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NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 741

RIN 3133-AD63

National Credit Union Share Insurance Fund Premium and One Percent Deposit

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: Section 741.4 of NCUA's rules describes the procedures for the capitalization and maintenance of the National Credit Union Share Insurance Fund (NCUSIF). The current rule, however, does not adequately address how credit unions that enter or depart the NCUSIF system in a given calendar year are affected by any NCUSIF premium or deposit replenishment assessments in that same year. NCUA is now adopting amendments to §741.4 to clarify these procedures. The final rule also adds Appendix A to Part 741, which repeats various examples of the application of §741.4, as discussed in the preamble to the proposed rule.

DATES: This rule is effective [insert date 30 days after date published in the FEDERAL REGISTER].

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SUPPLEMENTARY INFORMATION

A. Background and Comments

NCUA proposed amendments to §741.4 in July 2009. 74 FR 36618 (July 24, 2009). The amendments address how a credit union that enters NCUSIF coverage, or departs from NCUSIF coverage, in any given year calculates its share of any deposit replenishment assessment, premium assessment, or equity distribution in that year.

As described in the preamble to the proposed rule, both the Federal Credit Union Act (Act) and the prior version of §741.4 address NCUSIF's authority to assess federally insured credit unions for deposit replenishment and premiums when necessary to maintain NCUSIF's equity ratio. 74 FR 36618, 36619 (July 24, 2009). The current rule, however, does not clearly state NCUA's policy for calculating NCUSIF premium or deposit replenishment assessments for credit unions that enter or depart the NCUSIF system in a year when an assessment occurs. This final rule amends §741.4 to clarify these issues and other related issues.

NCUA received five comment letters on the proposal – two from national credit union trade associations, two from state credit union leagues, and one from an individual credit union. All commenters expressed support for the proposal and found it a helpful clarification of NCUA's current policies. Except as noted below, the Board is now adopting the rule as proposed.

Two commenters requested the final rule include a requirement for NCUA to provide detailed information about the cause, type, and amount of NCUSIF's expenses in connection with any assessments. The Board has not adopted such a requirement. By definition, all of NCUSIF's expenses result from insuring member shares, providing special assistance to avoid liquidation, and related administrative expenses. 12 U.S.C. 1783(a). Premium and one percent deposit replenishment assessments occur when NCUSIF expenses cause its equity ratio and/or available asset ratio to fall below certain levels. The Act allows NCUA to assess premiums when NCUSIF's equity ratio falls below the normal operating level established by the Board and requires NCUA to assess premiums when the equity ratio falls below 1.2 percent. 12 U.S.C. 1782(c)(2)(B)-(C). The Act also allows NCUA to expend the one percent deposit as necessary and provides for replenishment of the one percent deposit under procedures established by NCUA. 12 U.S.C. 1782(c)(1)(B)(iv).

Two commenters also expressed concern that when, as now, NCUSIF assessments resulting from expenses incurred one year are spread over multiple years, credit unions leaving NCUSIF and paying a pro-rated premium assessment for one year receive an unfair benefit because they escape the assessments in subsequent years. NCUA has made every attempt to treat credit unions leaving and entering NCUSIF equitably, but agrees credit unions leaving NCUSIF in the midst of a multi-year cycle of assessments may not pay their full share of the cost of NCUSIF coverage. The FCU Act requires, however, that credit unions converting to private share insurance pay pro-rated premium assessments. 12 U.S.C. 1786(d)(3). NCUA believes it is consistent with the FCU Act to also apply pro-rated premium assessments to credit unions leaving NCUSIF for other reasons, as stated in paragraph (j)(1)(iii) of the rule.

At this time, the Board is not adopting the proposed changes to §741.4(k) and §701.6(d) regarding late payment penalties for NCUSIF assessments and the federal credit union operating fee. The Board has decided to delay consideration of these potential changes until a later time, possibly 2011. Accordingly, the current provisions, providing for an administrative fee, interest, and the costs of collection, remain in force. One commenter on the late payment provisions asked that the regulation provide for partial waivers of late payment penalties. The Board has determined that the current language of §§741.4(k) and 701.6(d) would permit partial waivers. The same commenter also requested NCUA take a credit union's good faith effort to make timely payment into account when imposing penalties. The rule permits waiver "if circumstances warrant" and the Board will certainly consider a credit union's good faith efforts to pay in a timely manner when considering a penalty waiver request.

The only change from the current version of subsection 741.4(k) adopted in this final rule is the addition, in paragraph (4), of references to the penalties for late payment permitted under the FCU Act. The same provisions were proposed as paragraph (2) of this subsection.

The proposal specifically sought comments on whether the examples of specific calculations contained in that preamble should be incorporated in the rule text or in an appendix to the rule. The only commenter to address this issue requested including the examples in an appendix, and the final rule adopts this approach. Appendix A to Part 741 is entitled *Examples of Partial-Year NCUSIF Assessment and Distribution Calculations Under §741.4*.

One commenter suggested the proposal would be more clear if NCUA reversed the conditional and directive clauses in subparagraphs (i)(1)(ii) – (v) and (j)(1)(ii)-(iii). NCUA considered this suggestion but believes keeping the conditional clause first in these paragraphs facilitates determination of which situation applies in a particular year.

The Board is also adopting some minor recommendations from agency staff that clarify certain terms and procedures in several sections. The final rule revises the language in paragraphs (j)(1)(i) and (j)(2)(ii) of the proposal describing how the impairment of the one percent deposit affects the refundability of the deposit. The revised language states a credit union leaving NCUSIF coverage is entitled to a refund of "the full amount of its NCUSIF deposit paid, less any amounts applied to cover NCUSIF losses that exceed NCUSIF retained earnings." The Board also clarifies that for voluntary credit union liquidations, the one percent deposit refund is determined by whether any amount of the deposit has been applied to cover NCUSIF losses exceeding earnings as of the date of liquidation, which is the date members vote to liquidate. 12 C.F.R. 710.1(b).

The Board has revised paragraph (h) to remove a possible source of confusion. The intent of the proposal was to establish a deadline for NCUA to invoice for one percent deposit replenishments. As drafted, the proposal required the invoice to be sent no later than the annual or semiannual adjustments based on "insured shares as of December 31." The reference to the adjustment and the date was potentially confusing. As the current regulation has no specific invoicing deadline and none of the comments addressed this topic, the second sentence of paragraph (h) has been simplified to “The NCUSIF may invoice credit unions in an amount necessary to replenish the one percent deposit at any time following the effective date of the depletion.” The Board expects that invoicing for future one percent deposit replenishments will occur as soon as practicable but does not find it necessary to set a specific deadline at this time.

REGULATORY PROCEDURES

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a rule may have on a substantial number of small credit unions, defined as those under ten million dollars in assets. This rule clarifies existing requirements and will not impose any new regulatory requirements. The rule will not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget. 44 U.S.C. 3501 et seq.; 5 CFR part 1320.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Act of 1996 (P.L. 104-121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Acct 5. U.S.C. 551. NCUA does not believe this final rule is a "major rule" within the meaning of the relevant sections of SBREFA. NCUA has submitted the rule to the Office of Management and Budget for its determination in that regard.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999 – Assessment of Federal Regulations and Policies on Families

The NCUA has determined that the rule would not affect family well-being within the meaning of § 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105-277, 112 Stat. 2681 (1998).

List of Subjects in 12 CFR Part 741

Credit unions, insurance.

By the National Credit Union Administration Board on November 19, 2009.

Mary F. Rupp

Secretary of the Board

For the reasons set forth above, NCUA amends12 CFR part 741 as follows.

PART 741 — REQUIREMENTS FOR INSURANCE

1. The authority citation for part 741 continues to read as follows:

Authority: 12 U.S.C. 1757, 1766(a), 1781 – 1790, and 1790d: 31 U.S.C. 3717.

2. Revise §741.4 to read as follows:

§ 741.4 Insurance premium and one percent deposit.

(a) Scope. This section implements the requirements of Section 202 of the Act (12 U.S.C. 1782) providing for capitalization of the NCUSIF through the maintenance of a deposit by each insured credit union in an amount equaling one percent of its insured shares and payment of an insurance premium.

(b) Definitions. For purposes of this section:

Available assets ratio means the ratio of:

(i) The amount determined by subtracting all liabilities of the NCUSIF, including contingent liabilities for which no provision for losses has been made, from the sum of cash and the market value of unencumbered investments authorized under Section 203(c) of the Act (12. U.S.C. 1783(c)), to:

(ii) The aggregate amount of the insured shares in all insured credit unions.

(iii) Shown as an abbreviated mathematical formula, the available assets ratio is:

(cash + market value of unencumbered investments) -

(liabilities + contingent liabilities for which no provision for

losses has been made)

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aggregate amount of all insured shares from final reporting period

of calendar year

Equity ratio means the ratio of:

(i) The amount of NCUSIF's capitalization, meaning insured credit unions' one percent capitalization deposits plus the retained earnings balance of the NCUSIF (less contingent liabilities for which no provision for losses has been made) to:

(ii) The aggregate amount of the insured shares in all insured credit unions.

(iii) Shown as an abbreviated mathematical formula, the equity ratio is:

(insured credit unions' 1.0% capitalization deposits + (NCUSIF's

retained earnings - contingent liabilities for which no provision

for losses has been made)

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aggregate amount of all insured shares

Insured shares means the total amount of a federally-insured credit union's share, share draft and share certificate accounts, or their equivalent under state law (which may include deposit accounts), authorized to be issued to members, other credit unions, public units, or nonmembers (where permitted under the Act or equivalent state law), but does not include amounts in excess of insurance coverage as provided in part 745 of this chapter. For a credit union or other entity that is not federally insured, “insured shares” means, for purposes of this section only, the amount of deposits or shares that would have been insured by the NCUSIF under part 745 had the institution been federally insured on the date of measurement.

Modified premium/distribution ratio means one minus the premium/distribution ratio.

Normal operating level means an equity ratio not less than 1.2 percent and not more than 1.5 percent, as established by action of the NCUA Board.

Premium/distribution ratio means the number of full remaining months in the calendar year following the date of the institution's conversion or merger divided by 12.

Reporting period means calendar year for credit unions with total assets of less than $50,000,000 and means semiannual period for credit union with total assets of $50,000,000 or more.

(c) One percent deposit. Each insured credit union must maintain with the NCUSIF during each reporting period a deposit in an amount equaling one percent of the total of the credit union's insured shares at the close of the preceding reporting period. For credit unions with total assets of less than $50,000,000, insured shares will be measured and adjusted annually based on the insured shares reported in the credit union's 5300 report for December 31of each year. For credit unions with total assets of $50,000,000 or more, insured shares will be measured and adjusted semiannually based on the insured shares reported in the credit union's 5300 reports for December 31 and June 30 of each year.

(d) Insurance premium charges. (1) In general. Each insured credit union will pay to the NCUSIF, on dates the NCUA Board determines, but not more than twice in any calendar year, an insurance premium in an amount stated as a percentage of insured shares, which will be the same percentage for all insured credit unions.

(2) Relation of premium charge to equity ratio of NCUSIF. (i) The NCUA Board may assess a premium charge only if the NCUSIF's equity ratio is less than 1.3 percent and the premium charge does not exceed the amount necessary to restore the equity ratio to 1.3 percent.

(ii) If the equity ratio of the NCUSIF falls to between 1.0 and 1.2 percent, the NCUA Board is required to assess a premium in an amount it determines is necessary to restore the equity ratio to at least 1.2 percent, as provided for in the restoration plan adopted under Section 202(c)(2)(D) of the Act (12 U.S.C. 1782(c)(20(D)). If the equity ratio of the NCUSIF falls below 1.0 percent, the NCUA Board is required to assess a deposit replenishment charge in an amount it determines is necessary to restore the equity ratio to 1.0 percent and to assess a premium charge in an amount it determines is necessary to restore the equity ratio to, at least 1.2 percent, as provided for in the restoration plan adopted under Section 202(c)(2)(D) of the Act (12 U.S.C. 1782(c)(20(D))..

(e) Distribution of NCUSIF equity. If, as of the end of a calendar year, the NCUSIF exceeds its normal operating level and its available assets ratio exceeds 1.0 percent, the NCUA Board will make a proportionate distribution of NCUSIF equity to insured credit unions. The distribution will be the maximum amount possible that does not reduce the NCUSIF's equity ratio below its normal operating level and does not reduce its available assets ratio below 1.0 percent. The distribution will be after the calendar year and in the form determined by the NCUA Board. The form of the distribution may include a waiver of insurance premiums, premium rebates, or distributions from NCUSIF equity in the form of dividends. The NCUA Board will use the aggregate amount of the insured shares from all insured credit unions from the final reporting period of the calendar year in calculating the NCUSIF's equity ratio and available assets ratio for purposes of this paragraph.

(f) Invoices. The NCUA provides invoices to all federally insured credit unions stating any change in the amount of a credit union's one percent deposit and the computation and funding of any NCUSIF premium or deposit replenishment assessments due. Invoices for federal credit unions also include any annual operating fees that are due. Invoices are calculated based on a credit union's insured shares as of the most recently ended reporting period. The invoices may also provide for any distribution the NCUA Board declares in accordance with paragraph (e) of this section, resulting in a single net transfer of funds between a credit union and the NCUA.

(g) New charters. A newly-chartered credit union that obtains share insurance coverage from the NCUSIF during the calendar year in which it has obtained its charter will not be required to pay an insurance premium for that calendar year. The credit union will fund its one percent deposit on a date to be determined by the NCUA Board in the following calendar year, but will not participate in any distribution from NCUSIF equity related to the period prior to the credit union's funding of its deposit.

(h) Depletion of one percent deposit. All or part of the one percent deposit may be used by the NCUSIF if necessary to meet its expenses. The NCUSIF may invoice credit unions in an amount necessary to replenish the one percent deposit at any time following the effective date of the depletion.

(i) Conversion to Federal insurance.

(1) A credit union or other institution that converts to insurance coverage with the NCUSIF will:

(i) Immediately fund its one percent deposit based on the total of its insured shares as of the last day of the most recently ended reporting period prior to the date of conversion;

(ii) If the NCUSIF assesses a premium in the calendar year of conversion, pay a premium based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the invoice date times the institution's premium/distribution ratio;

(iii) If the NCUSIF declares, in the calendar year of conversion on or before the date of conversion, an assessment to replenish the one-percent deposit, pay nothing related to that assessment;

(iv) If the NCUSIF declares, at any time after the date of conversion through the end of that calendar year, an assessment to replenish the one-percent deposit, pay a replenishment amount based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the invoice date; and

(v) If the NCUSIF declares a distribution in the year following conversion based the NCUSIF's equity at the end of the year of conversion, receive a distribution based on the institution's insured shares as of the end of the year of conversion times the institution's premium/distribution ratio. With regard to distributions declared in the calendar year of conversion but based on the NCUSIF's equity from the end of the preceding year, the converting institution will receive no distribution.

(2) A federally-insured credit union that merges with a nonfederally-insured credit union or other non-federally insured institution (the "merging institution"), where the federally-insured credit union is the continuing institution, will:

(i) Immediately on the date of merger increase the amount of its NCUSIF deposit by an amount equal to one percent of the merging institution's insured shares as of the last day of the merging institution's most recently ended reporting period preceding the date of merger;

(ii) With regard to any NCUSIF premiums assessed in the calendar year of merger, pay a two-part premium, with one part calculated on the merging institution's insured shares as described in subparagraph (1)(ii) above, and the other part calculated on the continuing institution's insured shares as of the last day of its most recently ended reporting period preceding the date of merger; and

(iii) If the NCUSIF declares a distribution in the year following the merger based the NCUSIF's equity at the end of the year of merger, receive a distribution based on the continuing institution's insured shares as of the end of the year of merger. With regard to distributions declared in the calendar year of merger but based on the NCUSIF's equity from the end of the preceding year, the institution will receive a distribution based on its insured shares as of the end of the preceding year.

(j) Conversion from, or termination of, Federal share insurance.

(1) A federally-insured credit union whose insurance coverage with the NCUSIF terminates, including through a conversion to, or merger into, a nonfederally insured credit union or a non-credit union entity, will:

(i) Receive the full amount of its NCUSIF deposit paid, less any amounts applied to cover NCUSIF losses that exceed NCUSIF retained earnings, immediately after the final date on which any shares of the credit union are NCUSIF-insured;

(ii) If the NCUSIF declares a distribution at the end of the calendar year of conversion, receive a distribution based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the date of conversion times the institution's modified premium/distribution ratio; and

(iii) If the NCUSIF assesses a premium in the calendar year of conversion or merger on or before the day in which the conversion or merger is completed, pay a premium based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the conversion or merger date times the institution's modified premium/distribution ratio. If the institution has previously paid a premium based on this same assessment that exceeds this amount, the institution will receive a refund of the difference following completion of the conversion or merger.

(2) Notwithstanding the requirements of paragraph (j)(1) of this section:

(i) Any insolvent credit union that is closed for involuntary liquidation will not be entitled to a return of its deposit;

(ii) Any solvent credit union that is closed due to voluntary or involuntary liquidation will be entitled to a return of its deposit paid, less any amounts applied to cover NCUSIF losses that exceed NCUSIF retained earnings, prior to final distribution of member shares; and

(iii) The Board reserves the right to delay return of the deposit to any credit union converting from or terminating its federal insurance, or voluntarily liquidating, for up to one year if the Board determines that immediate repayment would jeopardize the NCUSIF.

(k) Assessment of administrative fee and interest for delinquent payment.

Each federally insured credit union must pay to the NCUA an administrative fee, the costs of collection, and interest on any delinquent payment of its capitalization deposit or insurance premium. A payment will be considered delinquent if it is postmarked or electronically posted later than the date stated in the invoice provided to the credit union. The NCUA may waive or abate charges or collection of interest, if circumstances warrant.

(1) The administrative fee for a delinquent payment shall be an amount as fixed from time to time by the NCUA Board based upon the administrative costs of such delinquent payments to the NCUA in the preceding year.

(2) The costs of collection shall be calculated as the actual hours expended by NCUA personnel multiplied by the average hourly cost of the salaries and benefits of such personnel.

(3) The interest rate charged on any delinquent payment shall be the U.S. Department of the Treasury Tax and loan Rate in effect on the date when the loan payment is due as provided in 31 U.S.C. 3717.

(4) The Act contains specific penalties and other consequences for delinquent payments, including, but not limited to:

(i) Section 202(d)(2)(B) of the Act (12 U.S.C. 1782(d)(2)(B)) provides that the Board may assess and collect a penalty from an insured credit union of not more than $20,000 for each day the credit union fails or refuses to pay any deposit or premium due to the fund; and

(ii) Section 202(d)(3) of the Act (12 U.S.C. 1782(d)(3)) provides, generally, that no insured credit union shall pay any dividends on its insured shares or distribute any of its assets while it remains in default in the payment of its deposit or any premium charge due to the fund. Section 202(d)(3) further provides that any director or officer of any insured credit union who knowingly participates in the declaration or payment of any such dividend or in any such distribution shall, upon conviction, be fined not more than $1,000 or imprisoned more than one year, or both.

3.   Add Appendix A to 12 CFR Part 741 to read as follows:

Appendix A to Part 741 – Examples of Partial-Year NCUSIF Assessment and Distribution Calculations Under §741.4.

The following examples illustrate the calculation of deposit and premium assessments under each circumstance addressed in paragraphs (i) and (j) of §741.4.

A. <u>Direct Conversion to NCUSIF Insurance</u>

Paragraph (i)(1)(i) provides:

> A credit union or other institution that converts to insurance coverage with the NCUSIF will: (i) Immediately fund its one percent deposit based on the total of its insured shares as of the last day of the most recently ended reporting period prior to the date of conversion . . . .

The following hypothetical illustrates the application of this provision. Assume Main Street Credit Union completes its conversion from nonfederal to federal insurance on May 15 of Year One. Assume further that Main Street credit union had 1,000 insured shares for the end of month in December of the previous year (Year zero), 1,100 insured shares for at the end of May, the month of conversion, and 1,200 insured shares at the end of June. This information is presented in this Table A:[1]

Table A

	End of month, December, Year Zero.	End of month, May, Year One (**Month conversion completed**).	End of month, June, Year One.
Main Street Credit Union's Federally Insured Shares:	1,000	1,100	1,200

Paragraph (i)(1)(i) requires that on the date of its conversion, Main Street fund its one percent deposit based on "the total of its insured shares as of the last day of the most recently ended reporting period prior to the date of conversion." Since Main Street has less than $50,000,000 in assets, its reporting period is annual,

[1] Although Main Street Credit Union was not federally insured as of December 31 of Year Zero, proposed 741.4(b)(3) provides that "For a credit union or other entity that is not federally insured, 'insured shares' means, for purposes of this section only, the amount of deposits or shares that would have been insured by the NCUSIF under part 745 had the institution been federally insured on the date of measurement."

and ends on December 31. 12 CFR 741.4(b)(6) (definition of "reporting period"). Main Street had $1,000 in insured shares on that date, and one percent of that is $10, and so that is the amount Main Street must immediately remit to the NCUSIF to establish its one percent deposit.

Paragraph (i)(1)(ii) provides that:

> A credit union or other institution that converts to insurance coverage with the NCUSIF will: . . . (ii) If the NCUSIF assesses a premium in the calendar year of conversion, pay a premium based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the invoice date times the institution's premium/distribution ratio . . . .

To illustrate the application of paragraph (i)(1)(ii), take the same facts in hypothetical A related to the conversion of Main Street from nonfederal to federal insurance. Now, further assume that on the previous March 15, NCUA had declared a premium assessment, and on September 15 following the conversion NCUA sent out the invoices for the March 15 assessment. Also assume that Main Street had grown to 1,300 insured shares at the end of September, the month the invoices were sent to Main Street and other credit unions. This information is presented in this Table B:

Table B

	End of month, December, Year Zero.	End of month, May, Year One (**Month conversion completed**).	End of month, June, Year One.	End of Month September, Year One (**Month invoice sent**).
Main Street Credit	1,000	1,100	1,200	1,300

Union's Federally Insured Shares:				

Paragraph (i)(1)(ii) requires Main Street pay a premium based on the institution's "insured shares as of the last day of the most recently ended reporting period preceding the invoice date times the institution's premium/distribution ratio." Again, because Main Street is under $50 million in assets, the most recently ended reporting period preceding the September 15 invoice date is all the way back to December of Year Zero, when Main Street had $1,000 in shares. Main Street's "premium/distribution ratio," as defined in §741.4(b)(5), is "the number of full remaining months in the calendar year following the date of the institution's conversion or merger divided by 12." Since Main Street completed its conversion in May, there are seven full months remaining in the calendar year (June through December), and Main Street's premium/distribution ratio is seven divided by 12. Accordingly, Main Street's premium will be assessed on $1,000 times seven divided by 12, or about $583.[2] Note that if Main Street's assets had exceeded $50 million as of June 30, it would have had semiannual reporting periods under §741.4(b)(6), and its "insured shares as of the last day of the most recently ended reporting period preceding the invoice date" would have been its insured shares as of June 30, Year One, and not as of December 31, Year Zero.

[2] Main Street's actual premium charge will be this $583 divided by the aggregate insured shares of all federally insured credit unions times the aggregate premium for all federally insured credit unions.

Paragraphs (i)(1)(iii) and (iv) describe the responsibility of a credit union or other entity converting to federal insurance to replenish a depleted NCUSIF deposit, as follows:

> A credit union or other institution that converts to insurance coverage with the NCUSIF will . . . (iii) If the NCUSIF declares, in the calendar year of conversion but on or before the date of conversion, an assessment to replenish the one-percent deposit, pay nothing related to that assessment; (iv) If the NCUSIF declares, at any time after the date of conversion through the end of that calendar year, an assessment to replenish the one-percent deposit, pay a replenishment amount based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the invoice date . . . .

Paragraph (i)(1)(iii) clarifies that a converting credit union has no responsibility to pay anything toward the replenishment of a depleted deposit that is declared on or before the date of conversion, even if NCUA sends out invoices related to the depletion after the date of conversion. Paragraph (i)(1)(iv) requires that a converting credit union replenish its deposit with regard to a depletion declared after the date of conversion through the end of the calendar year. Again, assume the same facts for Main Street as in Table B, but that the deposit depletion was announced in June, after Main Street converted, and that NCUA sent the invoices in September.

Table B

	End of month, December, Year Zero.	End of month, May, Year One (**Month conversion completed**).	End of month, June, Year One.	End of Month September, Year One (**Month invoice sent**).
Main Street Credit Union's Federally	1,000	1,100	1,200	1,300

Insured Shares:				

Main Street would receive an invoice amount "based on the [Main Street's] insured shares as of the last day of the most recently ended reporting period preceding the invoice date." Since Main Street has less than $50 million in shares, the most recently ended reporting period preceding the September invoice date was December 31, Year Zero, and it would pay for the replenishment based on $1,000 in insured shares. If Main Street, however, had had $50 million or more in assets on June 30, its most recently ended reporting period preceding the invoice date would have been the semiannual period ending on June 30, and Main Street would have used its insured shares as of June 30 to calculate the replenishment amount due to the NCUSIF.

Under the Federal Credit Union Act, distributions, if any, are declared once a year, early in the year, based on excess funds in the NCUSIF as of the prior December 31. Paragraph (i)(1)(v) describes the right of a credit union or other entity converting to federal insurance to receive a distribution from the NCUSIF, specifically:

> (1) A credit union or other institution that converts to insurance coverage with the NCUSIF will: . . . (v) If the NCUSIF declares a distribution in the year following conversion based the NCUSIF's equity at the end of the year of conversion, receive a distribution based on the institution's insured shares as of the end of the year of conversion times the institution's premium/distribution ratio. With regard to distributions declared in the calendar year of conversion but based on the NCUSIF's equity at the end of the preceding year, the converting institution will receive no distribution.

To illustrate how paragraph (i)(1)(v) works, assume that Main Street Credit Union converts to federal insurance in May of Year One, and that the NCUA declares a distribution in January of Year Two based on the NCUSIF equity as of December 31 of Year One. Then Main Street will be entitled to a pro rata portion of the distribution, calculated on its insured shares as of December 31 of Year One times its premium/distribution ratio. Since it converted in May of Year One, and there were seven full months remaining in Year One at on the date of conversion, Main Street's premium/distribution ratio under §741.4(b)(6) equals seven divided by 12.

On the other hand, if the NCUA declared a distribution a year earlier, that is, in January of Year One based on the NCUSIF's equity ratio as of December 31 in Year Zero, then under paragraph (i)(1)(v) Main Street would receive no part of this distribution. Main Street is not entitled to any part of this distribution because Main Street, which completed its conversion in Year One, did not contribute in any way to the excess funds in the NCUSIF as of the end of Year Zero.

B. <u>Conversion to NCUSIF Coverage Through Merger with a Federally Insured Credit Union</u>

Subparagraph (i)(2) addresses the NCUSIF premiums, deposit replenishments, and distribution calculations when a nonfederally insured credit union or entity converts to NCUSIF coverage by merging with a federally insured credit union.

Paragraph (i)(2)(i) provides:

> (2) A federally-insured credit union that merges with a nonfederally-insured credit union or other non-federally insured institution (the "merging institution"), where the federally-insured credit union is the continuing institution, will: (i) Immediately on the date of merger increase the amount of its NCUSIF deposit by an amount equal to one percent of the merging institution's insured shares as of the last day of the merging institution's most recently ended reporting period preceding the date of merger . . . .

To illustrate this provision, and the other provisions of paragraph (i)(2) related to mergers of nonfederally insured entities into federally-insured credit unions, consider the following hypothetical. Nonfederally-insured Credit Union A merges into federally-insured Credit Union B on August 15 of Year One. The relevant insured shares of Credit Union A and Credit Union B at various dates before and after the merger are reflected in Table D:

Table D

	End of month **December**, Year Zero.	End of month **June**, Year One.	End of month **August,** Year One (**Month merger completed**).	End of Month **September**, Year One (**Month invoice sent**).
Credit Union **A** Insured shares	1,000	1,100	N/A	N/A
Credit Union **B** Insured shares	9,000	9,900	12,900	14,000

Paragraph (i)(2)(i) requires that Credit Union B, the continuing credit union, immediately increase the amount of its deposit with the NCUSIF in an amount "equal to one percent of the merging institution's insured shares as of the last day of the merging institution's most recently ended reporting period preceding the date of merger." Since Credit Union A, the merging institution, has less than $50 million in assets, its reporting period is the calendar year, and its most recently ended reporting period preceding the August merger date is December 31 in Year Zero. Credit Union A had $1,000 in insured shares on that date. Accordingly, Credit Union B, the continuing credit union, must immediately increase the amount of its deposit with the NCUSIF by one percent of $1,000, or $10. Note that if Credit Union A had been a larger credit union, with $50 million or more in assets on June 30 in Year One, then Credit Union B would have used Credit Union A's insured shares as of June 30 in this calculation.

Paragraph (i)(2)(ii), relating to NCUSIF premium assessments, provides that the continuing institution will:

> (ii) With regard to any NCUSIF premiums assessed in the calendar year of merger, pay a two-part premium, with one part calculated on the merging institution's insured shares as described in subparagraph (1)(ii) above, and the other part calculated on the continuing institution's insured shares as of the last day of its most recently ended reporting period preceding the date of merger . . . .

Paragraph (i)(2)(ii) provides for a two-part calculation, with the first part relating to the merging credit union and the second part relating to the continuing credit union. Assuming the facts as in Table D, and assuming the premium is assessed sometime in Year One, calculate the insured shares of Credit Union A, the merging credit union, as in the example for paragraph (i)(1)(ii). Once again, because Credit Union A is under $50 million in assets, the most recently ended reporting period preceding the invoice date is December of Year Zero, when Credit Union A had $1,000 in shares. The merger was completed in August, leaving four full months in the calendar year, so the premium/distribution ratio is four divided by 12. Accordingly, this part of the premium will be assessed on $1,000 times four divided by 12, or about $333. Then calculate the insured shares of Credit Union B, the continuing credit union, "as of the last day of its most recently ended reporting period preceding the merger date." Since Credit Union B is also under $50 million in assets, "the last day of the most recently ended reporting period" is also December 31 of Year Zero. Credit Union B's insured shares on that date were $9,000, and so the combined insured shares for purposes of the premium assessment is $9,333. Note that if Credit Union B had $50 million or more in assets on June 30 of Year One, then Credit Union B's "most recently ended reporting period preceding the merger date" would have been June 30 of Year One, and not December 31 of Year Zero. The Board is aware that the NCUA might declare a NCUSIF premium, invoice it, and receive the premiums in Year One from the continuing institution before the continuing institution consummates its merger. In that case, the Board would invoice the continuing credit union again after the merger, but only for the difference between the amount previously invoiced and the amount calculated under paragraph (i)(2)(ii).

Paragraph (i)(2)(iii) prescribes the procedures for calculating the NCUSIF distribution when a nonfederally-insured credit union or entity merges into a federally insured credit union. Paragraph (i)(2)(iii) provides that the federally-insured credit union will:

> [i]f the NCUSIF declares a distribution in the year following the merger based on the NCUSIF's equity at the end of the year of merger, receive a distribution based on the continuing institution's insured shares as of the end of the year of merger. With regard to distributions declared in the calendar year of merger but based on the NCUSIF's equity from the end of the preceding year, the institution will receive a distribution based on its insured shares as of the end of the preceding year.

This formula recognizes that the merging institution did not contribute to the NCUSIF equity as of the end of the year preceding the merger and so no distribution is allotted against the merging institution's shares. As for distributions based on the NCUSIF equity at the end of the year of merger, this formula does not include any pro rata reduction for the merging institution's contribution. The Board determined that a pro rata reduction was unnecessary, given the generally small relative size of merging institutions to continuing institutions, and the fact that the Federal Credit Union Act does not require any sort of pro rata reduction or other pro rata calculation with regard to distributions.

C. <u>Conversion from, or termination of, Federal share insurance.</u>

Subparagraph (j)(1) addresses direct insurance conversions and conversions by merger. Subparagraph (j)(2) addresses liquidations and insurance termination.

Paragraph (j)(1)(i) provides:

> A federally-insured credit union whose insurance coverage with the NCUSIF terminates, including through a conversion to, or merger into, a nonfederally insured credit union or a non-credit union entity, will: (i) Receive the full amount of its NCUSIF deposit paid, less any amounts applied to cover NCUSIF losses that exceed NCUSIF retained earnings, immediately after the final date on which any shares of the credit union are NCUSIF-insured . . . .

To illustrate the application of this paragraph (j)(1)(i), consider the following hypothetical. Assume Anytown Credit Union, a credit union with $30 million in assets, converts from federal to nonfederal insurance on November 15. Also assume Anytown Credit Union had $20 million in insured shares as of the previous December 31, the end of its most recent reporting period. 12 CFR 741.4(b)(5), (c). The NCUSIF would return one percent of $20 million, or $200,000 to Anytown Credit Union immediately following the effective date of its conversion. Note that, if Anytown Credit Union had reported $50 million or more in assets on June 30, then June 30 would have been the end of its most recent reporting period. Now further assume that, on July 15 of that same year, the NCUSIF had announced an expense that reduced the equity ratio from 1.3 to .75, which would have included a write-off (depletion) of 25%, or 25 basis points, of the one percent deposit. The amount of the deposit returned to Anytown would be reduced by 25%, from $200,000 to $150,000. If the NCUSIF had announced expenses reducing the equity ratio to .75 after the November 15 conversion date, this announcement would have no effect on Anytown and it would still receive the full $200,000 from the NCUSIF.

Paragraph (j)(1)(ii) provides that:

> A federally-insured credit union whose insurance coverage with the NCUSIF terminates, including through a conversion to, or merger into, a nonfederally insured credit union or a non-credit union entity, will: . . . (ii) If the NCUSIF declares a distribution at the end of the calendar year of conversion, receive a distribution based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the date of conversion times the institution's modified premium/distribution ratio . . . .

To illustrate the application of this paragraph (j)(1)(ii), again assume Anytown Credit Union converts to nonfederal insurance on November 15, and in January of the following year, the NCUSIF declares a distribution based on the NCUSIF's equity ratio as of December 31. Anytown would receive a pro rata distribution calculated as its $20 million in insured shares multiplied by the modified premium/distribution ratio. Anytown's modified premium/distribution ratio, from the definition in §741.4(b)(5), is one minus Anytown's premium/ distribution ratio, which is one minus the ratio of the full number of months remaining in the year divided by twelve, which is one minus (one divided by twelve), which is eleven divided by twelve. So Anytown would receive a pro rata distribution based on $20 million of insured shares times eleven twelfths, or based on about $18.33 million in shares.[3]

[3] Anytown's actual distribution would be $18.33 million times the aggregate amount of the distribution divided by the aggregate amount of all insured shares at all federally insured credit unions.

Paragraph (j)(1)(iii) provides that:

> A federally-insured credit union whose insurance coverage with the NCUSIF terminates, including through a conversion to, or merger into, a nonfederally insured credit union or a non-credit union entity, will: . . . (iii) If the NCUSIF assesses a premium in the calendar year of conversion or merger on or before the day in which the conversion or merger is completed, pay a premium based on the institution's insured shares as of the last day of the most recently ended reporting period preceding the conversion or merger date times the institution's modified premium/distribution ratio. If the institution has previously paid a premium based on this same assessment that exceeds this amount, the institution will receive a refund of the difference following completion of the conversion or merger.

To illustrate these premium provisions, again assume Anytown Credit Union is a credit union with $30 million in assets that converts from federal to nonfederal insurance on November 15 of Year One, and that Anytown Credit Union had $20 million in insured shares as of the previous December 31 (of Year Zero), the end of its most recent reporting period. Further assume that NCUA declares a premium on February 12 of Year One and invoices the premium on November 15. Since the premium was declared "on or before the day in which [Anytown's] conversion [was] completed," §741.4(j)(1)(iii) applies. Anytown would then pay a premium based on $20 million (its "insured shares as of the last day of the most recently ended reporting period preceding the conversion or merger date") times eleven twelfths (its "modified premium/distribution ratio"), or based on about $18.33 million. Note that NCUA might have already have invoiced Anytown for the premium sometime between February 12 and Anytown's merger on November 15. If so, Anytown will likely receive a refund of some of this earlier premium, as provided in the last sentence of §741.1(j)(1)(iii), since it may have overpaid the earlier premium.