7535-01-U

NATIONAL CREDIT UNION ADMINISTRATION

[NCUA-2021-0038**]**

Policy for Setting the Normal Operating Level

AGENCY: National Credit Union Administration (NCUA).

ACTION: Notice; request for comment.

SUMMARY: The NCUA Board (Board) is requesting public comments on the policy to set the National Credit Union Share Insurance Fund (Insurance Fund) Normal Operating Level.

DATES: Comments must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

ADDRESSES: You may submit comments by any one of the following methods **(Please send comments by one method only)**:

- Federal eRulemaking Portal: Follow the instructions for submitting comments for NCUA-2021-0038.
- Fax: (703) 518-6319. Include "[Your name]—Comments on Policy for Setting the Normal Operating Level" in the subject line.

- Mail: Address to Melane Conyers-Ausbrooks, Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314-3428.
- Hand Delivery/Courier: Same as mailing address.

Public Inspection: You may view all public comments as submitted on the Federal eRulemaking Portal, except for those we cannot post for technical reasons. The NCUA will not edit or remove any identifying or contact information from the public comments submitted. Due to social distancing guidelines, the usual opportunity to inspect paper copies of comments in the NCUA's law library is not currently available. After social distancing measures are relaxed, visitors may make an appointment to review paper copies by calling (703) 518-6540 or e-mailing OGCMail@ncua.gov.

FOR FURTHER INFORMATION CONTACT: Russell Moore or Amy Ward, Risk Analysis Officers, Office of Examination and Insurance, National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314 or telephone: (703) 518-6383 or (703) 819-1770.

SUPPLEMENTARY INFORMATION

I. Background

On September 28, 2017, the Board approved the following actions:[1]

[1] 82 FR 42298 (Oct. 4, 2017).

- Closing the Temporary Corporate Credit Union Stabilization Fund (Stabilization Fund) and distributing its funds, property, and other assets and liabilities to the Insurance Fund, effective October 1, 2017.
- Setting the Normal Operating Level of the Insurance Fund to 1.39 percent, effective September 28, 2017.
- Adopting the policy for setting the Normal Operating Level, as outlined below.

Policy for Setting the Normal Operating Level

The policy for setting the Normal Operating Level adopted in 2017 established a periodic review of the equity needs of the Insurance Fund, the results of which are to be communicated to stakeholders.[2] At least annually, NCUA staff will review the level at which the NOL is set and report this information to the Board. Board action is only necessary when a change in the NOL is determined to be warranted. The policy establishes that any change to the Normal Operating Level of more than one basis point[3] shall be made only after a public announcement of the proposed adjustment and opportunity for comment. Further, in soliciting comment, the NCUA will issue a public report, including data supporting the proposal. The policy establishes the following objectives that the Board will seek to satisfy when setting the Normal Operating Level:

[2] As noted, the Board adopted this policy for setting the Normal Operating Level in 2017. The Board emphasizes that, as a general statement of the NCUA's policy regarding setting the Normal Operating Level, the Board is not required to follow the notice-and-comment rulemaking process when revising this policy. *See* 5 U.S.C. 553(b)(3)(a). Nevertheless, the Board is voluntarily soliciting public input on this policy.

[3] One basis point is one hundredth of one percent.

- Retain public confidence in federal share insurance;
- Prevent impairment of the one percent contributed capital deposit;[4] and
- Ensure the Insurance Fund can withstand a moderate recession without the equity ratio declining below 1.20 percent over a five-year period.

The current economic landscape and pending resolution of the obligations associated with the corporate credit union asset management estates and NCUA Guaranteed Notes (NGN) Program discussed later in this document warrant that the NCUA re-evaluate the current Normal Operating Level policy.

II. Legal Authority

Per the Federal Credit Union Act (Act), the Normal Operating Level is an equity ratio set by the Board and may not be less than 1.20 percent and not more than 1.50 percent.[5] The Board has historically set the Normal Operating Level as the target equity ratio for the Insurance Fund.

The Insurance Fund's calendar year-end equity ratio is part of the statutory basis to determine whether the NCUA must make a distribution to insured credit unions.[6] The Act states

[4] Federally insured credit unions are required to maintain a deposit equal to one percent of their insured shares with the Insurance Fund. 12 U.S.C. 1782(c)(1)(A)(i).

[5] 12 U.S.C. 1782(h)(4).

[6] The equity ratio is also part of the statutory basis for determining whether a premium or Insurance Fund restoration plan is necessary.

"the Board shall effect a pro rata distribution to insured credit unions after each calendar year if, as of the end of that calendar year –

- Any loans to the Fund from the Federal Government, and any interest on those loans, have been repaid;
- The Fund's equity ratio exceeds the Normal Operating Level; and
- The Fund's available assets ratio exceeds 1.0 percent."[7]

The provisions of the Act are implemented at 12 CFR part 741 of the NCUA's regulations.

III. Current Normal Operating Level Methodology and Process

To implement the current approved policy, the NCUA developed a calculation based on projections related to the following factors:

- The modeled performance of the Insurance Fund over a five-year period, assuming a moderate recession. The stress scenario entails estimating three primary drivers of outcomes: insurance losses, insured share growth, and yield on investments. The NCUA's analysis is based on the Federal Reserve's adverse economic scenario. However, the Federal Reserve did not publish an adverse scenario in 2020 or 2021. This necessitates the NCUA develop an adverse scenario based on the Federal Reserve's baseline and severely adverse scenarios.

[7] 12 U.S.C. 1782(c)(3). This section is also subject to 12 U.S.C. 1790e(e).

- The modeled potential decline in value of the Insurance Fund's claims on the corporate asset management estates in a moderate recession; and
- The projected equity ratio decline through the end of the following year without an economic downturn.

As noted, the current economic landscape and pending events related to the corporate asset management estates and NGN Program warrant a re-evaluation of the current Normal Operating Level policy. The current policy objectives include ensuring the Insurance Fund can withstand a moderate recession without the equity ratio declining below 1.2 percent over a five-year period. The economic conditions posed by the pandemic, including industry-wide, unprecedented share growth resulted in an equity ratio of 1.26 percent as of December 31, 2020. These issues have forced the NCUA to consider the ongoing feasibility of using a moderate recession and a five-year performance period as the basis for stressing the equity needs of the Insurance Fund.

Additionally, the asset management estates of the five failed corporate credit unions support the NGN program created as part of the Corporate System Resolution. The last of the NGNs is scheduled to mature on June 12, 2021. The amount of time needed after the last NGN matures to fully liquidate all the assets and satisfy all the liabilities of the corporate asset management estates will depend on market factors and ongoing litigation. The risk associated with the Insurance Fund's claims on, and obligations related to the corporate asset management estates will decline and end as the estates are wound down and closed. More information regarding the

NGN program and the Corporate System Resolution may be found on the NCUA's public website.[8]

Finally, the projected equity ratio decline through the end of the following year, assuming economic stability and normal growth, was originally devised as a backstop to ensure the Insurance Fund could stay above 1.20 percent under a moderate recession during the remaining life of the NGNs. With the upcoming maturity of the NGNs and pending conclusion of the corporate asset management estates, this factor may not be necessary going forward.

IV. Request for Comment

The Board seeks comments on the policy and approach for setting the Normal Operating Level of the Insurance Fund. Commenters are also encouraged to discuss any other relevant issues they believe the Board should consider. In particular, the Board is interested in comments addressing the following questions:

- Should a moderate recession be the basis for evaluating the Insurance Fund performance during an economic downturn, or should the NCUA change the policy to consider a severe recession?
- What data source(s) should the NCUA use for determining the characteristics of a potential moderate or severe recession - the Federal Reserve scenario, an independent source, or the NCUA's judgment?

[8] https://www.ncua.gov/support-services

- Should the NCUA continue modeling the performance of the Insurance Fund over a five-year period or a longer or shorter period?
- How should the NCUA utilize the modeled potential decline in value of the Insurance Fund's claims on the corporate asset management estates going forward until the estates are fully resolved?
- Should the NCUA continue to incorporate in the Normal Operating Level analysis the projected equity ratio decline through the end of the following year without an economic downturn? Should this period be longer or short, or not factored into the analysis at all.
- Given forecasting uncertainties and timing challenges, would it be reasonable for the NCUA to change the requirement to request public comment only if the Normal Operating Level were to change by a larger amount than just one basis point?
- Should the Normal Operating Level be re-evaluated in the midst of an economic downturn or should it be left unchanged until the onset of an economic recovery?
- Should the Normal Operative Level be re-evaluated on qualitative factors based on the COVID-19 pandemic?
- Is there any other information that the NCUA Board should consider when setting the NOL?

Commenters are encouraged to provide the specific basis for their comments and, to the extent feasible, documentation to support any recommendations. The Board will consider the comments, and if appropriate, issue a revised policy and publish it in the Federal Register. Should the NCUA implement any changes, the earliest they would take effect is the end of 2021.

By the National Credit Union Administration Board on May __, 2021.

Melane Conyers-Ausbrooks

Secretary of the Board