The NCUA REPORT

NATIONAL CREDIT UNION ADMINISTRATION

JUNE 2011 NUMBER 6 WWW.NCUA.GOV

HIGHLIGHTS

NCUA SEEKS INPUT ON VOLUNTARY PREPAID ASSESSMENTS

During nationwide appearances, many stakeholders have pressed NCUA Board Members to develop a program for prepaying the costs associated with the Temporary Corporate Credit Union Stabilization Fund (Stabilization Fund), similar to FDIC's mandatory Deposit Insurance Fund prepayment assessments. In response, NCUA on May 19 put out for public review a proposed Voluntary Prepaid Assessments Plan.

While NCUA lacks the statutory authority for a mandatory program, the agency can offer a voluntary plan. Generally, the plan would allow participating credit unions to make voluntary prepaid assessments in 2011. By permitting credit unions to prepay future assessments for 2013 and beyond, the plan would reduce anticipated assessments in 2011 and 2012.

The NCUA Board must make a final decision on the plan this month. Public input received by June 20 will determine interest in and possible refinements to the plan.

Cash Management, Not Cash Requirement

Nothing has changed in terms of cost expectations to resolve the corporate credit union system. The Stabilization Fund's cash flow projections still show a need for between $7 and $9.2 billion in cash outlays through Oct. 2012.

To cover these needs, NCUA will primarily borrow against a $6 billion U.S. Treasury credit line, maintaining a margin for contingencies. Credit union assessments in 2011 and 2012 will cover the majority of the remaining needs.

Potential Benefits of Voluntary Prepaid Assesments to Participating Credit Unions

- Prepay assessments this year when liquidity is high and interest rates are low.
- Reduce assessments on all credit unions in 2011 and 2012.
- Reduce participating credit unions' cash outlays for assessments starting in 2013.

Elements of the Plan

The Voluntary Prepaid Assessments Plan has several elements. First and foremost, participation would be determined by each credit union.

NCUA is considering setting the minimum advance amount for each federally insured credit union at $10,000 and a maximum advance amount of 36 basis points of a

CONTINUED ON PAGE 9

Chairman's Corner

EFFECTIVE EXAMINATIONS REQUIRE EFFECTIVE COMMUNICATIONS

Debbie Matz
Chairman

In college, examinations had a threatening decisiveness. We studied hard, sweating over how each test could affect our class standings. When we got a good grade, we celebrated.

Sometimes, when we got a lower-than-expected mark, we gathered the courage to ask the professor to alter it. Every once in a while, if we showed our work or thought process and demonstrated a sound grasp of the material, the appeal would work: The professor would change the grade.

An NCUA examination is much like a college test, but effective communication should occur much more frequently. Examiners do their best to provide regular feedback to credit unions, and management is encouraged to engage examiners before getting the final report. And of course, credit unions may appeal results.

NCUA holds examiners accountable for their findings, which is why they must be thorough and tough. This accountability, however, should not prevent ongoing dialogue between credit unions and examiners. NCUA also prioritizes the timely delivery of exams so a board of directors can take immediate action.

For this reason, credit unions should maintain continuing discussions with their examiners.

Sometimes, management may disagree with the facts an examiner presents, the analysis of those facts, the conclusions reached, or the tone or severity of a report. In such cases, credit unions should engage directly with their examiners to resolve these issues. By talking to each other, the parties frequently can come to a meeting of the minds. Direct communications often resolve issues like implementation timelines and the imposition of new controls.

If such interaction fails to resolve issues, credit unions have other options. These options are presented in the section below.

For the examination process to work well, examiners and credit unions must maintain open communication lines. Through dialogue, examiners and credit unions can often resolve issues quickly. In those cases where they cannot, NCUA has adopted formal and informal appeal mechanisms to consider and fix problems.

In other words, NCUA has an open-door policy for resolving complaints. Go ahead and knock!

Debbie Matz

BACKGROUND ON APPEALS PROCESS

Examiner. The first step in the formal appeals process is to approach your examiner. Using this step can be effective when there is disagreement over the facts, conclusions and tone of the report.

Supervisory Examiner. A second step in the formal appeal process after speaking to your examiner is to contact the supervisory examiner, who will evaluate the facts and review the analysis.

Regional Office. Credit unions may also send a letter to the regional office. In this third step, the regional director will weigh the facts and reach a decision.

Supervisory Review Committee. As a last step, a credit union may contact NCUA's Supervisory Review Committee. This panel, comprised of three senior NCUA executives, considers and makes recommendations on a variety of issues. Primarily, though, it handles appeals on CAMEL codes and reviews of Allowance for Loan and Lease Loss funding determinations.

Informal Methods. Informal dispute-resolution mechanisms include writing to the Office of General Counsel about legal issues or the Office of Examination and Insurance about safety-and-soundness matters.

Inspector General. If a credit union feels an examiner's behavior has been inappropriate, contact the Office of Inspector General at 800-778-4806.

Zero-Tolerance for Retribution Policy. NCUA has taken steps to ensure that credit unions may appeal without fear. To protect credit unions from any chance of reprisals, NCUA has instituted a zero-tolerance retaliation policy. Examiners may not take action against a credit union for using any formal or informal appeal channel. Moreover, NCUA examination report covers now contain a statement highlighting this policy.

BOARD ACTIONS May 19, 2011

BOARD VOTES TO EASE COMMUNITY DEVELOPMENT LOANS AND BLOCK UNWARRANTED GOLDEN PARACHUTES

In May, the National Credit Union Administration (NCUA) Board convened its fifth open meeting in 2011 at the agency's headquarters to consider:

- A plan for a program requested by stakeholders to allow voluntary prepayments of assessments in order to improve the liquidity of the Temporary Corporate Credit Union Stabilization Fund (Stabilization Fund);
- A proposed rule to ease regulatory burdens, improve transparency, and remove the interest rate barrier on the Community Development Revolving Loan Fund;
- A final rule to impose limits on golden parachutes and indemnification payments to block unwarranted payouts to individuals whose actions undermine a credit union's finances;
- Final revisions to NCUA's advertising regulation to enhance public understanding of credit unions protected by federal insurance; and
- A final rule to clarify the Dodd-Frank Act's requirement to provide temporary unlimited deposit insurance coverage for non-interest bearing transaction accounts.

The Board approved all proposed and final rules presented. The Board also received updates on the performance of the National Credit Union Share Insurance Fund (NCUSIF) and the Stabilization Fund. The NCUSIF, which recently received a clean 2010 audit, remained steady at the end of April with a 1.29 percent equity ratio for the seventh straight month. The Stabilization Fund's total assets grew by about $3 million in April.

NCUA Seeks Input on Plan for Voluntary Prepaid Assessments

The Board received a briefing about a proposal to create a voluntary prepaid assessments program. For more information, see story on page 1.

NCUA Proposes Streamlining Community Development Loan Process

In an effort to encourage low-income credit unions to apply for below-market-rate loans from NCUA, the Board issued a proposed rule intended to lessen regulatory burdens, eliminate outdated procedures, and advance transparency with respect to loans and technical assistance. Overall, the proposed rule greatly streamlines the program requirements and improves flexibility to administer the Community Development Revolving Loan Fund (Part 705).

NCUA anticipates the proposed rule will result in increased loan demand due, in part, to reduced program burdens on participating credit unions, thereby enhancing the provision of basic financial services for low-income households.

The proposed rule adds definitions, eligibility requirements, examples of how loans from this fund can be used, and greatly simplifies the current rule. Most significantly, the proposed rule removes the requirement that NCUA charge an interest rate between 1 and 3 percent APR. This change is intended to provide flexibility to charge a below-market APR no matter how low or how high the prevailing rates move in the future. The proposal also better details the application and award processes, and post-award reporting requirements.

By a 3–0 vote, the Board issued the proposed rule with a 60-day comment period.

Golden Parachute Rule Curtails Payouts at Troubled Credit Unions

To protect credit union members and guard against unwarranted disbursements to individuals whose actions may have contributed to a credit union's distressed financial condition, the Board approved a final rule covering golden parachutes and indemnification payments to institution-affiliated parties (Part 750).

The rule prevents federally insured credit unions from providing lucrative rewards to departing executives in certain situations. The "golden parachute" provisions would apply to troubled credit unions affected by insolvency, a conservatorship, or rated CAMEL 4 or 5. The rule additionally differentiates between legitimate severance payments or *bona fide* deferred compensation arrangements and improper golden parachutes.

The rule also establishes limits on a federally insured credit union's ability to provide indemnification. The new rule will only apply in conjunction with administrative enforcement actions brought by the agency or by a state regulator in the case of a state-chartered institution, such as the assessment of a civil monetary penalty, the imposition of a cease-and-desist order, or removal from office.

This rule has exemptions that apply to certain types of employee benefits, severance agreements and current employment contracts. The rule also provides for a method, under certain circumstances, in which a credit union may make an advanced indemnification payment.

As adopted, the final amendments also consolidate in one place those provisions that overlapped with the corporate credit union rule (Section

CONTINUED ON PAGE 6

The World Comes to Alexandria

FROM GIGI HYLAND, NCUA BOARD MEMBER

In early June, NCUA had the honor of hosting credit union regulators from around the world at its offices in Alexandria, Va. The meeting was the World Council of Credit Unions (WOCCU) International Credit Union Regulators' Roundtable, and I am privileged to serve as the NCUA Board representative to WOCCU.

More than 40 representatives from entities around the world that supervise credit unions attended the meeting. We had participants from 18 countries—from Canada to Tanzania, Brazil to Australia, and the United Kingdom to Korea.

Similar to last year's meeting, we discussed a wealth of subjects. One of the most interesting sessions was the so called "tour de table" where every participant had 5 minutes to discuss the top issues facing the credit union regulator in each country. It's stunning how the themes were so similar regardless of the credit union movement's size.

Attendees were treated to a fascinating Basel Committee update from the distinguished Karl Cordewener, Deputy Secretary General of the Basel Committee on Banking Supervision. In addition, topics of discussion included: successful tactics to restore problem institutions, supplemental capital, governance, over-indebtedness and credit union mergers.

As regulators, we wrestle with the financial crisis effects on our institutions. We share the goal of finding better ways to identify emerging risks timely and to take appropriate supervisory actions to address such risks.

The true benefit of this annual meeting was access to an incredible network of committed, talented regulators with whom to talk and from whom to learn. Understanding our different systems and sharing our experiences helped all of us to be better regulators.

A Two-Way Street

FROM MICHAEL E. FRYZEL, NCUA BOARD MEMBER

Occasionally, a credit union trade association, state league or credit union official will voice a complaint. That complaint will center on an NCUA examiner who someone believes is exceeding their scope, being too inquisitive or just looking to find problems that do not exist.

We all know this is not a perfect world, and we are all human. We each make mistakes and could easily fall into conflict with someone over methods, procedures or even a difference in personalities.

NCUA has always advised credit unions that if you disagree with an examiner's findings, conduct or questions, take your concerns up the chain of command. Contact the supervisory examiner and, if necessary, the regional office. NCUA will review and evaluate your concerns and, if necessary, take corrective action.

Keep in mind that we continue in difficult economic times. The main focus of NCUA remains to protect the deposits of more than 90 million Americans, keep the credit union system safe and sound, and maintain a strong insurance fund. To do that, we must make sure that every federally insured credit union operates in accordance with the law, in the best interest of its members, and that its officers and directors are held to the highest fiduciary standards. The NCUA examiner is on the front line of making sure every credit union meets those requirements.

I am pleased to say that the great majority of our credit unions rise to what is expected of member-owned, cooperative financial institutions. Most credit union managers and their boards of directors have set high standards for their respective credit unions.

As much as we would like to believe all credit union officials have the best interest of their credit union and its members at

CONTINUED ON NEXT PAGE

The NCUA Report is published by the National Credit Union Administration, the federal agency that supervises and insures most credit unions.

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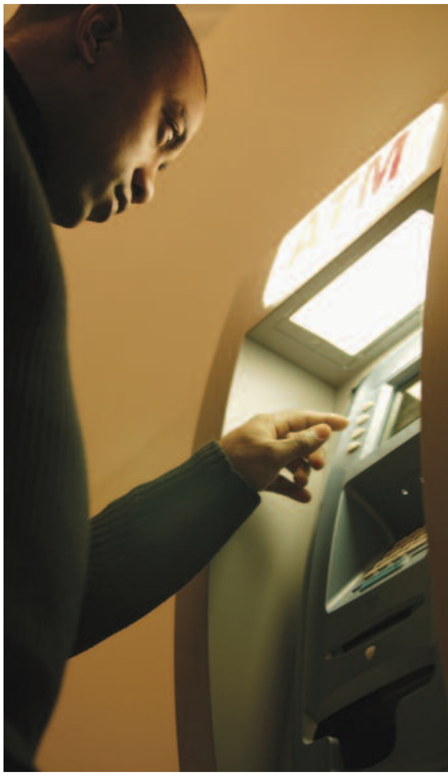
Office of Consumer Protection Report

AN OVERVIEW OF ATM DISCLOSURE RULES



The Electronic Fund Transfers Act provides a basic framework for the rights, responsibilities and liabilities of those entities offering electronic fund transfer (EFT) services. Under this statute, an operator must disclose fees imposed for using its automated teller machine (ATM). The law defines an ATM operator as any person who operates an ATM and who does not hold the account to or from which the EFT or balance inquiry is made.

To protect consumers, the law requires two notices. First, an ATM operator that charges a fee for EFT services must post a notice of that fact in a prominent and conspicuous location on or at the ATM. Second, the operator must disclose that a fee will be imposed and the amount of the fee before the consumer commits to completing the transaction.

This second disclosure may happen either through a display on the ATM's screen for a reasonable duration or by a paper notice. ATM operators cannot use a disclosure of the fee on a receipt after a transaction's completion to comply with the alternative paper notice procedure. In short, an ATM operator may not assess fees unless it provides proper notice and the consumer elects to complete the transaction.

Some ATM operators may only charge a fee for a specific type of transaction. In such cases, the notice may contain a general statement that a fee will be imposed for providing EFT services. Alternatively, the notice may specify the type of transaction for which the ATM operator will assess a fee.

Aside from making required disclosures, credit unions offering EFT services should develop and implement procedures to inspect their ATMs periodically and monitor disclosures posted on or at the terminals. Failure to provide the proper notices could result in civil liability for damages of up to the lesser of $500,000 or 1 percent of net worth, plus court costs and attorneys' fees. To avoid civil liability, a credit union must demonstrate that it posted the required notice and a person other than the ATM operator subsequently removed, damaged or altered the notice.

Since the law's enactment, the Federal Reserve Board has written the rules regarding EFT services. The new Consumer Financial Protection Bureau, however, will soon take over the responsibilities for drafting these regulations. NCUA will continue to enforce the law at federal credit unions with less than $10 billion in assets.

For additional information regarding ATM fee disclosures, please review the requirements at **http://go.usa.gov/DOZ** (Section 205.16 of Regulation E).

BOARD PERSPECTIVES (FROM PAGE 4)

heart, some, a very small number, unfortunately do not. And this is usually when an examiner is criticized for being too tough. Yet, this is when an NCUA examiner is at his/her best. Examiners find a problem and will continue to ask questions and look at the credit union's documents until they have confirmed they are right or wrong.

Recently, an NCUA examiner saw all of the red flags associated with serious problems at a credit union. When confronted with the suspicions, the CEO pushed back touting industry standing and vowing to fight and appeal the findings, which they did up the chain of command to the regional office. The entire time, the examiner remained professional and diligent, and the examination findings were confirmed at every level. As a result, NCUA found serious fraud and misappropriations. A bad apple: Every bushel has at least one.

So yes, examiners are sometimes difficult to deal with. Consider the stress they are under to insure safety and soundness in light of these difficult financial times. The NCUA Board holds our examiners to the highest standard, and they are some of the most dedicated and hardest working public employees.

Do not ever hesitate to exercise your rights if you feel unfairly treated. We will address and investigate the issues just as we will support the examiner who is doing his/her job. After all, it is a two-way street.

704.20). Upon the effective date, the final amendments to the new golden parachute rule delete the duplicative sections in the corporate credit union rule.

The Board unanimously approved the final rule. The rule changes become effective 30 days following publication in the *Federal Register*.

Advertising Rule Intended to Promote Federal Insurance

In an effort to improve public understanding about and confidence in credit unions' federal insurance coverage, the Board amended provisions of NCUA's advertising statement rule (Part 740).

The amendments require inclusion of a specified federal insurance coverage statement in a greater number of radio and television ads, annual reports and other statements of condition required by law. The amendments also dictate the size of the statement required in print advertising to ensure legibility.

Within the amended rule, NCUA newly defines the word "advertisement" as a "commercial message, in any medium, that is designed to attract public attention or patronage to a product or business." This meaning conforms to the Federal Deposit Insurance Corporation's definition.

The Board is sensitive to the needs of credit union access to affordable advertising outlets. As such, the Board changed the proposed rule from requiring the statement in all radio and television ads to only require the statement in ads 15 seconds or longer. Radio and television ads of that length will need to at least include the statement "Federally insured by NCUA." Print ads will need to include a similar statement or the official NCUA insurance sign.

The Board approved the amendments by a 2–1 vote. Although the rule's effective date occurs 30 days after publication in the *Federal Register*, mandatory compliance is delayed until Jan. 1, 2012, to ease the burden on credit unions that have already produced ad campaigns for 2011.

Board Clarifies Dodd-Frank's Share Insurance Changes

Upon enactment, Section 343 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 fully insured, on a temporary basis, the net amount depositors at insured credit unions maintain in non-interest bearing transaction accounts. The temporary insurance coverage remains in effect until Dec. 31, 2012.

To clarify several aspects related to this law, the Board approved a new rule with three parts (Part 745):

- The final rule defines a non-interest bearing transaction account to include "non-dividend bearing" to encompass standard credit union terminology, as well as including official checks from insured credit unions in the definition.
- The regulation provides that this new insurance coverage is separate from, and in addition to, other coverage by NCUA's share insurance rules.
- The rule imposes a requirement for certain notices and disclosures.

By a 3–0 vote, the Board approved the final rule without any changes from the proposal.

NCUSIF Equity Ratio Remains Steady, Scores Clean 2010 Audit

The NCUSIF received an unqualified or "clean" audit opinion for its 2010 financial reports. In addition, auditors recently certified the financial accuracy of the three other permanent NCUA funds: the Operating Fund, the Community Development Revolving Loan Fund, and the Central Liquidity Facility. KPMG LLP completed the audits of all four permanent funds. Expected this summer, KPMG also will provide its opinion of the financial statements for the temporary Corporate Stabilization Fund.

The NCUSIF remains stable, ending April with a 1.29 percent equity ratio for the seventh straight month. In addition, the NCUSIF ended the month with a $1.19 billion reserve balance.

During the first four months of 2011, the NCUSIF had total income of $76 million and total expenses of $39.6 million, resulting in net income of $36.4 million. Seven credit unions have failed during this period with year-to-date costs of $34.2 million.

In April, 374 federally insured credit unions with assets of $41.6 billion and shares of $36.9 billion had CAMEL code 4 or 5 designations. Additionally, 1,794 CAMEL code 3 credit unions had assets of $147.9 billion and shares of $130.9 billion. Overall, approximately 21 percent of all credit union assets were in CAMEL code 3, 4 or 5 institutions. The percentage of assets in CAMEL 1 and 2 credit unions has increased slightly in each of the past four months.

The Stabilization Fund total liabilities and net position stood at $393.9 million at the end of April, about $3 million higher than the end of March.

Financial data reported in 2011 for both the NCUSIF and the Stabilization Fund are preliminary and unaudited.

All open NCUA Board meetings are tweeted live. Follow @TheNCUA on Twitter. Board Action Memorandums are available online at www.ncua.gov under *Agency Leadership/NCUA Board and Actions/Draft Board Actions*. NCUA posts rule changes online at www.ncua.gov under *Resources/Regulations, Legal Opinions and Laws*.

Office of Capital Markets Report

SIZE MATTERS: ANOTHER PERSPECTIVE ON INTEREST RATE RISK

In March, the NCUA Board proposed a new rule on interest rate risk (IRR). This proposal calls for credit unions above $50 million in assets and those between $10 million and $50 million in assets with significant IRR exposures to maintain an effective, written IRR management policy.

To take advantage of today's steep yield curve, many credit unions have increasingly borrowed short and lent long, particularly with fixed-rate mortgages. The proposed rule was prompted by experience that such practices will cost credit unions through lost earnings and capital when rates rise.

The NCUA Report has recently explored IRR in different ways. An April story about the sharp rise in credit union residential mortgage lending—absolutely (as a percentage of assets) and relative to banks and thrifts—showed that a modest interest rate increase could reduce the net worth of a credit union with average exposure to long-term, fixed-rate mortgages by as much as 20 percent. A May column noted that relatively high holdings of net long-term assets, another measure of IRR exposure, did not vary greatly across NCUA's regions.

Averages, however, can be misleading given credit unions' ranges. Yet, 84 percent of credit unions are smaller than average.

For skewed distributions like credit union assets, medians better capture central tendencies than averages. The median credit union has about $18 million in assets. Viewed yet another way, nearly 2,800 credit unions are smaller than $10 million.

The table below illustrates potential IRR exposure by different credit union size groupings using three measures: first mortgages, fixed-rate mortgages, and long-term residential mortgages. Although adjustable-rate, balloon and hybrid mortgages can be quite complex, fixed-rate mortgages generally carry more IRR. Credit unions are also much more likely to make fixed-rate loans. Long-term mortgages—that is, residential mortgages repricing in 5 or more years—narrows the focus by excluding member business loans and loans with rates about to reset.

The table scales each measure by net worth to obtain a rough estimate of the ability to withstand a rate shock. The table also notes the percentage of credit unions in each size cohort holding each type of mortgage to show frequency in that asset range.

The table reveals a marked difference between large and small credit unions. More than 90 percent of institutions above $50 million in assets carry mortgages—a figure comparable to peer banks and thrifts. Mortgage holdings exceed net worth at the median credit union for all measures in all asset buckets greater than $50 million, save one.

Small credit unions, however, are positioned quite differently. By each measure, well below one-third of credit unions under $10 million in assets hold mortgages. These patterns explain why the proposed IRR rule excludes credit unions under $10 million in assets.

Potential IRR exposures for credit unions with $10–$50 million in assets are less clear. By every measure, more than two-thirds of these institutions carry mortgages. While significant, the median credit union's exposure in this group is still uniformly less than net worth.

CONTINUED ON PAGE 9

A Closer Look at Interest-Rate-Risk Exposure

As of December 31, 2010

Exposure Metric	FEDERALLY INSURED CREDIT UNION ASSET COHORT					All Credit Unions
	Below $10 Million	$10 – $50 Million	$50 – $100 Million	$100 – $500 Million	Above $500 Million	
Cohort Median, **First Mortgages** / Net Worth	0.0%	56.4%	140.1%	200.5%	265.7%	35.0%
Percent in Cohort with First Mortgages	19.0%	72.9%	96.1%	99.1%	99.7%	59.9%
Cohort Median, **Fixed-Rate Mortgages** / Net Worth	0.0%	29.6%	85.0%	121.7%	152.4%	14.3%
Percent in Cohort with Fixed-Rate Mortgages	16.6%	67.6%	93.2%	98.0%	99.7%	56.8%
Cohort Median, **Residential Real-Estate Repricing ≥ 5 Years** / Net Worth	0.0%	69.9%	128.6%	164.8%	188.2%	46.4%
Percent in Cohort with Residential Real-Estate Repricing ≥ 5 Years	26.0%	81.5%	96.7%	99.5%	99.7%	65.5%
Number of FICUs in cohort	2,781	2,395	794	1,000	369	7,339
FICUs in Cohort as Percentage of All FICUs	37.9%	32.6%	10.8%	13.6%	5.0%	100.0%
Total Assets in Cohort (in billions of dollars)	$ 10.8	$ 57.6	$ 55.7	$ 219.8	$ 570.5	$ 914.5
Assets in Cohort as Percentage of All FICUs Assets	1.2%	6.3%	6.1%	24.0%	62.4%	100.0%

John D. Worth
Chief Economist

Director's Report: Office of the Chief Economist

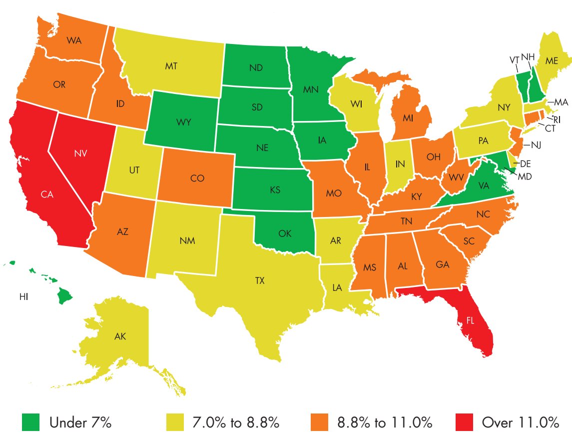
PROGRESS IN UNEMPLOYMENT

In the November 2010 edition of the NCUA Report, we looked at state-level unemployment rates and discussed the importance of local labor market experience as an accurate predictor of credit losses and loan demand. This column revisits this topic to provide an update on the state-level employment situation as we approach the end of the second year of the economic recovery.

Nationally, the unemployment rate remains high, but the employment situation is slowly improving. While many economists think the "full-employment" unemployment rate in the United States is 5.5 percent or less, the national unemployment rate edged back up to 9 percent in April, after falling to 8.8 percent in March. The unemployment rate peaked in October 2009 at 10.1 percent and was as high as 9.8 percent as recently as November 2010. Since then, the national rate has fallen nearly a full percentage point.

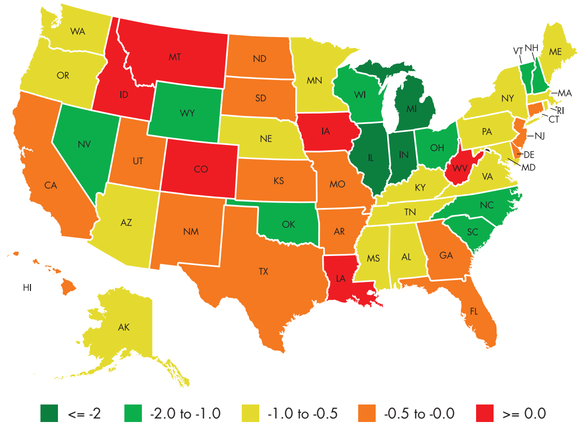
This trend reflects improved movement in private sector job creation. In the year ending in March, total nonfarm payrolls rose by 1.3 million jobs, with another nearly 250,000 jobs added in April. Private payrolls (excluding federal, state and local jobs) rose by nearly 1.7 million jobs.

State Unemployment Rates, March 2011



The recent improvement in the jobless rate shows up in other labor market indicators. In March, the number of job openings rose to 3.1 million, the highest level since the fall of 2008—when the financial crisis began to intensify—and the number of unemployed people per job opening fell to a ratio of 4.3 in March, down from a peak ratio of more than 6 in 2009.

Percentage Point Change in State Unemployment Rates from Year Earlier



State unemployment rates show considerable variation. Generally, western and southeastern states have unemployment rates higher than the March 8.8 percent national average (orange and red on the map), while states in the country's mid-section and in the Northeast generally have unemployment rates less than the national average (yellow and green on the map).

The high unemployment rates in California, Nevada and Florida are directly tied to the end of the housing bubble. At 3.6 percent, North Dakota had the lowest unemployment rate in the country in March.

State unemployment rates vary, but the direction of recent change has been more uniform. Most states have experienced declines in their unemployment rates during the past year. Unemployment has fallen in 44 states, while it has risen or stayed the same in only six states.

Michigan, with one of the highest unemployment rates in the nation in March, showed a 3 percentage point decline from a year ago. In the other high-unemployment

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DIRECTOR'S REPORT (FROM PREVIOUS PAGE)

states, the rate fell 1.6 percentage points in Nevada and a little less than half a percentage point in California during the past year.

The unemployment rate inched higher in Idaho and Louisiana, the two states showing the largest increase, by 0.7 and 0.9 percentage points, respectively. The effects of the tornados in the Southeast and flooding along the Mississippi may temporarily raise the unemployment rate in those areas over the next few months.

The unemployment rate is a good overall indicator of how well the economy is doing, both nationally, and in states and localities. How well these economies perform has an effect on credit unions. Analysis suggests that increases in state and national unemployment rates are associated with declines in credit union loan growth, higher levels of loan delinquency, higher loan charge-off rates, and a higher share of credit unions rated CAMEL 4 and 5.

We expect higher-than-normal unemployment rates to continue to pose challenges to credit unions for the next few years as the economy recovers from the effects of the recession. However, the recent improvement suggests most state labor markets are headed in a positive direction.

CAPITAL MARKETS REPORT (FROM PAGE 7)

To gain more insight, NCUA looked at the 2,395 credit unions in this asset range using a variety of IRR metrics. In the end, this analysis showed that a simple ratio—first mortgages plus long-term investments divided by net worth—did a very good job summarizing an institution's IRR exposure.

For credit unions in the \$10–\$50 million range with a ratio above one, median first mortgages to net worth stands at 179.9 percent and median long-term residential mortgages to net worth comes in at 148.1 percent. By comparison, institutions in this cohort with a ratio below one have median first mortgages to net worth of 2.7 percent and median long-term residential mortgages to net worth of 28.5 percent. These patterns explain why the proposed rule would apply to some, but not all, institutions in this cohort.

Specific strategies for reducing IRR exposure will differ across credit unions based on size, complexity, location and membership. But all strategies start with a simple rule: When you are in a hole, stop digging. In this context, putting down the shovel means recognizing the importance of an effective IRR management program to maintain long-term safety and soundness.

VOLUNTARY PREPAID ASSESSMENTS (FROM PAGE 1)

credit union's insured shares as of March 31, 2011.

To the extent sufficient participation exists, NCUA would lower the assessments all credit unions will need to pay in 2011 and 2012. For example, the first \$300 million of prepaid advances would decrease assessments by approximately 4 basis points total in 2011 and 2012.

The greater amount of prepaid assessments collected, the greater the reduction in 2011 and 2012 assessments. Maximum program participation could raise \$2.8 billion, which would result in a significant reduction of assessments and a decrease in borrowings from the U.S. Treasury.

NCUA is considering a minimum aggregate level of advanced assessments at \$300 million. This amount would give a credit union contemplating participation reasonable assurance of sufficient aggregate interest before committing funds. Credit unions interested in participating would pledge their amounts in advance. If, however, the minimum aggregate amount is not pledged, NCUA would not collect prepayments from any credit unions.

Other Program Considerations

Credit unions contemplating participation would need to weigh the associated lost opportunity cost and impact on liquidity of not having access to any funds provided to NCUA. NCUA anticipates that credit unions providing liquidity to the Stabilization Fund would not experience any material change in their net income or lending activities, given the current low-interest rate environment and substantial liquidity already existing in the credit union system.

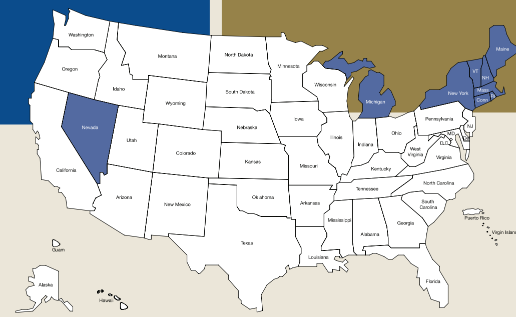
The plan's voluntary nature could also pose an economic free-rider issue, where all credit unions could benefit from assessment reductions in the short term at the expense of the subset of credit unions that voluntarily participate in the program.

Finally, NCUA expects participating credit unions should experience no adverse accounting implications. As part of due diligence, however, each credit union would need to research the appropriate accounting treatment prior to committing funds.

NCUA is soliciting public input by June 20 on whether to offer voluntary prepayments and, if so, what the criteria should be for participation. For more information about the Voluntary Prepaid Assessments Plan or to comment, go to **http://go.usa.gov/jVy.**

Region I Report

DOES YOUR CREDIT UNION'S BOARD OF DIRECTORS MEET NEW FINANCIAL LITERACY REQUIREMENTS?



REGION I

Credit union boards of directors have a responsibility to their memberships to provide the necessary direction and control of the institution. As such, directors need a basic level of financial skills consistent with the size and complexity of their credit union in accordance with NCUA's regulations (Section 701.4). The NCUA approved this new regulation Dec. 16, 2010.

The new rule requires a director to be able to read and understand the balance sheet and income statement. Directors must also be able to answer the following questions:

- What does each line item mean?
- Why is the line item important to the credit union?
- Is the value of the line item changing over time? If so, what does that change mean?
- Is the change important to the credit union?

To answer these questions, directors must understand the specific products and services provided to the credit union's membership, along with the potential risks associated with these products and services.

A credit union should have a policy that describes how the institution will make the appropriate training available to directors. Examiners will review that policy going forward.

Key Dates

Directors elected or appointed on or after Jan. 27, 2011, and who lack the requisite financial skills will have six months from the date of election or appointment to acquire them. Directors who were on board by Jan. 27 and who do not have the skills have until July 27, 2011, to comply with the new rules.

Available Training

For directors needing training, the 2011 Office of Small Credit Union Initiatives (OSCUI) annual workshops and roundtables include the topic. OSCUI oversees these training sessions with the assistance of economic development specialists.

Region I also aids small credit unions through the use of small credit unions program subject matter examiners. These examiners can assist small credit unions with issues such as policy development, obtaining a low-income designation, and expanding the field of membership. Currently, 36 credit unions in Region I receive such assistance. To obtain assistance, a Region I credit union can send a letter to regional director Mark A. Treichel requesting to be added to this program. Credit unions in other regions need to contact the appropriate regional office.

For board members of credit unions in Region I who need to obtain additional financial literacy training, upcoming OSCUI events include a workshop on July 23 in Albany, N.Y., and a workshop on Oct. 15 in Buffalo, N.Y.

Additional dates and locations are available nation wide. To determine the location and date of an event in your area, go to **www.ncua.gov** and click on upcoming events in the lower right hand corner to register.

Finally, a letter to federal credit unions from NCUA dated February 2011 addresses the requirements of NCUA's new financial literacy rules (LTCU No. 11-FCU-02). The letter includes more specifics concerning the policy requirements. As always, credit unions should contact their examiner for any questions.

The NCUA
REPORT

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