



# **NCUA**

National Credit Union Administration

# **The Share Insurance Fund Normal Operating Level for 2020**

## **Board Briefing**

### **December 12, 2019**

# What is the Normal Operating Level?

- Under the FCU Act, the normal operating level is the point at which excess equity is returned to credit unions in the form of a Share Insurance Fund distribution
  - Can be set from 1.20 to 1.50 percent (12 U.S.C. 1782(h)(4))
  - Distribution to credit unions required if the Fund's equity exceeds the normal operating level, and other statutory conditions met (12 U.S.C. 1782(c)(3) & 1790(e))
- The NCUA Board has historically set the normal operating level as the target equity ratio for the Share Insurance Fund
- The Board last set the normal operating level at 1.38% in December 2018 based on the methodology approved by the Board in September 2017

# Board Policy for Setting the Normal Operating Level

- Objectives
  - Retain public confidence in federal share insurance;
  - Prevent impairment of the 1 percent contributed capital deposit; and
  - Ensure the Insurance Fund can withstand a moderate recession without the equity ratio declining below 1.20 percent over a five year period.

# Method for Calculating the Normal Operating Level

- The calculation is based on projections related to the following factors:
  - Performance of the Share Insurance Fund in a moderate recession on three primary drivers: insurance losses, insured share growth, and yield on investments;
  - Potential decline in value of the SIF's claims on the corporate asset management estates in a moderate recession as modeled by BlackRock; and
  - Projected equity ratio decline through the end of 2020 without an economic downturn.
- Modeled performance of the Share Insurance Fund over five years, and decline in value of SIF's claims on corporate AMEs, in Adverse (moderate recession) economic scenario from the Federal Reserve Board

# Normal Operating Level

| <b>Component</b>   | <b>2019</b>  | <b>2020</b>  |
|--|--------------|--------------|
| <b>Statutory Minimum</b>   | <b>1.20%</b> | <b>1.20%</b> |
| <b>Plus: Potential Decline in Insurance Fund Performance</b>           | <b>0.13%</b> | <b>0.15%</b> |
| <b>Plus: Potential Decline of Value in Claims on Corporate Estates</b> | <b>0.02%</b> | <b>0.02%</b> |
| <b>Plus: Projected Equity Ratio Decline through December 2020</b>      | <b>0.03%</b> | <b>0.01%</b> |
| <b>Equals: Normal Operating Level</b>                                  | <b>1.38%</b> | <b>1.38%</b> |

# Results for Adverse & Severely Adverse

| Scenario (2019)   | Adverse      | Severely Adverse |
|---|--------------|------------------|
| Equity for Share Insurance Fund Stress                            | 1.35%        | 1.40%            |
| Plus: Equity for Potential Declines of Value in Claims on Estates | 0.02%        | 0.02%            |
| Plus: Projected Equity Ratio Decline in 2019 and 2020             | 0.01%        | 0.02%            |
| <b>Equals: Recommended Normal Operating Level</b>                 | <b>1.38%</b> | <b>1.44%</b>     |

- In a moderate recession, the equity ratio would not fall below 1.20 percent.
- Prevents impairment of the 1 percent contributed capital deposit.

# Actual Results May Vary Due to Various Factors

- Projected declines in the equity ratio, even under no economic stress
- Extraordinary losses and/or failures in credit unions that are not market-related, such as those from fraud or other asset “bubbles”
- Unusual or abnormally high insured share growth materially different from the historical correlation
- Economic conditions that involve greater volatility in one or more market indicators as compared to the stress scenarios modeled

# What to Expect Next

- Update the website for the 2020 Normal Operating Level.
- Once all required data is available, the actual Equity Ratio as of December 31, 2019, will be calculated.
  - The Share Insurance Fund's equity position at December 31, 2019, will be available by **February 14, 2020**, when the audited year-end financial statement is published.
  - Insured shares as of December 31, 2019, are expected to be available by **March 6, 2020**, once all year-end call reports are submitted and the data is validated and scrubbed.
- Determine whether a Share Insurance Fund distribution will occur in 2020.
  - If the year-end Equity Ratio is above the normal operating level, and the other statutory criteria are met, there will be a distribution sufficient to bring the Equity Ratio down to the normal operating level. This would occur no later than the end of the second quarter of 2020.
  - If the year-end Equity Ratio is below the normal operating level but above 1.30 percent, no premium can be assessed according to the FCU Act; premiums can only be assessed when the equity ratio is below 1.30 percent.