NATIONAL CREDIT UNION ADMINISTRATION
REGION II

LETTER OF UNDERSTANDING AND AGREEMENT ISSUED BY AND BETWEEN THE NATIONAL CREDIT UNION ADMINISTRATION AND CALCO FEDERAL CREDIT UNION

During the March 31, 1999, Supervisory Examination, conducted by the National Credit Union Administration (NCUA), Examiner Dominic J. Carullo identified adverse conditions and trends in the Calco Federal Credit Union (Credit Union). If left unresolved, these conditions and trends will continue to undermine the Credit Union's financial stability and/or operations to a point where it may no longer function as a viable separate credit union.

The examination identified the following adverse trends and conditions:

1) The board of directors has not properly planned, directed , and controlled credit union operations in accordance with Section 113 of the Federal Credit Union Act, resulting in numerous problems cited below. The officials have not fulfilled the agreements reached in the Letter of Understanding and Agreement they signed on June 25, 1997. Specifically, the following agreements were not kept:

    a) Management abandoned the marketing plan developed in 1997.

    b) The board of directors failed to achieve the December 31, 1998, capital goal of 8.0 percent and the net capital goal of 6.0 percent. In fact, net capital has decreased since the Letter of Understanding and Agreement was signed. The net capital ratio as of March 31, 1999, is 5.06 percent.

    c) The board of directors failed to adequately fund the Allowance for Loan Losses as of March 31, 1999.

    d) The board of directors failed to establish mortgage loan limits and minimum appraisal requirements in the credit union's lending policies.

2) The credit union is operating at a net loss from operations. The credit union lost $74,407 over the last 27 months. The adjusted March 31, 1999 loss is $20,673.

3) Operating expenses are high, and increasing, contributing to the net losses. The operating expense/average asset ratio increased from 4.04 percent at December 31, 1996, to 5.02 percent as of March 31, 1999. The net operating expense/average asset ratio, which excludes Provision for Loan Loss Expense (PLL), increased from 3.71 percent to 4.60 percent over this same period.

4) Loan delinquency is high at 5.34 percent of loans.

5) The loan participation program has not been properly managed or controlled. Adequate documentation has not been obtained for loan participation loans. Examples of inadequate management are: delinquent loan reports have not always been received, collection efforts have not been made,documented explanations of the risk ratings have not been provided, loan agreement forms are not proper, and loan payments have not been received on a timely basis.

6) Loan charge-offs are excessive. The credit union experienced net charge-off ratios of 1.66 percent for 1997, 0.67 percent for 1998, and 0.87 percent through March 31, 1999.

7) The credit union did not comply with Full and Fair Disclosure requirements as stated in NCUA Rules and Regulations, Part 702.3. The Allowance for Loan Loss Account was underfunded by $10,526 as of March 31, 1999.

8) Management submitted inconsistent Y2K Quarterly Reports to NCUA. The credit union reported 12 critical systems and 13 non-critical systems on it's quarterly reports through September 30, 1998. It reported 8 critical systems and 6 non-critical systems for December 31, 1998.

9) The internal Y2K reports to the Board of Directors are incomplete. The reports do not discuss the function and status of each critical and non-critical system reported in the NCUA Quarterly Y2K Reports.

AGREEMENTS AND TIME FRAMES

1) The board of directors will develop and adopt a capital accumulation plan by June 30, 1999, which will assure the following net worth goals are achieved:

Date	Net Worth Ratio
06/30/1999	5.30%
09/30/1999	5.55%
12/31/1999	5.80%
03/31/2000	6.05%
06/30/2000	6.30%
09/30/2000	6.55%
12/31/2000	6.80%
03/31/2001	7.05%

2) The board of directors will review the credit union's performance in relationship to the budget on a monthly basis and take action to reduce operating expenses so the net earnings will conform to the budget.

3) The board of directors will manage the income and expenses of the credit union to achieve an annualized return on average assets (ROA) of 1 percent each quarter beginning with the third quarter of 1999.

   For purposes of this Agreement, the return on average assets is defined as the net operating income remaining after accounting for all operating expenses, including provision for Full and Fair Disclosure, as required by NCUA Rules and Regulations, Part 702.3, dividends on all shares and exclusive of non-operating gains divided by the average assets for the period.

4) The credit union's delinquent loan ratio will be no greater than 4.25 percent by March 31, 2000. Management will aggressively pursue collection efforts for delinquent loan participation loans by working with the loan participation partner or by collecting the loans with its own personnel.

5. The board of directors will limit loan participation loans to 30 percent of the total loan portfolio and will assure proper documentation is obtained before loans are purchased.

6. The board of directors will fund the Allowance for Loan Losses account $10,526 by June 30, 1999. Management will ensure loan participation loans are adequately reserved for in the future.

7. The board of directors will submit consistent and accurate Y2K Quarterly Reports to NCUA.

8. The manager will provide comprehensive monthly Y2K reports to the board of directors. The reports will describe the function of each critical and non-critical system and communicate what was done to determine the current Y2K status of each system. The board of directors will be responsible for certifying the credit union is Y2K ready.

9. The board of directors will adopt an appropriate Y2K Business Resumption Plan and mail the plan to Examiner Carullo by June 30, 1999. The plan will be in conformance with the guidance provided in NCUA Letter 98-CU-12. The plan must include:
   a) Organizational planning guidelines to define the business continuity planning strategy,
   b) A business Impact analysis of each mission-critical system,
   c) A contingency plan for each mission-critical system, and
   d) A plan for validating each business resumption contingency plan.

This Letter of Understanding and Agreement shall remain in effect until the conditions cited above have been resolved and the agreements reached have been met. It is understood if the "agreed upon actions" are not finalized within the stated "time frames," NCUA may take administrative action to remove any official or management personnel, or use other available administrative remedies, including merger, liquidation, or conservatorship. This LUA will be published.

Therefore, the following individuals, as authorized by the board of directors of the Credit Union, indicate they understand and agree with the contents of this Agreement by affixing their signatures below. The officials understand by signing this Agreement, they must make a sustained and conscientious effort to resolve conditions and trends cited.

For the Calco Federal Credit Union:

Chairman of the Board of Directors	6-28-99 Date
Vice Chairman	6-28-99 Date
Treasurer	6/28/99 Date
Board Member	6-28-99 Date
Board Member	6-28-99 Date

For the National Credit Union Administration:

Examiner	6/28/99 Date
Supervisory Examiner	6/28/99 Date
for Regional Director, Region II (Capital)	6/30/99 Date