NCUA Board ("Board") took action to provide significant relief to credit unions in dealing with assessments related to corporate stabilization actions while maintaining a safe and strong National Credit Union Share Insurance Fund ("NCUSIF"). The purpose of this Letter is to outline the benefits and requirements of the new legislation; describe the actions taken to implement the legislation; and summarize the impact of the actions on the NCUSIF capitalization deposit and the premium assessment. This letter is the first of many communications we are planning with stakeholders. Additional information will be provided during the previously announced June 24th webcast. We also plan to issue answers to frequently asked questions regarding the issues addressed in this Letter in early July.

<u>Benefits and Responsibilities of the New Legislation</u>. On May 20, 2009, Congress enacted and the President signed into law the *Helping Families Save Their Homes Act of 2009 (*"Helping Families Act"). The legislation amended the Federal Credit Union Act providing several provisions favorable to credit unions:

- Create a Temporary Corporate Credit Union Stabilization Fund ("Stabilization Fund") to mitigate near-term corporate stabilization costs with Board authority to assess premiums over 7 years;
- Extend through 2013 the $250,000 share and deposit insurance ceiling Congress had enacted as part of the Emergency Economic Stabilization Act of 2008;
- Provide the NCUSIF authority to assess premiums over 8 years to rebuild the equity ratio should the ratio fall below 1.20%;
- Increase NCUA borrowing authority to $6 billion; and
- Establish NCUA emergency borrowing authority of $30 billion.

The Stabilization Fund provides an immediate opportunity to mitigate the onetime assessment burden on insured credit unions for corporate credit union stabilization actions. The authorities and obligations of the Stabilization Fund are summarized below:

- The Stabilization Fund is administered by the NCUA and is separate from the NCUSIF.
- The Stabilization Fund may borrow from the Treasury to make expenditures only in connection with the conservatorship, liquidation or threatened conservatorship or liquidation of a corporate credit union.
- The Stabilization Fund must repay all advances plus interest to the Treasury within seven years from the time of the first advance, unless the Board, with Treasury's approval, extends the final repayment date.
- The Board has discretion in setting the time and amount of repayments. At least 90 days prior to each repayment to Treasury, the Board will determine if the Stabilization Fund has sufficient funds to make the repayment. If the Stabilization Fund does not have sufficient funds, it must assess each federally insured credit union an aggregate amount necessary to make the payment to Treasury. The charge will be stated as a percent of insured shares as represented on the credit union's previous call report.
- The NCUSIF is prohibited from paying dividends to federally insured credit unions while the Stabilization Fund has an outstanding advance from the Treasury. Instead, the amount that would normally be paid as a dividend will be distributed to the Stabilization Fund.
- The Stabilization Fund is subject to the same administrative provisions as the NCUSIF including the preparation of an annual budget and audited financial statements.

Through a series of actions described below, the new Stabilization Fund allows the Board to improve the NCUSIF's equity ratio to better position the NCUSIF to cover future insurance losses. **Essentially, it means insured credit unions will not bear a significant, current, concentrated, onetime burden for stabilizing the corporate system. The September 2009 NCUSIF billing to insured credit unions will be significantly reduced.** While the Board has recognized the corporate stabilization costs under the Stabilization Fund, the Board at its discretion determines if, and when, to assess premiums over the next seven years. Credit unions will recognize assessments when levied by the Board.

Implementation of the Stabilization Fund. With the June 18, 2009 action, the Board authorized staff to establish the corporate governance structure of the Stabilization Fund. The Board has delegated operational oversight and provided authority to staff to borrow funds, invest, and approve assistance to corporate credit unions subject to limitations. Stabilization Fund staff will prepare an operating plan, a budget, a financial reporting structure, and other corporate governance oversight mechanisms as appropriate. Annual financial statement audits will be conducted for transparent financial reporting to the federal government and the credit union industry.

On June 18, 2009, the Board approved the following actions to legally obligate the Stabilization Fund for the costs of stabilizing the corporate system. In the process, the NCUSIF will be legally released from its present obligations related to corporate stabilization actions.

- The Stabilization Fund will pay the NCUSIF $1 billion for assignment of the full right, title and interest in the outstanding capital note extended to U.S. Central Federal Credit Union executed on January 28, 2009.

- Appropriate steps will be taken to legally obligate the Stabilization Fund for any liability arising from the Temporary Corporate Credit Union Share Guarantee Program ("TCCUSGP") and the Temporary Corporate Credit Union Liquidity Guarantee Program ("TCCULGP"). To the extent that any liability from the TCCUSGP or TCCULGP exceeds funds available from the Stabilization Fund, funds shall be made available from the NCUSIF.

Recapitalization of NCUSIF Deposit. The Board took additional actions that result in a fully restored and fully refundable NCUSIF capitalization deposit. Due to the financial and regulatory reporting implications of these issues, these actions and their impact on credit unions are discussed more fully in Enclosures A and B. Credit unions and their licensed, independent accountants will need to review this new information as they reevaluate expense estimates presently and into the immediate future.

Adjustments to the NCUSIF Capitalization Deposit for the Increase in the Share Insurance Limit. The Helping Families Act extended the $250,000 share and deposit insurance ceiling through 2013 and provided the authority to base assessments and the NCUSIF capitalization deposit balance on the higher maximum insurance amount. Accordingly, credit unions need to consider the impact of this higher assessment base on their expected insurance billing and plan for the increased cash needed to fund the capitalization deposit adjustment. Credit unions with $50 million or more in assets will receive their normal, semiannual NCUSIF capitalization deposit adjustment notice in the fall based on the June 30, 2009 report of insured shares. Credit unions with less than $50 million in assets will not receive their adjustment notice until the spring of 2010 and it will be based on insured shares reported as of December 31, 2009.

Reduction in Premium Assessment Billing Estimate. The implementation of the new legislation has provided greater discretion in the imposition of premiums; however, the bill for losses in both natural person credit unions and corporate credit unions will have to be paid. The Board will have to balance the need to maintain the NCUSIF's strength, against the desire to reduce the burden on credit unions during difficult economic times, while not creating long-term adverse financial consequences for credit unions from higher assessments over an extended period.

As part of the January corporate stabilization program action, the Board declared a premium assessment, to be collected later this year, sufficient to restore the NCUSIF equity ratio to 1.30 percent. In September the Board will evaluate all of the factors that impact the measures of strength of the NCUSIF and approve the level of premium necessary to maintain a strong NCUSIF that promotes confidence. When the one percent NCUSIF capitalization deposits are adjusted for the increase in the maximum insurance amount, the NCUSIF's equity ratio will decline. Additionally, losses incurred in the resolution of problems at natural person credit unions during this difficult time are expected to reduce the equity ratio.

Most credit unions have already recorded an estimated expense and contingent liability for the premium assessment based upon the expectation of a 0.30 percent of insured shares premium. Credit unions should adjust this premium expense estimate amount to 0.15 percent of insured shares which is the current estimate of the actual premium billing including potential assessments for the Stabilization Fund. The estimate is subject to change between now and September.

Prompt Corrective Action Implications. A credit union's obligations under Prompt Corrective Action ("PCA") will not change as a result of the stabilization expense entries made in either December 31, 2008 or March 31, 2009. As Enclosure A to this Letter states, "These new actions do not negate or cure impairment reported in past quarters or calendar year-end financial or regulatory reports." Except as explained below, credit unions having net worth between 6 and 6.99 percent are subject to an earnings retention requirement, and credit unions having net worth of less than 6 percent, must timely submit a Net Worth Restoration Plan ("NWRP") for approval.

A credit union having net worth between 6 and 6.99 percent may apply for a waiver of the earnings retention requirement by demonstrating that it is necessary to avoid a significant redemption of shares and will further the purpose of PCA. A credit union having net worth of less than 6 percent may incorporate a waiver of the earnings retention requirement in the NWRP it is required to submit for NCUA approval. NCUA will be receptive to granting a waiver under the following conditions:

1. The primary reason the credit union fell below 7 percent net worth is due to the recorded stabilization expense; and
2. Once the credit union records the entries as discussed in Enclosure A, the net worth ratio will exceed 6.99 percent.

A credit union seeking a waiver of the earnings retention requirement is urged to contact their district examiner or regional office.

NCUA will be receptive to approving NWRPs that allow maximum flexibility to the credit union, under the following conditions:

1. The stabilization expense is the reason for the decline to a lower PCA category; and

2. Recording the entries in Enclosure A restores the net worth ratio above 5.99 percent.

Under these conditions, an NWRP may merit approval if it consists of the single step of recording the entries addressed in Enclosure A and pro forma financial statements covering the next two years showing the net worth ratio remains above 6 percent for four consecutive quarters. Credit unions are again encouraged to contact their district examiner or regional office to discuss the content of an NWRP.

Conclusion. Congressional action enabled the creation of the Corporate Stabilization Fund to assist the credit union industry with managing the costs of stabilizing the corporate system. With the isolation of the corporate credit union stabilization costs in the Stabilization Fund, the result is improved capital for credit unions to meet the economic and financial challenges facing our nation.

In its first Letter to Credit Unions on the corporate stabilization actions, the Board indicated it would "*use its full rulemaking and supervisory authority and with the full participation of the credit union community, seek the lowest cost option to stabilize the corporate system*." In its March Letter notification to the industry that it had conserved U.S. Central Federal Credit Union and Western Corporate Federal Credit Union, the Board reaffirmed "*NCUA's primary goal is to minimize the adverse impact on natural person credit unions and their members so credit unions remain a vibrant and healthy sector of the U.S. financial system*." The NCUA Board has remained committed to this end and has acted accordingly.

If you have any questions related to this Letter, you should contact your regional office, district examiner, or appropriate state supervisory authority.

Sincerely,

/s/

Michael E. Fryzel
Chairman

Enclosures