

Semiannual Report to the Congress

April 1 – September 30, 2015





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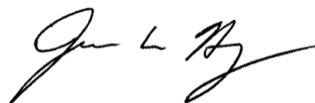
A MESSAGE FROM THE INSPECTOR GENERAL

On behalf of the Office of Inspector General (OIG) of the National Credit Union Administration (NCUA), I am pleased to present our Semiannual Report to the NCUA Board and Congress highlighting our accomplishments and ongoing work for the six-month period ending September 30, 2015. Thanks to the dedication of my staff, the audits, reviews, and investigations described in this report illustrate our office's commitment to promoting the integrity, efficiency, and effectiveness of NCUA programs and operations and to protecting against fraud, waste, and abuse. On behalf of the office, I underscore our commitment to our stakeholders, which includes NCUA, Congress, other regulatory agencies, OIG colleagues, law enforcement partners, and the public. We rely on the continued strength of positive working relationships with all of them as we strive to fulfill our statutory mission. The audits and investigations highlighted in this report demonstrate our commitment to that cause, as well as our goal of enhancing public confidence in the regulatory and supervisory process.

There have been numerous breaches of sensitive data in both the public and private sectors over the last few years. In late 2014, NCUA experienced an incident involving the breach of Palm Springs Federal Credit Union member information. To review NCUA's responsibility to ensure safe and sound credit unions as well as protect member information, we conducted an audit to determine whether NCUA had adequate controls in place to protect sensitive, confidential, or credit union member personally identifiable information (PII) during examinations. Although we determined examiners had the tools to securely receive electronic information from credit unions during the examination process, we made seven recommendations to NCUA management to correct weaknesses we identified within the internal control environment that, once instituted, will strengthen the agency's efforts to protect credit union member PII.

On the investigative side, the Office of Investigations (OI) opened two cases during the reporting period and closed four. Of the four cases we closed, all were opened in the previous reporting period. In total, the OI issued four Reports of Investigation, which detailed investigations that were handled as administrative misconduct cases.

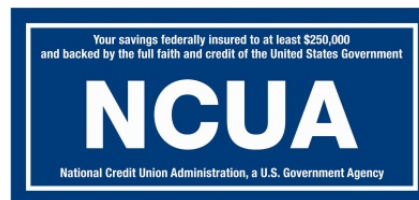
The NCUA Board and Management have been very receptive to the findings and recommendations set forth in our reports and investigations. Management continues to work with us to address our recommendations and implement corrective actions timely. For our part, we rely on the positive working relationships we have forged with them, as we strive to help NCUA accomplish its mission of providing the nation with a safe and sound credit union system.

A handwritten signature in black ink, appearing to read "James W. Hagen".

James W. Hagen
Inspector General

THE NATIONAL CREDIT UNION ADMINISTRATION MISSION

National Credit Union Administration's (NCUA) charge is to provide, through regulation and supervision, a safe and sound credit union system which promotes confidence in the national system of cooperative credit.



THE OFFICE OF INSPECTOR GENERAL MISSION

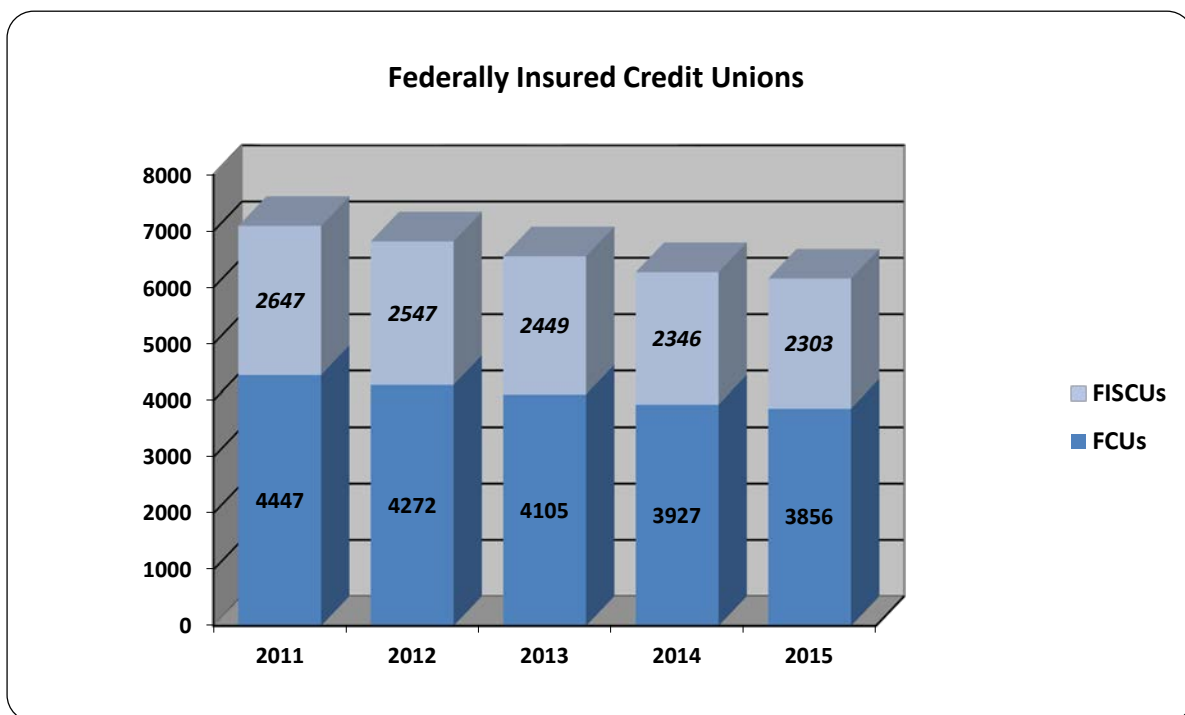
The Office of Inspector General (OIG) promotes the economy, efficiency, and effectiveness of NCUA programs and operations, and detects and deters fraud, waste, and abuse, thereby supporting the NCUA's mission of monitoring and promoting safe and sound federally insured credit unions.

We accomplish our mission by conducting independent audits, investigations, and other activities, and by keeping the NCUA Board and the Congress fully and currently informed of our work.



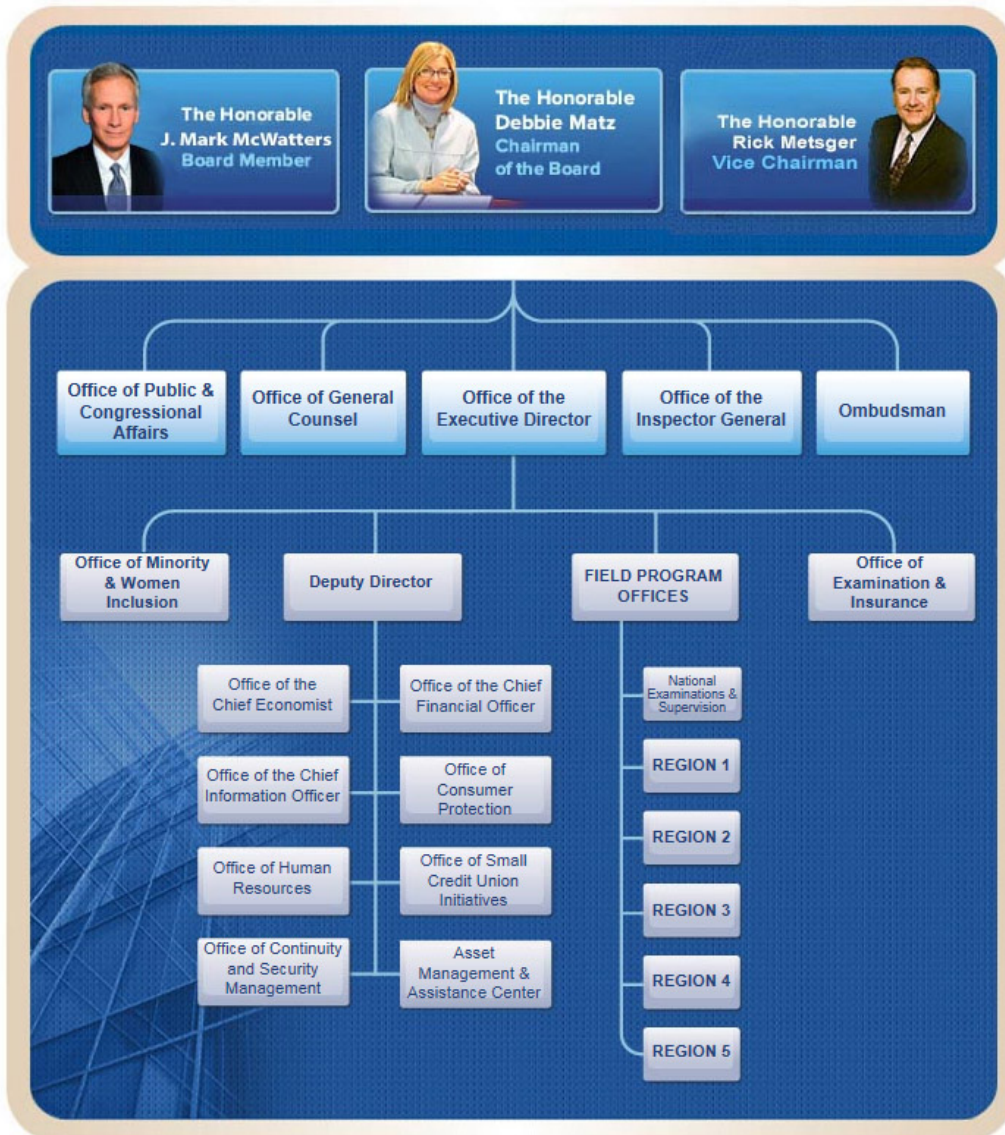
INTRODUCTION

The NCUA was established as an independent, federal regulatory agency on March 10, 1970. The agency is responsible for chartering, examining, supervising, and insuring federal credit unions. It also insures state-chartered credit unions that have applied for insurance and have met National Credit Union Share Insurance requirements. The NCUA is funded by the credit unions it supervises and insures. As of June 30, 2015, the NCUA was supervising and insuring 3,856 federal credit unions and insuring 2,303 state-chartered credit unions, a total of 6,159 institutions. This represents a decline of 71 federal and 43 state-chartered institutions since December 31, 2014, for a total decline of 114 credit unions nationwide, primarily as a result of mergers and liquidations.

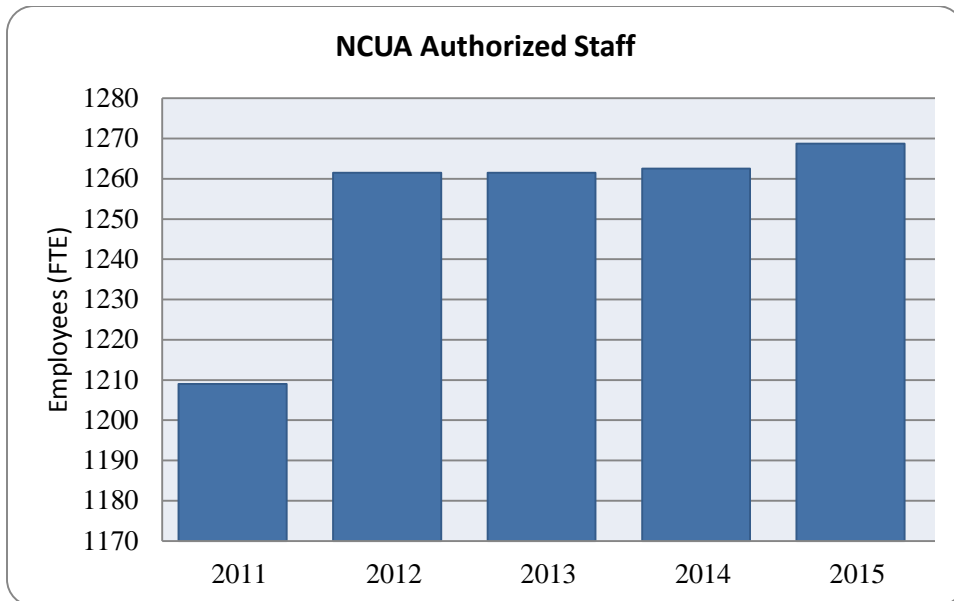
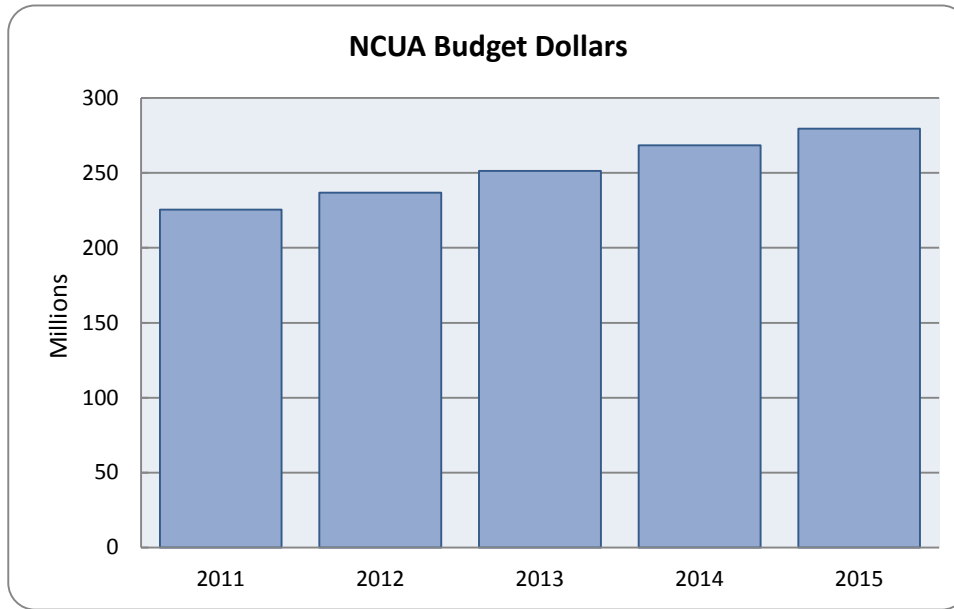


The NCUA operates under the direction of a Board composed of three members. Board members are appointed by the President and confirmed by the Senate. They serve six-year terms. Terms are staggered, so that one term expires every two years. The Board is responsible for the management of the NCUA, including the NCUA Operating Fund, the Share Insurance Fund, the Central Liquidity Facility, the Community Development Revolving Loan Fund, and the Temporary Corporate Credit Union Stabilization Fund.

The NCUA executes its program through its central office in Alexandria, Virginia and regional offices in Albany, New York; Alexandria, Virginia; Atlanta, Georgia; Austin, Texas; and Tempe, Arizona. The NCUA also operates the Asset Management and Assistance Center (AMAC) in Austin, Texas. Please refer to the NCUA organizational chart below.



The NCUA Board adopted its 2015 budget of \$279,477,779 on November 20, 2014. The Full-Time Equivalent (FTE) staffing authorization for 2015 is 1,268.7 representing an increase of six FTE from 2014.



NCUA HIGHLIGHTS

Corporate Stabilization Fund's Net Position Stays in the Black

During the May 2015 NCUA Board meeting, the Chief Financial Officer reported that for the quarter ending March 31, 2015, the Temporary Corporate Credit Union Stabilization Fund's net position increased by \$52.7 million to a positive \$291.2 million. The change was primarily due to improvements in projected cash flows relating to the legacy assets that secure the NCUA Guaranteed Notes (NGN) and guarantee fees earned. NCUA also reached a major milestone during the first quarter of 2015 by completing the sale of all real estate once owned by the five failed corporate credit unions.

As of June 30, 2015, the Corporate Stabilization Fund's net position increased by \$183.8 million to a positive \$475 million. The increase included a \$107.3 million recovery related to the sale of several securities originally held by failed corporate credit unions. It also included a \$65.6 million reduction in provisioning for insurance losses because of continuing improvements in projected cash flows relating to the legacy assets that secure the NGN.

In August, the Corporate Stabilization Fund repaid \$300 million to the U.S. Treasury reducing the balance of outstanding borrowings to \$2.3 billion. Although the Corporate Stabilization Fund continues to have a positive net position, no funds are available to provide federally insured credit unions with an immediate rebate because NCUA must first repay outstanding borrowings from the U.S. Treasury. However, a review of the performance of the legacy assets of five failed corporate credit unions and the NGN program indicated that future Corporate Stabilization Fund assessments were unlikely.

NCUA and NTEU Sign New Collective Bargaining Agreement

On July 7, 2015, NCUA Chairman Debbie Matz and National Treasury Employees Union (NTEU) President Colleen Kelley signed a new, five-year collective bargaining agreement (CBA). NCUA and NTEU negotiated 30 articles and agreements on major topics including employee pay and benefits, travel expense reimbursement, training, promotions, employee rights, employee telework and leave, and health and wellness.

The CBA modernizes the employee pay and benefits program and keeps it competitive with the other financial services regulators as required by law. The agreement also incorporates additional cost controls, such as pay caps at each pay grade. The CBA further revised the employee travel reimbursement program by recognizing needed changes in light of the increasing overnight staff travel required due to the declining number of local credit unions.

NTEU represents approximately 950 of NCUA's nearly 1,200 employees.

Fixed-Asset Rule Provides Relief to More than 3,800 Federal Credit Unions

During its July 2015 meeting, NCUA's Board unanimously approved a final rule (Part 701) amending the regulation on fixed assets. This final rule provides regulatory relief to more than 3,800 federal credit unions by eliminating the five percent cap on fixed-asset investments. In addition to eliminating the fixed-asset cap, the final rule simplifies partial occupancy requirements for federal credit union premises acquired for future expansion.

NCUA Agrees to 129.6 Million Offer from Royal Bank of Scotland - Recoveries in Securities Cases Reach More than \$1.9 Billion

On September 16, 2015, NCUA announced its acceptance of an offer of judgment for \$129.6 million from the Royal Bank of Scotland to resolve claims arising from losses related to purchases of residential mortgage-backed securities by Members United and Southwest corporate credit unions.

To date, NCUA has obtained over \$1.9 billion in legal recoveries from securities cases. NCUA uses the net proceeds to reduce Corporate Stabilization Fund assessments charged to federally insured credit unions to pay for the losses caused by the failure of five corporate credit unions. NCUA was the first federal regulatory agency for depository institutions to recover losses from investments in these securities on behalf of failed financial institutions

NCUA Board Doubles Small Credit Union Threshold to \$100 Million

During its September 2015 meeting, the NCUA Board raised the asset ceiling for a "small" credit union from \$50 million to \$100 million under the Regulatory Flexibility Act. Updating the definition of "small" means an additional 733 federally insured credit unions are eligible for special consideration of regulatory relief in future rulemakings and assistance from NCUA's Office of Small Credit Union Initiatives, including training and consulting. As a result, 4,690 or over three-quarters of federally insured credit unions qualify as small entities.

In approving the \$100 million asset ceiling, the NCUA Board analyzed a wide range of metrics, including growth rates for assets, deposits, loans and membership; the ratio of operating costs to assets; and merger and liquidation rates. Pursuant to the agency's rolling three-year regulatory review, the NCUA Board will reconsider the small credit union threshold in 2018.



FEDERALLY INSURED CREDIT UNION HIGHLIGHTS

Credit unions submit quarterly call reports (financial and operational data) to the NCUA. An NCUA staff assessment of the June 30, 2015, quarterly call reports submitted by all federally insured credit unions found that key financial indicators are positive.

Key Financial Indicators Favorable

Looking at the June 30, 2015, quarterly statistics for major balance sheet items and key ratios shows the following for the nation's 6,159 federally insured credit unions: assets grew 8.2 percent; net worth to assets ratio decreased from 10.96 to 10.92 percent; and the loan to share ratio increased from 74.92 percent to 75.52 percent. The delinquency ratio decreased from .85 to .74 percent. Credit union return on average assets increased from .80 to .81 percent.

Savings Shifting to Regular Shares

Total share accounts increased 7.58 percent. Regular shares increased 14.40 percent. Regular shares comprise 34.89 percent of total share accounts; share certificates comprise 19.12 percent; money market shares comprise 22.87 percent; share draft accounts comprise 13.91 percent; and all other share accounts comprise 9.23 percent.

Loan Volume Increasing

Loans increased 9.23 percent resulting in an increase in total loans by \$32.88 billion. Total net loans of \$738 billion comprise 63.19 percent of credit union assets. First mortgage real estate loans are the largest single asset category with \$306 billion accounting for 41.08 percent of all loans. Other real estate loans of \$72 billion account for 9.69 percent of all loans. Used car loans of \$153 billion were 20.52 percent of all loans, while new car loans amounted to \$93 billion or 12.46 percent of total loans. Credit card loans totaled \$46 billion or 6.15 percent of total loans, and other loans totaled \$75 billion or 10.09 percent of total loans.



LEGISLATIVE HIGHLIGHTS

Obtaining Vendor Authority Remains NCUA's Top Legislative Priority

In response to a Government Accountability Office (GAO) report examining financial institutions and cybersecurity risks, released on July 2, 2015, NCUA Chairman Debbie Matz commented favorably on GAO's recommendation to Congress that NCUA be granted enhanced examination authority over third-party technology service providers.

The GAO report examined financial institutions and cybersecurity risks. The report is available online [here](#).

In a July 6, 2015, statement, Matz said that “[w]e need to close this regulatory blind spot and better protect the credit union system by providing NCUA with the power to examine and take enforcement actions at third-party vendors.” She commented further that “[t]he GAO report’s recommendation reinforces NCUA’s long-standing request for legislative action and comes on the heels of a [similar recommendation](#) by the Financial Stability Oversight Council. Obtaining this authority would allow the agency to proactively address cyber threats and better position credit unions to avoid a crisis.”

The summary of the GAO report noted that “[c]yber risks affecting a depository institution can arise from weaknesses in the security practices of third parties that process information or provide other IT services to the institution. Bank regulators routinely conduct examinations of service providers’ information security. Authorizing NCUA to routinely conduct such examinations could help it better ensure that the service providers for credit unions also follow sound information security practices.”

In assessing current cybersecurity risks, GAO also referenced its 1999 and 2003 recommendations to provide NCUA with vendor authority. The 2003 assessment noted that third-party arrangements can help credit unions manage costs, provide expertise and improve services to credit union members, but they also present risks, such as threats to security systems, weakness of processing, and availability and integrity of the systems.

Obtaining vendor authority is NCUA’s top legislative priority.

“Stop and Study” Act Passes House Financial Services Committee

The Risk-Based Capital Study Act, [HR 2769](#), passed the House Financial Services Committee on September 30, 2015, with a 50-9 vote. The bill, named “The Credit Union Risk Based Capital Study Act of 2015,” directs the NCUA to conduct a public study of the appropriate capital

requirements for credit unions, as well as other stipulations regarding the agency’s actions in the matter. Known as the “Stop and Study” rule, the bill asks NCUA to provide:

- An analysis of the legal authority to impose a two-tiered system;
- A discussion of differences between credit unions and other types of depository institutions and the reasons why they should have similar or different risk weights;
- A discussion of the rationale behind the risk-weights assigned in the agency’s revised, proposed rule; and
- An analysis of the impact on capital buffers.

Finally, the bill asks NCUA to make “any legislative recommendations” to improve the capital system for credit unions or establish a risk-based capital system for credit unions.

NCUA Chairman Matz Joins Five Other Financial Regulators in Opposing “Independent Agency Regulatory Analysis Act of 2015”

In a letter dated July 27, 2015, to the Homeland Security and Governmental Affairs Committee, NCUA Chairman Matz joined the heads of five other federal financial regulators writing to express their concerns with S.1607, the “Independent Agency Regulatory Analysis Act of 2015.” The letter explained that independent regulatory agencies, including NCUA, were established by Congress to exercise policymaking functions—and in particular, rulemaking functions— independent of any Administration. S. 1607 authorizes the President to require independent regulatory agencies to submit their rulemakings to the Office of Management and Budget’s Office of Information and Regulatory Affairs for prior review. This, the letter stated, would give any President unprecedented authority to influence the policy and rulemaking functions of independent regulatory agencies and would constitute a fundamental change in the role of independent regulatory agencies. The bill would also, the signatories to the letter asserted, interfere with their ability to promulgate rules critical to their respective missions in a timely manner and would likely result in unnecessary and unwarranted litigation in connection with their rules.

Despite the letter’s request that the Committee consider the negative consequences of the bill, the Committee voted, on October 7, 2015, to approve it.

NCUA Chairman Matz, Board Member McWatters Weigh in on Budget Transparency

On July 23, 2015, NCUA Chairman Debbie Matz testified at a hearing on NCUA’s operations and budget before the House Financial Institutions and Consumer Credit Subcommittee. Matz testified that NCUA, heeding the lessons of the recent financial crisis, is committed to fiscal discipline, operational transparency, and open communication. With regard to NCUA’s annual budget, Matz stated that the budget is developed from the bottom up through a zero-based budgeting process in which every item is carefully scrutinized. Testifying that “NCUA leads financial institution regulators in budget transparency,” Matz explained that the agency provides

extensive detail on its annual budget in a dedicated [resource center](#) on NCUA’s website. The resource center includes annual fund audits, budget summaries and slides, office-by-office spending plans, and a host of other information.

In statements made the same day, NCUA Board Member J. Mark McWatters reiterated his continuing concerns with NCUA’s budget and the budget process. McWatters’ comments acknowledged that while “steps have been taken to provide information about NCUA’s resource allocation,” he urged “more meaningful transparency for the credit union system, in the context of our democratic system of government and the Federal Credit Union Act.”

McWatters expressed his view that the Board’s job “is not merely to follow the script set by other financial regulators, but to lead and to set the standard of transparency and accountability for all such regulators.”

McWatters has expressed his support of bipartisan legislation pending in both the Senate and the House that would require NCUA to hold public hearings and receive comments from the public on its budget ([HR. 2287](#), [S.924](#)).

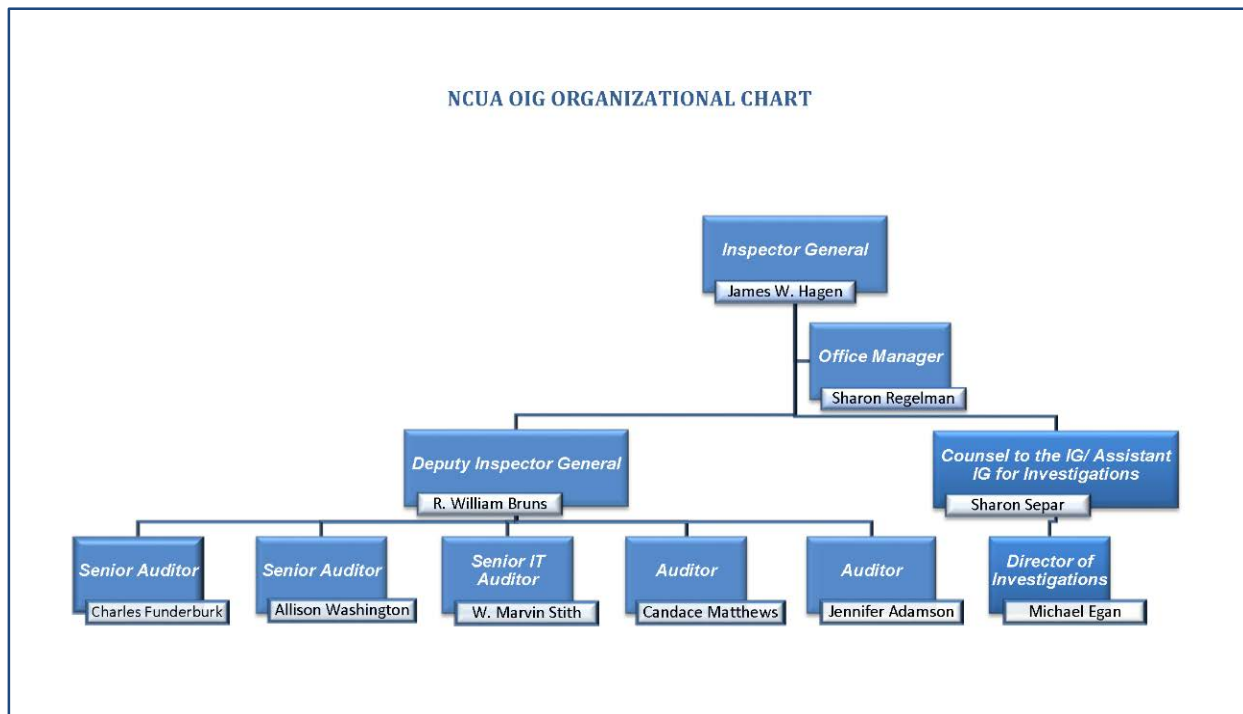


OFFICE OF THE INSPECTOR GENERAL

The Office of the Inspector General was established at the NCUA in 1989 under the authority of the Inspector General Act of 1978, as amended. The staff consists of the Inspector General, Deputy Inspector General, Counsel to the Inspector General/Assistant Inspector General for Investigations, Director of Investigations, Senior Information Technology Auditor, two Senior Auditors, two staff Auditors, and an Office Manager.

The Inspector General reports to, and is under the general supervision of, the NCUA Board. The Inspector General is responsible for:

1. Conducting, supervising, and coordinating audits and investigations of all NCUA programs and operations;
2. Reviewing policies and procedures to ensure efficient and economic operations as well as preventing and detecting fraud, waste, and abuse;
3. Reviewing existing and proposed legislation and regulations to evaluate their impact on the economic and efficient administration of agency programs; and
4. Keeping the NCUA Board and the Congress apprised of significant findings and recommendations.



AUDIT ACTIVITY

OIG-15-08 – June 1, 2015

[Coordination of Responsibilities Among the Consumer Financial Protection Bureau and the Prudential Regulators – Limited Scope Review](#)

The Subcommittee on Financial Institutions and Consumer Credit of the House Committee on Financial Services raised a concern regarding potential regulatory overlap between the Consumer Financial Protection Bureau (CFPB) and the Federal Deposit Insurance Corporation (FDIC). In subsequent conversations, the FDIC Office of Inspector General (OIG) notified the Subcommittee that it planned to coordinate with the OIGs of the other prudential regulators, including NCUA, to conduct a joint review and assess whether there are overlaps in how the CFPB and prudential regulators carry out their regulatory responsibilities.

The objective of the review was to assess the extent to which the CFPB and prudential regulators coordinated their supervisory activities to avoid duplication of regulatory oversight responsibilities. At the time of our review, the Government Accountability Office (GAO) had completed, ongoing, and planned assignments at CFPB that evaluated agency coordination efforts, among other matters. Accordingly, we tailored our review to complement, but not duplicate, GAO's work. The OIGs conducting the review agreed to a limited scope review rather than an audit.

We found that the CFPB and prudential regulators were generally coordinating their regulatory oversight activities for Federal consumer financial laws, consistent with the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and the provisions of a Memorandum of Understanding governing coordinating activities. Nonetheless, we determined that there are opportunities for enhanced coordination. We did not identify regulatory duplication of oversight responsibilities. Officials from the CFPB and prudential regulators reported that they were generally satisfied with the level of communication and coordination occurring, which has continued to improve since the inception of CFPB.

OIG-15-09 – June 8, 2015

[National Credit Union Administration's Measures to Protect Electronic Credit Union Member Information During the Examination Process](#)

The NCUA OIG conducted an audit to determine whether NCUA has adequate controls in place to protect sensitive, confidential, or personally identifiable electronic credit union information during examinations.

We determined that NCUA has provided examiners with appropriate tools with which to securely receive electronic information from credit unions during the examination process.

However, we also determined:

1. NCUA did not require credit unions to provide sensitive, confidential, and personally identifiable credit union member information to NCUA staff in a protected manner;
2. NCUA needed to improve its policies, procedures and training to help ensure NCUA staff take appropriate measures to protect sensitive, confidential, and personally identifiable electronic credit union member information during examinations; and
3. NCUA needed to improve its guidance to require NCUA staff to use specific tools to transfer sensitive, confidential, and personally identifiable electronic credit union member information during examinations.

This report made seven recommendations to NCUA management to help increase staff awareness regarding the importance of protecting sensitive credit union member information and to ultimately strengthen the agency's efforts to protect this information in its electronic format. NCUA management agreed to all recommendations and provided planned corrective actions.

AUDITS IN PROGRESS

Interest Rate Risk

The OIG is conducting an audit of NCUA's Interest Rate Risk (IRR) policy and program.

NCUA previously issued guidance on Asset and Liability Management (ALM) and IRR management through NCUA Letters to Credit Unions. Federally insured credit unions (FICUs) have relied on this guidance to manage their IRR. However, FICUs experienced increased exposure to IRR due to changes in balance sheet composition and increased uncertainty in the financial markets. This increase heightened the importance for FICUs to have strong policies and programs explicitly addressing the credit union's management of controls for IRR. Consequently, NCUA implemented 12 CFR Part 741, Interest Rate Risk Policy and Program, effective September 30, 2012. In this review, we will determine whether NCUA's IRR policy and procedures are having the desired effect of reducing interest rate risk for FICUs.

Restitution Orders

The OIG is currently conducting a review of NCUA's Restitution Orders process. Restitution is the monetary amount established by a court in a Judgment and Commitment Order that a party convicted of violating a law must pay to render a victim whole. The Mandatory Victim Restitution Act of 1996 (18 U.S.C. §3363A) requires an order of restitution that fully compensates the victim for the loss of or damage to the victim's property. When fraud is committed resulting in the failure of a credit union, NCUA is determined to be the victim. At the time of sentencing, the presiding judge will order the defendant to pay an award of restitution to



make the National Credit Union Share Insurance Fund (NCUSIF) whole. NCUA's Asset Management and Assistance Center (AMAC) assists the Department of Justice and state attorneys general in collection efforts.

Our objectives for this review are to (1) determine whether AMAC has effective policies, procedures and resources in place to recover money owed from restitution orders, and (2) assess the internal controls of AMAC's restitution order program.

[Independent Evaluation of NCUA's Compliance with the Federal Information Security Management Act 2015](#)

NCUA OIG engaged CliftonLarsonAllen, LLP (CLA) to independently evaluate its information systems and security program and controls for compliance with the Federal Information Security Management Act (FISMA), Title III of the E-Government Act of 2002.

CLA is evaluating NCUA's security program through interviews, documentation reviews, technical configuration reviews, social engineering testing, and sample testing. NCUA is being evaluated against standards and requirements for federal government agencies such as those provided through FISMA, National Institute of Standards and Technology Special Publications, and OMB memoranda. We anticipate issuing the final report in November 2015.

[Annual Financial Statement Audits](#)

The accounting firm of KPMG is conducting the 2015 financial statement audits of the NCUA Operating Fund, National Credit Union Share Insurance Fund, the Central Liquidity Facility, the Community Development Revolving Loan Fund, and the Temporary Corporate Credit Union Stabilization Fund.

- The NCUA Operating Fund was established as a revolving fund managed by the NCUA Board for the purpose of providing administration and service to the federal credit union system.
- The National Credit Union Share Insurance Fund was established as a revolving fund managed by the NCUA Board to insure member share deposits in all Federal credit unions and qualifying state credit unions.
- The Central Liquidity Facility was established as a mixed ownership government corporation managed by the NCUA Board to improve general financial stability by meeting the liquidity needs of credit unions.
- The purpose of the Community Development Revolving Loan Fund is to stimulate economic activities in the communities served by low-income credit unions. This in turn will result in increased income, ownership and employment opportunities for low-wealth residents and other economic growth.



- The Temporary Corporate Credit Union Stabilization Fund, established in 2009, allows NCUA to borrow money from the Treasury to pay for corporate credit union losses, and then pay back the Treasury over time with funds obtained from assessments on federally insured credit unions.

We expect to issue our report in February 2016.

Material Loss Reviews

The Federal Credit Union Act requires the NCUA OIG to conduct a Material Loss Review (MLR) of an insured credit union if the loss to the National Credit Union Share Insurance Fund (NCUSIF) exceeds \$25 million or an amount equal to 10 percent of the total assets of the credit union at the time in which the NCUA Board initiated assistance under Section 208 or was appointed liquidating agent. When losses exceed this materiality threshold, we review the loss to (1) determine the cause(s) of the credit union’s failure and the resulting loss to the NCUSIF, and (2) assess NCUA’s supervision of the credit union. The Dodd-Frank Act further requires the OIG to assess all losses to the NCUSIF under the \$25 million threshold to determine whether unusual circumstances exist to warrant conducting a full-scope MLR.

During this reporting period, NCUA did not have a loss to the NCUSIF greater than the \$25 million threshold. Therefore, the OIG did not conduct any full-scope MLRs. However, during the reporting period the NCUSIF did sustain losses under the \$25 million threshold. Accordingly, we conducted limited scope reviews of seven credit unions to determine whether unusual circumstances existed. Based on our findings, we determined not to conduct a full scope MLR for any of these credit unions. We discuss these cases in detail on page 17.

Significant Audit Recommendations on Which Corrective Action Has Not Been Completed

Following is a list of OIG reports with significant unimplemented recommendations as of September 30, 2015. NCUA management has agreed to implement corrective action, but has yet to complete those actions. This information was supplied by NCUA Office of Examination and Insurance and is monitored within the OIG’s report recommendation tracking system.

Report Number, Title, and Date

- OIG-10-20* OIG Capping Report on Material Loss Reviews, November 23, 2010
- OIG-12-14* Material Loss Review of Eastern New York FCU, November 19, 2012
- OIG-13-05* Material Loss Review of Telesis Community CU, March 14, 2013

Significant Recommendations Open and Brief Summary

1. Recommendation: *OIG-10-20, recommendation #5*. Determine whether to propose and/or change regulatory guidance to establish limits or other controls for concentrations that pose an unacceptable safety and soundness risk and determine an appropriate range of examiner response to high risk concentrations.

Status: Open. NCUA agreed with the OIG, provided training to examiners, and issued a Supervisory Letter to credit unions advising them how to evaluate and manage concentration risk. In addition, in January 2014, the NCUA Board issued a proposed rule (the Original Proposal) to amend NCUA's PCA regulations, part 702 of the Rules and Regulations (RR). The proposed rule incorporated risk based capital requirements. The 125-day comment period ended on May 28, 2014. NCUA received 2,053 comments.

The NCUA Board reviewed the comments and determined that it was appropriate to issue a second proposed rule. On January 15, 2015, NCUA issued proposed changes to Part 702 of the RR. The Board requested comments on this second proposed rule regarding risk-based capital. Based largely on comments received on the Original Proposal, the Board proposed many improvements to the Original Proposal. The changes incorporate risk based capital requirements including revised risk weights for mortgages, investments, member business loans, CUSOs, and corporate credit unions. The rule includes higher capital requirements for credit unions with very high concentrations of real estate loans and commercial loans. NCUA's estimated implementation date is December 31, 2015.

2. Recommendation: *OIG-12-14, recommendation #2*. Review current examination procedures over Credit Union Service Organizations (CUSO) to not only ensure regulatory compliance, but most importantly, to determine whether current procedures are adequate to identify the degree of risk the CUSO poses to the affiliated credit union.

Status: Open. NCUA has developed a CUSO Registry that is on track to be operational by December 31, 2015. NCUA also continues to seek vendor authority comparable to the other FFIEC agencies and recently met with the staff of two Senators who have shown interest in initiating or supporting this type of legislation. NCUA has also met with representatives of the OMB and shared the need for vendor authority. In addition, NCUA developed a CUSO working group that has submitted to NCUA's National Exam Committee an updated chapter to the Examiner's Guide that includes examination procedures and checklists for the examiner staff. NCUA plans to distribute the revised procedures for the regions to test and will incorporate any feedback. NCUA plans to have the stand alone review procedures finalized and distributed for use by December 31, 2015.

3. Recommendation: *OIG-13-05, recommendation #1*. We recommend NCUA management identify and amend, as applicable, NCUA Rules and Regulations to require a higher level of risk based net worth for credit unions with higher levels of concentration or other risks in their member business loan portfolio.

Status: Open. NCUA issued proposed changes to Part 702 of the RR on January 15, 2015. The proposed changes incorporate risk based capital requirements including revised risk weights for mortgages, investments, member business loans, CUSOs, and corporate credit unions. The rule includes higher capital requirements for credit unions with very high concentrations of real estate loans and commercial loans. NCUA's estimated implementation date is December 31, 2015.

Report on Credit Union Losses under Materiality Level of \$25 Million

The Dodd-Frank Act requires the NCUA OIG to perform a limited review where the NCUSIF incurred a loss below the \$25 million threshold with respect to an insured credit union. The OIG must report to the NCUA Board and the Congress every six months on the results of the limited reviews and the timeframe for performing any subsequent in-depth reviews we determine are necessary.

This report on losses below the \$25 million threshold covers the six-month period from April 1, 2015 to September 30, 2015. For all losses to the NCUSIF under the MLR threshold, we determined (1) why NCUA initiated assistance, and (2) whether any unusual circumstances existed that might warrant an in-depth review of the loss.

For each limited review, we performed procedures that included, but were not limited to (1) obtaining and analyzing the regulator's supervisory memoranda and other pertinent documents; (2) preparing a schedule of CAMEL ratings assigned to the institution through full scope or other examinations during the five years preceding the failure; (3) conducting interviews as needed; (4) inquiring about any investigative actions that were taken, planned, or considered involving credit union officials or others; and (5) analyzing supervisory history and other review methods.

We conducted limited scope reviews of seven credit unions that incurred losses to the NCUSIF under \$25 million between April 1, 2015 and September 30, 2015. Based on those limited reviews, we determined that none of the losses warranted conducting additional work because we found no unusual circumstances, or we had already addressed the reasons identified for the losses in recommendations to the agency in previous MLR reports.

The chart below provides details on the seven credit union losses to the NCUSIF below the \$25 million threshold. It provides details on the credit union, such as the date of failure, the estimated loss to the Share Insurance Fund, and grounds for conservatorship, merger, or other factors. The chart also provides our decision whether to terminate or proceed with a full scope MLR of the credit union.



DECISIONS REGARDING LOSSES LESS THAN \$25 MILLION					
OIG Decision**	Credit Union	Region	Date Closed	Estimated Loss to NCUSIF	Grounds for Liquidation or Appointment
Terminate	TLC Federal Credit Union	V	4/30/15	\$1,210,000	Insolvent due to lack of board oversight which led to gross mismanagement, the hiring of underqualified accounting and management staff, and critical undercapitalization of the credit union.
Terminate	65 Family Federal Credit Union	I	7/1/15	\$135, 713	Unprofitable operations since 2008, abandonment by the credit union sponsor and disinterest in continuing operations by the Board of Directors placed this credit union in danger of insolvency and led to an assisted merger.
Terminate	Kolmar NY Employees Federal Credit Union	I	7/1/15	\$310, 137	Insolvent due to losses caused by a former manager’s alleged fraudulent activity.
Terminate	Trailblazer Federal Credit Union	II	7/10/15	\$1,072,233	Insolvent due to alleged fraudulent activity related to negative member share accounts and unreconciled corporate losses.
Terminate	Lakeside Federal Credit Union	III	7/16/15	\$1,665,434	Insolvent due to losses caused by a former manager and employee’s alleged fraudulent activity, which led to a partial purchase and assumption.
Terminate	SCICAP Credit Union	IV	8/28/15	\$2,057,766	Insolvent due to admitted fraud by a credit union employee involving unrecorded/misappropriated member share deposits.
Terminate	Quemado Federal Credit Union	IV	9/30/2015	\$245,840	Merged with assistance due to management instability, poor loan quality, and a weak net worth placing the credit union in danger of becoming critically undercapitalized and subsequently insolvent.

***Criteria for each decision included: (1) dollar value and/or percentage of loss; (2) the institution’s background, such as charter type and history, geographic location, affiliations, business strategy; (3) uncommon cause of failure based on prior MLR findings; (4) unusual supervisory history, including the nature and timing of supervisory action taken, noncompliance with statutory examination requirements, and/or indications of rating disagreements between the state regulator and NCUA; and (5) other, such as apparent fraud, request by NCUA Board or management, Congressional interest, or IG request.*



Peer Reviews – April 1, 2015 through September 30, 2015

Government Auditing Standards require audit organizations that perform audits and attestation engagements of federal government programs and operations undergo an external peer review every three years. The objectives of an external peer review include a review of an audit organization's system of quality control to determine not only the suitability of the design, but also whether the audit organization is in compliance with its quality control system so as to provide reasonable assurance the audit organization conforms to applicable professional standards.

External Peer Review of NCUA OIG, Office of Audit

The Peace Corps OIG completed our most recent peer review on February 4, 2013, for the three-year period ended December 31, 2012. The Peace Corps OIG issued its report entitled System Review Report and rendered the opinion that the system of quality control for the NCUA OIG, Office of Audit, was suitably designed and complied with, thus providing reasonable assurance the system of controls conformed with applicable professional standards in all material respects. As a result, we received a peer rating of pass. In addition, we have no outstanding recommendations from this external peer review. A copy of this report is included herein as Appendix A.

External Peer Review of Architect of the Capitol OIG, Office of Audit

The NCUA OIG completed a peer review of the Architect of the Capitol (AOC) OIG. On September 4, 2015, we issued an external peer review report for the audit function of the AOC OIG for the three year period ended March 31, 2015. The AOC received a rating of pass and has no outstanding recommendations related to the peer review report.

INVESTIGATIVE ACTIVITY

In accordance with professional standards and guidelines established by the United States Department of Justice, the NCUA OIG, Office of Investigations (OI) conducts investigations of criminal, civil, and administrative wrongdoing involving the agency's programs, operations, and personnel. Our investigative mission is to fight fraud, waste, and abuse while promoting efficiency and economy within the NCUA and its programs and operations. In this regard, we investigate referrals and allegations of misconduct on the part of NCUA employees, former employees, and contractors. Investigations may involve possible violations of regulations involving Federal employee responsibilities and conduct, agency policies, Federal criminal law, and other statutes and regulations.

The OI also maintains a robust training program within the agency that encompasses integrity awareness briefings and orientation presentations regarding the role of the OIG within the agency and how to report wrongdoing to the OI. The instructional guidance the OI provides to new NCUA employees and newly appointed supervisors about the respective roles and responsibilities of the OIG and NCUA employees facilitates more open communication between both. The final product is a stronger agency. Additionally, we routinely receive complaints from credit union officials and their members involving NCUA programs. We examine these complaints and determine if there is any indication of misconduct or wrongdoing by an NCUA employee. If not, we refer the complaint to the NCUA Office of Consumer Protection (OCP) or appropriate regional office for response, or close the matter if contact with OCP or the regional office indicates that the matter has already been appropriately handled.

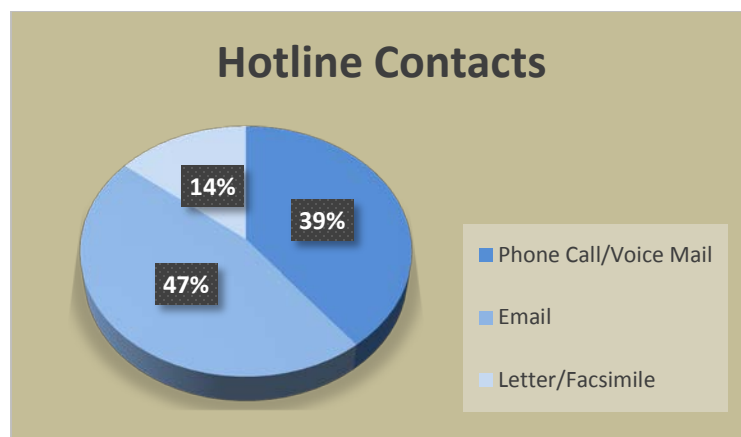
OIG Hotline Contacts

The OIG maintains a 24-hour toll free hotline to enable employees and citizens to call in and provide information about suspected fraud, waste, and abuse, or mismanagement involving agency programs or operations. Additionally, the OIG receives complaints from an off-site post office box, electronic mail, and facsimile messages. The OI has also developed an electronic version of a hotline complaint form, located on the NCUA intranet. The electronic form offers an additional venue for confidential employee and contractor communication with the OIG. All information received from any of these sources is referred to as a hotline contact. Our Office Manager, under the direction of the Director of Investigations, administers the OIG hotline program.

In recent years, the OIG Hotline has also become a valuable repository for reports of potential cases of fraud in credit unions. While the OIG does not, in most cases, have jurisdiction to investigate fraudulent activity that takes place in credit unions, it analyzes the information obtained through the Hotline and refers potential cases of fraud to the appropriate regional office, the Office of Examination and Insurance, and the Office of General Counsel for immediate review and action. Moreover, the OIG relays general information from these referrals at new

employee and supervisor training sessions to alert NCUA employees about the need for heightened fraud awareness.

During this six-month period, we processed approximately 155 hotline contacts, the majority of which were from consumers seeking assistance with problems encountered within their respective credit unions. As discussed above, these contacts were generally referred to OCP and regional offices for action. A relatively small number of these contacts required additional action by OI to determine whether the matter warranted investigation.



Phone Call/Voice Mail	61
Email	72
Letter/Facsimile	22
Total:	155

Investigations

Employee Misconduct (Appearance of Partiality)

The OIG investigated a complaint alleging a lack of impartiality and/or conflict of interest on the part of an NCUA senior manager during a prior reporting period. The investigation developed no evidence that the manager violated 5 CFR § 2635.502(a). Nevertheless, the investigation found that the manager’s conduct lent the appearance of partiality to his/her actions. The OIG issued a Report of Investigation. In response, NCUA management issued a letter of reprimand. The OIG closed the case during this reporting period.

Employee Misconduct (False Claims/False Statements)

During the previous reporting period, the OIG received an allegation that an NCUA examiner claimed and received approximately \$4,989.15 in travel reimbursements that the agency had

already paid. The OIG issued a Report of Investigation during this reporting period. The employee received a 14-day suspension and was ordered to repay the agency for the unauthorized payments.

Employee Misconduct (Alleged Unauthorized Disclosure to Media)

In the previous reporting period, the OIG obtained information regarding an unauthorized disclosure of internally-held information to media sources. A credit union trade magazine reported that two unnamed NCUA sources provided the information. The investigation could not substantiate that the information came from within NCUA or any of its employees. The OIG issued a Report of Investigation and closed the matter during the reporting period.

Employee Misconduct (False Statements; False Claims; Misuse of Government Property; Unprofessional Conduct)

In the previous reporting period, the OIG received allegations that a senior examiner had threatened his/her direct supervisor; exhibited unprofessional behavior towards co-workers and credit union personnel; and repeatedly lost and/or damaged government-issued property. The OIG issued a Report of Investigation detailing its findings that the employee had: (1) falsified time logs and travel claims; (2) lost or damaged government-issued electronic equipment (iPhones, hotspots, laptop computers) on several occasions; (3) behaved unprofessionally in the workplace and during credit union contacts; (4) made unauthorized purchases with a regional office corporate credit card; and (5) made inappropriate comments in the workplace. The agency recently issued a final decision letter sustaining the employee's removal from federal service. This investigation is closed.

Employee Misconduct (Inappropriate Comments/Behavior in the Workplace)

During this reporting period, the OIG received allegations that an NCUA examiner had made threatening remarks towards his/her supervisor and had exhibited unprofessional conduct during recent credit union examinations. The investigation substantiated both allegations. The NCUA examiner admitted to making the threats and acting unprofessionally while conducting NCUA examinations. The OIG issued a Report of Investigation. One week later, the employee resigned his/her position, prior to a decision of proposed agency action. This investigation is closed.

Employee Misconduct (False Claims)

During this reporting period, the OIG received allegations that a senior examiner was engaging in travel claim fraud. This investigation is ongoing.



Quality Assessment Review

The Federal Election Commission (FEC) OIG conducted an external Quality Assessment Review (QAR) of the NCUA OIG Office of Investigations (OI), in accordance with section 6(e)(7) of the Inspector General Act of 1978, as amended. The review was voluntary and concluded in September 2015. The FEC OIG found that OI was in full compliance with the prescribed Quality Standards for Investigations (2011) set forth by the Council of Inspectors General on Integrity and Efficiency (CIGIE). There are no outstanding recommendations from this external QAR.



LEGISLATIVE AND REGULATORY REVIEWS

Section 4(a) of the Inspector General Act requires the Inspector General to review existing and proposed legislation and regulations relating to the programs and operations of the NCUA and to make recommendations concerning their impact. Moreover, we routinely review agency program and policy guidance, in order to make recommendations concerning economy and efficiency in the administration of NCUA programs and operations and the prevention and detection of fraud, waste and abuse.

During the reporting period, the OIG reviewed 21 items, including proposed legislation, final regulations, Interpretive Rulings and Policy Statements (IRPS), NCUA Letters to Credit Unions, and the agency’s Delegations of Authority. The OIG also responded to six (6) Freedom of Information Act (FOIA) requests.

SUMMARY OF STATUTES AND REGULATIONS REVIEWED	
Legislation	Title
S. 579, H.R. 2395	Inspector General Empowerment Act of 2015
H.R. 2769	Risk-Based Capital Study Act of 2015
S. 1607	Independent Agency Regulatory Analysis Act of 2015
H.R. 2287, S. 924	National Credit Union Administration Budget Transparency Act
H.R. 2807	Sunshine on Government Act of 2015
S. 1990	Federal Computer Security Act of 2015
H.R. 1557	Federal Employee Antidiscrimination Act
Regulations/Rulings	Title
12 CFR Part 791	Final Action: Regulatory Flexibility Act Threshold
12 CFR Part 704	Final Action: Corporate Credit Unions
12 CFR Parts 740, 741, 747, and 796	Final Action: Civil Monetary Penalty Inflation Adjustment
12 CFR Part 702	Final Action: Capital Planning and Stress Testing – Schedule Shift
12 CFR Part 701	Final Action: Federal Credit Union Ownership of Fixed Assets
12 CFR Part 760	Final Action: Loans in Areas Having Special Flood Hazards



IRPS 13-1	Final Action: Minority Depository Institution Preservation Program
12 CFR Part 701, Appendix B	Final Action: Chartering and Field of Membership Manual

Letters to Credit Unions	Title
15-CU-05	Standards for Assessing Diversity Policies and Practices
15-CU-04	Improving the Process for Consumer Complaints
15-CU-03	Taxi Medallion Lending Questions and Answers
15-FCU-03	How to Add Associations to Your Field of Membership
15-FCU-02	Permissible Loan Interest Rate Ceiling Extended



TABLE I: ISSUED REPORTS WITH QUESTIONED COSTS				
		Number of Reports	Questioned Costs	Unsupported Costs
A.	For which no management decision had been made by the start of the reporting period.	0	\$0	\$0
B.	Which were issued during the reporting period.	0	0	0
	Subtotals (A + B)	0	0	0
C.	For which management decision was made during the reporting period.	0	0	0
	(i) Dollar value of disallowed costs	0	0	0
	(ii) Dollar value of costs not allowed	0	0	0
D.	For which no management decision has been made by the end of the reporting period.	0	0	0
E.	Reports for which no management decision was made within six months of issuance.	0	0	0

Questioned costs are those costs the OIG has questioned because of alleged violations of laws, regulations, contracts, or other agreements; findings which at the time of the audit are not supported by adequate documentation; or the expenditure for the intended purpose is unnecessary or unreasonable.

Unsupported costs (included in "Questioned Costs") are those costs the OIG has questioned because of the lack of adequate documentation at the time of the audit.



TABLE II: ISSUED REPORTS WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE			
		Number of Reports	Dollar Value
A.	For which no management decision had been made by the start of the reporting period.	0	\$0
B.	Which were issued during the reporting period.	0	0
	Subtotals (A + B)	0	0
C.	For which management decision was made during the reporting period.	0	0
	(i) Dollar value of recommendations agreed to by management.	N/A	N/A
	(ii) Dollar value of recommendations not agreed to by management.	N/A	N/A
D.	For which no management decision was made by the end of the reporting period.	0	0
E.	For which no management decision was made within six months of issuance.	0	0

Recommendations that "Funds to be put to Better Use" are those OIG recommendations that funds could be used more efficiently if management took actions to reduce outlays, de-obligate funds from programs/operations, avoid unnecessary expenditures noted in pre-award reviews of contracts, or any other specifically identified savings.



TABLE III: SUMMARY OF OIG ACTIVITY

April 1 through September 30, 2015

Part I – Audit Reports Issued

Report Number	Title	Date Issued
OIG-15-08	Coordination of Responsibilities Among the Consumer Financial Protection Bureau and the Prudential Regulators – A Limited Scope Review	6/1/2015
OIG-15-09	Audit of NCUA’s Measures to Protect Electronic Credit Union Member Information During the Examination Process	6/8/2015

Part II – Audits in Progress (*as of September 30, 2015*)


Interest Rate Risk
Financial Stability Oversight Council (FSOC) Interest Rate Risk
Restitution Orders
Review of National Credit Union Administration's Purchase and Travel Card Programs



INDEX OF REPORTING REQUIREMENTS		
Section	Data Required	Page Ref
4(a)(2)	Review of legislation and regulations	25
5(a)(1)	Significant problems, abuses, or deficiencies relating to the administration of programs and operations disclosed during the reporting period.	13
5(a)(3)	Recommendations with respect to significant problems, abuses or deficiencies	13
5(a)(3)	Significant recommendations described in previous semiannual reports on which corrective action has not been completed.	15
5(a)(4)	Summary of matters referred to prosecution authorities and prosecutions which have resulted.	None
5(a)(5)	Summary of each report to the Board detailing cases where access to all records was not provided or where information was refused.	None
5(a)(6)	List of audit reports issued during the reporting period.	28
5(a)(7)	Summary of particularly significant reports.	13
5(a)(8)	Statistical tables on audit reports with questioned costs.	26
5(a)(9)	Statistical tables on audit reports with recommendations that funds be put to better use.	27
5(a)(10)	Summary of each audit report issued before the start of the reporting period for which no management decision has been made by the end of the reporting period.	None
5(a)(11)	Description and explanation of reasons for any significant revised management decision made during the reporting period.	None
5(a)(12)	Information concerning significant management decisions with which the Inspector General is in disagreement.	None
5(a)(14)	An appendix containing the results of any peer review conducted by another OIG during the reporting period or, if no peer review was conducted within that reporting period, a statement identifying the date of the last peer review conducted by another OIG.	30
5(a)(15)	List of outstanding recommendations from any peer review conducted by another OIG that have not been fully implemented.	None
5(a)(16)	A list of any peer reviews conducted by the IG of another OIG during the reporting period, including a list of any outstanding recommendations made that remain outstanding or have not been fully implemented.	19



Appendix A: System Review Report (Peer Review of NCUA OIG)



Office of Inspector General

Office
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OIG Reports

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OIG@peacecorps.gov

System Review Report

February 4, 2013

William DeSarno
Inspector General
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Mr. DeSarno,

We have reviewed the system of quality control for the audit organization of National Credit Union Administration (NCUA), Office of Inspector General (OIG) in effect for the year ended December 31, 2012. A system of quality control encompasses NCUA OIG’s organizational structure and the policies adopted and procedures established to provide it with reasonable assurance of conforming with *Government Auditing Standards*. The elements of quality control are described in *Government Auditing Standards*. NCUA OIG is responsible for designing a system of quality control and complying with it to provide NCUA OIG with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and NCUA OIG’s compliance therewith based on our review.

Our review was conducted in accordance with *Government Auditing Standards* and guidelines established by the Council of the Inspectors General on Integrity and Efficiency (CIGIE). During our review, we interviewed NCUA OIG personnel and obtained an understanding of the nature of the NCUA OIG audit organization, and the design of the NCUA OIG’s system of quality control sufficient to assess the risks implicit in its audit function. Based on our assessments, we selected engagements and administrative files to test for conformity with professional standards and compliance with the NCUA OIG’s system of quality control. The engagements selected represented a reasonable cross-section of the NCUA OIG’s audit organization, with emphasis on higher-risk engagements. Prior to concluding the review, we reassessed the adequacy of the scope of the peer review procedures and met with NCUA OIG management to discuss the results of our review. We believe that the procedures we performed provide a reasonable basis for our opinion.

In performing our review, we obtained an understanding of the system of quality control for the NCUA OIG’s audit organization. In addition, we tested compliance with the NCUA OIG’s quality control policies and procedures to the extent we considered appropriate. These tests covered the application of the NCUA OIG’s policies and procedures on selected engagements Enclosure 1 to this report identifies the offices of the NCUA OIG that we visited and the engagements that we reviewed. Our review was based on selected tests; therefore, it would not necessarily detect all weaknesses in the system of quality control or all instances of noncompliance with it.

There are inherent limitations in the effectiveness of any system of quality control, and therefore noncompliance with the system of quality control may occur and not be detected. Projection of any evaluation of a system of quality control to future periods is subject to the risk that the system of quality control may become inadequate because of changes in conditions, or because the degree of compliance with the policies or procedures may deteriorate.

1



In our opinion, the system of quality control for the audit organization of NCUA OIG in effect for the year ended December 31, 2012, has been suitably designed and complied with to provide NCUA OIG with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Federal audit organizations can receive a rating of *pass*, *pass with deficiencies*, or *fail*. NCUA OIG has received a peer review rating of *pass*.

In addition to reviewing its system of quality control to ensure adherence with *Government Auditing Standards*, we applied certain limited procedures in accordance with guidance established by the CIGIE related to NCUA OIG's monitoring of engagements performed by Independent Public Accountants (IPA) under contract where the IPA served as the principal auditor. It should be noted that monitoring of engagements performed by IPAs is not an audit and therefore is not subject to the requirements of *Government Auditing Standards*. The purpose of our limited procedures was to determine whether NCUA OIG had controls to ensure IPAs performed contracted work in accordance with professional standards. However, our objective was not to express an opinion and accordingly, we do not express an opinion, on NCUA OIG's monitoring of work performed by IPAs.

Sincerely,

A handwritten signature in black ink, appearing to read "Kathy A. Buller".

Kathy A. Buller
Inspector General

Enclosure