Voluntary Prepayment of Corporate Stabilization Fund Assessments
Frequently Asked Questions

<u>General Program</u>

1. Is the program mandatory?

No. The program was developed solely in response to credit union requests. The Federal Credit Union Act does not allow the National Credit Union Administration (NCUA) to charge a mandatory prepaid assessment to all credit unions. The program, however, allows eligible credit unions to prepay some of their Stabilization Fund assessments on a voluntary basis. Each credit union will therefore decide whether to participate in the Voluntary Prepayment of Corporate Stabilization Fund Assessments program.

2. Why does the program to prepay Stabilization Fund assessments have to be voluntary?

The Federal Credit Union Act does not allow NCUA to charge a mandatory prepaid assessment to all credit unions. The law, however, does allow credit unions to make voluntary prepayments under certain conditions.

3. How does this program differ from the mandatory nature of FDIC's program?

The Federal Deposit Insurance Act allows the Federal Deposit Insurance Corporation (FDIC) to assess mandatory prepayments of assessments. The Federal Credit Union Act, however, does not allow NCUA to require federally insured credit unions to make mandatory prepayments of assessments. As a result, NCUA has created a voluntary program.

4. Why is NCUA making this program available?

NCUA developed this voluntary program in response to requests from credit unions desiring to prepay Stabilization Fund assessments. Nothing has changed at this time in terms of NCUA's estimates related to the Stabilization Fund.

5. What are the differences between the approved Voluntary Prepayment of Corporate Stabilization Fund Assessments plan and the proposal released in May? Did the NCUA Board consider the comment letters before the approving the program?

Yes. NCUA released a proposal in May to gather public feedback on permitting credit unions to voluntarily prepay Stabilization Fund assessments. In response, NCUA received 184 comments from a variety of sources. The overwhelming majority of respondents favored moving forward with a formal plan.

As a result of suggestions received from the respondents and additional research by agency staff, NCUA incorporated several changes into the final program approved by the Board:

- First, NCUA lowered the minimum participation amount from $10,000 to the greater of $1,000 or 0.05 percent (5 basis points) of March 31, 2011, insured shares.
- Second, NCUA increased the maximum participation amount from 0.36 percent (36 basis points) to 0.48 percent (48 basis points) of March 31, 2011, insured shares.
- Third, NCUA increased the aggregate amount required to go forward with the program from $300 million to $500 million.
- Finally, NCUA committed to using all of the funds received from the voluntary prepayment of Corporate Stabilization Fund assessments for a dollar-for-dollar decrease in 2011 assessments.

With this last change, however, NCUA also determined that to ensure that assessments stayed on a reasonable payment trajectory and to maintain a responsible level of borrowing capacity, the agency needed to set the program's size at $500 million. If an oversubscription occurs, NCUA will prorate credit union commitments to achieve the $500 million level.

6. Why did NCUA select $500 million as the size for the program?

NCUA set a specific program goal to satisfy credit unions preference to have funds raised by the program apply dollar-for-dollar to reduce assessments in 2011. The specific program goal of $500 million preserves NCUA's flexibility in managing:

- The regular annual assessments over the life of the Stabilization Fund (especially in the next 4 to 5 years), which are an expense to credit unions, in as counter-cyclical a manner as possible; and
- The cash needs and contingency funding available to the Stabilization Fund.

The $500 million goal is also intended to ensure broad participation and that the program results in a meaningful reduction in the 2011 assessment.

7. What is the minimum and maximum amount I can prepay, and why are there these parameters?

The minimum amount is the greater of $1,000 or 0.05 percent (5 basis points) of March 31, 2011, insured shares. The maximum amount is 0.48 percent (48 basis points) of March 31, 2011, insured shares. NCUA set a minimum due to the administrative costs associated with the program. The maximum amount ensures that the prepayment is not material in relation to the credit union's balance sheet and also encourages wide-spread participation in the Voluntary Prepayment of Corporate Stabilization Fund Assessments program rather than just a select few institutions carrying the entire load.

8. It seems like an individual credit union should be able to prepay as much as it wants. Why is NCUA limiting prepayments to 48 basis points of insured shares?

NCUA limited the amount any one credit union could prepay for two reasons.

First, the amount needed to be immaterial to the credit union's balance sheet and the earnings immaterial to the credit union's income statement. As the funds will be tied up for some time, depending on the amount committed, NCUA wanted to ensure that there would be no future adverse impact to the credit union from the long-term nature of the asset and the lack of earnings from the asset. As NCUA could not draft a program that looked at the unique risk profile in each credit union, the agency established a limit that was small enough and which fit within the risk profile of most credit unions. The 48 basis points level also limits the likelihood prepaid funds will never be used for offsetting regular assessments, and then need to be returned at the end of the Stabilization Fund's life.

Second, NCUA established a limit to ensure wide-spread participation from credit unions. NCUA did not want a handful of credit unions to accept the onus for the assessment reductions and put themselves at a competitive disadvantage as a result of their commitment to the industry and credit union movement as a whole.

9. Will NCUA make interest payments to credit unions on their prepaid assessments?

No. The interest rate on prepayments is zero. Participating credit unions will not receive any interest or any other form of compensation from NCUA in connection with the Voluntary Prepayment of Corporate Stabilization Fund Assessments program.

NCUA is implementing the program based on its authority, under Section 127 of the Federal Credit Union Act. An interest-free prepayment is permitted. However, NCUA does not have direct authority to issue interest-bearing debt.

10. What is the purpose of the program to allow for the voluntary prepayment of Corporate Stabilization Fund assessments?

When NCUA implemented the Corporate System Resolution plan in September 2010, communications made clear the need for larger cash outlays in 2011 and 2012 than in later years. The higher levels of cash are needed to satisfy obligations under the Temporary Corporate Credit Union Liquidity Guarantee Program and the Temporary Corporate Credit Union Share Guarantee Program.

During town hall meetings about the Corporate System Resolution, many credit unions requested that NCUA develop a program similar to one imposed by the FDIC to prepay assessments to provide the cash needed in the near term without a corresponding requirement to expense a regular assessment. NCUA developed this voluntary program to respond to these requests within the agency's existing statutory and regulatory framework.

11. How will NCUA use the funds collected through the Voluntary Prepayment of Corporate Stabilization Fund Assessments program?

NCUA will use the prepayments to reduce, dollar-for-dollar, the 2011 assessment. There are obligations NCUA must satisfy from the asset management estates arising from the Temporary Corporate Credit Union Liquidity Guarantee Program and the Temporary Corporate Credit Union Share Guarantee Program. Specifically, the funds will cover the repayment of guaranteed corporate medium-term notes, guaranteed notes payable to the bridge corporates net of the amount raised via the NCUA Guaranteed Notes securitization program, and a small amount of other miscellaneous obligations of the corporates' asset management estates.

12. Are all federally insured credit unions eligible to participate?

More than 98 percent of credit unions are presently eligible to participate in the Voluntary Prepayment of Corporate Stabilization Fund Assessments program. Under the program, all federally insured credit unions are eligible to participate as long as their asset size is sufficient such that the program's $1,000 minimum amount for participation does not exceed 0.48 percent (48 basis points) of their March 31, 2011, insured shares. Using this criterion, a credit union must have at least $230,000 in assets to participate.

13. Will NCUA publicize which credit unions participate and how much they prepay?

No. The prepayment of Corporate Stabilization Fund assessments is a voluntary program developed at the request of credit unions. As a result, NCUA does not intend to publish a list of which credit unions participate in the program or the amount of a credit union's participation. A published list could make it appear that NCUA is pressuring credit unions to participate. Whether a credit union participates is solely a business decision of the credit union.

To facilitate the automated calculation of risk based net worth, NCUA will, however, establish a line on the September 30, 2011, Call Report to account for the amount of a credit union's participation in the program. Because this information will be publicly available, it is possible that others will create and publish a list of participating credit unions and the amount of participation.

14. Is there sufficient capacity in the credit union system to create a Voluntary Prepayment of Corporate Stabilization Fund Assessments program?

Yes. NCUA has determined that the credit union system has sufficient capacity through the normal assessment process to meet the guarantee obligations for 2011 and 2012. Within the framework established by Board, the credit union system also has enough liquidity to cover commitments made through the Voluntary Prepayment of Corporate Stabilization Fund Assessments. The program, created solely in response to credit union requests, is a way to ease the expense side of the equation. NCUA remains neutral as to whether credit unions should participate in the voluntary program.

<u>Effect on Corporate Stabilization Fund</u>

15. How will the voluntary prepaid Corporate Stabilization Fund assessments ultimately affect the costs of the Corporate System Resolution process?

The voluntary prepayment of Corporate Stabilization Fund assessments will have no effect on the overall cost of the Corporate System Resolution process. Prepayments received through the program will change the timing of the collection of assessments for participating credit unions, but not the aggregate assessments that credit unions provide to the Stabilization Fund over time.

In town hall meetings and webinars about the Corporate System Resolution plan, NCUA has indicated that the current best estimate of the amount credit unions will pay in assessments going forward is between $7 billion and $9.2 billion. This amount takes into consideration the total losses, less the capital in the corporate credit unions that was depleted, and less the assessment amounts already paid. As time goes by, this estimate may change, but currently this range represents NCUA's present best estimate of losses going forward.

16. How much participation is necessary for the Voluntary Prepayment of Corporate Stabilization Fund Assessments program to really make a difference in 2011 assessments?

NCUA determined that $500 million is the appropriate size for the program. This level of funding allows NCUA to use the prepayments to reduce assessments in 2011 dollar-for-dollar as credit unions requested. If credit unions prepay the $500 million target amount, projected assessments would be reduced by 6.4 basis points in 2011.

NCUA will also continue with Treasury borrowings and repayments as originally planned. The $500 million in voluntary prepayments will allow NCUA to manage the program without creating assessment spikes in the out years.

17. Would the program reduce credit unions' Corporate Stabilization Fund assessments? If so, then for how long?

Yes and no. The program would affect the amount of each year's assessment through time, but not the total amount of assessments. The program would reduce the size of assessments in 2011, but as a result assessments would be higher in 2013 and later than they would be without the program.

18. How much would this program reduce Corporate Stabilization Fund assessments in 2011?

With the $500 million target amount, projected assessments would drop 6.4 basis points in 2011, from 24.9 basis points to 18.5 basis points.

19. Will the program affect assessments after 2012?

Yes. Without the program, NCUA estimates Corporate Stabilization Fund assessments of approximately 25 basis points in 2011 and 13 basis points in 2012. The program, however, will lower assessments in 2011 by 6.4 basis points; therefore, assessments in later years must naturally be larger.

20. NCUA previously indicated that the voluntary prepaid assessment amounts would be offset against the Corporate Stabilization Fund assessments for the years 2013 and beyond. Is this what credit unions really want?

In response to the request for public feedback about the voluntary prepayment initiative, 133 of the 169 commenting credit unions stated they would participate in the program. In town hall meetings and other venues, NCUA Board and staff members have also heard that some credit unions want to pay all of the costs associated with the Corporate Stabilization Fund at once, while others want to spread out the payments as much as possible. The Voluntary Prepayment of Corporate Stabilization Fund Assessments program does not allow credit unions to expense the prepaid amount, but it allows more flexibility in annual assessments in 2011 for purely cash management needs. To date and in accordance with the statutory requirements of the Stabilization Fund, the Board has sought to be as flexible and counter-cyclical in assessments as prudently possible, balancing short- and long-term considerations.

21. Why does NCUA have higher cash needs in 2011 and 2012?

As part of stabilizing the corporate credit union system and preventing the cascade of losses throughout the industry, NCUA put into place several programs to maintain liquidity in the system until the legacy assets could be effectively dealt with permanently and at the least cost to credit unions, subject to sound public policy. Those programs established guarantee obligations that will come due in 2011 and 2012. The higher cash needs in 2011 and 2012 were always part of the overall resolution plan and were explained in the materials NCUA provided when implementing the Corporate System Resolution plan in September 2010.

22. Will NCUA have different assessment levels for credit unions that do not prepay and those who do prepay? If not, why not?

No. By law, NCUA must assess all credit unions their *pro rata* share of the losses. The decision of a credit union to establish or not to establish a prepayment amount does not affect this statutory requirement.

Effect on Individual Credit Unions

23. What incentives are there for credit unions to participate in the Voluntary Prepayment of Corporate Stabilization Fund Assessments program?

The $500 million program goal equates to 6.4 basis points of system-wide insured shares, and would reduce the projected 2011 regular assessment dollar-for-dollar from 24.9 basis points to 18.5 basis points.

24. What are the benefits of participating in the prepayment program?

Participating credit unions will be able to prepay assessments in a year when liquidity is high and interest rates are low. The program also will reduce assessments for all credit unions, regardless of their participation, in 2011. Participating credit unions will have reduced cash outlays for Corporate Stabilization Fund assessments starting in 2013.

25. What are the potential risks to a credit union associated with the program?

Credit unions should explore several factors and consider a number of possibilities before making the decision to participate in the Voluntary Prepayment of Corporate Stabilization Fund Assessments program. The credit union should perform a risk assessment on the impact to their earnings, liquidity and interest rate risk profile. Depending upon the amount of the credit union's participation, the funds could be tied up through 2021. Credit unions need to take this longer time horizon into account when determining whether they will participate and the amount of the participation.

In addition, credit unions should check with their accounting practitioner to determine what accounting treatment the practitioner believes is required for fair presentation of the asset on balance sheets and income statements.

26. Will each credit union's assessment reduction be tied to the amount it decides to prepay?

No. If the $500 million program goal is met, then all credit unions will receive a reduction in assessments in 2011 regardless of participation and the amount prepaid.

27. If a credit union prepays some future assessments in 2011, when would NCUA draw on that prepayment to cover future assessments?

NCUA would begin drawing against prepayments for assessments beginning in 2013. Participating credit unions would begin expensing assessments against the prepaid asset in 2013, while non-participating credit unions would pay the full amount.

28. Why doesn't the use of a credit union's offsetting prepaid assessment kick in until 2013?

Because the function of the prepayments is to raise additional cash, if NCUA were to offset 2011 and 2012 assessments against that cash it would defeat the purpose of the program. For example, if NCUA needed $3 billion in cash for the next two years, and raised $500 million through the prepayment program, NCUA would then assess the remaining $2.5 billion in 2011 and 2012. If credit unions were able to offset the prepayments immediately, NCUA would either be short the $500 million of the prepayments or have to assess the original $3 billion to come out even. Consequently, NCUA cannot start offsetting against the prepayment amounts until 2013.

29. Why can't NCUA pay interest to credit unions that prepay Corporate Stabilization Fund assessments?

Participating credit unions will not receive any interest or any other form of compensation from NCUA in connection with the Voluntary Prepayment of Corporate Stabilization Fund Assessments program. NCUA is implementing the program based on its authority, under Section 127 of the Federal Credit Union Act. An interest-free prepayment is permitted. NCUA does not have direct authority to issue interest-bearing debt.

30. Has NCUA indicated how credit unions would account for the prepaid assessments? Why is NCUA telling credit unions to consult their accountants on the proper accounting treatment for the prepayments instead of deciding what the treatment should be?

NCUA strongly encourages credit unions interested in participating in the Voluntary Prepayment of Corporate Stabilization Fund Assessments program to consult with their accountants. Under the proposal, the prepayments would be prepaid assets from which actual assessments for 2013 and later would be paid. The prepayments would be treated by participating credit unions as an asset purchase instead of an expense until they are used by the Corporate Stabilization Fund to cover assessments. Participating credit unions would record their assessment expense annually as they are assessed by the NCUA Board.

31. As a credit union, what should I be considering before participating in the program?

In determining whether to participate in NCUA's Voluntary Prepayment of Corporate Stabilization Fund Assessments program, there are many issues that credit union boards and management should consider. Some of these issues include:

- Does the program benefit members of the credit union?
- Does the credit union have sufficient liquidity to commit to the prepaid assessment?
- Will the loss of interest income on the prepaid assessments be justified?
- Is the minimum to participate in the program appropriate for the credit union?
- Do the credit union's accountants have any issues regarding the accounting treatment of the prepayment?

32. How will a credit union's prepaid assessment be treated for risk based net worth calculations?

NCUA has determined that this "other asset" will be excluded from the risk based net worth calculation. As a result, starting with the September 30, 2011, cycle there will be a separate line on the Call Report to capture the amount of any prepayment outstanding.

33. If my credit union does not participate in the program, what will happen?

The program is entirely voluntary. Each credit union will decide for itself whether to prepay Corporate Stabilization Fund assessments. If the program meets the needed $500 million in assessments, then all credit unions, both participating and non-participating, would receive a reduction in anticipated assessments in 2011.

<u>Process Questions</u>

34. Has NCUA established a process for credit unions to inform the agency that they want to participate?

Yes. NCUA will send a Letter to Credit Unions that includes the following attachments: Program Agreement Instructions, Program Agreement, and an Authorization Agreement for Electronic Funds Transfer Payments. The instructions walk through the process of submitting the Program Agreement. This agreement is the notification and commitment that the credit union wants to participate in the program.

35. How does a credit union commit an amount, and when will the Program Agreement be due to NCUA?

A credit union will need to complete the Program Agreement and submit it to NCUA via e-mail, fax, or regular ground mail. The amount of prepayment is one of the items to be completed as part of the Program Agreement discussed in the above question. NCUA must receive the Program Agreement by Friday, July 29, 2011. The Program Agreement and its corresponding instructions are attachments to NCUA's Letter to Credit Unions about the program.

36. How and when will a credit union know if the aggregate program amount is reached?

Program Agreements are due to NCUA by Friday, July 29, 2011. On Tuesday, August 9, 2011, NCUA will notify interested credit unions by e-mail whether the $500 million target amount was reached or exceeded. If it was not reached, no further action will be taken.

37. How will the prepayment of Corporate Stabilization Fund assessments be made? When will NCUA debit a participating credit union's account?

To participate in the program, credit unions must have an Authorization Agreement for Electronic Funds Transfer Payments on file with NCUA. If a credit union wants to participate, but does not have the form on file, it needs to include the completed form with the Program Agreement. On Thursday, August 18, 2011, if the target amount is reached, NCUA will debit the credit union's account for either the amount of their commitment or the prorated amount of their commitment if the target amount is exceeded. The debit will flow through the Pay.gov system.

38. Will NCUA be providing Stabilization Fund financial statements?

Yes. Every month, the Stabilization Fund financial statements are part of the Chief Financial Officer's presentation to the NCUA Board. The presentation packet and the financial statement can be found on NCUA's website under Board Actions. Pull up the agenda for the month in question, and the presentation is a link inside that document.

Additional Questions

39. Why isn't NCUA using the Central Liquidity Facility for its additional cash needs?

Statutorily, the Central Liquidity Facility (CLF) can only provide secured borrowings to natural person credit unions for liquidity purposes. The CLF, by law, cannot lend to or provide payments of obligations on behalf of the Stabilization Fund.

In addition, the future borrowing potential for the CLF is undergoing review with the changes within the corporate credit union system. U.S. Central had subscribed to the CLF's capital stock on behalf of all credit unions. With the change in U.S. Central's circumstances, the disposition of this capital stock subscription is still under discussion with the remaining corporate credit unions. As the CLF's borrowing authority is a function of the level of capital stock and retained earnings it holds, until a clear disposition of the capital stock is made, the amount of the future borrowing authority remains in flux.

40. Why isn't NCUA using its emergency borrowing authority for additional cash needs?

Enacted in May 2009, NCUA's emergency borrowing authority sunset December 31, 2010. NCUA's current borrowing authority is $6 billion shared between the Stabilization Fund and the NCUSIF. All of that borrowing line, less a small contingency carve-out, will be used to fund the cash needs to meet the Stabilization Fund's guarantee payments in 2011 and 2012. NCUA does not expect to start paying down the Treasury line, and freeing up needed liquidity contingency funding, until Stabilization Fund assessments in 2013.

41. Why doesn't NCUA just assess the entire $9.2 billion and be done with it?

The impact of a one-time assessment for the entire amount to close out the Stabilization Fund would have a negative impact on the credit union industry and the NCUSIF. NCUA's estimates indicate that assessing the $9.2 billion would create an assessment of 118 basis points and reduce credit union net worth an average of 90 basis points. The result would be an additional 6,438 credit unions would become negative earners, 607 credit unions that are currently well-capitalized would fall below that level, and 19 credit unions would fail with an estimated cost to the NCUSIF of $686 million. In other words, while "ripping the band-aid off" sounds like a good approach, for many credit unions it would send the wrong signals to members in our currently recovering economy.

42. Why is NCUA using prepayments rather than just borrowing the full amount needed from the Treasury?

NCUA has a fixed borrowing line established by Congress. That line is $6 billion shared between the Stabilization Fund and the NCUSIF. NCUA is planning to keep $500 million available for contingency funding for other issues at the borrowing high point, but will be using $5.5 billion of the available credit line to meet the Stabilization Fund's cash requirements in 2011 and 2012. In looking at the complexity of credit union balance sheets, the interest rate risk and its corresponding liquidity implications, and the potential for a slow economic recovery, it is vital that NCUA keep some of the borrowing available for contingent needs and begin increasing this level over time. In moving forward NCUA will need to maintain a planned Treasury borrowing pay-down trajectory to free up more of the line for contingency purposes as part of the agency's management of the Stabilization Fund and NCUSIF.

43. Why doesn't NCUA use the NCUSIF to provide the needed cash for the Stabilization Fund cash needs?

The Stabilization Fund was established to provide the industry a way to ring-fence the losses attributable to the corporate credit union crisis and pay for those losses over time. Using the NCUSIF to meet the cash needs of the Stabilization Fund begins to blur the lines between the two funds and is not sound public policy. Also, as the shared Treasury borrowing line is taken up by Stabilization Fund uses, the need to keep the NCUSIF liquid and available to deal with any potential wide-spread liquidity or loss event precludes using it for Stabilization Fund cash management needs or expense payments.

Credit unions with further questions about the Voluntary Prepayment of Corporate Stabilization Fund Assessments program may either call (703) 518-6337 or send an e-mail to assessments@ncua.gov for more information.