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March 22, 2017

SENT BY E-MAIL

RE: FOIA 17-FOI-00015

This responds to your Freedom of Information Act (FOIA) request to the National Credit Union Administration (NCUA) on January 3, 2017. You requested a digital/electronic copy of the following: 1) Enforcement Manual (NCUA Instruction 4820); 2) Administrative Remedies (Supervisory Letter 10-04); 3) Special Assistance Manual (NCUA Instruction 4810); and 4) NCUA Personnel Manual (table of contents).

Your request is granted in part. We previously sent you the responsive records for 1), 2), and 4) and currently are sending document 3) (attached). Redacted material qualifies for withholding from FOIA release under one or both of the FOIA exemptions at (b)(7)(E) and (b)(8), as follows.

- Exemption (b)(7)(E) protects records compiled for a law enforcement purpose where the release of information would disclose techniques and procedures for law enforcement investigations or prosecutions, or would disclose guidelines for law enforcement investigations or prosecutions if such disclosure could reasonably be expected to risk circumvention of the law. 5 U.S.C. 552(b)(7)(E).
- Exemption (b)(8) protects information "contained in or related to examination, operating or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions." 5 U.S.C. 552(b)(8). Exemption (b)(8) helps safeguard the relationship between credit unions and NCUA.

For further assistance or to discuss your request, feel free to contact me directly at 703-518-6561, as well as the agency FOIA Requester Service Center or FOIA Public Liaison by e-mail at FOIA@ncua.gov or phone at 703-518-6540. Additionally, you have the option to contact the Office of Government Information Services (OGIS) at the National Archives and Records Administration (NARA) to inquire about FOIA mediation services. Contact information is OGIS: NARA, 8601 Adelphi Road-OGIS, College Park, Maryland 20740-6001, e-mail at ogis@nara.gov; telephone at 202-741-5770; toll free at 1-877-684-6448; or facsimile at 202-741-5769.

If you are not satisfied with the FOIA response, you may file an administrative appeal. It must be in writing and postmarked, or electronically transmitted, within 90 days from today. If you file an appeal, please write "FOIA-APPEAL" in the letter and on the envelope (or in the subject line if by e-mail to FOIA@ncua.gov) and address it to: National Credit Union Administration, Office of General Counsel - FOIA APPEAL, 1775 Duke Street, Alexandria, VA 22314-3428.

Sincerely,



Regina M. Metz
Senior Attorney Advisor

GC/RM:CS
17-FOI-00015

NCUA



INSTRUCTION

NO. 4820	DATE: September 16, 2004
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SUBJECT: Enforcement Manual

TO: All NCUA Staff

ENCL: Enforcement Manual

1. **PURPOSE.** To describe NCUA's policy for taking appropriate enforcement action in response to violations of law, rules, regulations, final agency orders and/or unsafe and unsound practices or conditions.
2. **CANCELLATION.** NCUA Bulletin 4810B – Agency Guidance – Appropriate Language for Letters of Understanding and Agreement (LUA) issued on April 26, 2000, and NCUA Instruction 12710.01 – Agency Guidance – Publication of Letter of Understanding and Agreement (LUAs) issued on December 27, 1999. These instructions have been incorporated into the Enforcement Manual.
3. **BACKGROUND.** Close supervision and the use of informal enforcement actions are the methods customarily used to resolve safety and soundness concerns however, the NCUA has broad enforcement powers under the Federal Credit Union Act to issue formal enforcement actions when necessary.
4. **GENERAL POLICY.** Agency staff should use this manual in selecting and processing enforcement action decisions and adhere to the policies, guidelines and procedures incorporated.
5. **EFFECTIVE DATE.** This instruction is effective immediately, and will remain in effect until cancelled.

/S/

J. Leonard Skiles
Executive Director

Enclosure

ENFORCEMENT MANUAL



August 2004

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(b)(7)(E) (b)(8)

OVERVIEW

Purpose of this Manual

This manual describes NCUA's policy for taking appropriate enforcement action in response to violations of law, rules, regulations, final agency orders and/or unsafe and unsound practices or conditions.

These policies and procedures provide only internal NCUA guidance. They are not intended, do not, and may not be relied upon to create rights, substantive or procedural, enforceable at law or in any administrative proceeding.

Chapter 1

Enforcement Action Overview and General Policy

1. What is the purpose of this chapter?

This chapter discusses:

- The agency's philosophy on using enforcement actions.
- The available types of enforcement actions.
- The proper use of enforcement actions.
- The authority and responsible parties for enforcement actions.
- The requirements and process for public disclosure of enforcement actions.

2. What is the agency's philosophy on enforcement actions?

NCUA must deal with a credit union's problems before they become fatal. Success requires appropriate action and timing. It also requires clear communications between NCUA and the credit union's senior management and board of directors. Enforcement actions focus special attention on the problems or weaknesses and prompts corrections by credit union officials and management. Once NCUA staff identifies and communicates problems or weaknesses to the credit union, senior management and the board of directors are to correct them promptly.

The examination report is the first step in determining if an enforcement action is necessary. The actions a credit union takes or agrees to take in response to the examination report will help determine whether to take enforcement action and if so, what type.

Enforcement actions may be taken as a result of findings in an examination report or other supervision contact. Field staff need not wait for the completion of the formal examination or follow-up examination report to initiate these actions.

This manual provides guidance in selecting the action or combination of actions best suited to accomplish corrective or remedial measures. The manual also promotes consistency while preserving flexibility for specific circumstances. NCUA's long-term supervision strategy takes into consideration not only the measures needed to address the credit union's problems currently but also what measures will be needed in the future if the credit union's problems develop into serious supervisory issues threatening viability.

Certain types of enforcement action may also provide better transitions to more severe supervisory responses later if the condition of the credit union warrants. This manual provides guidance on the long-term strategy aspects of documentation for enforcement actions. The documentation of earlier enforcement actions, of failure to comply, and of the consequences for the credit union of that failure is an important part of establishing the record for more severe subsequent action.

3. What enforcement actions are available?

Enforcement actions fall into two broad categories: informal and formal.

a. Informal enforcement actions

Use *Informal* enforcement actions when a credit union's overall condition is sound, but written commitments from the board of directors is needed to ensure that it will correct problems and weaknesses identified by NCUA staff. These enforcement actions provide a credit union with more explicit guidance and direction than is normally contained in an examination report. Agreement to an informal action is evidence of the board's commitment to correct problems before they hurt the credit union's performance or cause further decline in its financial condition.

Regional directors (RD) are delegated the authority to issue informal enforcement actions. Informal enforcement actions are:

- Regional director letters.
- Non-published letter of understanding and agreement.
- Establishment of special reserves¹.
- Preliminary warning letters.

¹ Refer to NCUA Delegations of Authority – SUP 4 and regional procedures for guidance in processing special reserves.

b. Formal enforcement actions

The NCUA may use a wide variety of *formal* enforcement actions to support its supervisory objectives. Unlike most informal actions, formal enforcement actions are authorized by statute (mandated in some cases), are generally more severe, and are disclosed to the public. Also, formal actions are enforceable through other formal enforcement actions, such as the assessment of civil money penalties, and may require litigation before an administrative law judge or a federal district court.

Formal actions against a credit union are:

- Published letters of understanding and agreement.
- Cease and desist orders.
- Civil money penalties.
- Prompt Corrective Action (PCA) directives.
- Termination of insurance.
- Conservatorship.
- Liquidation.

4. How do I determine the appropriate type of enforcement actions to use?

Tailor the enforcement action to the institution. Design an action to correct deficiencies and return the credit union to a safe and sound condition as soon as possible. Normally start with the lowest level of enforcement needed to correct the credit union's problems. Enforcement actions normally rise from informal to formal as the administrative record develops, but you may start with formal actions.

Determining the appropriate informal or formal action depends on:

- The overall condition of the credit union (both current and projected).
- The severity of the credit union's weaknesses.
- Whether the board and management demonstrate the commitment and ability to correct the weaknesses.
- The existence of previously identified but unaddressed weaknesses.
- The credit union's composite CAMEL rating.

If a credit union fails to comply with an informal enforcement action within the specified time and doesn't justify the delay, promptly proceed with a formal enforcement action.

If a credit union fails to comply with a formal enforcement action, use even stronger actions, such as:

- Assessing civil money penalties against the board of directors and credit union management.
- Enforcing the action in federal court.
- Starting a new enforcement action such as requirement for merger, conservatorship, or liquidation of the credit union.

(b)(7)(E),(b)(8)

Some Cautions: Do not discuss a pending enforcement action with the general public or press. Only NCUA staff with authority to do so can make such disclosures. The Office of Public and Congressional Affairs, together with General Counsel, must clear any public statements regarding officially approved enforcement actions or public inquiries about enforcement actions. With few exceptions, only the NCUA Board has the authority to approve formal enforcement actions. Regional directors have delegated authority to initiate certain types of enforcement actions. These delegated authorities can only be initiated following strict criteria and concurrence procedures, as outlined in the NCUA Delegations of Authority.

A fine line exists between recommending corrective actions and threatening enforcement actions. Use care when discussing potential actions with credit union officials, employees, and other related third parties so as not to misstate your own authority. This is especially true when discussing possible enforcement actions with a credit union that fails to initiate adequate corrective actions. Do not disclose pending enforcement actions to the credit union at any time without approval from your supervisory examiner.

However, you may discuss the issues, corrective actions, and the potential for agreement if contacted by the credit union's officials or staff. These discussions do not preclude the action from proceeding forward. Never threaten an enforcement action; you may only *recommend* enforcement action to the regional director.

Prompt Corrective Action (PCA) does not limit the authority of NCUA under any other provision of the law to take additional supervisory action to address unsafe or unsound practices or conditions, or violations of applicable law or regulations. Action taken under PCA may be taken independently of, in conjunction with, or in addition to any other enforcement action.

5. Who is responsible for enforcement actions?

Examiner/PCO

- Identify the need for formal or informal enforcement action.
- Recommend an enforcement action as appropriate.
- Develop the administrative record.
- Prepare supporting documentation.
- Monitor compliance with outstanding enforcement actions.
- Recommend removal of enforcement actions when warranted.

Supervisory Examiner/Director of Special Actions

- Review the recommendation of an enforcement action.
- Ensure an adequate administrative record is established and maintained.
- Ensure outstanding enforcement actions are monitored.
- Ensure outstanding enforcement actions are removed when warranted.

Regional Director

- Consult with the Office of General Counsel as needed.
- Inform the Executive Director and Director of E&I of all anticipated material formal enforcement actions.
- Obtain concurrence as required by delegations.
- Request action by the NCUA Board as necessary.
- Issue the enforcement actions as authorized.
- Take action when enforcement actions are violated.
- Remove enforcement actions when warranted.

Office of Examination and Insurance

- Provide expert advice and guidance on the use and issuance of enforcement actions.
- Provide training on the use of enforcement actions.
- Maintain template documents.
- Provide concurrence as required.
- Monitor outstanding enforcement actions.

Office of General Counsel

- Review proposed enforcement actions upon request by the regional director.
- Advise regional staff on the preparation of the contents of enforcement action documents.

- Provide concurrence as required by the delegations.
- Coordinate NCUA's response to any legal challenges to enforcement orders.
- Assist the region in enforcing enforcement orders.
- Publish applicable enforcement documents.

Office of Public and Congressional Affairs

- Publish applicable enforcement documents.
- Respond to public inquiries.

6. What do I need to do leading up to the issuance of an enforcement action?

(b)(7)(E) (b)(8)

b. Timeliness of enforcement actions

You should recommend taking an enforcement action as soon as practical once you identify the need for such action, including during an examination if circumstances warrant.

c. Steps to take when the credit union must sign the action

If a decision has been made by authorized staff to take an enforcement action that requires NCUA staff to obtain the signature of the credit union's board (e.g. a published LUA or consent to a cease and desist order):

(b)(7)(E) (b)(8)

If the board of directors does not sign the enforcement action and the board of directors is not properly served with a Notice of Charges for Issuance of a Cease

and Desist Order, the regional director or authorized representatives has 30 days to negotiate the execution of the action or serve a Notice of Charges.

NCUA Rules and Regulations §747, Subpart L, contains the procedure for issuance, review, and enforcement of orders imposing Prompt Corrective Action.

d. Content of enforcement actions

In enforcement action documents, address only substantive supervisory problems. For each action, clearly list any prohibited or restricted activities, prioritize the remedial measures, and assign deadlines. Explicitly state what action is expected of those parties subject to the document.

(b)(7)(E) (b)(8)

7. How do I deliver the action and what happens in a challenge to the action?

a. Delivery of enforcement actions

Deliver enforcement actions by postal mail (certified receipt) or personally. The regional director usually assigns who delivers the notice (or order) to the credit union or individual.

(b)(7)(E) (b)(8)

b. Challenges to enforcement actions

In the case of a Temporary Cease and Desist Order, Immediate Suspension or Prohibition, Conservatorship, or Title II involuntary liquidation, the FCU Act permits a challenge of NCUA's action in U.S. District Court within 10 days of service of the order. A credit union or individual also may sue NCUA even though the FCU Act does not provide for it.

(b)(7)(E),(b)(8)

8. What are my responsibilities following issuance of all enforcement actions?

Early assessment and written feedback on a credit union's efforts to comply with a new enforcement action are critical to helping credit union management and the board understand what's required, and to achieve timely compliance. So you and your supervisory examiner are encouraged to do an on-site assessment of the credit union's compliance with the enforcement action shortly after the action has been taken.

If the enforcement action is formal, you must do an on-site assessment within 60 days of the latest due date in the action. Most articles in an enforcement action require corrective action within a specified time period after the effective date of the document. For example, if the latest due date is 90 days, then the on-site assessment of compliance with the document starts within 60 days after those 90 days. Articles requiring cessation of specific activities usually require immediate action and should be assessed on-site shortly after the enforcement action becomes effective. If all articles in a document require immediate action, start on-site assessment of compliance shortly after the formal enforcement action becomes effective and no later than 60 days after the completed date of the enforcement action.

Thoroughly document the success or failure of the credit union in complying with the enforcement action, and the impact on the credit union of the continuation of the problems. Noncompliance with the enforcement action will be part of your support for a more severe enforcement action.

Your region is responsible for ensuring that the enforcement actions are appropriately monitored and provide any reports on outstanding actions the central office may require.

a. Assessing compliance with enforcement actions

A credit union can achieve a rating of *in-compliance* on a particular article only after the credit union:

- Has taken all of the corrective actions in the article.
- The corrective actions are effective in addressing the credit union's problems.
- You have verified through the examination and supervision process that this has been accomplished.

You should not consider a credit union to be in compliance with an article simply because it has made progress or a good faith effort toward complying.

Articles for which the credit union has not achieved compliance fall into two categories:

- Articles where the credit union has made and begun to make all the corrective actions required by the article. However, sufficient time has not passed to verify that the actions have been fully implemented, are being adhered to, and are effective in addressing the credit union's problems. In these situations management and the board must continue to monitor and test the credit union's progress to ensure that corrective actions are fully implemented, adhered to, and are effective.
- Articles where additional action is required on the part of the credit union, its board, and management. This includes, but is not limited to, where the credit union has not:
 - Adopted policies, procedures, and systems within required time frames.
 - Adopted policies, procedures, and systems to address all required items in the article.
 - Fully complied with immediately effective requirements.
 - Ceased activities prohibited by the article.
 - Fully implemented or adhered to corrective actions.

NCUA may grant in writing reasonable extensions of time to comply with articles that require developing and implementing policies, procedures, systems, and controls. Credit union requests for extensions will be fully supported and documented in writing.

For those articles with which the credit union has not achieved compliance (both categories), you must identify in your examination report or other written communication to the credit union why the article is not in compliance, and what must be done to achieve compliance.

b. Termination of enforcement actions

The decision to terminate an enforcement action is the responsibility of your regional director. Usually you and your supervisor recommend termination based on the assessment of compliance contained in your examination report. Wait to recommend termination of an enforcement action until the credit union has complied with all of the articles in the document. But you may recommend termination sooner in a few cases. For example, a credit union has complied with all material requirements, and the articles in noncompliance have become outdated or irrelevant to the current situation.

Enforcement actions the NCUA Board approved normally require NCUA Board action to remove.

9. What are the public disclosure requirements?

NCUA must publicly disclose all final orders entered into under §206(s) of the FCU Act, 12 U.S.C. §1786(s), such as terminations of insurance, cease and desist orders, civil money penalties (including those for late or inaccurate call reports), removal orders, conservatorship, and any modification and/or termination of such actions. Under certain very limited circumstances, NCUA may delay mandatory public disclosure for a reasonable period of time or may file documents under seal if disclosure of the document would be contrary to the public interest.

NCUA Rules and Regulations §747, Subpart L, addresses the disclosure of any final PCA directives.

There is no legal requirement for the NCUA to publicly disclose temporary orders to cease and desist or any informal enforcement actions.

Once a month, the NCUA's Office of General Counsel publishes a list of formal enforcement actions that includes the name of the person or credit union involved, the type of action, and the date of the action. The enforcement actions are posted and available through the NCUA's public Internet site and may also be obtained in hard copy upon request.

(b)(7)(E) (b)(8)

Chapter 2

Letters of Understanding and Agreement

1. What is the purpose of this chapter?

This chapter includes guidance and procedures for processing Letters of Understanding and agreement (LUAs). This chapter incorporates the guidance on LUAs formerly provided in NCUA Bulletin 4810B, NCUA Instruction 4900.01, and NCUA Instruction No. 12710.01.

2. What is a Letter of Understanding and Agreement?

An LUA is a bilateral document signed by the credit union's board of directors and the regional director (RD). The credit union agrees to take, or not take, a certain specified action(s). RDs often issue LUAs when credit unions have not adequately responded to less severe measures, such as Documents of Resolution. NCUA also requires LUAs for newly chartered credit unions and for the granting of permanent special assistance.

Delegation of Authority SUP 16 authorizes RDs to enter into LUAs with elected and appointed officials of FCUs and FISCUs. RDs discuss and negotiate publication with credit unions to prevent unfair surprises to credit unions and their officials. The RDs will address the issue of publication in every LUA between NCUA and a credit union by including one of the following three provisions:²

1. This LUA will not be published.
2. This LUA will be published.
3. The RD is reserving for a reasonable time his/her right to publish this LUA.³

² Minor modifications and variations of the listed provisions that clearly communicate the same ideas are acceptable.

³ This third provision can also specify the period of time within which the RD will decide whether to publish the LUA or can correlate publication to a specified event (or the failure of an event to occur).

(b)(7)(E) (b)(8)

(b)(7)(E) (b)(8)

b. Published Letter of Understanding and Agreement

The FCU Act §206(s)(1)(A), 12 U.S.C. §1786(s)(1)(A), requires the NCUA Board to publish and make available to the public "any written agreement or other written statement for which a violation may be enforced by the Board unless the Board, in its discretion, determines that publication would be contrary to the public interest." LUAs must be published if violations are to be considered enforceable. The NCUA Board may take administrative actions against credit unions or officials when they fail to meet terms of published LUAs. Violations of the terms of a published LUA alone are grounds for administrative action and, although not required, the LUA should include language to that effect as stated above.

NCUA may enforce a published LUA by bringing an enforcement action, such as a cease and desist order or civil money penalty, and proving noncompliance with the published LUA.

These publication requirements apply to all LUAs, including those issued to newly chartered credit unions, as well as those issued in connection with special assistance. NCUA may take an enforcement action, even if the LUA is not published, if the credit union fails to comply with the terms of the LUA and the credit union's conduct constitutes a material safety and soundness violation or violation of law or regulation.

While not required by the delegation, the regions should provide the Office of General Counsel and E&I with a draft of an LUA considered for publication two business days prior to its delivery to the officials of the credit union for signature.

c. Non-Published Letters of Understanding and Agreement

Non-published LUAs are not enforceable. The mere violation of a non-published LUA is not grounds for a formal enforcement action, but may serve as the basis for developing grounds for a formal enforcement action if underlying safety and soundness concerns or violations of statutes or regulations exist.

The FCU Act provides that NCUA may enforce the terms of an unpublished LUA if the NCUA Board approves non-publication based upon a finding that publication would be contrary to the public interest. If the RD recommends to the NCUA Board that an LUA not be published because publication would be contrary to the public interest, and the NCUA Board issues this determination, the LUA will still be enforceable. The RD's recommendation must clearly show why publication would be contrary to the public interest. The FCU Act requires a quarterly written report to Congress to summarize all non-published LUAs that are enforceable under this exception. This exception to publication should be used rarely and only when conditions justify a conclusion that non-publication is in the public interest.

d. LUAs with Federally Insured State-Chartered Credit Unions (FISCUs)

NCUA may independently or jointly with the SSA issue an LUA to a FISCU. The requirement for publication applies if NCUA attempts to take action based on a violation of the terms of the LUA. Therefore, RDs will include one of the three publication provisions discussed above in all LUAs issued jointly with NCUA and a SSA.

Chapter 3

Cease and Desist Order and Civil Money Penalties

1. What is the purpose of this chapter?

This chapter includes policy and procedures for processing cease and desist orders (C&D) and assessing civil money penalties.

2. What is a Cease and Desist Order?

A Cease and Desist (C&D) Order normally requires the credit union to stop illegal or unsafe or unsound activities which caused or is likely to cause more than a minimal financial loss to, or have a significant adverse effect on, the insured credit union. A document called Notice of Charges and Hearing sets out the specific charges and statement of facts supporting the charges. The Notice also arranges for an administrative hearing. The C&D contains the required corrective actions. The C&D action is designed to address only actions necessary to correct the most significant items.

A C&D Order can be issued against an insured credit union or an institution-affiliated party. The term institution-affiliated party means any of the following:

- Any committee member, director, officer, or employee of, or agent for, an insured credit union.
- Any consultant, joint venture partner, and any other person as determined by the NCUA Board who participates in the conduct of the affairs of an insured credit union.
- Any independent contractor who knowingly or recklessly participates in any violation of any law or regulation, any breach of fiduciary duty, or any unsafe or unsound practice.

The types of violations most likely to be remedied by a C&D Order include:

- Failure to maintain adequate books and records.
- Deficient appraisal reports.
- Transactions involving conflicts of interest.
- Inadequate due diligence.
- Inadequate control and oversight of operations.

There is a great deal of flexibility in what actions NCUA may require. In addition to ordering a cessation of certain activities, a C&D Order may require affirmative corrective action, including:

- Making restitution or provide reimbursement, indemnification, or guarantee against loss under specific conditions.
- Restricting growth.
- Rescinding an agreement or contract.
- Disposing of any loan or asset.
- Employing qualified officers or employees.
- Taking such other action NCUA determines to be appropriate.

Orders to Cease and Desist are issued pursuant to the FCU Act §206(e), 12 U.S.C. §1786(e). The provisions for the C&D Order are set out in article-by-article form and prescribe those restrictions and corrective and remedial measures necessary to correct deficiencies or violations in the credit union and return it to a safe and sound condition. Violations of a C&D Order can provide the legal basis for assessing civil money penalties (CMPs) against directors, officers, and other institution-affiliated parties. A C&D Order may also be enforced through application to a U.S. district court. Moreover, a willful violation of a Final C&D Order is itself grounds for conservatorship under the FCU Act §206(h)(1)(D), 12 U.S.C. §1786(h)(1)(D).

There are three types of cease and desist orders available to NCUA:

a. Consent Order

A Consent Order is an Order to Cease and Desist that is entered into and becomes final through the board of directors' execution of a Stipulation and Consent document on behalf of the credit union. This type of order also requires the issuance of a Notice of Charges. The NCUA Board issues the Consent Order without the need for an administrative hearing. The Consent Order becomes effective at the time specified in the Order.

b. Final (Permanent) Cease and Desist Order

Aside from its title, a Final C&D Order is identical in form and legal effect to a Consent Order. However, a Final C&D Order is imposed on an involuntary basis after issuance of a Notice of Charges, a hearing before an administrative law judge,

and a final decision and order issued by the NCUA Board. A Final C&D Order is effective 30 days after service upon the credit union. Any Final C&D Order is subject to review by a U.S. Court of Appeals.

c. Temporary Cease and Desist Order

A Temporary C&D Order is an interim order issued by the NCUA pursuant to its authority under the FCU Act §206(f), 12 U.S.C. §1786(f), and is used to impose measures immediately pending resolution of a Final C&D Order. Such orders are typically used only when immediately necessary to protect the credit union against ongoing or expected harm. A Temporary C&D Order may be challenged in U.S. District Court within 10 days of issuance, but it is effective upon issuance and remains in effect unless overturned by the court or until a final order is in place.

To issue a temporary order, NCUA must also issue a Notice of Charges initiating a proceeding to obtain a Final C&D Order. In order to issue a Temporary C&D Order, NCUA must determine that the violation or threatened violation or the unsafe or unsound practice(s) is likely to either:

- Cause insolvency or significant dissipation of assets or earnings.
- Weaken the condition of the credit union or otherwise prejudice the interest of the credit union's members.

The FCU Act §206(f)(3), 12 U.S.C. §1786(f)(3), provides for the issuance of a Temporary C&D Order when an insured credit union's books and records are so incomplete or inaccurate that the financial condition of the credit union or details or the purpose of any material transaction can not be determined. This section also applies when a credit union does not provide adequate access to the books and records.

3. What are the grounds for issuance of a Cease and Desist Order?

The grounds for a cease and desist action are set forth in the FCU Act §206(e)(1), 12 U.S.C. §1786(e)(1). A C&D Order can be issued if any insured credit union or institution-affiliated party is either:

- Engaging in or has engaged in, or the examiner has reasonable cause to believe that the credit union or the persons involved are about to engage in, an unsafe or an unsound practice in conducting the business of the credit union.
- Violating or has violated, or the examiner has reasonable cause to believe that the credit union or persons involved are about to violate a law, a rule, a regulation, any condition imposed in writing by the NCUA Board, or any written agreement entered into with the NCUA Board, as long as the

agreement has been published in accordance with the FCU Act 206(s), 12 U.S.C. § 1786(s).

The FCU Act §206(q)(3), 12 U.S.C. §1786(q)(3), requires that the NCUA shall issue a cease and desist order requiring correction of certain Bank Secrecy Act problems, such as failure to establish a program or failure to correct a problem with its procedures that have previously been identified by an examiner.

4. How are Cease and Desist Orders processed?

NCUA Rules and Regulations §747, Subpart A, contains the rules and regulations governing cease and desist administrative hearings.

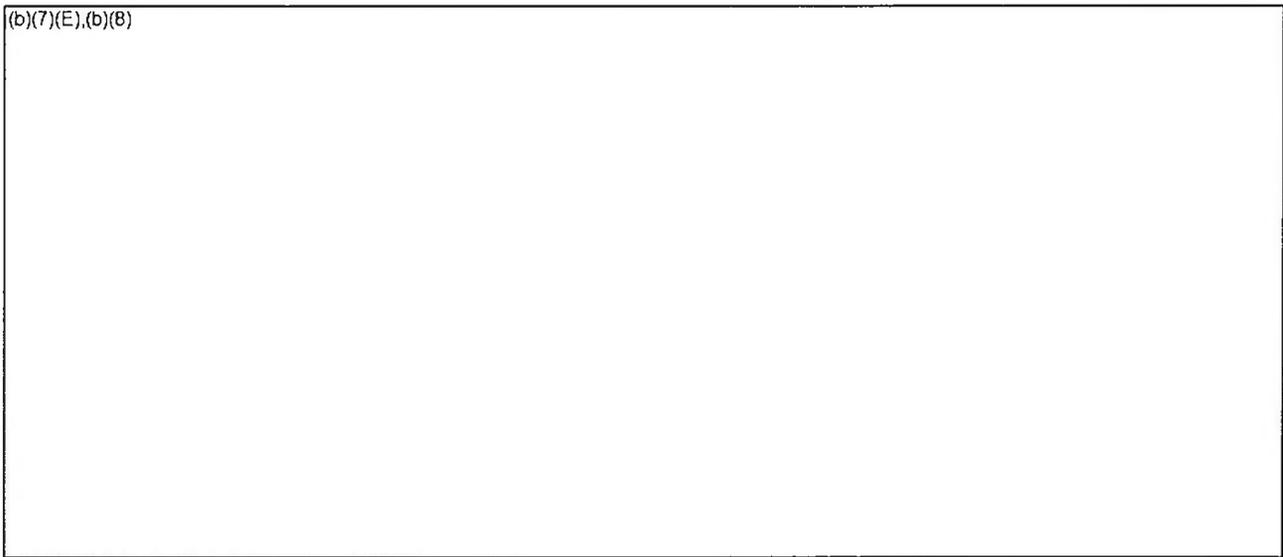
a. Delegation of Authority

NCUA Delegation of Authority SUP 8 provides regional directors, with the prior concurrence from General Counsel, the authority to:

- (1) Issue Notice of Charges and Hearing for C&D orders.
- (2) Issue and remove Temporary C&D Orders pending completion of the administrative procedures.

The NCUA Board must approve the issuance, modification, and termination of Final C&D Orders.

(b)(7)(E),(b)(8)



c. Mechanics for Final (permanent) Cease and Desist Order and Consent Order

Final C&D Orders are processed in the following manner:

1. Notice of Charges is issued setting out charges and statement of facts supporting charges. Notice fixes a time and place for a hearing between 30 and 60 days.
2. Respondent may consent, in which case a final order is issued by the Board without the need for an administrative hearing. If no consent, a hearing is held before an Administrative Law Judge (ALJ).
3. ALJ sends Recommended Decision and hearing record to the NCUA Board.
4. Within 90 days the Board must render its final decision. The Board may disagree with the ALJ, but the decision must be supported by the evidence.
5. Appeal by the respondent, within 30 days after service of the final order, to the U.S. Court of Appeals. The respondent must prove NCUA acted in an arbitrary and capricious manner. The Order is in effect unless stayed or modified by the court.
6. Order is effective 30 days after service on respondent. Violation of Order could result in civil money penalties of up to \$1,000,000 per day.

d. Mechanics for Temporary Cease and Desist Order

Temporary C&D Orders are processed in the following manner:

1. The regional director, with GC concurrence, issues Temporary Cease and Desist Order, usually along with the Notice of Charges and Hearing which starts the normal C&D administrative process.
2. The administrative process for the Final Cease and Desist Order continues while the credit union is subject to the temporary restrictions. Even if a court modifies or lifts the temporary order, the Notice of Charges and Hearing is still in effect and the administrative process goes forward.

e. Violations of Cease and Desist Orders

If an institution or individual fails to comply with a final order, NCUA may seek enforcement through federal district court. If the court determines that a violation, threatened violation, or failure to obey has occurred, by law the court must enforce the order.

In addition, any credit union or individual that violates the terms of any final C&D can be ordered by NCUA to pay a civil money penalty of up to \$1,000,000 a day for each day the violation continues, provided specific statutory criteria are met.

f. Removing Cease and Desist Orders

The NCUA Board may withdraw a C&D at any time during the administrative process.

A Temporary C&D Order terminates automatically when the charges in the notice initiating the proceeding for the Final C&D Order are dismissed by the agency or when a Final C&D Order against the same party becomes effective.

If the NCUA Board approved the issuance of the C&D action, the removal action will need to be approved by the NCUA Board.

5. What are civil money penalties?

The FCU Act §206(k), 12 U.S.C. §1786(k), contains NCUA's authority to issue civil money penalties; NCUA Rules and Regulations. Section 747, Subpart A, contains the rules and regulations governing civil money penalty administrative hearings. The NCUA Board may assess civil money penalties against either a credit union or an institution-affiliated party (see definition of institution-affiliated party above). The FCU Act specifies three tiers of civil money penalties, as follows:

- First tier. Any credit union or institution-affiliated party that violates a law or regulation, a final order of the NCUA Board, a published agreement with the Board (such as a published Letter of Understanding and Agreement), or a condition imposed in a published writing by the Board in connection with the granting of any application (such as the Insurance Agreement), may receive a penalty of not more than \$5,000 for each day of the violation. First tier penalties may apply to credit unions that, even after warnings, repeatedly submit late or substantially inaccurate call reports.
- Second tier. If the credit union or institution-affiliated party commits a first tier violation, and exhibits reckless conduct or a breach of fiduciary duty, and the violation, practice or breach is part of a pattern of misconduct, or causes more than a minimal loss to the credit union, or results in a monetary gain or other benefit to the institution-affiliated party, then the NCUA Board may assess a civil money penalty of not more than \$25,000 per day for each day of the violation.
- Third tier. Any credit union or institution-affiliated party that knowingly commits the first tier violations, knowingly engages in unsafe or unsound practices, knowingly breaches any fiduciary duty, or knowingly or recklessly causes a substantial loss to the credit union or a substantial monetary gain or other benefit to a party because of the violation, breach, or practice, may receive assessment of a civil money penalty of not more than \$1,000,000 per

day for each day of the violation, or in the case of a credit union, 1 percent of assets, whichever is less.

6. How are civil money penalties assessed?

The normal administrative procedure for a civil money penalty action is as follows:

1. The regional director notifies the party of his or her intent to recommend to the NCUA Board the issuance of a civil money penalty, requesting a written response from the party.
2. The NCUA Board issues a Notice of Assessment, setting forth a statement of the law and facts on which it bases the assessment.
3. The assessed party has 90 days to make payment, but may request a hearing within 20 days.
4. An administrative law judge will hold a formal hearing if requested.
5. After the administrative hearing, the administrative law judge submits a recommended decision to the NCUA Board.
6. The NCUA Board issues its final order.
7. An institution-affiliated party or credit union may appeal to the U.S. Court of Appeals within 20 days of receipt of the final order.

CHAPTER 4

REMOVAL OF OFFICIALS AND PROHIBITIONS

1. What is the purpose of this chapter?

This chapter includes advice and procedures in processing Removal and Prohibition Actions.

2. What is a removal action?

A removal action is the administrative action to remove directors, officers, or committee members. This action is available as an initial course of action or as a continuation of a cease and desist order if the officials refuse to comply as directed. Whether this enforcement action is an initial course or a continuation of a cease and desist order, it is separate and has its own applicability to particular situations. Section 206(g) of the FCU Act, 12 U.S.C. §1786(g), contains NCUA's authority to issue a removal order; NCUA Rules and Regulations §747, Subpart A, contains the rules and regulations governing removal administrative hearings.

It may become necessary to initiate formal removal action where a breach of fiduciary duty occurs on the part of the director, officer, or committee member and where the credit union's board will not or cannot discharge the responsible person and where that person does not voluntarily resign.

Removal of a director, an officer, or a committee member is not anticipatory in nature as in a cease and desist action. Removal is appropriate only when an official committed an act that constitutes grounds for removal, i.e., it cannot be imposed for future or threatened conduct. Removal can follow only if NCUA has issued a Notice of Intent to Remove or a Notice of Suspension and Intent to Remove and after completion of the appropriate administrative proceedings as provided in the FCU Act and NCUA Rules and Regulations.

NCUA may remove a person even if they voluntarily resign or are terminated by the credit union. A removal action may be brought any time up to six years after resignation, termination of employment, liquidation, or any other termination of a relationship with the credit union (see §206(k)(3) of the FCU Act, 12 U.S.C. §1786(k)(3)).

Any party who has been removed or suspended from office is also automatically removed, suspended, and prohibited from participating in the affairs of any federally insured financial institution without the express written consent of the appropriate regulatory authority.

3. What are the grounds for removal of an official?

NCUA can remove from office any directors, officers, or committee members if:

They directly or indirectly violated one of the following:
<ul style="list-style-type: none">➤ A statute or regulation.➤ A provision of a <u>Final</u> C&D Order.➤ Any published written agreement between the NCUA Board and the credit union.➤ Any condition imposed in writing by the NCUA Board related to granting any application or request by the CU (e.g. application for insurance or 208 Assistance).➤ Engaged or participated in any unsafe or unsound practice related to the credit union.➤ Committed or engaged in any act, omission, or practice constituting a breach of fiduciary duty.

And

Their actions either:
<ul style="list-style-type: none">➤ Involved personal dishonesty.➤ Demonstrated their unfitness to participate in the credit union's affairs.

And

Their actions resulted in at least one of the following:
<ul style="list-style-type: none">➤ The credit union has or will suffer financial loss or other damage.➤ The interests of the members have or could be prejudiced.➤ The party receives financial gain or others benefit because of the violation, practice, or breach.

An official's past or current violation of the Depository Institution Management Interlocks Act is an additional ground for removal.

4. What is an immediate suspension of an official?

An immediate suspension is similar to a Temporary C&D Order. If found necessary to protect the credit union or the interests of its members, NCUA can immediately suspend an official from all official duties pending completion of an administrative hearing. This would be appropriate, for example, when it appears that the individual, once served with a Notice of Intent to Remove, likely will cause further loss to the credit union or destroy credit union records before completion of the hearing or the issuance of the NCUA Board's final Order of Removal.

An Immediate Suspension will usually be a part of or will be served simultaneously with the Notice of Intent to Remove, although it may be served any time after the notice. It, too, becomes effective immediately upon service and remains in effect until dismissed or until the NCUA Board issues a final order. The official may challenge it in court within 10 days of service, and the NCUA Board may enforce the order by suing in U.S. District Court or by assessing civil money penalties.

5. What are the mechanics for removal of an official?

(b)(7)(E) (b)(8)

6. What dismissal authority exists within PCA?

Subject to the applicable procedures for issuing, reviewing, and enforcing directives set forth in §747, Subpart L, of the NCUA Rules and Regulations, the NCUA Board may take discretionary supervisory action against any credit union classified less than

"undercapitalized" requiring them to dismiss a director or senior executive officer. A dismissal under this clause shall not be construed to be a formal administrative action for removal under §206(g) of the FCU Act, 12 U.S.C. §1786(g).

7. What is a prohibition?

A prohibition action is similar to, but broader in scope, than a removal proceeding. A removal action removes a person from a specified official position in a credit union, while a prohibition action stops any institution-affiliated party from participating in the affairs of a federally-insured financial institution. Because institution-affiliated parties are not always elected or appointed officials of an insured credit union, they may not always be removed as directors, officers, or committee members. Instead, NCUA prohibits them from further participation in the affairs of an insured credit union. The FCU Act §206(g), 12 U.S.C. §1786(g), contains NCUA's authority to issue a prohibition order. NCUA Rules and Regulations §747, Subpart A, contains the rules and regulations governing prohibition hearings.

Prohibition of a person, like the removal of an official, is not anticipatory in nature as in a cease and desist action. Prohibition can follow only if NCUA issued a Notice of Intent to Prohibit and completed the appropriate enforcement proceedings or the institution-affiliated party consented. NCUA may combine proceedings for removal and prohibition if appropriate. The procedures for a prohibition action are essentially the same as those for a removal action.

NCUA is not precluded from issuing a notice of prohibition where the person voluntarily withdraws or when the credit union terminates services after discovering financial loss or other damage. NCUA may bring a prohibition action any time up to six years after resignation, termination of employment, liquidation, or any other termination of a relationship with the credit union (see §206(k)(3) of the FCU Act, 12 U.S.C. §1786(k)(3)).

NCUA may issue an immediate prohibition order to protect the credit union or the interest of its members on the same basis and for the same reasons as an immediate suspension of official order. The discussion in the section, Immediate Suspension of an Official, applies equally here.

8. What are the grounds for prohibition of an official?

The grounds for a prohibition are the same as for removal.

9. What are the mechanics for prohibition?

The examiner prepares a recommendation for prohibition in the same manner as other enforcement actions. The recommendation includes:

- Recipient of the prohibition action, i.e., name of the person, business address, and position with the company, group or enterprise (including name of the proprietorship, partnership, or corporation) and the relationship with the credit union.
- Sufficient evidence to establish the grounds necessary for a prohibition action.
- Specifics of the prohibition action, e.g., events causing the insured credit union's (or the other business enterprise's) realized or probable financial loss (or other damage) or events that allowed the institution-affiliated party to profit.

When NCUA determines that grounds for a prohibition action exist, General Counsel will serve a Notice of Intent to Prohibit upon the party.

General Counsel or the examiner will inform the person served with the notice of the basic requirements regarding the hearing, which is held not less than 30 days and not more than 60 days after delivery, as stated in the notice.

10. What are the procedures for removal and prohibition involving a felony?

§206(i) of the FCU Act, 12 U.S.C. §1786(i), contains NCUA's authority to issue a removal or prohibition order for cases involving a felony; NCUA Rules and Regulations. §747, Subpart D, contains the rules and regulations governing prohibition hearings. If examiners learn of any criminal charges brought against institution-affiliated parties involving dishonesty or breach of trust, they should report this and include any evidence supporting a possible felony to their supervisory examiner. In no instance should the examiner proceed to investigate any complaints or indictments brought against institution-affiliated parties without first consulting with the supervisory examiner.

The examiner will report findings in support of a recommendation to suspend the official or to prohibit the person, if an official or other institution-affiliated party meets all of the following:

- Is charged with a crime involving dishonesty or breach of trust.
- The crime is punishable under federal or state law by imprisonment for more than one year.
- The continued service or participation by such party may pose a threat to the interests of the credit union's members or threaten to impair public confidence in the credit union.

The examiner must develop tangible evidence to show that these grounds exist. Examples of tangible evidence supporting suspension of the person as an official could include:

- A membership meeting called in an attempt to force the resignation of the official or the termination of a person's participation.
- Share outflows.
- Membership cancellations directly attributed to general membership dissatisfaction over the continuation of the person as an official.
- Significant adverse publicity.
- Inability of the credit union to obtain loans from regular sources.

The examiner should refrain from expressing an opinion of guilt or innocence in the recommendation for suspension or for prohibition. The suspension or the prohibition remains in effect until the court finally disposes of the information, the indictment, or the complaint, or until NCUA terminates the administrative action.

If the final verdict is guilty, and the judgment is no longer subject to appeal, or if the individual enters a pretrial diversion or other similar program, NCUA may issue and have the examiner serve upon the person a final order removing or prohibiting that individual from participating further in the credit union's affairs. A not guilty verdict will not preclude NCUA from instituting removal or prohibition proceedings under the general removal and prohibition provisions previously discussed. The examiner will need to maintain close follow-up on the legal proceedings and immediately report to the supervisory examiner any new developments which may affect the order issued or pending.

The administrative procedures for felony removal or prohibition are as follows:

1. The NCUA Board issues a Notice of Suspension and/or Prohibition, effective immediately.
2. The NCUA Board holds no administrative hearing unless the official or other person requests one from the Board in writing within 30 days.
3. If the institution-affiliated party requests, the NCUA Board or its designated hearing officer holds the hearing in Washington, DC. The hearing is not the type of formal administrative proceeding held for the other types of administrative actions and does not take place before an administrative law judge.
4. If the court convicts the institution-affiliated party, and that conviction is no longer subject to appellate review, the Board may issue a final Notice of Removal or Prohibition.
5. If the court acquits the institution-affiliated party, the Board may still proceed with a removal or prohibition, but it must be a FCU Act §206(g), 12 U.S.C. §2786(g), type removal or prohibition.
6. When a respondent requests an informal hearing, the presiding officer at the hearing makes his recommended decision to the Board within 10 days.
7. The Board issues its decision within 60 days.

CHAPTER 5

ADMINISTERING PCA DIRECTIVES AND RELATED ACTIONS

1. What is the purpose of this chapter?

This chapter contains procedures for processing specific measures under Part 702 of NCUA Rules and Regulations, Prompt Corrective Action (PCA), for federally insured credit unions that are not defined as "new" by the regulation.

A "new" credit union has more flexibility because it may remain *uncapitalized* or insolvent if its approved business plan provides for this. A "new" credit union is subject to PCA liquidation and conservatorship if it remains *uncapitalized* or insolvent longer than its initial business plan allows or if the credit union has no reasonable prospect of becoming "adequately capitalized." See NCUA Rules and Regulations §§702.304(c) and 702.305(c)(2). Contact the Office of Examination and Insurance (E&I) for guidance regarding PCA or special assistance for "new" credit unions.

NCUA Instruction No. 3501.01 – *Discretionary Supervisory Actions (DSAs) under Prompt Corrective Action (PCA)* provides more specific guidance on the issuance of DSAs.

2. What powers does PCA provide?

PCA actions are triggered by a credit union's net worth as defined in the FCU Act §216; 12 U.S.C. §1790(d). Depending on a credit union's PCA classification, certain restrictions and actions are automatically imposed by operation of law. Discretionary PCA actions include the issuance of directives that impose actions or restrictions permitted or otherwise required. NCUA will consider imposing these discretionary PCA actions whenever it is consistent with PCA's purpose, which is to "resolve the problems of problem institutions at the least possible long-term cost to the deposit insurance fund."

Congress mandated that NCUA follow the strict statutory timeframes of PCA to help reduce the risk of loss to the NCUSIF. These timeframes are integral to all actions NCUA takes regarding *critically undercapitalized* credit unions including administering §208 Special Assistance as well as supervising dissolution. NCUA's adherence to these deadlines is very important. Outside entities such as the U.S. Treasury and the Government Accounting Office (GAO) monitor NCUA's compliance with PCA.

The crux of the PCA powers is contained in NCUA Rules and Regulations §702.204(c)(1), Mandatory Conservatorship, Liquidation or Action in Lieu Thereof, which provides that within 90 days of the effective date of classification as *critically undercapitalized*:

- The NCUA Board must place a credit union into conservatorship or liquidation, regardless of the credit union's prospect of becoming adequately capitalized; or
- The NCUA Board may impose other corrective action (OCA) in lieu of conservatorship or liquidation, if OCA would further the purpose of PCA. The purpose of PCA is to resolve the credit union's problems while minimizing long-term losses to the NCUSIF.

The NCUA Board did not delegate PCA conservatorship and liquidation regardless of the credit union's asset size. However, regional directors (RDs) may impose OCA under delegated authority if the credit union has less than \$5 million in assets.

(b)(7)(E),(b)(8)

Under the FCU Act §216(h), 12 U.S.C. §1790(h), and NCUA Rules and Regulations §701.102(b), if the NCUA Board determines, after written notice and an opportunity for an informal hearing, that a credit union is in an unsafe or unsound condition or is engaging in an unsafe or unsound practice, the NCUA may:

- Reclassify a *well-capitalized* credit union as *adequately capitalized*;
- Require an *adequately capitalized* credit union to comply with one or more requirements applicable to an *undercapitalized* credit union; or
- Require an *undercapitalized* credit union to take one or more actions applicable to *significantly undercapitalized* credit unions.

NCUA may also impose more severe limitations than a credit union's PCA classification would otherwise permit or require if it is determined that the credit union is in an unsafe

or unsound condition or engaging in an unsafe or unsound practice; or it is determined, with respect to *undercapitalized* or *significantly undercapitalized* credit unions that the use of more severe measures is necessary to carry out the purposes of PCA. See NCUA Rules and Regulations §702.202(b)(9) and §702.203(b)(11).

When an *undercapitalized*, *significantly undercapitalized*, or *critically undercapitalized* credit union is already subject to a formal enforcement action under the FCU Act §206, 12 U.S.C. §1786, the NCUA may elect to:

- (i) Modify the §1786 document to reflect any additional requirements deemed necessary in view of the credit union's condition and capital category;
- (ii) Replace the document with a PCA directive; or
- (iii) Impose a PCA directive while also maintaining the formal enforcement action against the credit union.

Whatever option is chosen, mandatory PCA restrictions applicable to such credit unions will apply automatically.

3. What are staff responsibilities for monitoring *critically undercapitalized* credit unions and processing PCA measures?

Examiner, Problem Case Officer, Regional Analyst, Director of Special Actions

- Monitor credit unions that fall into the *critically undercapitalized* net worth category to ensure adherence to statutory timeframes.

Regional Director

- Resolve PCA cases within the statutory timeframes.
- Confer and consult with State Supervisory Authority (SSA) on PCA matters involving FISCUs.
- Provide copies to the E&I Director of all requests for OCA approved under delegated authority.
- Report to E&I on the status and supervisory plans for all *critically undercapitalized* credit unions as requested.
- Inform the Office of the Executive Director and the NCUA Board Secretary of any PCA cases that may require Board approval.
- Submit packages requiring NCUA Board approval to NCUA Board Secretary after implementing any corrections noted by E&I or the Office of General Counsel (GC).

Office of Examination and Insurance

- Coordinate the processing of PCA concurrence packages.
- Verify that PCA concurrence packages comply with the policies and procedures in this manual.
- Provide expert advice to the regions regarding the imposition of PCA.

Office of General Counsel

- Provide consultation and concurrence on PCA actions as applicable.

4. When are PCA Liquidations & PCA Conservatorships used and what documentation is required?

a. PCA liquidation

A PCA liquidation under the FCU Act §206A(a)(3)(A)(ii), 12 U.S.C. §1787(a)(3)(A)(ii), requires the RD to support that the credit union is *critically undercapitalized*. Proof of insolvency is not required. The PCA liquidation order takes place immediately upon service to the credit union. It does not involve an administrative hearing. The FCU Act does not provide a right to appeal a PCA liquidation either within NCUA or in court.

NCUA would pursue a PCA liquidation under the following circumstances:

- The credit union has no reasonable prospect for returning to a 2% net worth ratio (NWR) within the 18 to 23 months as required under NCUA Rules and Regulations §702.204(c)(3)(i); and
- The prospects for merger or purchase & assumption (P&A) are not favorable; and
- The *critically undercapitalized* credit union is a federal credit union with a NWR greater than 0% (solvent);⁴ or
- The *critically undercapitalized* credit union is a (solvent or insolvent) FISCU that poses a significant risk of loss if it is not placed into liquidation.

Without the state supervisory authority (SSA) appointing NCUA as liquidating agent, a PCA liquidation is the only avenue to liquidate a state chartered credit union. In such cases, the RD must demonstrate compliance with the FCU Act §216(l), 12 U.S.C. §1790d(l), entitled *Consultation and Cooperation with State Credit Union Supervisors*, and §702.205 of the NCUA Rules and Regulations entitled *Consultation with State Officials on Proposed Prompt Corrective Action*.

A PCA liquidation action requires NCUA Board approval and the concurrence of the Office of General Counsel (GC) and E&I.

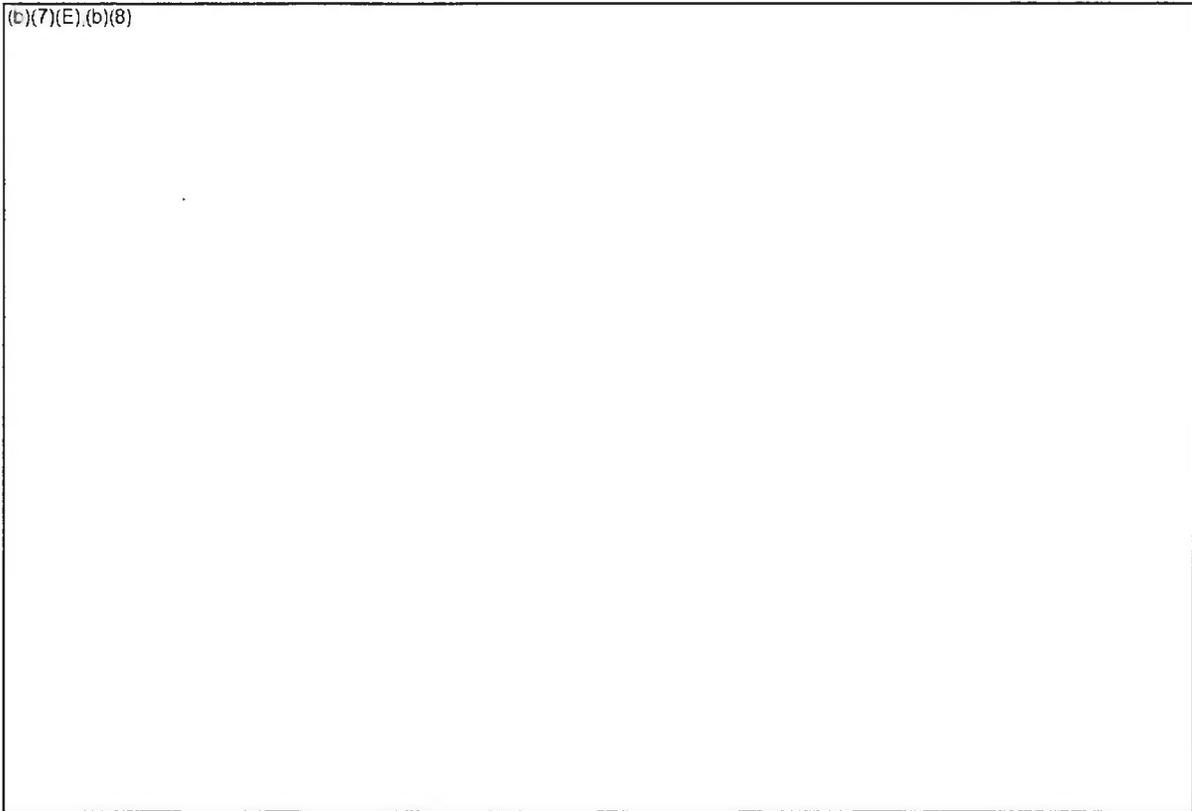
The concurrence package for a PCA liquidation should demonstrate the following:

⁴ RDs have authority to liquidate insolvent FCUs outside of PCA. A *critically undercapitalized* federal credit union that has a net worth ratio of less than zero percent (0%) may be placed into liquidation on grounds of insolvency pursuant to the FCU Act §207(a)(1)(A), 12 U.S.C. 1787(a)(1)(A). Accordingly, the RD may liquidate as provided under delegation LIQ 1.

- The credit union is *critically undercapitalized*. The package should note insolvency if it exists, but the objective is not to prove insolvency.
- The credit union is unlikely to return to a 2% net worth ratio within the 18 to 23 month timeframe as required by §702.204(c)(3). Therefore, OCA to continue operations by adhering to a net worth restoration plan is not feasible or has already failed.
- Section 208 Special Assistance to assist the credit union in achieving a 2% NWR is not a viable option. For example, the credit union has no record of accomplishment and success is unlikely.

RDs should attempt to limit items included in the PCA liquidation concurrence package to those listed below. Only include additional items that are relevant to supporting the objectives above.

(b)(7)(E),(b)(8)



b. PCA conservatorship

Similar to a PCA liquidation, a PCA conservatorship under the FCU Act §206(h)(1)(G), 12 U.S.C. §1786(h)(1)(G), requires the RD to support the credit union is *critically undercapitalized*. The PCA conservatorship order takes place immediately upon service to the credit union. It does not involve an administrative hearing.

Prior to developing a PCA conservatorship package, regional staff should consult with E&I and GC to discuss the advantages of a PCA conservatorship versus a non-PCA conservatorship that uses the broader statutory criteria under the FCU Act §206(h)(1)(A)-(E), 12 U.S.C. §1786(h)(1)(A)-(E).

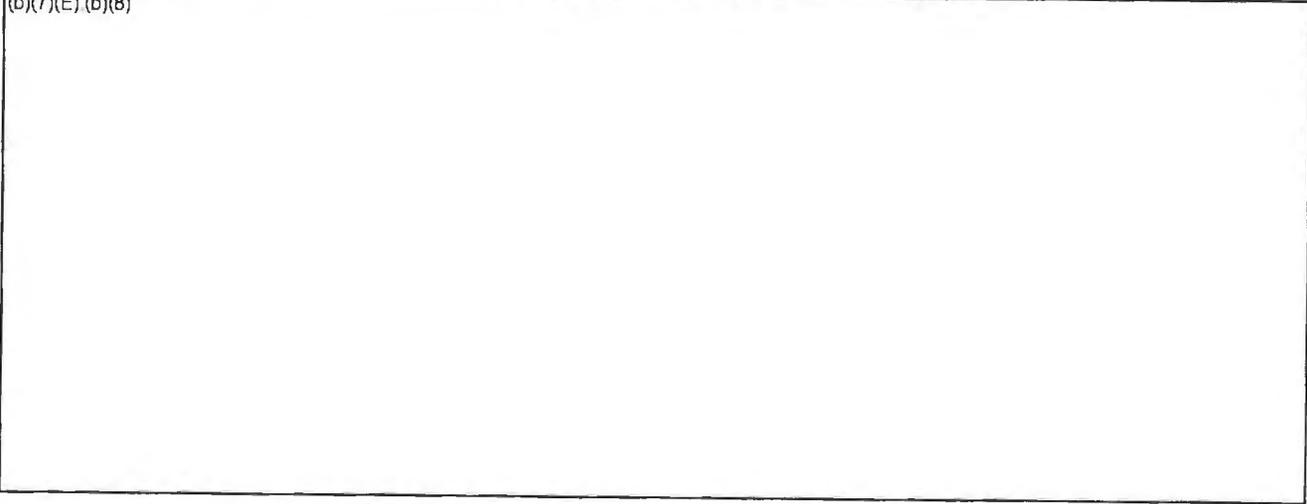
NCUA would most likely pursue a PCA conservatorship under the following circumstances:

- The credit union has no reasonable prospect for returning to a 2% net worth ratio (NWR) within the 18 to 23 months as required under NCUA Rules and Regulations §702.204(3)(i) and any of the following are true:
 - Urgent action is required.
 - Management has abandoned the credit union.
 - Management is inadequate to cope with severe financial or operational problems that must be immediately brought under control.
 - Merger is the best resolution but credit union management will not agree to merge

A PCA conservatorship action requires NCUA Board approval and the concurrence of GC and E&I. Please note that a SSA administered conservatorship does not satisfy the requirement of a conservatorship under §702.204(c)(1).

The objectives for a PCA conservatorship are the same as listed above for a PCA liquidation.

(b)(7)(E), (b)(8)



(b)(7)(E) (b)(8)

NCUA must still adhere to the statutory timeframes required under §702.204(c)(3) of NCUA Rules and Regulations. If a credit union remains *critically undercapitalized* after the 18 to 23 months expire, liquidation is required.

Refer to Chapter 6, *Conservatorship*, for other areas related to the maintenance of a conservatorship.

5. How are requests for Other Corrective Action (OCA) in lieu of conservatorship or liquidation processed?

NCUA may impose OCA upon a credit union with the intent of continuing operations and restoring the NWR to 2%. Alternatively, NCUA may impose OCA to help facilitate the dissolution of a credit union via merger, liquidation, or purchase and assumption. The region must support that the intended action furthers the purpose of PCA by reducing the long-term risk of loss to the NCUSIF.

Cases involving the imposition of OCA require NCUA Board approval as well as concurrence from E&I, unless the credit union has less than \$5,000,000 in total assets. These are cases RDs may process under delegated authority. OCA approved under delegated authority should contain equivalent documentation and analysis to those requiring board approval.

a. OCA to continue operations

Generally, OCA to continue operations under §702.204(c)(1)(iii) of NCUA Rules and Regulations will consist of adherence to the quarterly timetable of steps and meeting quarterly net worth targets in an approved Net Worth Restoration Plan (NWRP).

The objectives of the concurrence package are as follows:

- The OCA proposal should demonstrate that the probability of long-term NCUSIF loss is reduced by allowing the credit union to remain in operation as opposed to liquidation within 90 days of the effective date of the *critically undercapitalized* net worth classification (NCUA Rules and Regulations §702.204(c)(1)(iii)).

- The OCA proposal and NWRP must demonstrate the credit union is viable and will return to a 2% net worth ratio within the 18 to 23 month mandatory time frame pursuant to §702.204(c)(3) of NCUA Rules and Regulations.
- Support any §208 Special Assistance, if necessary. If the credit union cannot achieve a 2% NWR within the 18 to 23 month statutory timeframe on its own, the NWRP must demonstrate how §208 assistance will aid the credit union in achieving this goal.

If necessary, the RD must renew OCA prior to expiration. OCA can range from a period of 1 to 180 days, and will expire unless renewed prior to expiration, regardless of the time limit of any previously approved NWRP.⁵

NWRPs and plans for special assistance to return the credit union to a 2 percent net worth ratio cannot extend beyond a total of 23 months from the effective date of classification as *critically undercapitalized*. Beginning and ending dates for OCA are critical during the 18 to 23 months following the effective date of the *critically undercapitalized* net worth classification.

b. OCA leading to dissolution of the credit union via merger or purchase and assumption

If the credit union is not viable, but the credit union board has agreed to merge or enter into a P&A, NCUA can impose OCA limited to allowing the credit union time to complete a merger or P&A under NCUA supervision.

(b)(7)(E), (b)(8)

⁵ If the credit union remains critically undercapitalized and NCUA does not renew OCA, the NCUA Board generally will immediately place the credit union into conservatorship or liquidation. §702.204(c)(2.)

(b)(7)(E) (b)(8)

6. References

- Federal Credit Union Act
- NCUA Rules and Regulations
- Examiner's Guide
- NCUA Instruction No. 3501.01 – Discretionary Supervisory Actions (DSAs) under Prompt Corrective Action (PCA)

NCUA



BULLETIN

NO. 4820B

DATE: December 29, 2016

SUBJ: Conservatorship Policy and Capital Note Addendum

TO: All NCUA Staff

ENCL: Conservatorship Policy and Capital Note Addendum

REF: NCUA Instruction 4820 *Enforcement Manual*

1. **PURPOSE.** To revise NCUA's policy regarding conservatorships and capital notes.
2. **CANCELLATION.** This NCUA Bulletin replaces Chapter 6: Conservatorship of the *Enforcement Manual*, issued under NCUA Instruction 4820, *Enforcement Manual*, dated September 16, 2004 and Bulletin 4820B, *Conservatorship Policy and Capital Note Addendum*, issued on September 16, 2015 and should be removed from the files.
3. **BACKGROUND.** In September 2015, NCUA issued Bulletin 4820B to replace the prior Conservatorship Chapter of NCUA's *Enforcement Manual* (Instruction 4820). This Bulletin updates the policy released in September 2015 by updating one section of the Conservatorship Chapter. The applicable update amends the requirement for regions to allow the membership to choose among continuing credit unions when multiple no-cost proposals are obtained.
4. **POLICY.** See the attached *Conservatorship Policy and Capital Note Addendum* for the revised policy.
5. **EFFECTIVE DATE.** This bulletin is effect immediately and will remain in effect until the policy is published as part of the updated *Enforcement Manual*.

/s/

Larry Fazio

Director, Office of Examination and Insurance

Enclosure

Authoring Office
E&I

1. Overview

The Federal Credit Union Act (Act) empowers the NCUA Board (Board) to appoint itself or another, such as a state official, as conservator¹ of any federally insured credit union when grounds established in the Act are met.² This includes circumstances where:

- The Board determines that such action is necessary to conserve the assets of any insured credit union or to protect the National Credit Union Share Insurance Fund (NCUSIF) or the interests of the members of such insured credit union.
- An insured credit union, by a resolution of its board of directors, consents to such an action by the Board.
- The Attorney General of the United States notifies the Board in writing that an insured credit union has been found guilty of a criminal offense under §1956 or 1957 of title 18 or §5322 or 5324 of title 31.
- There is a willful violation of a cease-and-desist order, which has become final.
- There is concealment of books, papers, records, or assets of the credit union or refusal to submit books, papers, records, or affairs of the credit union for inspection to any examiner or to any lawful agent of the Board.
- The credit union is significantly undercapitalized, as defined in Section 216(d) of the Act (12 U.S.C. §1790(d)), and has no reasonable prospect of becoming adequately capitalized, as defined in Section 216(d) of the Act (12 U.S.C. §1790(d)).
- The credit union is critically undercapitalized, as defined in Section 216(d) of the Act (12 U.S.C. §1790(d)).

A conservatorship does not require an administrative hearing; however, the credit union may challenge the action in U.S. District Court within 10 calendar days of NCUA placing it into conservatorship.

Conservatorship is used to resolve problem credit unions at the least long-term cost to the NCUSIF. Generally, the term of a conservatorship should not exceed 36 months.³

a. Authority

NCUA Delegation of Authority

¹ The conservator shall have all the powers of the members, the directors, the officers, and the committees of the credit union and shall be authorized to operate the credit union in its own name or to conserve its assets in the manner and to the extent authorized by the Board.

² Section 206(h)(1) of the Act, 12 U.S.C. §1786(h)(1).

³ This timeframe does not include any potential wind-down period needed to provide for an orderly resolution.

Placing a credit union into or taking it out of conservatorship requires NCUA Board approval and the concurrence of the Office of General Counsel (OGC) and the Office of Examination and Insurance (E&I). Regional Directors⁴ and the Asset Management and Assistance Center (AMAC) President may accept appointment from a State Supervisory Authority (SSA) to act as state conservator.⁵ The NCUA Board will decide which Regional Director will accept appointment in conservatorships expected to last more than 180 days.

Federally Insured, State-Chartered Credit Union

NCUA must first request written approval from the SSA to conserve a federally insured, state-chartered credit union (FISCU). If the state does not provide approval within 30 days of NCUA's notification of grounds, the NCUA Board may, by unanimous vote, proceed without state approval. Before taking action, the NCUA Board must respond in writing to reasons the state provides for withholding approval.⁶

(b)(7)(E) (b)(8)

b. Special Assistance and Other Supervisory Matters

Credit unions in conservatorship must follow all NCUA concurrence and approval procedures for special assistance requests. All waivers and other regulatory requests (*e.g.*, Net Worth Restoration Plan approvals) will be approved by the Regional Director assigned to supervise the credit union (also known as the supervising Regional Director).⁷

(b)(7)(E) (b)(8)

⁴ Throughout this chapter, "Regional Director" includes all Regional Directors and the Director of the Office of National Examinations and Supervision, as applicable.

⁵ NCUA Delegations of Authority: AMAC 10; LIQ 13; SUP 19

⁶ Section 206(h)(2) of the Act, 12 U.S.C. §1786(h)(2).

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(b)(7)(E) (b)(8)

Notice to Call Center

Upon receiving NCUA Board approval of the conservatorship action, the region will notify the Director of the Office of Consumer Protection's (OCP) Division of Consumer Affairs of the planned date of the action and the need for call center support. OCP will ensure the call center is adequately staffed based on the region's knowledge of member issues or anticipated media interest.

(b)(7)(E) (b)(8)

c. Oversight of the Conservatorship

NCUA is responsible for determining the actions taken on behalf of the credit union membership are appropriate and properly consider the impact on the NCUSIF. NCUA has established a comprehensive oversight process that includes sound policy, reporting, and monitoring requirements. Section 6 includes a detailed description of the oversight for various types of conservatorships.

Conservatorship Plan

The Conservatorship Plan replaces the Preliminary Operating Plan established at the onset of conservatorship. The Agent will determine the anticipated plans of action for resolution as soon as possible after the initiation of the conservatorship and develop a Conservatorship Plan for any credit union in conservatorship more than 90 days.

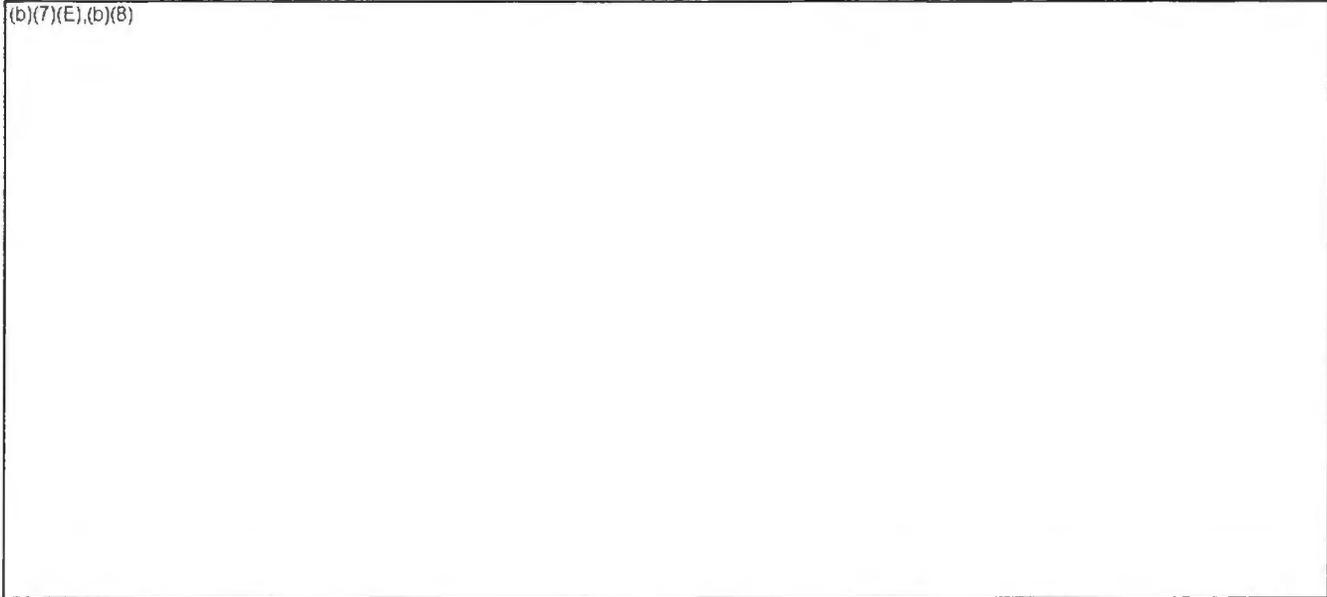
The Conservatorship Plan will outline the anticipated timeframe for conservatorship. The timeframe will vary based on individual circumstances and the planned resolution. Thorough planning is important before and throughout the process to ensure timely resolution and uninterrupted operations.

The Agent will submit the Conservatorship Plan to the supervising Regional Director for approval within 75 days after conservatorship. The supervising Regional Director will provide a copy to E&I within 90 days after conservatorship.

¹¹ Generally, 90 days is considered a reasonable period. However, what is a reasonable period depends upon the facts of every case and may vary from one jurisdiction to the next..

¹² Section 207(c) of the Act, 12 U.S.C. 1787(c).

(b)(7)(E),(b)(8)



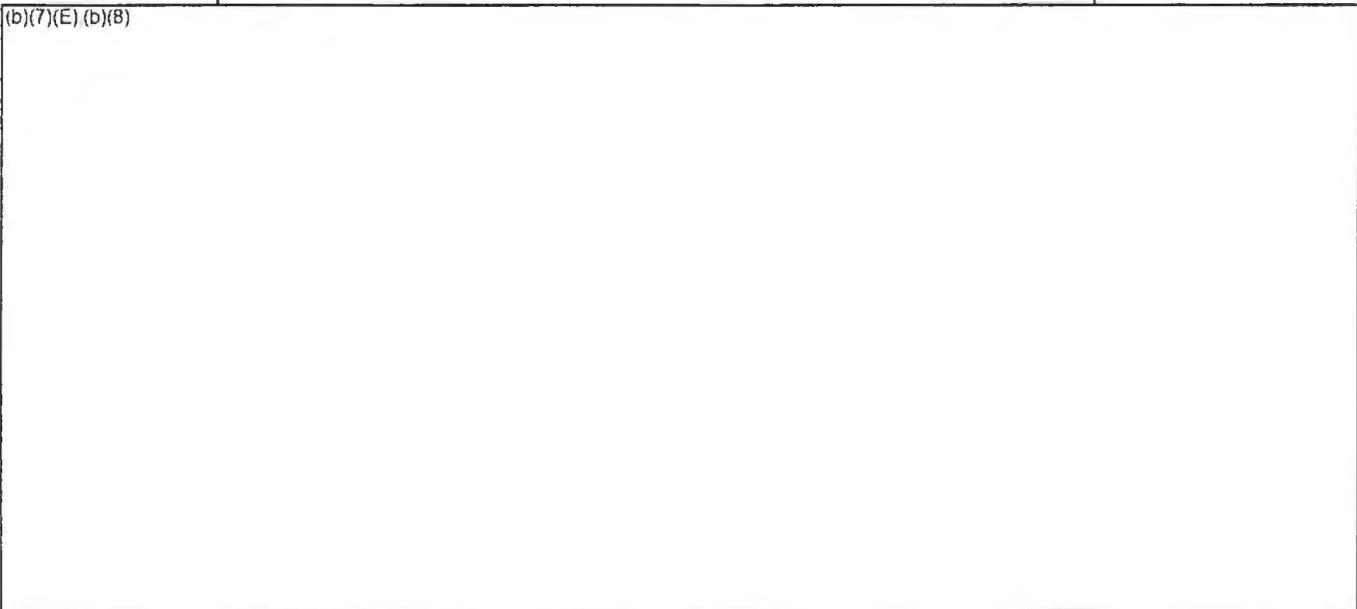
If the credit union must file a Net Worth Restoration Plan (NWRP) under Prompt Corrective Action (PCA), the Conservatorship Plan may serve as the NWRP and must address the information required by NCUA Rules & Regulations §702.206.¹⁵ If the credit union is not meeting the goals outlined in the plan, the supervising Regional Director can issue a Regional Director Letter requiring the credit union to submit an updated plan. Before release from conservatorship, the conservatorship management team will submit a formal NWRP for the supervising Regional Director's approval, if applicable.

Expense Approvals

Approval of operational decisions are necessary to ensure the credit union's operations are uninterrupted.

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(b)(7)(E) (b)(8)



¹⁵ A NWRP may not be submitted in lieu of a Conservatorship Plan.

Annual Examination

The supervising Regional Director will ensure an examination is completed within 12 months of the appointment of a conservator. Staff supervising the credit union will follow all relevant *National Supervision Policy Manual* (NSPM) requirements during conservatorship.

Senior examination staff (principal examiner or higher) will serve as Examiner-In-Charge (EIC) and lead the annual examination and conduct at least one follow-up contact semiannually. At the conclusion of the examination and contact, the EIC will hold a joint conference with the Agent and conservatorship management. The examination report will require a formal, written response to the supervising Regional Director from conservatorship management within 30 days of the joint conference. The supervising Regional Director is responsible for following-up on any outstanding material concerns identified in the examination report.

Additionally, the supervising Regional Director is responsible for quality control over the examination process (*e.g.*, Quality Control Reviews, RATE).

Annual Audit/Verification of Accounts

A Certified Public Accountant (CPA) will perform the required annual audit regardless of the credit union's asset size. Both the audit and the verification of members' accounts will comply with the requirements of Part 715 of NCUA Rules and Regulations. The Agent is responsible for contracting for the annual audit and verification of accounts.

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(b)(7)(E) (b)(8)

4. Share Insurance and Conservatorships

a. Handling Share Insurance Inquiries following Conservatorship

Handling Member Inquiries

(b)(7)(E) (b)(8)

During a conservatorship, credit union members will likely ask NCUA staff and credit union employees about the safety of their money and their share insurance coverage. Questions may include:

- Should I move my money?
- How can I restructure my accounts to be fully insured?
- Is the credit union going to fail?
- If the credit union fails, will I lose access to my money?
- If the credit union fails, will I lose my uninsured funds?

NCUA's policy is that credit union employees and NCUA staff will direct all member inquiries related to share insurance to the designated point(s) of contact. Conservatorship management will designate a single point of contact (or small group of contacts if the credit union is a larger institution) to address members' questions about share insurance coverage. The contact person(s) should be an employee of the conserved credit union.

No credit union employee should contact individual members to inform them that their shares may be uninsured. However, credit union staff may contact members regarding share accounts if incomplete records or inconsistent information is identified regarding account ownership. In response to member initiated requests, the designated point(s) of contact may advise members on how to structure their accounts to fully insure their funds. The designated point(s) of contact must document the member initiated the request.

The Agent will provide the designated point(s) of contact with a script, the questions and answers found in PACA's release issued in conjunction with the conservatorship, OCP's Your Insured Funds booklet (available at <http://go.usa.gov/BD3d>) and a set of frequently asked questions so that the message remains factual and consistent. (b)(7)(E),(b)(8)

(b)(7)(E), (b)(8)

NCUA Staff Responsibilities

After conserving a credit union, NCUA staff will:

- Post notices at the credit union (including all branches) and on the credit union's website to provide members with general share insurance coverage information.²¹ The Agent will provide a standard notice to all members of the conservatorship team in advance of the conservatorship action.

²¹ Letters or other correspondence regarding share insurance coverage will not be mailed to members.

- Make NCUA share insurance resources readily accessible to credit union staff.
- Review the credit union’s calculation of uninsured shares for accuracy. Credit union staff will make appropriate changes to identified errors and produce an accurate report of uninsured shares.

NCUA staff onsite at the conserved credit union will not provide specific advice about members’ accounts. Members will need to review their own accounts in conjunction with the share insurance resources described below to make this determination on their own, or work with the designated point(s) of contact. If a member asks for an individual share insurance determination, NCUA staff may only:

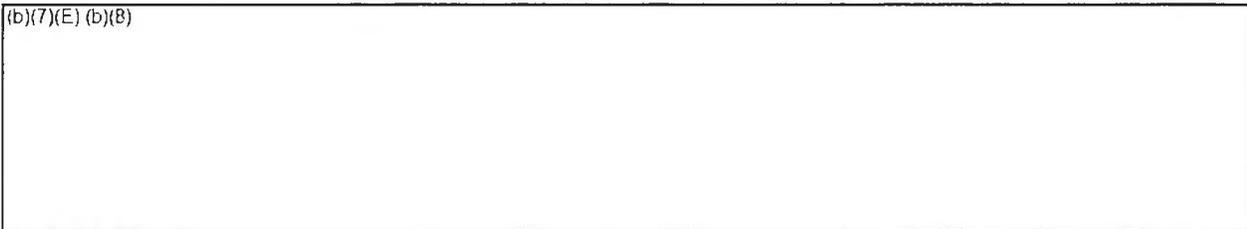
- Inform the member that share insurance coverage remains unchanged despite the conservatorship.
- Provide the member with published share insurance resources, like OCP’s How Your Accounts Are Federally Insured pamphlet and the Your Insured Funds booklet.
- Inform the member of the availability of the NCUA Share Insurance Estimator (<http://www.mycreditunion.gov/estimator/Pages/index.html>) and other resources at www.mycreditunion.gov.
- Encourage the member to talk to the designated point(s) of contact handling share insurance questions, call NCUA’s Consumer Assistance call center at 1-800-755-1030, or contact his or her attorney or financial professional.

b. Share Insurance Resources

Part 745 of NCUA’s Rules and Regulations governs the determination of share insurance coverage. NCUA staff and credit union employees should refer members to this regulation, but also direct members to the following share insurance resources to help the member better understand NCUSIF coverage:

- Appendix to 12 C.F.R, Part 745
- NCUA.gov: “Your Insured Funds” available at <http://www.ncua.gov/Legal/GuidesEtc/GuidesManuals/NCUAYourInsuredFunds.pdf>
- Mycreditunion.gov: “Is My Money Safe in a Credit Union?” available at <http://www.mycreditunion.gov/protect/Pages/SI.aspx>
- NCUA.gov: “Share Insurance FAQ & Share Insurance Toolkit” available at <http://www.ncua.gov/DataApps/Pages/SI-Tools.aspx>

(b)(7)(E) (b)(8)



7. Capital Note Addendum

a. Overview

The Federal Credit Union Act, §208, permits NCUA to use funds from the National Credit Union Share Insurance Fund (NCUSIF) to provide special assistance to a federal credit union or state-chartered, federally insured credit union in troubled financial condition. Assistance provided under §208 can be either permanent (cash or non-cash) or temporary (*i.e.*, dividends).²⁵ Capital note assistance is a permanent, cash form of §208 assistance. In these cases, the NCUSIF provides cash (a credit union asset) to the troubled credit union along with a note (a credit union liability) to establish an NCUSIF subordinated note.²⁶

Impact on Net Worth

Public Law No: 111-382²⁷, signed on January 4, 2011, amended the statutory definition of net worth to include assistance provided by NCUA under §208 be included in regulatory net worth. In September 2011, NCUA amended §702.2(f)(4) of NCUA's Rules and Regulations establishing the following requirements for §208 assistance to be included in net worth:

- Remaining maturity of more than 5 years.
- Subordinate to all other claims including those of shareholders, creditors and the NCUSIF.
- Not pledged as security on a loan to, or other obligation of, any party.
- Not insured by the NCUSIF.
- Non-cumulative dividends.
- Transferable.
- Available to cover operating losses realized by the insured credit union that exceed its available retained earnings.

When to Use an NCUSIF Capital Note

NCUA rarely uses capital notes. Historically, capital notes have only been issued to support credit unions in the wake of a significant economic recession. During economic downturns, potential merger or liquidation partners are less willing to assume the risk of combining with a troubled institution, resulting in higher-cost resolution alternatives.

²⁵ Each type of §208 assistance is discussed in greater detail in the Special Assistance Manual.

²⁶ A sample subordinated capital note and repayment schedule is provided as on E&I's NCUACentral site.

²⁷ Entitled, "A bill to clarify the National Credit Union Administration authority to make stabilization fund expenditures without borrowing from the Treasury."

NCUA only uses capital notes to facilitate the continued independent operations of a credit union where the benefit of using a capital note is materially superior to all other alternatives.²⁸ Capital notes also may be used to facilitate the orderly dissolution of a credit union, thereby protecting the NCUSIF from higher levels of loss.²⁹

In the use of capital notes, NCUA seeks to minimize losses to the NCUSIF consistent with sound public policy. Because of public policy considerations, NCUA's use of capital notes is limited to a strict set of applicable criteria and controls as defined below. NCUA minimizes the moral hazard concerns by implementing well-defined criteria for the use of capital notes that discourages institutions from accepting greater levels of risk with the prospect of government assistance.

(b)(7)(E),(b)(8)

CHAPTER 7

INVOLUNTARY LIQUIDATIONS

1. What is the purpose of this chapter?

This chapter provides guidance in processing involuntary liquidations.

2. What are the types of involuntary liquidations?

a. Title I involuntary

Under §120 of the FCU Act, 12 U.S.C. §1766, the NCUA Board can place a solvent federal credit union into involuntary liquidation for violations of its charter, its bylaws, the FCU Act, or the NCUA Rules and Regulations. Also, under §120, 12 U.S.C. §1766, the NCUA Board can place a federal credit union into involuntary liquidation upon finding that the board or liquidating agent did not conduct a voluntary liquidation in an orderly or efficient manner or in the best interests of the members.

The rules and regulations relating to these administrative proceedings are contained in NCUA Rules and Regulations §747, Subpart E. The effect of this action is the elimination of a federal credit union as a legal entity after due process provided for by §120(b) of the FCU Act, 12 U.S.C. §1766, and Part 747, Subpart E, of the NCUA Rules and Regulations. It is the most drastic enforcement action that can be taken against a solvent federal credit union.

Since Title I liquidation is not a commonly used administrative action, examiner involvement will differ from case-to-case.

b. Title II involuntary

Section 207 of the FCU Act, 12 U.S.C. §1787, requires the NCUA Board to close for liquidation any federal credit union it deems bankrupt or insolvent. In these cases, the NCUA Board must also appoint itself as liquidating agent. In addition, the NCUA

Board can accept appointment as liquidating agent of a bankrupt or insolvent federally-insured, state-chartered credit union.

c. Purchase and assumption

A purchase and assumption (P&A) is an action similar to a merger, but unlike a merger the NCUA Board places the credit union into involuntary liquidation first. In a P&A, another credit union or another financial institution assumes all or part of the assets, liabilities, and shares.

3. What are the goals for an involuntary liquidation?

The primary goals of an involuntary liquidation are:

- Prompt return of members' shares.
- Payment to the creditors.
- Disposition of the remaining assets to the NCUSIF.

Once the regional director decides to liquidate the credit union, the examiner ensures the records are current and in balance.

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4. What are the grounds for an involuntary liquidation of an insolvent credit union pursuant to §207 of FCU Act?

The grounds for this most severe action is insolvency or bankruptcy as defined in §700.2(e) of NCUA Rules and Regulations.

For a liquidation pursuant to §207, 12 U.S.C. 1787, of the FCU Act, the credit union has no right to a pre-closure administrative hearing. The federal credit union's charter is immediately revoked and the credit union is placed into involuntary liquidation. The credit union may, however, challenge the action in U.S. District Court within 10 days. It is critical, therefore, that the finding of insolvency be based upon tangible evidence and indisputable circumstances using the most current information available.

The examiner prepares a supplemental memorandum for the liquidation package that contains all significant data to support the recommended action, including an analysis of the various exceptions to insolvency set forth in §700.2(e) of the regulations. It is imperative that the administrative record adequately supports insolvency. The examiner must be prepared to testify in court to establish the reasonableness of the insolvency calculation. For this reason, involuntary liquidations require the concurrence of the Office of General Counsel to ensure that the liquidation package is legally sufficient.

A Notice of Revocation of Charter and Involuntary Liquidation and Appointment of a Liquidating Agent will be served on the federal credit union. The order is effective immediately upon service, and all assets, books and records of the credit union immediately become the property of the NCUA. Agents for the Liquidating Agent will be appointed as provided in §207(a) of the FCU Act, 12 U.S.C. §1787.

5. What are the grounds for an involuntary liquidation of a solvent credit union?

Pursuant to the authority in §120(b)(1) of the FCU Act, 12 U.S.C. §1766(b)(1), the NCUA Board may suspend or revoke the charter of a federal credit union that has violated any provision of its charter, its bylaws, the FCU Act, or NCUA regulations. This type of action may also be taken for reasons of bankruptcy, but generally liquidation of insolvent credit unions are initiated under §207 of the FCU Act, 12 U.S.C. §1787. Examples of conditions that may warrant recommending revocation of charter in a solvent credit union include:

- Abandonment of the credit union's operations and affairs by the officials.
- Plant closing and officials refusing to vote to present the question of liquidation to the members. Such plant closing may force insolvency under the concept of an ongoing concern, or may cause a dissipation of the assets and expose the creditors and the NCUSIF to a greater than normal risk.
- Other specific serious violations of its charter, its bylaws, the FCU Act, or regulations that cannot be reversed and that may cause insolvency.
- Serious operational deficiencies that the officials have not acted to correct and which, if allowed to continue, may cause insolvency.

Abandonment shall be deemed to have occurred when all or most of the elected and the appointed officials have demonstrated by their actions, or failure to act, an intent to end operations. Proof is evidenced when an active quorum cannot or will not be formed by the remaining officials.

The examiner recommends a Notice of Intent to Revoke Charter whenever the timeframe for due process will not create a greater risk of loss to the members, the creditors, and the NCUSIF than exists at the time of the recommendation. The examiner should be aware that the credit union will continue to conduct business during the effective time of this notice.

The examiner determines whether or not a greater risk for loss exists by allowing the credit union to conduct business in the interim based on the conditions and the circumstances in each case. However, if a greater risk for loss is likely to exist, a recommendation for conservatorship or a Notice of Suspension of Charter and Intent to Revoke Charter and Place Into Involuntary Liquidation may be appropriate.

The credit union has 40 days from the date the Notice of Intent is served to:

- File a written statement with NCUA setting forth the reasons why it should not be placed into involuntary liquidation; or
- In lieu of a written statement, request that an oral hearing be conducted in accordance with Part 747 of the NCUA Rules and Regulations; or
- Consent to the Notice by resolution of its board of directors.

The written statement, request for an oral hearing, or consent must be accompanied by a certified copy of a resolution by the board, signed by the president and the secretary authorizing such statement, request, or consent.

At the time of delivery of the Notice, the examiner advises the officials of their options and of the timeframes in which their options must be exercised. The examiner makes it known to the officials that if the credit union fails to exercise any of its alternatives as provided in the NCUA Rules and Regulations within the prescribed timeframes, it will be deemed to have consented to the action being sought by NCUA.

6. What is involved in an involuntary liquidation of a state-chartered federally insured credit union?

When the appropriate state authority declares an insured state credit union insolvent or bankrupt, the state usually appoints the NCUA Board as liquidating agent, receiver, or conservator. Under delegated authority, the president of AMAC becomes the liquidating agent in these cases.

See Chapter 5 of this Manual, *Administering PCA Directives and Related Actions*, for guidance in placing a FISCU into liquidation under PCA.

7. What are the mechanics for an involuntary liquidation?

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(b)(7)(E), (b)(8)

10. References

- *Field Examiners Guide to On-Site Involuntary Liquidation Procedures*

CHAPTER 8

TERMINATION OF INSURANCE

1. What is the purpose of this chapter?

This chapter provides guidance on the processing of an action to terminate insurance.

2. What is termination of insurance?

§206(b) of the FCU Act, 12 U.S.C. §1786(b), contains the authority to terminate an insured credit union's share insurance; NCUA Rules and Regulations §747, Subpart C, contains the rules and regulations governing a termination of insurance action.

Although the NCUA Board can theoretically take this action against a federal credit union, the Board most often reserves it for federally insured state-chartered credit unions. As federal credit unions must be federally insured, a termination of insurance would result in liquidation, unless the credit union could convert to a state charter before completing the proceeding. Therefore, the recommended course of action for a federal credit union is immediate liquidation, if insolvent, or Notice of Suspension of Charter and/or Notice of Intent to Place into Involuntary Liquidation, for problems other than insolvency.

For federally insured state-chartered credit unions, termination of insurance is the most severe action NCUA can initiate. It protects the NCUSIF when the credit union is unwilling or unable to take corrective action.

Termination of insurance will most likely force the state credit union into involuntary liquidation unless the credit union has an alternative share insurance program for which it can qualify and can thereby maintain member confidence. For these reasons, the regional office will closely communicate with the state regulatory agency whenever it contemplates this administrative action against any federally insured state-chartered credit union.

The credit union is subject to the same duties and obligations of an insured credit union for one year after the effective date of the Notice of Termination of Insured Status; shares on deposit when insurance is terminated remain insured for the following year. Any shares purchased after the effective date of the final order are not insured by the NCUSIF. An examiner may be asked to follow up on the final order to determine if the credit union is fulfilling its duties and obligations to its members and to the NCUSIF.

3. What are the grounds for termination of insurance?

The grounds for a termination of insurance action are essentially the same as those for a cease and desist action, as follows:

- Unsafe or unsound practices or conditions; or
- Violations of law, rule, regulation, any condition imposed in writing by the NCUA Board, or any written agreement entered into with the NCUA Board. To be enforceable, the Board must have previously published the agreement.

Termination of insurance action serves as an initial course of action or as a continuation of a cease and desist order if the officials refuse to comply as directed. Examples of conditions that might warrant a recommendation for termination of share insurance include:

- Insolvency as defined in §700.2(e) of the NCUA Rules and Regulations, and the unwillingness of the credit union's board of directors or state regulator to place the credit union into involuntary liquidation or to act appropriately to minimize risk and potential loss to the NCUSIF;
- Abandonment of the credit union's operations by the elected and the appointed officials, and the state regulator's inaction to minimize risk and potential loss to the NCUSIF;
- Plant closing, extended work stoppage, or breakdown in membership confidence that causes a major outflow of shares and of liquidity, or general mismanagement of the operations by the officials that is causing or will cause an insolvent condition, and the officials or state regulator are not acting to minimize risk and potential loss to the NCUSIF; or
- An unsafe or unsound practice or a serious violation of an applicable law, rule, regulation, order, or any condition imposed by the NCUA Board that is causing or will cause an insolvent condition, and the officials or state regulator are not acting to minimize risk and potential loss to the NCUSIF.

4. What are the mechanics for termination of insurance?

The following are the administrative procedures for termination of insurance:

1. The NCUA Board issues a Notice of Charges, with a request for corrective action. The notice will contain a statement of fact about the alleged unsafe or unsound practices or violations and sets the time and place for a hearing (30 to 60 days after service). The credit union has 120 days to make corrections, although the Board may reduce this time to not less than 20 days if the insurance risk is sufficient. A copy of the Notice is also sent to the state regulatory agency.
2. If the credit union does not take corrective action, then the NCUA Board may issue a Notice of Intent to Terminate Insured Status. This sets out a statement of the facts justifying termination, and establishes a time and place for an administrative hearing within 30 to 60 days.
3. An administrative law judge (ALJ) holds an administrative hearing.
4. The ALJ files a recommended decision with the NCUA Board.
5. The NCUA Board issues its final order. Before the effective date of termination of insurance, the credit union is required to mail to each member and to publish in at least two issues of a local newspaper of general circulation the Notice of Termination of Insured Status. The format for this notice is specified in §747.207 of the NCUA Rules and Regulations. Specific duties of the credit union after termination of share insurance are specified in §747.208 of the NCUA Rules and Regulations.
6. The credit union may appeal to the U.S. Court of Appeals, but the order is effective unless modified or lifted by the Board or the Court.

NCUA



INSTRUCTION

NO. 4810	DATE: September 16, 2004
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SUBJECT: Special Assistance Manual

TO: All NCUA Staff

ENCL: Special Assistance Manual

1. **PURPOSE.** To transmit the agency's special assistance policies, guidelines and procedures.
2. **CANCELLATION.** The E&I Special Assistance Manual distributed in April 2001, NCUA Instruction 7900.2 - Definition of Merger, Liquidation, and Purchase and Assumption issued on February 11, 1983, and NCUA Instruction 4820 – Loan Guarantees issued on December 22, 1975 are cancelled and replaced by this instruction.
3. **BACKGROUND.** In February 2001, the NCUA Board approved the Special Assistance Program, outlining the types of special assistance, limitations on assistance, and qualifications for special assistance. The Special Assistance Program is included as Chapter 1 of the Special Assistance Manual. The Special Assistance Manual consolidates the agency's policies, guidelines, and procedures for administration of the Special Assistance Program.
4. **REVISIONS.** Significant revisions to the manual are colored blue in Microsoft Word. Significant revisions include:
 - a. Increased emphasis on AMAC's role in reviewing and processing asset guarantees (page 12).
 - b. Increased guidance on the calculation of the "least possible long-term loss to the NCUSIF" (page 12).
 - c. Added requirement that credit providers subject to an NCUSIF Guaranteed Line of Credit secure a properly recorded first position security interest on the benefiting credit union property and assets (page 15).
 - d. Clarified the items to be covered within a Regional Summary (page 24).
 - e. Clarified how to request payment from the NCUSIF for approved assistance (page 28).
 - f. (b)(7)(E) (b)(8)

g.

(b)(7)(E) (b)(8)

h.

5. **GENERAL POLICY.** Agency staff should use this manual in making special assistance decisions and adhere to the policies, guidelines and procedures incorporated.
6. **EFFECTIVE DATE.** This instruction is effective immediately, and will remain in effect until cancelled.

/s/

J. Leonard Skiles
Executive Director

Enclosure

SPECIAL ASSISTANCE MANUAL



August 2004

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Overview

Purpose of this Manual

The Special Assistance Manual addresses the following items:

- Chapter 1 contains the NCUA Board Approved Special Assistance Program, which outlines the requirements for a credit union to receive special assistance, and the types of assistance the Board has authorized staff to provide.
- Chapter 2 contains procedures for requesting and maintaining special assistance.
- Chapter 3 contains the requirements for the preparation of postmortems

(b)(7)(E) (b)(8)

These policies and procedures provide only internal NCUA guidance. They do not create rights, substantive or procedural, that are enforceable at law or in any administrative proceeding.

Chapter 1

Special Assistance Program

1. Purpose

The NCUA Board approved this program to:

- a. Prescribe the types of NCUSIF special assistance that may be provided to "critically undercapitalized" credit unions, "uncapitalized" "new" credit unions, and credit unions "in danger of closing."
- b. Establish limits on the types of special assistance.
- c. Provide guidance on the implementation of special assistance.
- d. Establish reporting responsibilities.
- e. Clarify that special assistance is not a grant, must be justified, and must assist in making a qualified credit union a financially viable, self-sustaining institution.
- f. Ensure special assistance is provided in the best interest of the credit union's members, in the best interest of the NCUSIF, and to further the purpose of Prompt Corrective Action (PCA).

The Board, in its discretion, may approve the use of the NCUSIF for special assistance in accordance with the FCU Act. Special assistance is a last resort measure. The Board will approve special assistance only after the credit union exhausts all reasonable corrective efforts to become a viable, self-sustained institution, with or without guidance from appropriate supervisory and/or regulatory authorities.

Accounting for special assistance must conform to Generally Accepted Accounting Principles (GAAP) in most cases. The Credit Union Membership Access Act

(CUMAA) requires that only credit unions with \$10 million or more in assets comply with GAAP. However, GAAP treatment will enable NCUA to most precisely and favorably evaluate a credit union's financial performance while the credit union operates under special assistance, regardless of the credit union's asset size.

2. Background

§208 and §216 of the Federal Credit Union Act provide the NCUA Board the discretion and authority to provide special assistance to Federally Insured Credit Unions.

3. Definitions

Except as provided below, the terms used in this program have the same meanings as set forth in Part 702 of NCUA Rules and Regulations.

a. In danger of closing describes a credit union that:

- Is subject to mandatory conservatorship, liquidation or "other corrective action" as provided in sections 702.204(c) or 702.305(c) of the NCUA Rules and Regulations and is unable to increase net worth sufficiently through net income retention or other sources (e.g. secondary capital);
- Is subject to discretionary conservatorship or liquidation as provided by section 702.203(c), or is required to merge as provided by section 702.203(b)(12);
- Is a "new" credit union subject to discretionary conservatorship or liquidation as provided by section 702.304(c) because it has no reasonable prospect of attaining a net worth of 4 percent within 10 years of operation; or,
- Is subject to a high probability of sustaining an identifiable loss (e.g. fraud, unexpected and sudden outflow of funds, operational failure, natural disaster, etc.) that would cause it to become "critically undercapitalized" or subject to conservatorship or liquidation under section 702.304(c).

b. No reasonable prospect of becoming adequately capitalized describes a credit union that:

- Is "significantly undercapitalized" and unable to rise to at least "undercapitalized" through the retention of actual or reasonably projected net income or by acquiring other sources of net worth (e.g., secondary capital) within a reasonable timeframe.

- Is a "new" credit union that is either "moderately capitalized," "marginally capitalized" or "minimally capitalized" and unable to attain a net worth of 4 percent within 10 years of operation through the retention of actual or reasonably projected net income or by acquiring other sources of net worth (e.g., secondary capital).
- c. **Permanent Special Assistance** describes special assistance granted to a credit union to continue independent operations. Typically, permanent assistance is granted after temporary special assistance (i.e., temporary dividend approval) is granted.
- d. **Person** means any credit union, individual, partnership, corporation, trust, estate, cooperative, association, government or governmental subdivision or agency or other entity.
- e. **Section 208 Assistance** means special assistance granted under the authority of section 208(a)(1) of the FCU Act. The term of section 208 assistance will not exceed 33 months from the "effective date" of the adverse net worth classification.¹ Section 208 assistance must be accompanied by a written agreement. Section 208 special assistance is limited to the following purposes:
- Reopen a closed insured credit union or to prevent the closing of an insured credit union which is in danger of closing or to assist in the voluntary liquidation of a solvent credit union;
 - Protect the fund or the interest of the members of the credit union; or,
 - Reduce risk or avert a threatened loss to the fund and facilitate a merger or consolidation of an insured credit union with another insured credit union, or facilitate the sale of assets of an open or closed credit union to an assumption of its liabilities by another person.
- f. **Section 216 Assistance** means special assistance granted under the authority of Section 216, PCA, of the FCU Act. Section 702.204 of NCUA Rules and Regulations allows NCUA to take other corrective action, in lieu of conservatorship or liquidation, to better achieve the purpose of PCA, provided the Board documents why such action would do so. Other corrective action includes section 216 (i.e. workout plan may include reduction in earnings transfer) and 208 assistance.

¹ "Uncapitalized" for a "new" credit union and "critically undercapitalized" for all other credit unions.

4. Responsibilities

a. NCUA Board

Establishes authority for special assistance and approves all special assistance requests outside of delegated authority. National Credit Union Administration regulations require Board approval of PCA-based liquidation, conservatorship, and "other corrective action" outside of delegated authority.

b. Examination and Insurance (E&I)

Develops and establishes controls and procedures to implement the objectives of this program. E&I monitors all credit unions receiving special assistance and provides concurrence on applicable requests for special assistance. E&I conducts quality control reviews of assistance requests submitted for concurrence and/or Board approval.

c. Office of General Counsel

Reviews cases where officials or NCUA need to replace ineffective or incompetent management before receiving special assistance. Certifies that credit unions meets the definition for "critically undercapitalized" in emergency merger situations. Provides concurrence on all liquidations.

d. Office of Chief Financial Officer

Lists all asset guarantees on the NCUSIF monthly report.

e. Asset Management & Assistance Center (AMAC)

Reviews and provides comments on asset (loan) guarantee agreements, payment of asset (loan) guarantees, asset purchase agreements, and indemnification agreements.

f. Regional Director

Approves all special assistance requests, with concurrence from appropriate offices as required by delegations, and ensures all requests conform to applicable policies and procedures. Ensures the administrative record fully supports the request for special assistance. Also ensures that key monthly data is provided to the Office of Examination and Insurance for all credit unions receiving special assistance. The Regional Director must seek the views of the appropriate State official for all requests for special assistance from state-chartered credit unions, as well as proposed PCA-based actions against a federally insured state-chartered credit union (FISCU).

The Regional Director must develop procedures to ensure compliance with Part 702, PCA, and act within the delegated authority for PCA actions.

5. Request for assistance

Credit unions initiate requests for special assistance by writing to the Regional Director. Requests for assistance must comply with Section 216, PCA, of the FCU act and further the purpose of Part 702. The requests must justify the proposed plan is the best alternative for use of NCUSIF funds and must document that the credit union receiving permanent special assistance has a reasonable prospect for becoming a viable, self-sustaining institution as demonstrated by recent actual performance. The requests for permanent special assistance must document that competent management is in place or document how competent management will be secured. Permanent special assistance is limited to a maximum term of 24 months.

6. Approved types of assistance

a. Asset (Loan) Guarantee

An asset guarantee is section 208 assistance (non-cash). An asset guarantee protects any person against loss by reason of his assuming the liabilities and purchasing the assets of an open or closed insured credit union. An asset guarantee is generally utilized to arrange a merger, purchase and assumption, or liquidation when interest is limited, fair value of the assets cannot be readily determined, expediency is critical, or the uncertainty of recovering the full value of the asset(s) is questionable. AMAC must review and comment on the language of the guarantee agreement and payment for asset guarantees. Agreement terms will usually not exceed 12 months unless justified, with a maximum of 24 months. Delegated authority limits the approval levels.

b. Asset Purchase

An asset purchase is section 208 assistance (cash). An asset purchase involves the use of NCUSIF funds to purchase a specific asset. An asset purchase is generally utilized as part of a workout plan for a potentially viable, self-sustained institution with a specific problem related to the asset being purchased. AMAC must review and comment on the asset purchase agreement. Delegated authority limits the approval levels.

c. Cash Payment

Cash payment assistance is section 208 assistance (cash). Cash payment involves the use of NCUSIF funds paid to a person. A cash payment is generally utilized to arrange a merger, purchase and assumption or liquidation of an insolvent ("uncapitalized") or "critically undercapitalized" credit union. In rare occasions, other poorly capitalized credit unions may receive a cash payment as part of a well-conceived Net Worth Restoration Plan. Delegated authority limits the approval levels.

d. Charge to Reserve

A charge to reserve is section 216 assistance (non-cash). A credit union implements a charge to reserves by transferring funds from the regular reserve account to undivided earnings. A charge to reserves is appropriate for credit unions incurring a deficit in undivided earnings but still have regular reserves. A credit union must deplete its undivided earnings and other reserves before it can charge its regular reserve. A credit union does not need approval if the charge to reserves will not reduce the credit union's net worth classification to below "well capitalized." A charge to reserves resulting in a net worth classification below "well capitalized" requires the Regional Director's approval, and, if state-chartered, the appropriate State official's approval. Replenishment of a charge to reserves is discretionary but must conform to requirements of PCA.

e. Indemnification

Indemnification is section 208 assistance. Indemnification involves the potential use of NCUSIF funds to restore a person incurring a loss, in whole or in part, by payment, guarantee, repair, or replacement. Indemnification should only be considered in rare situations to initiate a merger or purchase and assumption in order to reduce potential loss exposure to the continuing credit union where there is a perceived or real threat of litigation regarding the affairs of the liquidating/merging credit union and the bond claim is inadequate to cover potential losses. AMAC must review and comment on indemnification agreements. Indemnification agreements must have the concurrence of General Counsel and the Office of Examination and Insurance.

f. NCUSIF Guaranteed Line of Credit

A guaranteed line of credit is section 208 assistance (non-cash). The NCUSIF will guarantee the line of credit at the corporate credit union or a suitable credit provider. A guaranteed line of credit is appropriate for credit unions with liquidity needs where the corporate credit union or other credit provider refuses to extend or increase the credit union's line-of-credit. Credit unions receiving a guaranteed line of credit must be insolvent or "in danger of closing". NCUSIF loan

guarantees are limited to a total term of two years. Delegated authority limits the approval level for NCUSIF loan guarantees.

g. NCUSIF Loan

An NCUSIF loan is section 208 assistance (cash). An NCUSIF loan involves the use of NCUSIF funds for a loan secured in whole or in part by assets of an open or closed credit union. The loan may be in subordination to the rights of members. The purpose of the loan is to improve liquidity and provide a sufficient spread to improve the credit union's net worth and long-term viability. Loans are repaid in full. Appropriate limitations must be placed upon the use of the NCUSIF funds to ensure adequate liquidity is available upon maturity. Delegated authority limits the approval levels.

h. NCUSIF Share Deposit

An NCUSIF share deposit is section 208 assistance (cash). A share deposit involves the deposit of NCUSIF funds into the credit union. The purpose of the share deposit is to improve liquidity and provide a sufficient spread to improve the credit union's net worth and long-term viability. Deposits are to be repaid in full. Appropriate limitations must be placed upon the use of the NCUSIF funds to ensure adequate liquidity is available upon maturity. Delegated authority limits the approval levels.

i. NCUSIF Subordinated Note

Subordinated note assistance is section 208 assistance (cash). A subordinated note involves the use of NCUSIF funds to establish a subordinated liability with repayment terms. The repayment terms may include "Incentive Forgiveness" by meeting pre-established goals tied to specific, measurable financial and/or operational performance benchmarks. "Incentive Forgiveness" will not be repaid to comply with FASB 116. A capital note is appropriate when a cash infusion by the NCUSIF, at minimal cost or no cost to the credit union, is necessary to restore profitability and to achieve minimum net worth requirements for a potentially viable, self-sustained institution. Limits must be established on the use of the funds consistent with the recipient's liquidity, the repayment terms of the note (if applicable), and ALM position. Delegated authority limits the approval levels.

Regional Directors have authority to void any "Incentive Forgiveness" repayment provisions in place as of December 31, 2000, if the provisions have an adverse effect on a credit union's net worth. The Regional Director will notify, in writing, the Director of E&I within 10 days of the reasons for voiding the repayment.

j. Prior Undivided Earnings Deficit (PUED) – NCUSIF Guaranteed Account

A PUED -NCUSIF guaranteed account is section 208 assistance (non-cash). The credit union with a deficit in undivided earnings transfers the negative balance to the PUED-NCUSIF guarantee account. A guaranteed PUED is appropriate for insolvent credit unions with a realistic opportunity to recover or rebuild capital without other special assistance (i.e. bond claim recovery) and applicable to "new" credit unions with a deficit paying a dividend according to its approved Revised Business Plan. This type of assistance for a "new" credit union must not exceed 24 months. Delegated authority limits the approval levels for PUED-NCUSIF Guaranteed Accounts.

k. Reduction in Earnings Transfer

Reductions in earnings transfer is permitted under section 216(e)(2)(A) of the FCU Act and section 702.201(b) of NCUA Rules and Regulations. These provisions allow a credit union, with NCUA Board approval, to reduce its quarterly transfer of earnings to an amount less than the statutory minimum that is the equivalent of 1/10th percent (0.1%) of its total assets. This assistance is commonly utilized simultaneously with other special assistance. By regulation, the reduction in earnings must:

- Be necessary to avoid a significant redemption of shares; and
- Further the purpose of NCUA Rules and Regulations Part 702.

Earnings transfer requirements for "new" credit unions, which are not subject to a minimum amount, are established within the approved initial or revised business plan until the credit union is "moderately capitalized."

Regional Directors have delegated authority to approve reductions in earnings transfers provided they meet the requirements set forth by the regulation.

A reduction in earnings transfer is subject to review and revocation no less frequently than quarterly.

l. Temporary Dividends

Temporary dividends are section 208 assistance (non-cash). Credit unions with deficits in undivided earnings shall not disburse dividends without the concurrence of NCUA. Credit unions receiving temporary dividend approval will transfer the deficit to a PUED – NCUSIF guaranteed account. Temporary dividends are utilized to provide time to identify and correct root problems, make necessary management changes, provide clean financial statements, or prepare the credit union for merger, purchase and assumption, or liquidation. Dividends must be

reasonable compared to the local market and liquidity position. Documentation must contain enough information to show that the dividend payment is beneficial to both the credit union and the NCUSIF. Temporary dividends are limited to 2 quarters or 6 months. Delegated authority limits the approval levels.

Chapter 2

How and when to Obtain Concurrence for Special Assistance

1. What is the purpose of this chapter?

Consistent with the requirements of Chapter 1, this chapter establishes procedures for processing requests for special assistance and actions requiring concurrence from the Director of Examination and Insurance (E&I) or approval from the NCUA Board. Regional directors maintain procedures for processing special assistance under delegated authority.

2. What are the NCUA staff responsibilities?

Delegated authority and regional instructions will often dictate ultimate approval authority and staff responsibilities for individual types of actions. The following responsibilities apply more generally to most types of assistance requiring concurrence.

a. Regional Staff

- Develop concurrence packages according to this manual.
- Develop and maintain a proper administrative record.
- Coordinate communications with credit unions.
- Monitor and report all special assistance cases monthly.

b. Regional Director (RD)

- Ensure staff prepares complete concurrence packages justifying the request.
- Inform the Director of E&I of anticipated concurrence requests.
- Confer and consult with State Supervisory Authority (SSA) on requests for FISCUs.

- Inform the Director of E&I of any failing workout plans in special assistance cases.
 - Provide copies to the Director of E&I of all special assistance agreements approved under delegated authority.
- c. **Loss/Risk Analysis Officer**
- Coordinate processing of concurrence packages.
 - Verify concurrence packages comply with the policies and procedures in this directive.
 - Perform reviews of concurrence requests, provide recommendations to the region, and recommend action by the Director of E&I.
 - Prepare applicable correspondence to the region or other requesting parties.
 - Prepare quarterly summary of all special assistance cases.
- d. **Director, Division of Risk Management**
- Supervise the concurrence process.
 - Oversee compliance with this manual.
 - Maintain this manual.
- e. **Director of E&I**
- Approve or deny concurrence requests.
 - Inform the NCUA Board of all actions taken under delegated authority as required under SUP 3.
- f. **Asset Management and Assistance Center**
- Review and comment on all proposed asset guarantee agreements.
 - Review all requests for payment on asset guarantees.
 - Prepare requests for payment from the NCUSIF for asset guarantees.

3. What are the types and appropriate uses of special assistance?

This section expands on the types of assistance approved by the NCUA Board in Chapter 1 and addresses when a particular type of assistance is appropriate. Certain types of assistance are subject to limitations contained in the NCUA Delegations of Authority. See the Appendix of this chapter for the applicable delegations.

The Federal Credit Union Act (§216(a)(1), 12 U.S.C. §1790(d)(a)(1)), requires NCUA "to resolve the problems of insured credit unions at the least possible long-term loss to the Fund." For failing credit unions, the region must support that the resolution method selected results in the least possible long-term loss to the NCUSIF, after analyzing all possible resolution alternatives and associated costs. This analysis should include recognition of NCUA expenditures in implementing the resolution method and any material adverse effects on the membership or the economic

conditions and financial stability in the impacted area. The overall cost to the NCUSIF for a failed credit union is affected by such factors as these:

- The difference between total book value of assets and liabilities of the credit union.
- The amount of uninsured shares.
- The quality of the loans (impacted by documentation, collateral, insurance, payment history, interest rates).
- The quality of the investments (impacted by maturity, complexity, marketability).
- The quality of the fixed assets (impacted by building location, condition and local market values).
- The quality of the deposits (impacted by share balance amounts, share structure, certificate rates).
- Outstanding contracts.
- The reliability of the records.
- Contingent claims.
- The potential for recovery against the surety.
- The impact on the market value for assets marketed by AMAC.
- Cost incurred in processing share payouts.

a. Prior Undivided Earnings Deficit (PUED) – NCUSIF Guaranteed Account

When NCUA approves special assistance for a credit union with a deficit in Undivided Earnings, the credit union transfers the deficit to a capital account titled "Prior Undivided Earnings Deficit (PUED) – NCUSIF Guaranteed." This account is most often used in temporary 208 assistance (temporary dividends) and permanent 208 assistance cases.

b. Temporary 208 Assistance – Temporary Dividends

If a deficit in Undivided Earnings (UE) exists before, or is likely to result from paying dividends, the credit union must have NCUA approval to pay dividends on any share type (including share certificates, nonmember shares, etc.).² If Regular Reserves are available, §702.403 of NCUA Rules and Regulations applies.

The projected UE deficit determines the level of delegated authority and concurrence. Delegated authority limits temporary dividends to six months without NCUA Board approval. Based upon the projected UE deficit, regions may request E&I concurrence for each dividend period, or request concurrence for multiple dividend periods.

² Some FISCUs pay interest on non-share deposits pursuant to a contractual obligation and restricting the payment of interest would cause the credit union to breach its deposit contract with the member. By comparison, dividends paid on shares entail no such contractual obligation.

Credit unions authorized to pay temporary dividends are subject to the PCA timeframes for mandatory conservatorship, liquidation, or other corrective action under §702.204(c) and 702.305(c).

Upon approval of temporary 208 assistance (temporary dividends), the credit union transfers the UE deficit to a capital account titled "Prior Undivided Earnings Deficit (PUED) – NCUSIF Guaranteed" account.

c. Special Assistance for mergers, involuntary liquidations, and purchase and assumptions (P&As)

Special assistance for mergers, involuntary liquidations, and P&As can take many forms, such as:

- Asset guarantee
- Asset purchase
- Cash payment
- Indemnification

The Chartering and Field of Membership (FOM) Manual addresses FOM expansion for credit unions involved in mergers and P&As. Concurrence packages should address and document any unusual FOM issues.

Each potentially failing credit union is unique, and the value determined by potential acquirers varies based on how the transaction fits their respective business plans and the value they assign to the assets and liabilities. Allowing the potential acquirers to propose multiple types of transactions (such as whole credit union transaction, P&A with loan pools, branch breakup, etc.) creates greater flexibility for potential acquirers, thereby reducing the long-term cost to the Fund. The region should help a merging or liquidating credit union contact all qualified (adequate financial and management ability) credit unions potentially interested in its assets, shares, or liabilities. The region may assist the credit union in preparing an information package. A good information package can expedite the merger/liquidation process. The information package may include, but is not limited to:

- Financial statements
- Delinquent loan schedules
- Investment schedules
- Fixed asset schedules
- Share schedules

NCUA staff must take appropriate steps to control the disclosure of confidential credit union financial information (NCUA Instruction 4900.02, Guidance on Release of Credit Union Financial Information). Each credit union that receives an information package should provide a Confidentiality Statement (included in

the Instruction). Include an analysis of each proposal received in the assisted merger and P&A concurrence packages.

The selection of the acquirer must be consistent with the requirement that NCUA resolve the problems at the least possible long-term loss to the Fund.

d. NCUSIF Guaranteed Line of Credit (LOC)

NCUA may grant an NCUSIF guaranteed line of credit (LOC) in cooperation with a third-party credit provider, such as a corporate credit union or bank, if a credit union has a current or imminent liquidity concern and the credit provider refuses to extend credit without a guarantee. The credit provider must secure a properly recorded first position security interest on the credit union's property and assets within 30 days of receiving an NCUSIF Guaranteed LOC.

The requesting credit union must meet the requirements for special assistance as defined in the NCUA Board Special Assistance Program (Chapter 1) to receive an NCUSIF guaranteed LOC.

Typically, an NCUSIF guarantee is granted to a corporate credit union since they are the primary correspondent for most credit unions. The NCUSIF guarantee transfers all credit risk of the LOC from the credit provider to the NCUSIF. The credit provider should charge an interest rate reflecting a reasonable margin over its cost of funds sufficient to cover administrative costs. E&I will negotiate the rate within the applicable delegation of authority. In the rare instance where a credit provider refuses to accept the NCUSIF guarantee agreement, or cannot fund the requested LOC, the region should instruct the credit union to apply for other NCUSIF cash assistance (e.g. NCUSIF deposit or loan).

The maturity or term of an NCUSIF guaranteed LOC should be as short as practical; generally less than one year. The term should provide enough time for the credit union to resolve its liquidity problems or more accurately determine future liquidity needs. The NCUA Board must approve requests that extend more than two years and/or amounts greater than \$5 million.

The amount of the NCUSIF guaranteed LOC should be tied to anticipated funding needs and must be justified. The amount requested should normally not exceed the statutory borrowing limit.³

(b)(7)(E) (b)(8)

The region must contact E&I before the maturity date with their plans for an expiring NCUSIF guaranteed LOC. Should there be a need to continue the guarantee, the region initiates the action to extend the maturity date using the

³ A direct loan from the NCUSIF (NCUSIF Loan or NCUSIF Guaranteed LOC) can exceed the statutory borrowing limit.

same procedures for processing a new NCUSIF guaranteed LOC. The region also needs to notify E&I of NCUSIF guaranteed LOC cancellations or other terminations. E&I will then provide notice to the credit provider.

In an emergency, the RD may initiate an NCUSIF guarantee via e-mail or phone call to the Director of Risk Management. The Division of Risk Management can expedite the approval process using the information provided and usually informs the region of approval or denial the same day. Risk Management staff prepares the guarantee agreements once the terms of the LOC are arranged. The region sends the required concurrence request documents to E&I to complete the process for emergency requests by the close of the following business day.

e. NCUSIF Loan and NCUSIF Deposit

NCUA may grant an NCUSIF loan or NCUSIF deposit to provide liquidity and/or enhanced earnings ability to an eligible credit union.

The request for an NCUSIF loan or NCUSIF deposit must include:

- An analysis of how the credit union will use the funds.
- Any limitations on the credit union's use of the funds (normally in the LUA).
- The proposed interest/dividend rate the credit union will pay to the NCUSIF for the funds.
- An analysis supporting the proposed rate the credit union will pay.
- The credit union's liquidity plan for repayment.

f. Asset Guarantees

NCUA may consider special assistance in the form of an asset guarantee for:

- Accounts receivable
- Investments
- Collection problem loans
- Delinquent loans
- Real estate loans
- Bond claims
- Other assets where the market value is not readily determinable

Asset guarantees will only be used in rare situations and normally for short periods. The amount of the guarantee must be the minimum practical amount. Asset guarantees have an impact upon the NCUSIF's available asset ratio and could limit the NCUSIF's ability to pay dividends.

NCUA may grant an asset guarantee when the loan portfolio cannot be sold for a price that allows a par share distribution for an involuntary liquidation of a solvent

credit union. Asset guarantees are appropriate when the market value of the asset is questionable and time is of the essence (loan servicing, large operating losses, etc.). Normally, the pool of assets subject to an asset guarantee request can be separated and retained by NCUA in a P&A or merger, thus avoiding the need for a guarantee.

Before requesting an asset guarantee, the region (or credit union) should attempt to invite at least 5 qualified credit unions potentially interested in the assets, shares, and liabilities to perform due diligence. If less than 5 credit unions are contacted, the region should explain the reasons in the Regional Summary. The receipt of proposals placing the value of the assets near or below the liquidation value provides initial support for considering an asset guarantee. The loan valuation worksheet provided by AMAC (included in the Appendix) or a similar document must be utilized to substantiate the loan liquidation value.

Although the value of guaranteed assets may be questionable, a reasonable market price must be provided. The receipt of proposals to purchase the asset(s) without a guarantee is a good indicator of the market value. AMAC can perform a market analysis of the assets. E&I analyzes this information to determine if the NCUSIF can realize tangible benefit by using a guarantee. When recommending an asset guarantee, the concurrence package must show that the guarantee results in less cost to the NCUSIF.

Before executing a guarantee agreement, the guarantee recipient's ability to carry out the contract must be analyzed. A credit union that receives a loan guarantee must have a history of adequate collections and strong collection policies. The region must address any past history with NCUSIF asset guarantees.

The RD must request AMAC's review of all proposed asset guarantee agreements. AMAC is also responsible for:

- Reviewing requests for payment on guarantees.
- Preparing requests for payment on guarantees from the NCUSIF using procedures outlined in Section 9 of this Chapter. (The request must include an analysis of the guaranteed assets they propose the NCUSIF to purchase.)
- Monitoring all outstanding asset guarantees.

g. Asset Purchase

The NCUSIF may purchase a specific asset of an eligible credit union. An asset purchase must resolve the existing or potential problem. The concurrence package must fully support the benefit of an asset purchase.

The region must request review and comments on proposed asset purchases and the related agreements from the following:

- **AMAC** - purchases of land, buildings, equipment, loans, OREO, and bond claim receipts.
- **Office of Strategic Program Support and Planning** - purchases of investments or negotiable instruments.

The amount of assistance provided for an asset purchase is the greater of:

- Current market value less the actual purchase price.
- Book value less the actual purchase price.

Example: A building purchased for \$1 million, with a current book value of \$950,000 and a current market value (per appraisal) of \$800,000 which the NCUSIF will purchase for \$750,000. The current market value less the purchase price is \$50,000 (\$800,000 - \$750,000) and the book value less the actual purchase price is \$200,000 (\$950,000-\$750,000).

h. Indemnification

Indemnification agreements require concurrence from the Office of General Counsel and E&I. AMAC must also review and comment on the agreement. AMAC monitors indemnification agreements since they normally involve liquidated credit unions.

The concurrence request must document the amount of indemnification and the potential NCUSIF exposure. The indemnification amount is included when calculating total NCUSIF assistance.

i. Permanent Special Assistance for Continued Operations

The NCUA may grant permanent special assistance to a credit union continuing independent operations, if the credit union proves it will be a viable self-sustained institution. Field staff must complete an examination, follow-up examination, insurance review, or supervision contact with an effective date no more than 90 days prior to a request for permanent special assistance. The contact ensures that the proposed workout plan is reasonable and that management is capable.

In addition, NCUA field staff, along with credit union management, ensures that the following nine preliminary requirements are in place before requesting permanent special assistance:

- Viable FOM.
- Capable management.
- Accurate and current books.
- Full and fair financial disclosure.
- Proper written policies and procedures (or realistic plan to put them in place).
- Approved NWRP or RBP (including the impact of assistance repayment).
- Established positive history of financial performance and problem resolution.
- Corrected root problems.
- Developed a system for monitoring on-going performance.

The concurrence package must address the nine requirements listed above. The Appendix to this chapter contains a sample table of contents for a permanent assistance package.

j. NCUSIF Subordinated Note

NCUA may use an NCUSIF subordinated note as part of a permanent special assistance workout plan.

The NCUSIF provides cash to the assisted credit union (credit union asset) along with a note (credit union liability) to establish an NCUSIF subordinated note. The concurrence package must include:

- How the credit union plans to use the cash.
- How NCUA will limit the use of the cash (normally included in the LUA).
- When the credit union must repay the note.
- How the credit union plans to repay the note.
- What interest rate the credit union will pay to the NCUSIF for the note (including a supporting analysis that the rate is appropriate).

"Incentive forgiveness" represents the portion of a NCUSIF subordinated note for which NCUA waives repayment. If the recommended repayment terms include "incentive forgiveness", provide the projected amount and support for the forgiveness in the concurrence package. The note/loan agreement must tie "incentive forgiveness" provisions to specific measurable financial and/or operational performance benchmarks. The credit union recognizes and records "incentive forgiveness" as income and is a loss to the NCUSIF.

If NCUA determines that a credit union is no longer in danger of closing prior to the expiration of the original assistance agreement, the credit union must repay the note.

4. How are requests for assistance processed?

Credit unions request special assistance with a letter addressed to the RD. The

(b)(7)(E) (b)(8)

NCUA processes the request according to who must provide the approval, which is based on the amount of special assistance. The amount of special assistance is computed as follows:

- For permanent special assistance, the amount of assistance is the total amount of cash and non-cash assistance.
- For temporary special assistance (temporary dividends) the amount of assistance is based on the estimated/anticipated Undivided Earnings deficit.

(b)(7)(E) (b)(8)

5. What documents are required for most concurrence items?

While the documentation required may vary depending upon the type of assistance requested, the following documents are generally required for all concurrence requests.

a. Concurrence memorandum

The RD signs concurrence memorandums for all concurrence requests. Concurrence memorandums should include the following:

- Concurrence action requested (type and amount of assistance).
- Anticipated amount of the Undivided Earnings deficit.
- Expiration date of the assistance requested (if applicable).
- Anticipated repayment/amortization date (if applicable).
- Anticipated date and type of NCUA Board action (if applicable).
- Signature blocks for concurring office(s).

b. Credit union request letter

Credit unions request special assistance by letter addressed to the RD. The letter should include the following:

- Type of assistance requested.
- Amount of assistance requested.
- Term of assistance.
- Dividend rates, total dividend amount, frequency of payment, and dividend rate comparison with local market (temporary dividend).
- Signature of appropriate official.

c. Examination report(s)

Include the pertinent sections of the examination reports (examinations, follow-up examinations, insurance reviews, and supervision contacts) supporting the administrative record. The examination reports supporting the administrative record are useful to General Counsel. If the request does not require General Counsel concurrence, the concurrence package can reference the pertinent sections of examination reports that have been uploaded and E&I will access the reports.

d. Financial statements

Provide current financial statements. The financial statements should include appropriate supporting schedules (for example: shares by type, loans by type,

investment schedules, etc.) along with a current analysis of the adequacy of the Allowance for Loan and Lease Losses (ALLL) and the process used to evaluate the ALLL. In the case of assisted mergers or P&As, include consolidated financial statements and key ratios.

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e. Historical financial trends

(b)(7)(E) (b)(8)

f. Written agreement

NCUA must document all special assistance using a written agreement with the credit union receiving the assistance. The agreement outlines the terms of the special assistance and can take any of the following forms:

- A proposed LUA that will be put in place with the special assistance.
- A current LUA.
- A Cease and Desist Order.
- A Regional Director Transmittal Letter.

NCUA requires a written agreement for all permanent special assistance to operating credit unions, addressing:

- Conditions of the assistance.
- Performance goals and benchmarks.
- Limitations on the use of cash assistance provided (if applicable).
- Amortization and repayment terms of the assistance (if applicable).
- Notification of ability to publish the document.

g. Net Worth Restoration Plan/Revised Business Plan/Budget

See the *Examiner's Guide* and regional instructions for the recommended content and official approval process for Net Worth Restoration Plans (NWRPs)

and Revised Business Plans (RBPs). The region's analysis of the plan should also be included.

h. Regional summary

The regional summary is a clear, concise, and complete document that justifies the requested special assistance and supports the administrative record.

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9. How do I request payment from the NCUSIF for approved assistance?

Prior to payment from the NCUSIF, the requesting office will need to contact the Office of the Chief Financial Officer (OCFO), Division of Insurance, to determine if a contract/control number is needed as follows:

Description of Transaction	Contract/Control Number Needed
Merger agreement with an asset guarantee (loans or other assets) only	Asset guarantee/loan guarantee number
Merger agreement with both up-front cash assistance and an asset guarantee	Asset guarantee/loan guarantee number
Merger agreement with up-front cash only	Assisted merger control number
Involuntary Liquidation	Involuntary liquidation case number
P&A	Involuntary liquidation case number and purchase and assumption case number

(b)(7)(E) (b)(8)

10. What are the reporting and maintenance requirements for outstanding assistance?

a. Accounting

Credit unions report special assistance on their financial statements following Generally Accepted Accounting Principles (GAAP).

b. Assistance approved under regional director delegation

(b)(7)(E) (b)(8)

(b)(7)(E) (b)(8)

11. References

- Federal Credit Union Act
- Examiner's Guide
- Enforcement Manual
- Board Secretary's Guidelines for Placing an Item on the Board's Agenda
- Chartering and FOM Manual
- NCUA Instruction 4900.2 – Guidance on Release of Credit Union Financial Information

Sample Table of Contents – Temporary Dividend

TABLE OF CONTENTS XXX CREDIT UNION CHARTER/INSURANCE CERTIFICATE NUMBER 00000 MONTH YEAR

TAB	CONTENTS
1	Office of Examination and Insurance Routing and Transmittal Slip (Sup 3.doc)
2	Concurrence memorandum to Director, Office of Examination and Insurance (EI concur.doc)
3	Regional Summary (Regional summary.doc)
4	Credit Union Request (request letter.tif)
5	Proposed LUA and Letter to Credit Union (draft LUA.doc)
6	Current Letter of Understanding and Agreement signed Month Day, Year with Status (current LUA.doc)
7	Financial Statements (statements.tif)
8	SATEX (satex.xls)
9	Solvency Evaluation (solvency.xls)
10	U/E reconciliation (deficit.xls)
11	Rate Survey (survey.tif)
12	Projected Financial Statements (projections.xls)

Sample Table of Contents – Permanent Assistance

TABLE OF CONTENTS XXX CREDIT UNION CHARTER/INSURANCE CERTIFICATE NUMBER 00000 Month Year

TAB	CONTENTS
1	Sup 3 Submission (sup-3.doc)
2	Concurrence Memorandum to E&I (EI concur.doc)
3	Regional Summary (Regional Summary.doc)
4	Proposed LUA (Draft LUA.doc)
5	Net Worth Restoration Plan (NWRP.zip)
6	Credit Union Request (Request.tif)
7	Financial Statements (statements.tif)
8	Supervision Chronology (Supervision Chronology.doc)
9	SATEX as of Month Day, Year with Status Report (satex.xls & status.doc)
10	Analysis of Alternatives (alternatives.xls)
11	AMAC Loan Valuation Worksheet (AMAC loan valuation.xls)
12	Solvency Evaluation (PAS) (Solvency.xls)
13	Current LUA with status (current LUA.doc)
14	Follow-up Examination (Follow-up.zip)

Sample Table of Contents – Purchase and Assumption

TABLE OF CONTENTS XXX CREDIT UNION CHARTER/INSURANCE CERTIFICATE NUMBER 00000 Month Year

TAB CONTENTS

- 1 Sup 3 Submission (sup-3.doc)
- 2 Concurrence Memorandum to General Counsel (GC concur.doc)
- 3 Concurrence Memorandum to E&I (EI concur.doc)
- 4 Regional Summary (Regional Summary.doc)
- 5 Supervision Chronology (Supervision Chronology.doc)
- 6 SATEX as of Month Day, Year with Status Report (satex.xls & status.doc)
- 7 Pro-forma SATEX (proforma.xls)
- 8 Calculation of Liquidation Costs (Liquidation Cost.xls)
- 9 AMAC Loan Valuation Worksheet (AMAC loan valuation.xls)
- 10 Solvency Evaluation (PAS) (Solvency.xls)
- 11 Analysis of Competing Proposals (bid1.tif, bidreview.xls)
- 12 Consolidated Financial Statements and Key Ratios (consol FS.xls)
- 13 Follow-up Examination (Follow-up.zip)
- 14 Draft P&A Agreement (P&A Agreement.doc)

Chapter 3

Postmortems

1. What is the purpose of this chapter?

This chapter provides guidance on reviews of failed credit unions consisting of postmortem reports, abridged postmortem reports, and the credit union failure questionnaire.

2. What is a postmortem?

A postmortem is an educational examination and analysis of a failed credit union, most often one that caused a significant loss to the NCUSIF. The purpose of the postmortem is to:

- Determine and analyze the types of problems that result in losses to the NCUSIF.
- Learn how to better identify and address problems before they result in losses to the NCUSIF.
- Assess the strengths and weaknesses of NCUA's various risk management policies and programs.
- Translate the results into recommendations to improve NCUA's systems and training.

3. When is a postmortem prepared?

A postmortem analysis and summary is required on any credit union causing a loss to the NCUSIF of \$1 million or more. The FCU Act requires the NCUA Inspector General to perform a review when the loss both exceeds \$10 million and exceeds 10 percent of the total credit union assets.

4. Who is responsible for postmortem preparation?

Either the respective region or the Division of Risk Management (DRM) prepares the postmortem, depending on the size of the loss. The DRM will maintain a postmortem tracking report to monitor compliance with this policy and will annually distribute the tracking report.

a. \$1 Million to \$2 Million Loss

The respective region prepares a postmortem for any credit union causing the NCUSIF a net loss of \$1 million through \$2 million. An RD may establish a lower threshold for quality control purposes. RDs may require a postmortem for any failed credit union if they deem it necessary to alert staff to specific problems.

Staff not involved in the supervision of the failed credit union will prepare the postmortem. Assigned staff must be free from apparent conflicts of interest or possible lack of objectivity.

The region will forward a draft copy of the postmortem to the Office of Examination and Insurance (E&I) and the Office of General Counsel (GC) for comment. (b)(7)(E) (b)(8) □

b. Loss \$2 Million to \$10 Million

E&I will prepare postmortems for all cases where net losses are from \$2 million to \$10 million. E&I may perform postmortems on selected cases that caused losses of less than \$2 million at the discretion of the Director of E&I.

E&I will forward a draft copy of the postmortem to the respective region for comment. (b)(7)(E) (b)(8) □

c. Loss over \$10 Million

The IG will prepare postmortems for all cases where net losses exceed \$10 million. IG may perform postmortems on selected cases that caused losses of less than \$10 million at the discretion of the IG.

(b)(7)(E) (b)(8)