



volunteer  
corporate

2008

financial  
analysis



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## introduction

An integral part of a credit union's investment policies, procedures and practices is the analysis of all institutions in which it has invested its surplus funds—including corporate credit unions. Part 703 of the National Credit Union Administration's (NCUA) Rules and Regulations states,

*“A Federal credit union must conduct and document a credit analysis on an investment and the issuing entity before purchasing it, except for investments issued or fully guaranteed as to principal and interest by the U.S. government or its agencies, enterprises, or corporations or fully insured (including accumulated interest) by the National Credit Union Administration or the Federal Deposit Insurance Corporation. A Federal credit union must update this analysis at least annually for as long as it holds the investment.”*

In its preamble to the regulation, NCUA further clarified its position on the analysis of corporate credit unions.

*“NCUA recognizes that a small credit union may be unable to perform a detailed credit analysis. For a small credit union, investing funds in corporate credit unions is an appropriate risk management alternative to investing in securities. NCUA will not take exception to a small credit union investing all of its surplus funds in a corporate credit union.”*

### ASSETS (in thousands)

December 31,	2008	2007	2006	2005	2004
Cash and Uncollected Cash Items	\$ 59,065	\$ 53,960	\$ 54,464	\$ 39,412	\$ 28,383
U.S. Central Credit Union	660,397	508,686	844,592	715,065	887,926
Government and Agencies, CMOs, REMICs, & Pass-thrus	134,785	63,919	79,525	121,505	139,780
Commercial Paper/Term Fed Funds	-	-	-	-	-
Repurchase Agreements	-	-	19,379	4,769	-
Asset-backed Securities	65,041	8,479	6,554	12,738	17,409
Other Investments	83,116	554,583	20,852	1,502	1,099
<b>Total Investments</b>	<b>943,339</b>	<b>1,135,667</b>	<b>970,902</b>	<b>\$855,579</b>	<b>\$1,046,214</b>
Unrealized Gains and Losses on AFS	(10,928)	(353)	(635)	(436)	(97)
Net Investments	932,411	1,135,314	970,267	\$855,143	\$1,046,117
Demand Loans	3,154	660	5,417	6,096	3,314
Accrued Income	3,158	11,160	5,839	3,062	3,289
Fixed Assets	3,123	2,783	2,848	3,006	2,942
NCUSIF Capitalization Deposit	69	232	230	236	239
All Other Assets	2,082	2,245	2,063	2,095	2,009
<b>TOTAL ASSETS</b>	<b>\$1,003,062</b>	<b>\$1,206,354</b>	<b>\$1,041,128</b>	<b>\$909,050</b>	<b>\$1,086,293</b>

introduction continued

NCUA expects a larger credit union, however, to perform a credit analysis whenever there is credit risk. The uninsured portion of an investment in a corporate credit union presents such risk.

*“A credit union’s membership relationship with its corporate should assist it in evaluating the corporate’s operations and financial condition. A credit union should review the corporate credit union’s earnings performance, capital level, and investment portfolio. A credit union should also be aware of the corporate’s operating level under Part 704 and its exposure to a 300 basis point shift in interest rates.”*

Though NCUA’s investment regulation specifically exempts state-chartered credit unions, most are using the regulation as a guideline in their investment policies, procedures, and practices. Recognizing that the analysis of a corporate credit union, as outlined under Part 703.40(d), can be burdensome and that some information may not be readily available, we are providing you this comprehensive analysis of Volunteer Corporate Credit Union. This analysis addresses the processes outlined in NCUA’s investment regulation and explains the new regulatory requirements of NCUA’s corporate regulations.

## Liabilities and Equity

(in thousands)

December 31,	2008	2007	2006	2005	2004
Accounts Payable	\$ 3,229	\$ 6,055	\$ 4,119	\$ 1,569	\$ 1,912
Uncollected Funds	39,958	34,989	31,372	18,750	16,891
Repurchase Agreements	-	-	19,379	4,769	-
CLF Membership Notes Payable	-	-	-	-	-
<b>Total Liabilities</b>	<b>\$ 43,187</b>	<b>\$ 41,044</b>	<b>\$ 54,870</b>	<b>\$ 25,088</b>	<b>\$ 18,803</b>
Daily Shares	558,968	671,748	655,081	554,293	438,703
Term Shares	338,198	417,151	258,090	257,995	559,309
<b>Total Shares</b>	<b>\$ 897,166</b>	<b>\$1,088,899</b>	<b>\$ 913,171</b>	<b>\$ 812,288</b>	<b>\$ 998,012</b>
Member Capital Shares	51,432	48,370	47,053	46,313	27,820
Paid-in Capital	-	-	-	-	17,000
Reserves and Undivided Earnings	22,205	28,394	26,669	25,797	24,755
Unrealized Gains and Losses on AFS	(10,928)	(353)	(635)	(436)	(97)
<b>Total Capital</b>	<b>\$ 62,709</b>	<b>\$ 76,411</b>	<b>\$ 73,087</b>	<b>\$ 71,674</b>	<b>\$ 69,478</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b><u>\$1,003,062</u></b>	<b><u>\$1,206,354</u></b>	<b><u>\$1,041,128</u></b>	<b><u>\$909,050</u></b>	<b><u>\$1,086,293</u></b>

# capital

## REGULATORY ISSUES

Under the regulatory requirements of Part 704 of the NCUA's Rules and Regulations, corporate credit unions' capital is segregated into two categories. These categories are *Retained Earnings* and *Capital*. The category of *Retained Earnings* is defined as,

*"The total of the corporate credit union's undivided earnings, reserves, and any other appropriations designated by management or regulatory authorities."*

*Capital* is defined as,

*"The sum of a corporate credit union's retained earnings, paid-in capital, and membership capital."*

There are two ratios that corporate credit unions calculate to determine the adequacy of capital and reserving requirements. These are the Capital Ratio and the Retained Earnings Ratio.

The Capital Ratio equals,

*"The corporate credit union's capital divided by its moving daily average net assets,"*

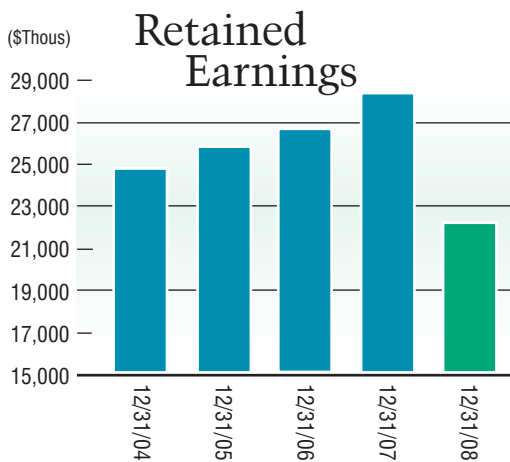
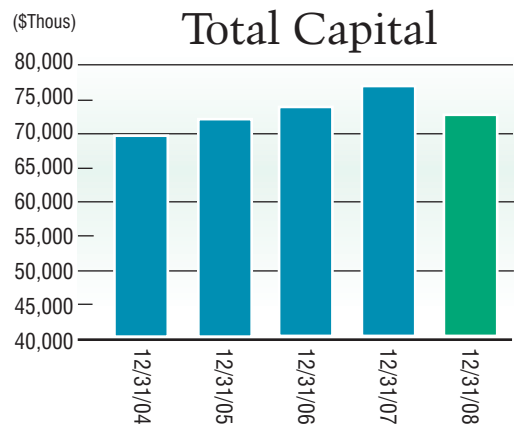
and the Retained Earnings Ratio equals,

*"The corporate credit union's retained earnings divided by its moving daily average net assets."*

NCUA's capital requirements for corporates are fairly straightforward: According to Part 704.3,

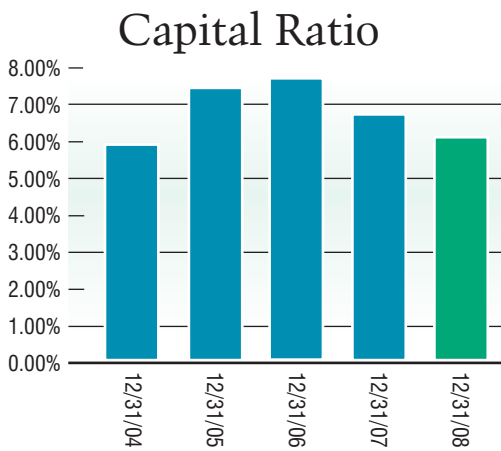
*"A corporate credit union will maintain a minimum capital ratio of 4 percent, except as otherwise provided in this Part. A corporate credit union must calculate its capital ratio at least monthly. A corporate credit union must increase retained earnings if the prior month-end retained earnings ratio is less than 2 percent. Its retained earnings must increase during the current month, by an amount equal to or greater than the*

*monthly earnings retention amount; or during the current and prior two months, by an amount equal to or greater than the quarterly earnings retention amount. Earnings retention amounts are calculated as follows: The monthly earnings retention amount is determined by multiplying the earnings retention factor by the prior month-end moving daily average net assets; and, the quarterly earnings retention amount is determined by multiplying the earnings retention factor by moving daily average net assets for each of the prior three month-ends. The earnings retention factor is determined as follows: If the prior month-end retained earnings ratio is less than 2 percent and the core capital ratio is less than 3 percent, the earnings retention factor is .15 percent per annum; or, if the prior month-end retained earnings ratio is less than 2 percent and the core capital ratio is equal to or greater than 3 percent, the earnings retention factor is .10 percent per annum."*



### RETAINED EARNINGS AND TOTAL CAPITAL

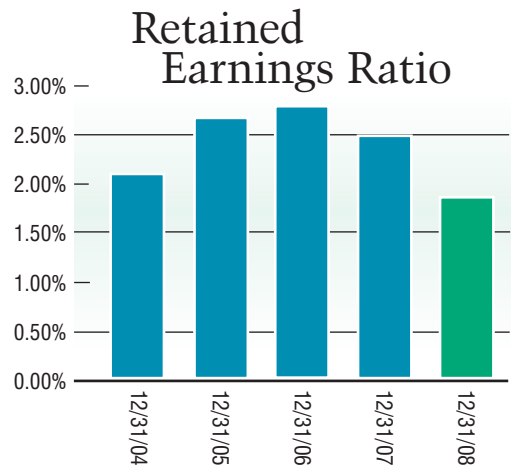
There were two significant occurrences in 2008 that dramatically impacted VolCorp's Retained Earnings and Total Capital. First, VolCorp turned in one of its strongest years in its history. Second, the strong year was inverted to a substantial loss when U.S. Central reported Other-Than-Temporary-Impairment (OTTI) losses that cost VolCorp (and all other corporates) a significant capital impairment. Prior to the U.S. Central Capital impairment (the impairment), VolCorp total retained earnings equaled \$32,901,371; representing an increase of \$4,507,652, or 15.9 percent, over year-end 2007 levels. This increase was due, in large part, to the historically wide spread between Fed Funds and Libor and higher than forecasted assets. However, subsequent to the end of 2008, it was determined that VolCorp's pro-rata share of the impairment was \$10.5 million. VolCorp also booked its share of the NCUSIF impairment at \$153 thousand (which would subsequently be reversed in 2009). After both impairments were booked, VolCorp's earnings for the year inverted from a net gain of \$4.5 million to a loss for 2008 of approximately \$6.2 million. This left VolCorp with a Retained Earnings position at year-end of \$22.2 million. VolCorp did not have any OTTI charges of its own in 2008, therefore, the Retained Earnings position took no additional adjustments as a result of VolCorp's investment portfolio.



Corporate credit unions' balance sheets reflect the liquidity needs and cash flows of its members. Therefore, it is not unusual for a corporate credit union to experience asset fluctuations of 25 percent or more not only from month-to-month but also within periods of less than 30 days. In addition, corporate credit unions' month-end assets are often significantly inflated due to routine payrolls that flow into their member credit unions. As a result, it can be misleading to analyze a corporate credit union's retained earnings and capital ratios using month-end data. NCUA recognized the distortion such fluctuations can cause, and, in its corporate credit union regulations, adopted the concept of using the corporates' moving daily average net assets when calculating the retained earnings and capital ratios.

For the twelve-month period ending December 31, 2008, Volunteer Corporate's moving daily average net assets, (DANA) equaled \$1,191,338,782 compared with \$1,142,290,941 for 2007. This reflects a 4.3 percent growth rate during 2008, a year

in which VolCorp recognized record asset levels in the first quarter. The growth in assets in the first half of 2008 was partly attributable to solid performance of Corporates, highly competitive rates, and plentiful liquidity in the system. Assets remained high in the second half of the year and into 2009 as a result of a flight to quality due to the escalation of market turmoil. Credit Unions saw the steady earnings, competitive rates, excellent performance of VolCorp's securities portfolio, and ample liquidity position and felt comfortable leaving their deposits with VolCorp. These realities lead to the record asset levels and increase in DANA. Retained earnings grew during the year at a rate of 15.9 percent (prior to the impairment) resulting in a retained earnings ratio of 2.76 percent at December 31, 2008, as compared to 2.48 percent in 2007. For the same reasons, the capital ratio also increased from 6.70 percent in 2007 to 7.00 percent at year-end 2008. However, after the impairment was booked, VolCorp's retained earnings and capital ratios at December 31, 2008 were 1.86 percent and 6.10 percent respectively.

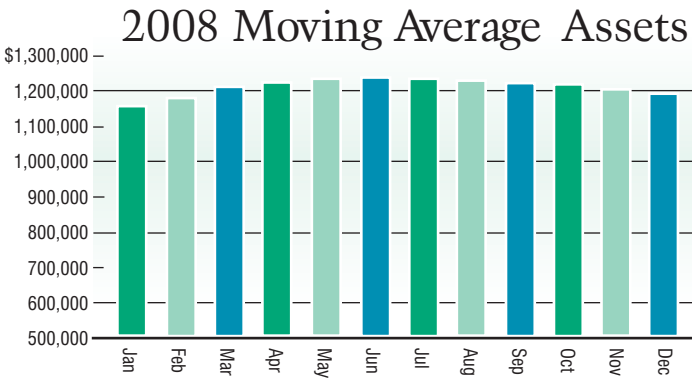
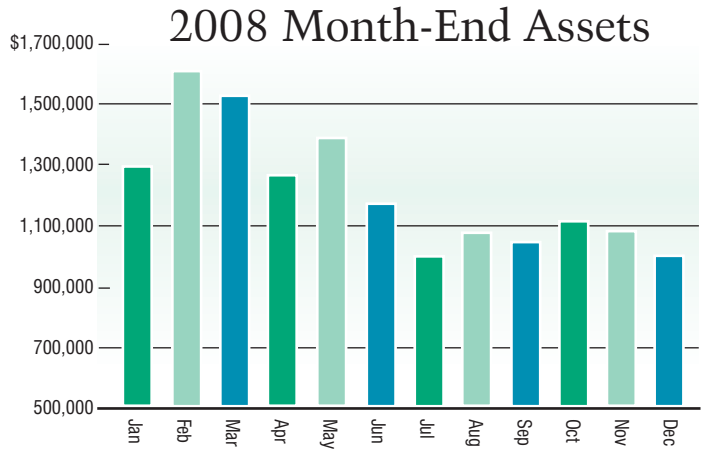


**NET ECONOMIC VALUE (NEV) ANALYSIS**

NEV is the net present value of a corporate's assets and the value of the assets' embedded options, minus the net present value of the corporate's shares and liabilities and the value of the shares' and liabilities' embedded options. A corporate's NEV Ratio is computed by dividing the NEV by the mark-to-market value of assets. NEV and the NEV Ratio are used to measure the inherent risk in a financial institution's balance sheet and as a proxy assessment of the liquidation value of the financial institution under certain interest environments. Under part 704.8(d)(ii) of its Rules and Regulations, the NCUA Board set a minimum base NEV Ratio of 2 percent for all corporate credit unions. In addition, the Board set a minimum NEV Ratio and maximum permissible downward NEV shifts under industry standard +/- 100, 200, and 300 basis point rate shocks. Shocking a corporate's balance sheet means determining the impact on the NEV and the NEV Ratio of an immediate, parallel, and sustained upward and downward shift in market interest rates. The NEV shift is the percent increase and percent decrease of current capital. Current capital is the difference between the mark-to-market value of assets and liabilities at current interest rates. The permissible, downward NEV shift is dependent, in part, upon the level

of authority granted each corporate by the NCUA Board. As a starting point, all corporate credit unions have the authority to operate at Base level. At this level, the permissible negative shift in the corporates' NEV Ratios is 15 percent under a +/- 100, 200, and 300 basis point rate shocks. Each corporate credit union may petition the NCUA Board

to operate under expanded authority. To obtain such authority, the corporate credit union must meet all the requirements of Part 704 of NCUA's Rules and Regulations and fulfill additional capital, management, infrastructure, and asset liability requirements.



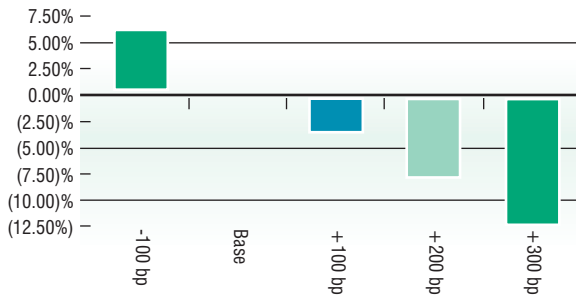
capital continued

In September 1997, Volunteer Corporate’s Board of Directors requested authority to operate at the expanded level termed Base Plus. In November 1997, Volunteer Corporate became the first corporate credit union to receive authority by the NCUA Board to operate above Base level. At Base Plus, the Corporate’s permissible negative NEV shift increased from 15 percent to 20 percent. As of December 31, 2008, the cumulative change in Volunteer Corporate’s NEV is a decrease of \$8,084,038 in an immediate up 300-basis point scenario and an increase of \$3,969,031 in an immediate down 100-basis point scenario. (Given the December 31, 2008 level of interest rates with the Fed Target rate set at 0-25 basis points, a down 300-basis point scenario is non-applicable.) This equates to NEV shifts of negative 12.49 percent and positive 6.13 percent, respectively—well below the maximum 20 percent negative shift permitted by Federal law.

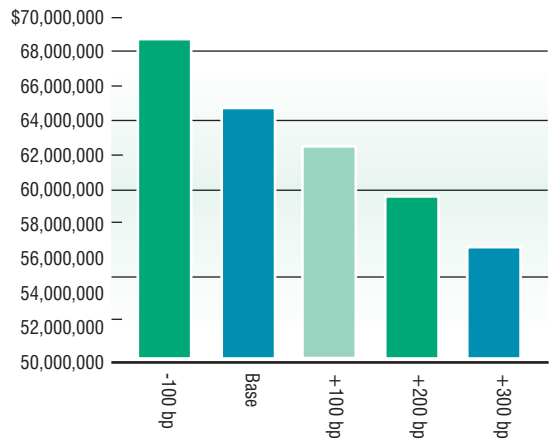
The following table shows the impact on Volunteer Corporate’s Net Economic Value of the various interest rate scenarios:

	(100) bp	Base	100 bp	200 bp	300 bp
NEV (thous.)	\$68,692	\$64,723	\$62,414	\$59,543	\$56,639
ΔNEV (from Base, thous.)	\$3,969	\$0	\$(2,309)	\$(5,179)	\$(8,084)
%ΔNEV (from Base)	6.13%	0.00%	(3.57)%	(8.00)%	(12.49)%

### NEV Shift



### Net Economic Value

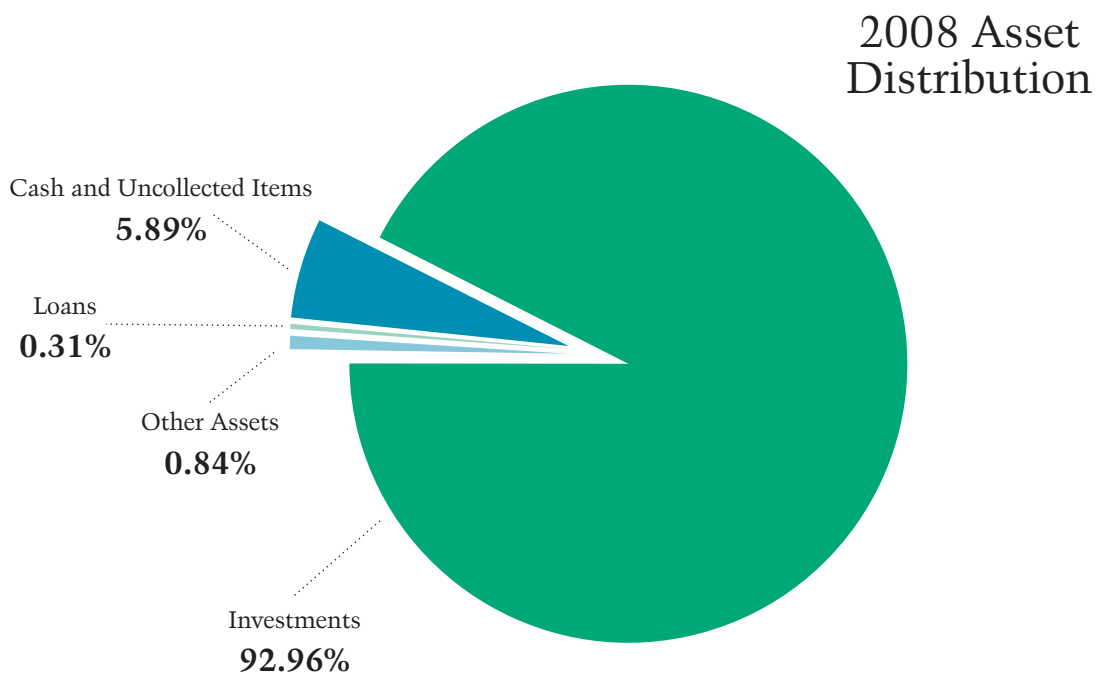


## assets

The quality of a financial institution's assets is one of the most important factors contributing to its financial soundness. In its 1997 study of the credit union movement, the Treasury addressed the quality of the corporate credit unions' assets in general when it said, "Corporate credit unions invest in high-quality assets and thus have limited exposure to credit risk. In general, corporate credit unions' investment portfolios are of very high credit quality." As of December 31, 2008, 99.2 percent of the Corporate's assets consisted of cash and uncollected cash items, loans to member credit unions, and high-quality, low credit-risk investments. Furthermore, as of December 31, 2008, 96% of VolCorp's marketable security holdings were rated AAA and 63% were issued by U.S. Government Agencies. Also, 100% of VolCorp's holdings in U.S. Central fall under the Temporary Corporate Credit Union Share Guarantee Program (TCCUSGP) guaranteeing them through December 31, 2011. Volunteer Corporate monitors the quality of its assets through extensive monthly credit analysis and portfolio modeling and has a qualified third party perform Impairment Analysis on all non-agency securities as needed.

### MEMBER LOANS

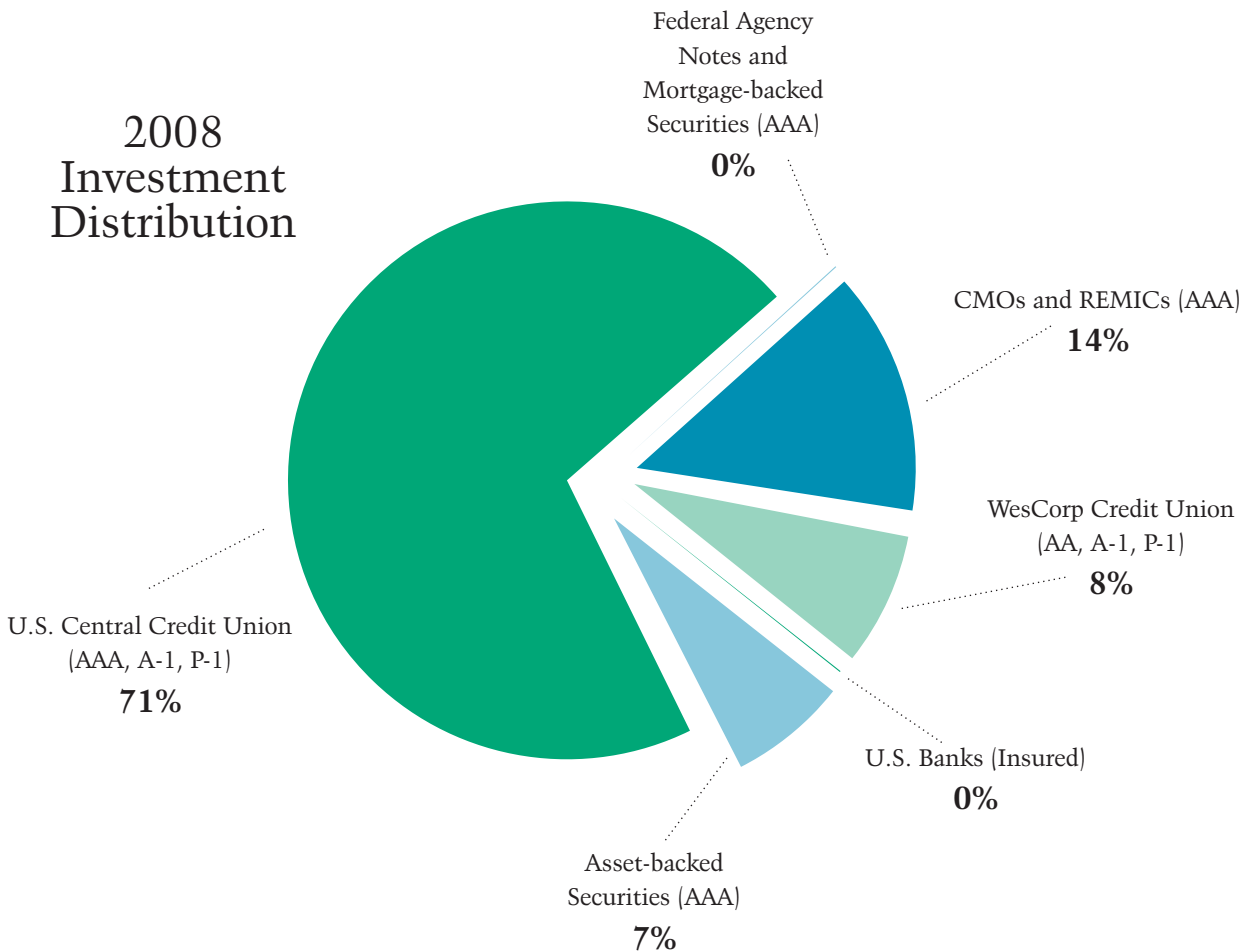
The Corporate has a responsibility to meet the liquidity needs of its membership, while protecting the deposits of its member credit unions. As of December 31, 2008, the Corporate's total outstanding loans and lines of credit to its members equaled only \$3,153,543, approximately 378% more than year-end 2007, but still well below one percent of total assets. However, member credit unions had 193 approved lines established with Volunteer Corporate totaling \$629,872,040. The quality of the loan portfolio is governed by the loan policies established by the Board of Directors and by the procedures followed by management in implementing these policies. All lines are reviewed on a semi-annual basis and detailed financial analyses are performed. From this review, it is determined which credit unions will be monitored on a more frequent basis and which credit unions may need additional attention. Moreover, each line of credit is secured by a general pledge of the borrowing credit union's assets. No loans at Volunteer Corporate are currently delinquent and delinquency is extremely rare. Since its charter, Volunteer Corporate has never charged off a loan to a member credit union.



### INVESTMENTS

When making investment decisions, Volunteer Corporate has always kept a close eye on safety, liquidity, and yield. In order to minimize credit risk, Volunteer Corporate's policies allow funds to be placed only in U.S. Central and other Corporate Credit Unions, U.S. Government securities, federal agency securities or in the top-rated banks and domestically chartered corporations. These policies further limit investments in banks and corporations individually and in aggregate and require extensive analysis and monitoring. The Corporate's approved-institution analysis considers size, capital adequacy, asset quality, management, earnings performance, and liquidity.

As the market turmoil and dislocation that began in 2007 escalated in 2008, VolCorp began to take an even closer look at its portfolio diversification. At the beginning of 2008, VolCorp held only 6.37% of its investments in marketable securities, while over 93% were invested in U.S. Central and WesCorp. By the end of 2008, 21.44% of VolCorp's investment holdings were marketable securities, and as of month-end September 2009, marketable securities comprise 32.67% of VolCorp's investment holdings. Of those securities, 98% of those are AAA rated and 77% are issued or guaranteed by U.S. Government Agencies.



## earnings

Like all other credit unions, Volunteer Corporate is a not-for-profit organization, existing solely for the benefit of its members. The Corporate's policy is to help its members increase their net income by providing cost-effective services and attractive investment yields. Since any profit would come at the expense of its owner/members, it is not the policy of Volunteer Corporate to earn the maximum net income possible. Even so, the corporate must maintain a stable earnings position in order to pay dividends, cover budgeted expenses, develop new services, maintain capital adequacy, and meet statutory reserve requirements. With the market dislocation, and subsequently the impairment at U.S. Central, earnings became all the more paramount in shielding VolCorp members from losses. It is the policy of the Corporate's Board of Directors to not increase earnings by sacrificing the safety of the members' shares through high risk investments or investment practices. As a result, Volunteer Corporate operates on an extremely thin operating margin and can do so only if efficiencies are maximized and expenses are controlled. Net income for 2007 equaled \$1,725,000 for a 14 basis point return on assets. For the year ending December 31, 2008, Volunteer Corporate was able to continue aggressive rate paying strategies and realize \$4,507,652 in net income, maintaining a 38 basis point return on assets prior to the impairment. After booking the impairment, VolCorp yielded a net loss for 2008 of \$6.2 million, all of which was absorbed through retained earnings, protecting member capital.

### Comparative Income

(in thousands)

December 31,	2008	2007	2006	2005	2004
<b>Interest Income:</b>					
U.S. Central	\$33,303	\$51,330	\$35,181	\$24,026	\$19,315
Investment Securities	4,910	4,310	6,125	5,528	2,813
Loans	<u>42</u>	<u>322</u>	<u>872</u>	<u>316</u>	<u>182</u>
<b>Total Interest Income</b>	38,255	55,962	42,178	29,870	22,310
<b>Interest Expense:</b>					
Dividends on Shares	30,391	51,955	38,543	26,002	18,022
Interest on Borrowed Funds	<u>654</u>	<u>276</u>	<u>1,138</u>	<u>981</u>	<u>824</u>
<b>Total Interest Expense</b>	<u>31,045</u>	<u>52,231</u>	<u>39,681</u>	<u>26,983</u>	<u>18,846</u>
<b>Net Interest Income</b>	7,210	3,731	2,497	2,887	3,464
<b>Non-Interest Income:</b>					
Item Processing	3,309	3,249	3,017	2,871	2,783
Gain(Loss) on Securities	-	-	-	51	(31)
Other	<u>1,764</u>	<u>2,312</u>	<u>2,253</u>	<u>1,707</u>	<u>1,286</u>
<b>Total Non-Interest Income</b>	5,073	5,561	5,270	4,629	4,038
<b>Non-Interest Expenses:</b>					
Salaries and Benefits	3,914	3,771	3,260	3,270	3,042
Other	<u>14,558</u>	<u>3,796</u>	<u>3,635</u>	<u>3,204</u>	<u>2,880</u>
<b>Total Non-Interest Expenses</b>	<u>18,472</u>	<u>7,567</u>	<u>6,895</u>	<u>6,474</u>	<u>5,922</u>
<b>Net Contribution to Reserves</b>	<u><u>\$(6,189)</u></u>	<u><u>\$ 1,725</u></u>	<u><u>\$ 872</u></u>	<u><u>\$ 1,042</u></u>	<u><u>\$ 1,580</u></u>

## Liquidity

Volunteer Corporate is the primary depository institution and source of liquidity for the majority of its member credit unions. As such, the corporate has the responsibility of protecting the safety of its members' deposits while providing sufficient liquidity to meet their cash flow needs. To meet this responsibility, Volunteer Corporate maintains sufficient cash and overnight investments to provide for reasonable cash flow demands. The Corporate's liquidity position is monitored daily and adjusted, as necessary, for seasonal and anticipated fluctuations in our members' liquidity needs. By virtue of their membership in Volunteer Corporate, our member credit unions have access to the Central Liquidity Facility (CLF) without having to purchase CLF stock. Acting as an agent member of the CLF, the Corporate can assist its members in meeting their liquidity needs through access to this Federal liquidity center chartered exclusively for credit unions.

## o f f i c e i n f o r m a t i o n

**ADDRESS:**

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[www.volcorpdesign.org](http://www.volcorpdesign.org)

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Main Fax: (615) 232-7999  
Item Processing Fax: (615) 232-7979

**DIRECT-DIAL EXTENSIONS:**

Member Services/Operations/  
Item Processing/ACH . . . 1  
Investments and Finance . . . 2  
Marketing and Business Development . . . 3  
Administration and President's Office . . . 4  
Product Support . . . 5  
Operator . . . 0

**OFFICE HOURS:**

VolCorp is open Monday, Tuesday, Wednesday and Friday from 7:30 a.m. to 4:30 p.m. (Central time). On Thursdays, hours are from 8:30 a.m. to 4:30 p.m. (Central time). Our Member Services Department closes at 4:00 p.m. (Central time) each day. Office closings are coordinated with the Federal Reserve Bank holiday schedule.





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