



Background Information For NCUA Corporate Credit Union ANPR Process

Corporate Structure and Governance

There are 27 corporate credit unions (CCUs), including U.S. Central, serving the nation's natural person credit unions (NPCUs). Similar to NPCUs, CCUs are guided by volunteer boards of directors, are totally owned and directed by their member/owners (which, in the case of corporates, are NPCUs) and were organized for the express purpose of providing low-cost financial services and competitive investment and lending rates to their member/owners.

Appendix A provides a glossary of accounting terms in light of all the accounting-centered discussion on corporates. Appendix B displays a map indicating the location of each CCU and Appendix C provides a timeline of selected system history events.

At least a majority of CCU board directors, including the chair, must come from member credit unions. The chair of the board may not serve simultaneously as an officer, director, or employee of a credit union trade association and a majority of directors may not serve simultaneously as officers, directors or employees of the same credit union trade association or its affiliates (not including chapters or other subunits of a state trade association).

Profit is not the driving force; rather, CCUs exist solely for the benefit of their member credit unions and, ultimately, all consumers – a key difference from other financial service providers. There is a unique philosophy of cooperation, self-help and economic democracy among the nation's CCUs and NPCUs.

CCUs operate with comprehensive policies and procedures commensurate with the risks and activities they undertake. These include, but aren't limited to, investments, credit risk management, asset and liability management and liquidity management.

Liquidity Management

The scope of CCU liquidity management encompasses the entire balance sheet as well as off-balance sheet exposures and addresses funding plan phases that cover conditions of

successively deteriorating liquidity scenarios. It involves assessing and managing both asset liquidity and liability liquidity and includes approaches that draw together all sources and uses of liquidity.

The primary objective is to strike a balance between liquidity, earnings and interest-rate sensitivity considerations in order to provide ongoing operations and safety for all member credit unions/owners. Liquidity management requires meeting the day-to-day and intraday cash flow needs primarily in the areas of payment processing, liability maturities, withdrawals and loans.

The investment guidelines of a Corporate Credit Union incorporate the investment practices that enable CCUs to maintain appropriate liquidity for their members. This provides a framework within which liquidity can be measured, reported and adjusted as appropriate.

Capital

Regulatory capital in the corporate system consists of retained and undivided earnings (RUDE), membership capital shares or MCS (typically a 3-year notice account) and paid-in-capital or PIC (some with notice features, some perpetual). MCS is considered regulatory capital, but ratings agencies do not consider it as true equity capital because of the notice feature. MCS and PIC are not subject to share insurance coverage by the NCUSIF or other deposit insurer and cannot be pledged against borrowings.

Membership capital is available to cover losses that exceed retained earnings and paid-in capital. PIC is callable only at the option of the corporate credit union and only if the corporate credit union meets its minimum required capital and NEV ratios after the funds are called. PIC is available to cover losses that exceed retained earnings, is generally perpetual in maturity, and is a noncumulative dividend account.

Based on November 2008 call report data:

- Total CCU assets equal \$73.4 billion (\$87 billion DANA - Daily Average Net Assets) – excluding U.S. Central. U.S. Central's assets at the end of November were \$36.1 billion (\$41.6 billion DANA).
- As of November, CCUs (excluding U.S. Central) had total regulatory capital of \$6.044 billion, encompassing \$2.49 billion in RUDE, \$495 million in PIC and \$3.06 billion in MCS. Average capital ratios as of November 2008 were 2.87% RUDE, 3.44% Core Capital (RUDE plus PIC) and 6.95% Total Capital (RUDE, PIC and MCS).
- U.S. Central had total regulatory capital of \$2.681 billion, encompassing \$697 million in RUDE, \$300 million in PIC and \$1.684 billion in MCS. Capital ratios at U.S. Central as of November 2008 were 1.68% RUDE, 2.4% Core Capital, 6.45% Total Capital.

- Total regulatory capital in the corporate system as of November 2008 equaled \$8.726 billion. Total Core Capital in the corporate system equaled \$3.98 billion.

Regulatory Framework

Corporate credit unions can be either state or federally chartered. The National Credit Union Administration (NCUA) Rules and Regulations apply to all federally chartered and state-chartered corporates. To protect the National Credit Union Share Insurance Fund (NCUSIF), federal and state examiners jointly examine state-chartered corporates. In addition, the NCUA has an office devoted to examining corporate credit unions (Office of Corporate Credit Unions).

All federally chartered corporates operate under federal corporate bylaws. State chartered corporates operate under state bylaws. All corporates have extensive policies and procedures appropriate to their business model, strategies and operating risks.

Expanded Authorities

The board of directors and senior management of each corporate periodically assesses the need for expanded investment authority in light of the products and services each corporate offers, or plans to offer, to their members. There are six distinct expanded authority alternatives (Base-Plus, Parts I, II, III, IV, and V) as set forth under Appendix B of Part 704 of NCUA's Rules and Regulations.

CCUs seeking expanded authorities must have the systems, support and operational capacity to identify, measure, monitor, report and control risk related to current and projected risk activities. Approval of expanded authorities may require extensive revisions to existing policies and procedures relating to, at a minimum, investments and asset and liability management. Other areas of operations will also be impacted and the policies and procedures governing those areas must be updated and managed accordingly.

The request for expanded authorities is a two-part process. A corporate must submit to NCUA a self-assessment plan supporting its request. The self-assessment plan must include draft policies and procedures, and the proposed systems and personnel needed to efficiently and effectively manage the proposed risk activity. NCUA reviews the plan and assesses management's ability to engage in the proposed risk activity given the infrastructure and other resource requirements described in the plan.

The second part of the process is implementation of the approved plan. NCUA staff perform an on-site reviews of the corporate's financial and operational condition before actual expanded authority transactions take place. This review includes evaluating the corporate's self-assessment plan, interviewing selected corporate staff and/or officials, and reviewing the adequacy of the systems most relevant to the proposed activity. Each

corporate must demonstrate its ability to operate safely and soundly under the additional authorities.

Services and Other Information

Corporate credit unions continue to fulfill their traditional roles while evolving to meet the growing demands for a full range of financial, investment, credit, funds-transfer, settlement and educational services by the credit union industry. Collaboration and partnerships between corporates of all sizes allows many services to be developed in a cooperative, low-cost/high-value manner that ultimately saves credit unions money.

Corporate credit unions process and settle more than 184 million transactions totaling more than \$588 billion on a monthly basis for the credit union system in ACH, wire transfers, bill pay, item processing and other payment-related services. In addition, corporates add value to the credit union system through their brokerage services, ALM and risk management services, member business services and a number of other services that have been created from the demand of NPCUs and their members.

These products and services are in addition to the multiple investment options, settlement, and lending services that are at the core of every corporate's business model. NPCUs depend on CCUs for competitive rates and a full range of financial services. The 90 million Americans who use credit unions benefit from the synergy of the Corporate Network through increased back-office efficiencies, financial safety and soundness, efficient and cooperatively priced payment services.

Corporate Credit Unions' strength is their ability to leverage economies of scale in the areas of item processing, payment systems, settlement, investments and liquidity for their members' benefit. They serve as an integral link in the chain of financial transactions initiated at the credit union member/consumer level.

The cooperative credit union tradition revolves around societal responsibility. The credit union movement has influenced the financial industry in ways that benefit members and non-members alike by providing low-cost financial services, competitive deposit and loan rates and financial education.

Corporate credit unions facilitate much of this benefit by virtue of their unique role in support of the credit union industry. Significantly, because of our not-for-profit status, corporate and natural person credit unions return profits back to their member/owners – the credit unions and millions of members served by credit unions. As a result, credit union products and services often are more affordable to American consumers than similar offerings of other financial institutions. Since the cost of financial products and services typically are a concern in low-income communities, credit unions frequently are the only affordable alternative for many community members.

Corporates add to this cooperative societal responsibility by reinvesting in the movement in many ways. For example, corporates are the largest contributors to the National Credit Union Foundation's Community Investment Fund, a unique investment program that helps finance national and state-level credit union projects and programs that support credit union development initiatives, public education and community outreach efforts, programs that extend credit union services to the under-served, national model programs and much more. Further, corporates actively participate in and fund many initiatives at the local, state and regional levels that enhance communities throughout the nation. Corporates also are actively engaged in lending their operational and payment system expertise to the international development of credit unions through the World Council of Credit Unions.

Appendix A

Glossary of Accounting Terms

**Accumulated Other
Comprehensive
Income (AOCI):**

A separate component of equity used to account for unrealized gains and losses on available-for-sale (AFS) securities. It also is used to account for unrealized losses on cash-flow hedges under FAS 133 and the unrealized loss on any AFS securities transferred to HTM at the time of transfer.

Available-for-Sale: One of three asset classifications under FAS 115. Securities accounted for as Available-for-Sale (AFS) are carried on balance sheets at fair value, with changes in fair value (unrealized gain or loss) included in a separate component of equity, and not reflected in earnings. The separate component of equity is known as Accumulated Other Comprehensive Income (AOCI).

Capital: For corporate credit unions, the term capital is defined in regulation as the sum of retained earnings, Membership Capital Shares (MCS) and Member Paid-in Capital (PIC).

Fair Value: The price that would be received to sell an asset or transfer a liability in an orderly market between willing market participants as of a given date.

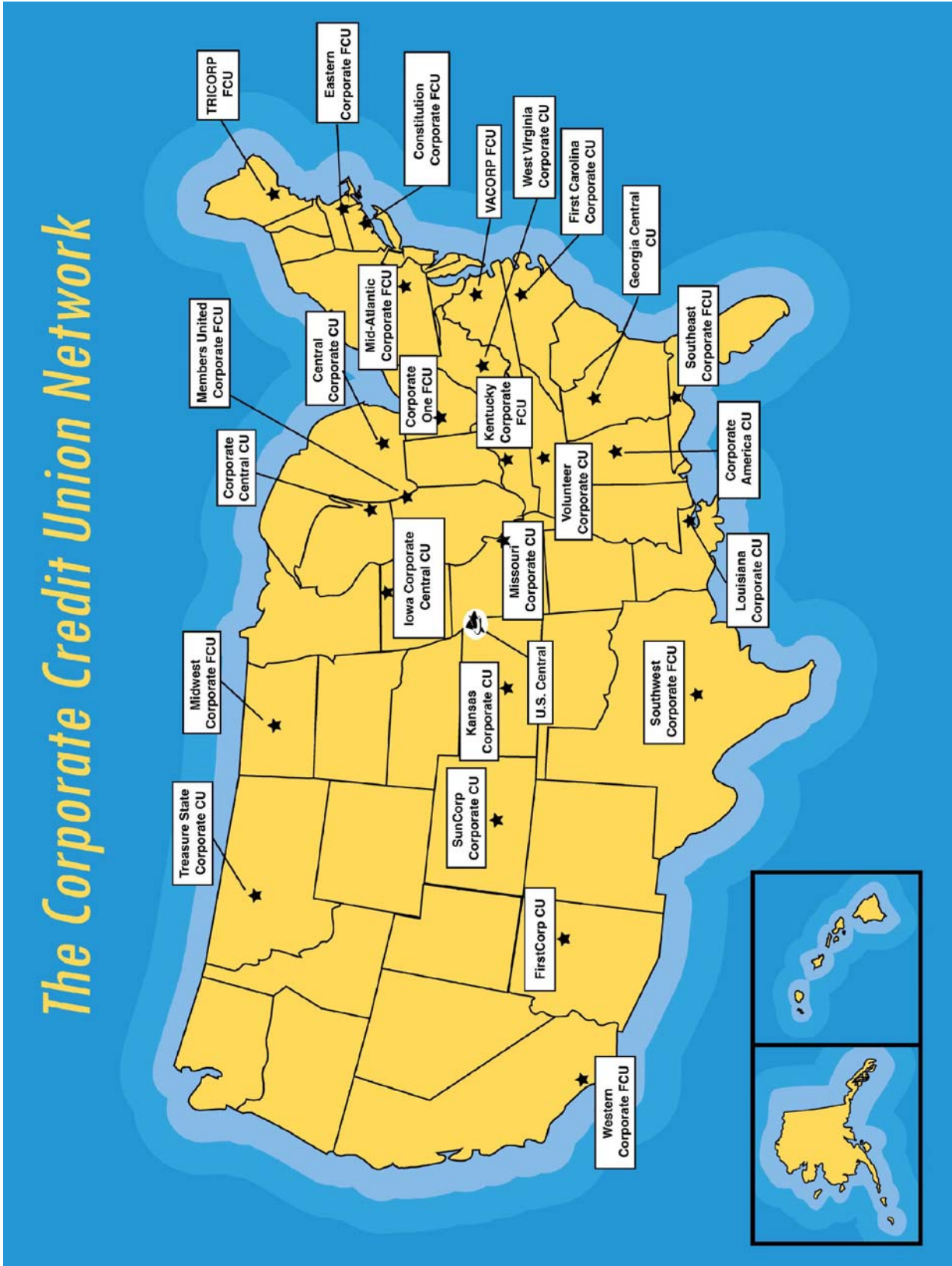
Held-to-Maturity: One of three asset classifications under FAS 115. Securities accounted for as Held-to-Maturity (HTM) are carried at an amortized cost on balance sheets (*i.e.* no recognition of unrealized gains or losses on either the balance sheet or income statement).

**Other-Than-
Temporary-
Impairment
(OTTI):**

Earnings charges required by FAS 115 when all principal and interest on AFS or HTM securities are not expected to be received. The amount of the required charge is equal to the unrealized loss at the date the impairment is deemed to have occurred, which could be more (or less) than the expected loss of principal.

- Realized Gain:** Amount by which the proceeds from the sale of an asset exceed (or the settlement costs of a liability are less than) the cost basis.
- Realized Loss:** Amount by which the proceeds from the sale of an asset are less than (or the settlement costs of a liability exceed) the cost basis.
- Trading:** One of three asset classifications under FAS 115. Securities accounted for as trading are carried on balance sheets at fair value with changes in fair value included in earnings.
- Unrealized Gain:** The dollar amount by which the fair value of a financial instrument, such as an investment security, exceeds its cost basis. The term “unrealized” indicates that an entity still holds the instrument. Also referred to as a “holding” gain. Unrealized gains and unrealized losses are netted together and reflected on the balance sheet in the AOCI line.
- Unrealized Loss:** The dollar amount by which the fair value of a financial instrument, such as an investment security, is less than its cost basis. The term “unrealized” indicates that an entity still holds the instrument. Also referred to as a “holding” loss. Unrealized gains and unrealized losses are netted together and reflected on the balance sheet in the AOCI line.

Appendix B



Appendix C

Selected System History Timeline

◆ 1932 – 1954

The first central credit unions were established: Central Credit Union Fund (Massachusetts), 1932; Georgia Central Credit Union, 1934; and Kansas Central Credit Union, 1954. The first federally chartered central credit union was established in California in 1969.

◆ 1959

On Sept. 22, Congress formalized the role of central credit unions by amending the Federal Credit Union Act, “to establish a further market for securities of the United States and to make more available to people of small means credit for provident purposes through a national system of cooperative credit, thereby helping to stabilize the credit structure of the United States.”

◆ 1974

On Feb. 12, credit union leaders met in Washington, D.C., making an initial collective deposit of \$60 to organize U.S. Central Credit Union. By the end of the year, it had \$22 million in assets and 11 member corporates.

U.S. Central was chartered on March 25, 1974, and began operation in September out of the Kansas Credit Union League offices in Wichita, Kansas. Through CUNA, U.S. Central entered into a management agreement with ICU Services Corporation in Madison, Wisconsin.

◆ 1975

U.S. Central’s assets exceeded \$100 million by the end of 1975, its first full year of operation.

◆ 1977

Credit unions began to rely on electronic funds transfer systems for payments rather than paper documents.

◆ 1978

The Central Liquidity Facility bill was introduced in Congress, which established an additional source of liquidity for credit unions. Credit unions could become members of the facility by submitting for facility capital, stock in an amount equal to 0.5 percent of their year-end assets with the facility – 0.25 percent would be funding immediately and 0.25 percent would be held on call.



1979

The Automated Settlement Program was piloted.

On Oct. 1, Congress established the Central Liquidity Facility (CLF) to provide the credit union movement with backup liquidity options to protect its safety and soundness.



1980

U.S. Central established a centralized cash concentration and wire transfer facility via an online connection with the Federal Reserve Bank of Kansas City.



1982

Wire Transfer, Automated Settlement, and Coin & Currency services were initiated and a Variable Rate Account was introduced and designed to enable credit unions to offer IRAs and Keoghs.

Arrangements were finalized for the Securities Liquidity and Services Safekeeping programs to provide credit unions with an efficient and low-cost source of liquidity and safekeeping services for government and government-agency securities.

U.S. Central issued commercial paper, which received the highest ratings of “A1+” from Standard & Poor’s Corporation and “P-1” from Moody’s Investors Service.



1983

On Dec. 1, the Corporate Credit Union Network transaction-processing system (CCUN) was implemented, to provide automated processing of financial and payment systems among U.S. Central, corporates and credit unions.

On Oct. 4, 1983, the U.S. Central Agent Group, comprising all corporate credit union members with U.S. Central as the agent corporate representative, became a member of the CLF.



1984

U.S. Central reached \$8 billion in assets – 10 years after it was chartered.



1986

Corporates began offering an international check collection program, and Lockbox services were introduced.



1988

Wire Transfer services were expanded to provide international wires.

Through Corporate Network Brokerage Services, Inc. (CNBS), corporates began offering their members broker-dealer and advisory services.

- 1989
First international ACH transactions were completed with transfers to institutions in England and Germany.
- 1993
The Medium-Term Note (MTN) Program was developed, with the first notes issued in November. U.S. Central's MTN program received the highest ratings available from three of four nationally recognized rating agencies and the second-highest rating from the fourth agency.
- 1994
CNBS Investment Advisory Service exceeded \$1 billion under management.
- 1995
Automated Settlement was enhanced with new software technology to meet future credit union settlement needs.

NCUA revised the corporate credit union regulation, Part 704.
- 1997
CNBS Holding Company, Inc. was converted from a holding company for CNBS to an operating subsidiary of U.S. Central, providing broker-dealer and investment services to corporate credit unions.
- 1998
Ownership of CNBS was transferred, through a special stock dividend, to the corporate credit union members of U.S. Central.

The Network Liquidity Acceptance Company, LLC (NLAC) was developed as a wholly owned subsidiary of U.S. Central. NLAC acts as a conduit, buying credit union loans with assistance from corporates and holding the loans for securitization and sale.
- 1999
Corporates focused on Year 2000 (Y2K) readiness, both in system preparedness and liquidity availability. By mid-year, all critical and essential business functions were Y2K ready, and contingency plans were in place.

Corporate Network eCom, LLC, providing Internet banking with bill payment and bill presentment, is launched.
- 2002
Corporate Exchange, LLC, a CUSO owned by corporate credit unions is formed to manage the SimpliCD (insured jumbo CD) program.

• 2007 - present

Market and economic events of epic historical proportions impact virtually all U.S. financial institutions and global institutions.

U.S. financial institutions record \$700 billion in losses and have raised \$560 billion in capital – nearly half of this from direct capital infusions and other government programs (not including the trillions in deposits that are guaranteed)

The financial crisis impacts all financial institutions and numerous banking companies fail, including Bear Stearns (after 85 years), Lehman Brothers (after 158 years), Countrywide (39 years), WAMU, Wachovia, AIG, Merrill Lynch ...

Eight of the twenty largest mortgage lenders fail, Fannie/Freddie are nationalized, Monoline insurers lose AAA rating, 50,000 + bond downgrades

• 2009

NCUA implements Corporate Stabilization Program and issues Advance Notice of Proposed Rulemaking for industry comments on the future role of the corporate system.