

NATIONAL CREDIT UNION ADMINISTRATION
OFFICE OF INSPECTOR GENERAL

REVIEW OF NCUA'S EXAMINATION
AND COMPLAINT PROCESSES FOR
SMALL CREDIT UNIONS

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ACRONYMS AND ABBREVIATIONS

ADR	Alternative Dispute Resolution
AIRES	Automated Integrated Regulatory Examination Software
ARDP	Assistant Regional Director Programs
ARDO	Assistant Regional Director Operations
BAM	Board Action Memorandum
DCCO	Division of Consumer Compliance and Outreach
DOS	Division of Supervision
E&I	Division of Examination and Insurance
EIC	Examiner-in-Charge
FCU	Federal Credit Union
FCU Act	Federal Credit Union Act
FDIC	Federal Deposit Insurance Corporation
FISCU	Federally Insured State-Chartered Credit Union
FRB	Federal Reserve Board
IDP	Individual Development Plan
IRPS	Interpretive Ruling and Policy Statement
MARS	Management Automated Resource System
NCUA	National Credit Union Administration
NCUSIF	National Credit Union Share Insurance Fund
NSPM	National Supervision Policy Manual
OCP	Office of Consumer Protection
OED	Office of the Executive Director
OGC	Office of General Counsel
OIG	Office of Inspector General
PE	Principal Examiner
QCR	Quality Control Review
RD	Regional Director
Riegle Act	Riegle Community Development and Regulatory Improvement Act of 1994
RFE	Risk-Focused Examination Program
SCUEP	Small Credit Union Examination Program
SRC	Supervisory Review Committee
SE	Supervisory Examiner
Treasury	U.S. Department of the Treasury
WCC	Work Classification Code

Preface

On February 10, 2012, the National Credit Union Administration (NCUA) Office of Inspector General (OIG), along with Inspectors General at the U.S. Department of the Treasury (Treasury), the Federal Reserve Board (FRB), and the Federal Deposit Insurance Corporation (FDIC), received a request from Senator Tim Johnson, Chairman, United States Senate, Committee on Banking, Housing, and Urban Affairs, to conduct an audit at each agency under their purview regarding each agency's examination process for small community banks and credit unions.

Although NCUA defines small credit unions as those having \$10 million or less in assets, all natural-person credit unions with assets less than \$1 billion are examined using the same Risk-Focused Examination (RFE) process. Therefore, the results of this report apply to all natural-person credit unions with \$1 billion or less in assets. Consequently, this report on NCUA's examination process covers over 97 percent of all federally insured credit unions.¹

In addition, the Senator's request also asked the Inspectors General to include examination timelines and discuss how agencies ensure consistency in the administration of examinations across the country, as well as the ability of regulated institutions to question examination results such as through an Ombudsman, an appeals process, or informal channels, and the frequency and success of such appeals.

This report outlines NCUA's policies, procedures, and processes for examinations and complaints, and provides the OIG's assessment of NCUA's adherence to its guidance. This report makes four recommendations, which the OIG believes can improve NCUA's examination and complaint processes, as well as assist Chairman Johnson and members of the Senate Committee on Banking, Housing, and Urban Affairs better understand these areas of NCUA's programs.

¹ The results of this review do not pertain to Corporate Credit Union examinations, which do not use the RFE program. Additionally, in January 2012, NCUA examinations of small credit unions – those with less than \$10 million in assets – are examined under the Small Credit Union Examination Program (SCUEP), which still uses the same RFE program, but has different minimum scope requirements. This reduced scope only applies to small credit unions that are operationally sound and have lower risk (CAMEL 1, 2, and 3) ratings.

Executive Summary

At the request of the Chairman of the Senate Committee on Banking, Housing, and Urban Affairs, the NCUA-OIG conducted a review of NCUA's examination and complaint processes to determine: (1) the NCUA's examination process for small credit unions; and (2) the ability of insured credit unions to question examination results. Consistent with the request, we placed a particular emphasis on reviewing examination policies and procedures, as well as examination timeliness to determine how NCUA ensures consistency on a national basis in the administration of examinations, including the tools to accomplish the process. Our review also concentrated on complaints related to safety and soundness issues to ensure credit unions can seek informal review of disputed issues at the examiner/regional level, as well as through a formal appeals process. To achieve these objectives, we interviewed management and staff and/or obtained documentation from NCUA's Office of the Executive Director (OED); Office of Examination and Insurance (E&I); Office of Consumer Protection (OCP); Office of General Counsel (OGC); and each of NCUA's five regional offices. We reviewed NCUA policies and procedures related to examination and complaint processes and benchmarked with our counterparts from the other Federal agencies identified in the Senate Committee's request.²

Overall, we determined NCUA's examination process has clear standards and policies to conduct examinations. However, we noted inconsistencies in the manner in which NCUA carried out the procedures to implement those policies. Despite inconsistencies in the manner in which NCUA implemented its examination policies, we are not making recommendations to the examination process because NCUA has recently implemented a National Supervision Policy Manual (NSPM) that we believe addresses the inconsistent procedures we noted.

In addition, we determined NCUA has an adequate appeals process, which allows credit unions to question examination results. However, we determined there are operational and organizational deficiencies related to compliance monitoring, the regional determination process, the Supervisory Review Committee (SRC), and the Ombudsman position, respectively, which we believe NCUA management could improve. As a result, we are making four recommendations to correct identified deficiencies.

We appreciate the cooperation and courtesies NCUA management and staff provided to us during this review.

² We benchmarked with OIG staff from FDIC, FRB, and Treasury.

Background

Examination Process

The Federal Credit Union Act (FCU Act)³ requires each federally insured credit union be subject to examination by any person designated by the NCUA Board.

The principal method by which NCUA carries out its supervisory responsibility is through on-site examinations. These examinations, designed to determine the risk to the National Credit Union Share Insurance Fund (NCUSIF), focus on a credit union's ability to identify, measure, monitor, and control risk. As of June 2012, NCUA supervised 6,960 natural-person credit unions, of which 4,366 (63 percent) were federally insured federal credit unions (FCUs) and 2,594 (37 percent) were federally insured, state chartered credit unions (FISCUs).

NCUA encourages examiners to discuss problems and/or conditions that impair or may impair the safety and soundness of the credit union with the appropriate credit union officials and employees throughout the examination. At the conclusion of the examination, examiners prepare and provide officials with a written report highlighting the results of the examination. The credit union's board of directors and committee members use the report to take necessary corrective actions to ensure the identified problems are corrected.

In addition to providing credit union officials with a report of examination, through conferences with officials, examiners also assist in the development of plans designed to overcome underlying causes of current or potential problems. This further ensures officials understand what must be done to improve operations.

Examiner Guidance

During the scope period of our review, NCUA used the Examiner's Guide to provide guidance to examiners conducting examinations and supervision contacts of credit unions. In addition to the Examiner's Guide, each of NCUA's five regions has long had its own unique regional supervision manuals⁴ to instruct and guide examiners in carrying out supervision and examinations of credit unions in accordance with regional policies. On July 1, 2012, NCUA issued the new NSPM to instruct and guide examiners in the supervision and examination of credit unions on a national level.

Total Analysis Process

NCUA uses a total analysis process which includes: collecting, reviewing, and interpreting data; reaching conclusions; making recommendations; and developing

³ FCU Act, 12 U.S.C., §1756 – *Reports and Examinations*.

⁴ Regional Directors (RD) based their regional supervision manuals on the Examiner's Guide, as well as incorporating NCUA Instructions, Directives, and Supervisory Letters issued to field staff on any number of examination-related topics.

action plans. The objectives of the total analysis process include evaluating CAMEL⁵ components, and reviewing qualitative and quantitative measures.

NCUA uses the CAMEL Rating System to provide an accurate and consistent assessment of a credit union's financial condition and operations. The CAMEL rating includes consideration of key ratios, supporting ratios, and trends. Generally, examiners use the key ratios to evaluate and appraise the credit union's overall financial condition. During an examination, examiners assign a CAMEL rating, which completes the examination process.

Examiner judgment affects the overall analytical process. An examiner's review of data includes structural analysis,⁶ trend analysis,⁷ reasonableness analysis,⁸ variable data analysis,⁹ and qualitative data analysis.¹⁰ Numerous ratios measuring a variety of credit union functions provide the basis for analysis. Examiners must understand these ratios both individually and as a group because some individual ratios may not provide an accurate picture without a review of the related trends. Financial indicators such as adverse trends, unusual growth patterns, or concentration activities can serve as triggers of changing risk and possible causes for future problems. NCUA also instructs examiners to look behind the numbers to determine the significance of the supporting ratios and trends. Furthermore, NCUA requires examiners to determine whether material negative trends exist; ascertain the action needed to reverse unfavorable trends; and formulate, with credit union management, recommendations and plans to ensure implementation of these actions.

Risk-Focused Examination Program

In 2002, NCUA implemented the Risk-Focused Examination (RFE) program.¹¹ Risk-focused examinations are not audits. The RFE objectives are to determine whether a credit union is financially sound and whether officials conduct operations in compliance with applicable laws and regulations.

Supervision is the ongoing monitoring of a credit union's financial and operational condition. Risk-focused supervision procedures often include both off-site and on-site work that includes reviewing off-site monitoring tools and risk evaluation reports. During

⁵ The acronym CAMEL derived its name from the following examination components: [C]apital Adequacy, [A]sset Quality, [M]anagement, [E]arnings, and [L]iquidity/Asset-Liability Management.

⁶ Structural analysis includes the review of the component parts of a financial statement in relation to the complete financial statement.

⁷ Trend analysis involves comparing the component parts of a structural ratio to itself over several periods.

⁸ As needed, the examiner performs reasonableness tests to ensure the accuracy of financial performance ratios.

⁹ Examiners can often analyze an examination area in many different ways. NCUA's total analysis process enables examiners to look beyond the "static" balance sheet figures to assess the financial condition, quality of service, and risk potential.

¹⁰ Qualitative data includes information and conditions that are not measurable in dollars and cents, percentages, numbers, etc., which have an important bearing on the credit union's current condition, and its future. Qualitative data analysis may include assessing lending policies and practices, internal controls, attitude and ability of the officials, risk measurement tools, risk management, and economic conditions.

¹¹ Letter to Federal Credit Unions 02-FCU-09, *Risk-Focused Examination Program*, May 2002.

supervision within the risk-focused program, the examiner looks forward at the direction a credit union will take and the decisions it will make. Examiners can then anticipate when those decisions might result in the credit union assuming undue risk or failing to manage the risk it has taken. Examiners may determine or adjust the timing of the examination based on conditions revealed during the supervision process.

The RFE process includes reviewing seven categories of risk: *Credit, Interest Rate, Liquidity, Transaction, Compliance, Strategic, and Reputation*. Examination planning tasks may include: (a) reviewing the prior examination report to identify the credit union's highest risk areas and areas that require examiner follow-up, and (b) analyzing Call Report and Financial Performance Report trends. The extent of supervision plans depends largely on the severity and direction of the risks detected in the credit union's operation and on management's demonstrated ability to manage those risks. A credit union's risk profile may change between examinations. Therefore, the supervision process encourages examiners to identify those changes in profile through the following:

- Review of Call Reports
- Communication with credit union staff
- Knowledge of current events affecting the credit union

On November 20, 2008, the NCUA Board approved changes to the risk-based examination scheduling policy, creating the Annual Examination Scheduling Program.¹² NCUA indicated these changes were necessary due to adverse economic conditions and distress in the nation's entire financial structure, which placed credit unions at greater risk of loss. NCUA stated at the time that this new program would provide more timely relevant qualitative and quantitative data to recognize any sudden turn in a credit union's performance.

In 2009, NCUA developed a new examination policy¹³ that resulted in additional minimum required examination procedures based on a national review of risk. The policy directed a periodic national review of risk issues and adjustment to the minimum review procedures. NCUA indicated the intent of the policy was to shape its examination and supervision program to consistently identify and mitigate emerging risks in response to changing environmental factors within the credit union industry. As a result of this policy, E&I, with input from the regions, now updates the minimum scope procedures, as necessary, by focusing on emerging risks, risk monitoring observations, results of quality control reviews, regulatory changes, and lessons learned from NCUA OIG Material Loss Reviews.

¹² The Annual Examination Scheduling Program requires either an examination or a material on-site supervision contact within a 10 to 14 month timeframe based on risk-based scheduling eligibility. Maximum and minimum time between the completion dates of one examination to the completion date of the next examination is 23 months and 8 months, respectively.

¹³ NCUA revised this policy with Instruction No. 5000.20 (Rev. 4), *Risk-Focused Examinations – Minimum Scope Requirements*, on June 25, 2012.

In 2011, NCUA's Region I piloted a Small Credit Union Examination Program (SCUEP) to determine whether examination resources could be better aligned with industry risks. Essentially, the SCUEP expanded the minimum required examination scope for nationally identified areas of elevated risk and reduced the minimum required examination scope in CAMEL 1, 2, or 3 FCUs with less than \$10 million in total assets.

Based on the success of the pilot, NCUA established the SCUEP on a national basis in January 2012. NCUA officials indicated that the new scope requirements supplement existing RFE practices and do not replace the examiner's judgment and responsibility to refine and adjust their scope, noting that examiners should continue to follow the concepts of the RFE process outlined in the Examiner's Guide for areas of elevated risk. For a complete list of current SCUEP minimum scope requirements and minimum required questionnaires examiners are to complete, see Appendix A.

Complaint Process

In 1994, Congress enacted the *Riegle Community Development and Regulatory Improvement Act of 1994*¹⁴ (Riegle Act). Section 309 of the Riegle Act required, among other things, that the NCUA and the federal banking agencies each establish an independent appellate process to review material supervisory determinations. Specifically, the Riegle Act required the NCUA to establish:

[a]n independent intra-agency review process for material supervisory determinations, appoint an Ombudsman, and develop an alternative dispute resolution program.

In response, the NCUA Board: (1) established an SRC; (2) established an Ombudsman position; and (3) issued an alternative dispute resolution (ADR) program Policy Statement.¹⁵

Examiner and Supervisory Examiner (SE) Appeals

NCUA policy requires examiners to maintain good communication with all credit unions it supervises by encouraging that disagreements get resolved informally and expeditiously during the normal course of an examination. The first step of the appeals process is informal complaint resolution, which generally consists of credit union management working through disagreements at the examiner or SE level before examination report issuance.

¹⁴ Public Law No.: 103-325, §309(a), 108 Stat. 2160.

¹⁵ 61 FR 11433-34 (March 20, 1996). Section 309(e) of the Riegle Act envisioned the use of ADR methods to resolve (a) claims against insured credit unions for which NCUA has been appointed conservator or liquidating agent; (b) actions taken by NCUA in its capacity as conservator or liquidating agent; and (3) any other issue for which the NCUA Board determines that ADR would be appropriate. In this regard, see NCUA Regulations at 12 CFR § 709.8(c).

Regional Director Appeals

If, after receiving an examiner's final determination, credit union management still does not agree with the report results, FCUs and FISCUs can request a regional determination. Credit unions seeking a regional determination must contact the region within 30 days of the examiner's final determination. After receiving the credit union's request, the regional office first verifies that an NCUA examiner made the determination. If so, the region will handle the dispute. A credit union may file an appeal to the SRC either 30 days after the RD has made its determination, or 60 days after contacting the regional office if the region has not made a determination. If the regional office determines a state examiner made the decision, the region will turn the appeal over to the appropriate state regulatory authority for a determination.

The SRC consists of three members of NCUA's senior staff appointed by the NCUA Chairman. None of the members may simultaneously serve as Regional Director, Associate Regional Director, Executive Director, Director of the Office of Small Credit Union Initiatives, or Senior Policy Advisor or Chief of Staff to a Board Member. The NCUA Chairman designates one member as chairperson and all three committee members serve for one-year terms and may be reappointed for additional terms. Each member of the SRC has one vote and a quorum (two members) must be present at each meeting, which is held in person or via teleconference. A majority vote of the full SRC (two votes) is required for action on an appeal.

Ombudsman

In a Board Action Memorandum (BAM) approved by the NCUA Board on March 13, 1995, the Board established an Ombudsman position. In the BAM, the Board stated that the Ombudsman position (1) would be held by an existing NCUA employee appointed by the Chairman; (2) the functions of the position would be collateral to the appointee's current duties; and (3) the Ombudsman would report to the NCUA Board. In addition, the Board authorized the appointee to act independently of NCUA program functions and have access to agency records. The Board further authorized the Ombudsman to keep confidential any information and material he/she obtained as a result of investigating complaints.

Objectives, Scope, and Methodology

The objectives of our review were to determine: (1) NCUA's examination process for small credit unions; and (2) the ability of insured credit unions to question examination results. Within these objectives, we placed a particular emphasis upon reviewing examination timelines and how NCUA ensures consistency in the administration of examinations across the country. In addition, we reviewed NCUA's SRC and the role of the Ombudsman within the OCP.

The scope of our review covered the current examination process and complaints (safety and soundness related, as well as consumer) during the five-year period from January 1, 2007 to December 31, 2011.

To accomplish our objectives we:

- Interviewed management and staff in NCUA's OED, E&I, OCP, OGC; and reviewed documentation received from each of the five regional offices;
- Reviewed NCUA policies and procedures related to examination and complaint processes; and
- Analyzed examination and complaint data.

We conducted this review from March 2012 through August 2012 in accordance with generally accepted government auditing standards, and included such tests of internal controls as we considered necessary under the circumstances. Those standards require that we plan and perform the review to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our review objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our review objectives.

Results in Detail

Overall, we determined NCUA's examination process for small credit unions has clear standards and policies to conduct examinations. However, inconsistencies existed in the manner in which NCUA carried out the procedures to implement those policies. In addition, we determined NCUA has a robust appeals process which allows credit unions to question examination results. However, we determined there are operational and organizational deficiencies related to regional determinations, the SRC, and the Ombudsman position, respectively, that NCUA management could improve.

A. Examination Process

**Clear Policies, but
Inconsistently
Applied Examination
Procedures**

We determined NCUA management has provided examiners with clear standards and policies governing its examination process. However, inconsistencies existed in how NCUA allowed its examiners to carry out those policies. Specifically, we found NCUA management provides examiners with sufficient national guidance

through its policies and tools to ensure credit unions, nationally, receive a thorough and professionally conducted examination or supervision contact. However, we believe the agency's organizational structure – consisting of five separately run regional offices, each having its own supervision manual – may have created quality control issues, which contributed to the perception that nationally, examiners conducted examinations with *"inconsistent application of agency policies and procedures"* as stated in the Senate Committee's February 10, 2012, letter to the OIG.

For well over a decade, NCUA's five regional offices have each had in place its own unique supervision manuals that incorporated NCUA's national Examiner's Guide and other related policies, instructions, and directives for overseeing and conducting RFEs. However, we determined no two regional supervision manuals were the same, with each region having its own customized approach to conducting RFEs.

When the economic downturn occurred in 2008, NCUA reorganized two regions that were once defined geographically in order to better optimize resources. NCUA officials moved supervision responsibility of all California credit unions from Region V to Region II and supervision of all Nevada credit unions from Region V to Region I. After the reorganization, NCUA officials received feedback from regional office management and field staff about quality control issues related to conducting RFEs and realized they needed to implement a national supervision manual to provide consistent guidance to examiners and supervisors, rather than allowing the continued use of five separate regional manuals.

The process to develop the NSPM began in earnest in May 2010 and used a bottom-up approach that initially began with representatives from each regional office helping create a draft manual based largely on regional policies. Following the development of the draft manual, a national working group made substantive changes based on input

from groups made up of regional management and examination staff, as well as management and staff at NCUA's Central Office. Additionally, in November 2010, the OIG issued its MLR Capping Report with recommendations to NCUA management for several changes to the examination process, which were eventually incorporated into the new supervision manual.

Prior to finalizing the NSPM in April 2012, NCUA held comprehensive examiner training at its National Training Conference where agency trainers outlined the new NSPM and received constructive feedback. By conducting the training at the conference, NCUA officials assured themselves that all examiners, regardless of region, heard the same message, which NCUA officials indicated would result in a more consistent message regarding supervision and examination standards for credit unions.

On July 1, 2012, NCUA management issued its new NSPM, which incorporates, by reference, the Examiner's Guide, NCUA instructions, Letters to Credit Unions, and other directives and guidance on the examination process.

NCUA officials described the purpose of creating the NSPM as the removal of regional differences in quality control by standardizing the most effective supervision policies of the five regions and implementing them nationally to ensure greater consistency in examinations and supervision practices as regions share examiner resources. We agree with NCUA officials and believe that moving forward, the new single NSPM – not five regional variations – will provide greater quality control and direction to all examiners, thereby creating consistency in the examination process. As a result of the recently implemented NSPM, we believe NCUA management has taken appropriate action to correct the identified deficiency and are therefore making no recommendations at this time.

Clear Standards and Adequate Tools for the Examination Process

As previously noted, we determined NCUA provided examiners with clear standards and policies for the examination process, as well as adequate tools to ensure examiners provide credit unions with professionally conducted examinations and supervisory contacts.

During the scope period of our review, the Examiner's Guide served as NCUA's national reference manual, which the examiners used to supplement regional procedures. Revised in 2002 to incorporate the RFE program, the Examiner's Guide provided clear and concise standards, which provided examiners with sound fundamental examination protocol to ensure the overall safety and soundness of the credit union system. However, as discussed above, the Examiner's Guide had become outdated and NCUA needed a different approach to ensure consistent examinations across regional offices.

We believe the new NSPM is a comprehensive source of guidance for examiners, supervisors, regional offices, and Central Office staff. The focus of the NSPM is on providing examiners and supervisors with thorough and concise national instruction for

performing examinations and supervisory contacts through an across-the-board approach that guides examiners from planning through execution and follow-up.

NCUA divided the NSPM into 12 Chapters, incorporating all examination-related instructions and bulletins by reference within each chapter, as appropriate. The NSPM covers key examination topics such as:

- FCU and FISCU Programs and Procedures;
- Quality Assurance;
- Audits, Recordkeeping, and Fraud;
- Regulatory Waivers, Change of Officials, and other Regulatory Actions;
- Credit Union Service Organizations;
- Office of Small Credit Union Initiatives and the National Small Credit Union Program;
- Bank Secrecy Act Enforcement; and
- Prompt Corrective Action and Administrative Remedies.

Although regional policies and procedures historically adhered to national standards, we believe the NSPM provides one comprehensive document, which ensures a consistent method regarding how examiners should conduct a complete and thorough risk-focused examination or supervision contact.

In addition to relying on written guidance to direct and control the examination process, NCUA relies on tools which include software such as NCUA's Automated Integrated Regulatory Examination Software (AIRES) and Management Automated Resource System (MARS) to ensure consistent data capture and analysis. Other tools include examiner training initiatives such as annually developed Individual Development Plans (IDP) to ensure examiners receive levels of training commensurate with their experience, as well as attendance at national and regional training conferences and webinars, both of which we believe contribute to an effective and consistent examination environment.

Examinations Completed Timely

We determined that NCUA, on average, ensures the completion of examinations and supervision contacts well within established timeframes. NCUA guidelines state examiners should complete all examinations/supervision contacts within 60 calendar days from the start date, with supervisory approval needed to extend the completion timeframe if completion within 60 days is not possible.

We determined that nationally, NCUA completed regular FCU examinations (Work Classification Code (WCC) 10)¹⁶ in an average of 28 days, and regular joint FISCU

¹⁶ WCC 10 is a regular examination of a federally chartered credit union.

examinations (Work Classification Code (WCC) 11)¹⁷ in an average of 32 days. In addition, our analysis showed, predictably, those credit unions with CAMEL composite ratings of 1 or 2 took fewer days to complete than did credit unions with CAMEL 4 or 5 composite ratings. In fact, for FCU examinations, NCUA was able to complete CAMEL 1 and 2 composite rated credit union examinations an average of anywhere from six to eighteen days sooner. In all cases, however, NCUA far exceeded expectations with an average duration to complete examinations within the 60-day timeframe.

Table 1 (below) provides NCUA's average number of days to complete a regular examination for FCUs and FISCUs, broken down by regional office, CAMEL rating, and asset size for WCCs 10 and 11, during the period from January 2007 through December 2011.

¹⁷ WCC 11 is a regular joint examination or insurance review of any state chartered credit union.

Table 1

Average Days Duration – FCU (WCC 10) and FISCU (WCC 11) Examinations January 1, 2007 through December 31, 2011												
	Region I		Region II		Region III		Region IV		Region V		National Averages**	
	WCC		WCC		WCC		WCC		WCC		WCC	
	10	11	10	11	10	11	10	11	10	11	10	11
CAMEL 1	28	33	35	52	19	25	22	25	28	32	26	32
<\$2M	26	14	26		14	9	17	7	64		22	9
<\$10M	22		24		15	13	18	17	18	16	19	15
<\$50M	26	17	31		19	11	20	26	24	18	23	20
<\$100M	26	72	36	59	22	24	23	21	32		27	36
<\$500M	31	29	37	66	23	25	26	25	32	11	30	28
\$500M or >	39	37	49	49	21	27	37	28	37	37	37	35
CAMEL 2	30	35	32	45	20	24	23	26	27	31	27	31
<\$2M	27	9	27	15	16	8	20	20	20	16	23	17
<\$10M	27	34	28	36	18	20	21	20	23	10	24	23
<\$50M	30	28	31	31	21	19	23	20	27	26	26	22
<\$100M	32	33	39	38	23	19	26	26	30	29	31	28
<\$500M	33	34	40	40	23	23	30	29	37	28	33	31
\$500M or >	42	43	48	56	24	29	35	33	35	41	39	40
CAMEL 3	32	41	34	46	23	25	26	28	30	29	29	32
<\$2M	29	27	29	45	21	9	25	21	23	15	27	25
<\$10M	29	29	32	35	21	12	24	27	24	27	27	26
<\$50M	33	38	36	42	23	18	26	26	30	19	30	28
<\$100M	39	40	43	45	25	22	33	34	33	34	36	36
<\$500M	40	47	48	43	29	30	31	31	39	29	39	37
\$500M or >	47	61	56	57	33	39	33	38	49	41	43	48
CAMEL 4	34	41	43	49	24	30	27	30	31	30	33	36
<\$2M	35	27	37	52	22	15	27	32	19	33	29	31
<\$10M	32	32	38	37	21	25	26	24	28	32	29	28
<\$50M	32	37	41	43	27	26	26	26	31	22	33	31
<\$100M	37	40	57	41	32	88	44	35	41	27	46	38
<\$500M	49	65	53	56	34	30	43	34	38	32	46	43
\$500M or >	42	72	58	52	58	47		43	39	46	51	50
CAMEL 5	64	56	49	62	29	32	22	26	45	44	44	44
<\$2M	55	47	53		20		21	24		35	38	32
<\$10M	48		52		44	34	26		26	57	45	45
<\$50M	40	62	36	56				30	44		40	53
<\$100M	196	55				29				42	196	44
<\$500M	39		36	65	18				67		40	65
National Average	30	38	34	47	21	25	24	27	28	31	28	32

Source: AIREs

** Any discrepancies in the National Averages are due to rounding.

Resource Hours Adequately Budgeted

During our review we determined NCUA does not have a policy that expressly establishes a targeted number of hours examiners are expected to adhere to when conducting examinations and supervision contacts. Rather, NCUA's national policy

uses a tiered approach to annually budget hours and resources to ensure examiners allocate budget hours consistent with the size, complexity, and risk profile of individual credit unions.¹⁸ NCUA then expects examiners to adhere to the approved budgeted hours for their assigned credit unions and must justify and obtain approval for exceeding the budgeted hours.

NCUA guidance states:

Budgeting and scheduling of examination work is critical to effectively manage resources and ensure timely examinations/supervision contacts. Appropriate scheduling ensures resource allocation can be directed to the credit unions of regional and national significance as needs arise and helps to ensure the NCUA achieves its mission.

Although we found no criterion which expressly established an average number of hours to complete examinations, we determined that nationally, NCUA completed all regular FCU examinations in an average of 96 hours, and regular joint FISCU examinations in an average of 117 hours. Similar to our analysis of the average number of days in Table 1, our analysis of NCUA's average number of hours to complete examinations was lower for credit unions with CAMEL composite ratings of 1 or 2 than credit unions with CAMEL composite ratings of 4 or 5. Specifically, NCUA was able to complete CAMEL 1 composite rated FCU examinations versus CAMEL 5 composite rated FCUs an average of 61 hours sooner. We believe this difference in hours is attributable to the greater time commitment involved in working on troubled institutions.

Table 2 (below) provides NCUA's average number of hours to complete a regular examination for FCUs and FISCUs broken down by regional office, CAMEL rating, and asset size for WCCs 10 and 11, during the period from January 2007 through December 2011.

¹⁸ With the establishment of the SCUPEP, NCUA requires an average target time of 40 hours to complete small credit union examinations, but acknowledges actual exam hours can vary depending on the complexity of the credit union and problems identified.

Table 2

Average Hours – FCU (WCC 10) and FISCU (WCC 11) Examinations January 1, 2007 through December 31, 2011												
	Region I		Region II		Region III		Region IV		Region V		National Averages**	
	WCC		WCC		WCC		WCC		WCC		WCC	
	10	11	10	11	10	11	10	11	10	11	10	11
CAMEL 1	128	136	141	161	101	143	109	120	129	147	120	137
<\$2M	39	9	46		36	40	42	13	42		41	19
<\$10M	48		54		44	69	47	24	52	49	48	47
<\$50M	71	80	75		61	54	69	31	80	45	70	45
<\$100M	108	80	109	58	92	38	104	34	112		105	45
<\$500M	168	99	167	78	159	115	176	92	167	102	168	96
\$500M or >	316	171	367	187	246	170	339	175	311	164	318	173
CAMEL 2	93	110	95	152	80	139	84	104	102	120	90	119
<\$2M	46	20	48	137	40	29	41	24	47	27	45	37
<\$10M	57	38	56	38	49	42	53	33	59	33	54	35
<\$50M	82	48	84	45	71	49	81	44	86	52	80	46
<\$100M	125	75	129	85	110	75	130	63	119	94	123	73
<\$500M	195	106	191	125	167	141	194	112	187	105	185	116
\$500M or >	371	181	337	228	298	230	332	226	308	174	332	208
CAMEL 3	91	102	88	166	83	142	85	68	116	104	89	98
<\$2M	51	38	50	40	46	35	48	31	51	36	49	33
<\$10M	66	45	65	52	57	36	62	39	67	43	63	40
<\$50M	104	62	101	80	87	74	104	54	97	55	98	60
<\$100M	143	99	155	110	130	121	158	82	156	95	149	97
<\$500M	234	141	218	195	218	146	210	124	223	130	220	144
\$500M or >	407	202	410	311	325	325	378	282	380	203	369	279
CAMEL 4	123	114	140	205	94	108	80	106	159	148	117	134
<\$2M	64	42	61	58	53	35	54	31	58	36	57	35
<\$10M	96	54	90	62	67	49	74	49	96	61	82	53
<\$50M	135	85	133	104	113	87	122	63	125	76	127	78
<\$100M	271	127	214	134	180	113	231	145	214	121	217	133
<\$500M	316	240	324	237	279	142	295	258	301	207	310	224
\$500M or >	320	513	425	358	473	399		696	405	285	411	412
CAMEL 5	344	326	176	1,060	120	182	70	192	153	162	181	310
<\$2M	130	134	87		68		70	200		37	84	135
<\$10M	289		213		155	197	69		66	212	184	205
<\$50M	242	244	427	285				169	83		250	235
<\$100M	1,247	504				152				187	1,247	253
<\$500M	399		206	1,447	238				379		305	1,447
National Average	99	113	100	174	85	138	89	90	112	124	96	117

Source: AIRES

** Any discrepancies in National Averages are due to rounding.

NCUA's budgeting process for planning examination resource hours begins with examiners. Examiners are responsible and accountable for using historical knowledge of the credit unions assigned to them in their district. Examiners use modules in MARS and ARIES to view previously recommended examination and supervision hours for

each district credit union. Based on this information, examiners submit recommended estimated hours to their supervisor during an annual resource planning process.

In addition, examiners may recommend specialized resources in consultation with their supervisor when the size, complexity, or potential risk to the NCUSIF warrants the use of specialized expertise such as Regional office staff, Central office staff, Asset Management Assistance Center staff, and outside contractors.¹⁹ Examiners are also required to consult with their supervisors during the year if conditions warrant changes to the examination budget.

Supervisory Examiners are responsible and accountable for:

- Managing resources on an ongoing basis throughout the year to ensure examiners are properly developed and that examination and supervision programs are adequately completed;
- Managing resources to effectively examine large, complex and problematic institutions;
- Evaluating the annual budget recommendation (resources and scheduling) for their group after consultation with examiners in their district;
- Monitoring and reconciling group budgets monthly using the MARS online system and according to Assistant Regional Director, Programs (ARDP) direction; and
- Reporting the group program status, variances, and shortfalls to the ARDP monthly, and adjust budgets, or request assistance when group resources are not sufficient to complete the examination program, or as conditions warrant.

ARDPs are responsible and accountable for:

- Managing the regional resources budget and keeping the Regional Directors (RD) informed of the status of regional examination/supervision programs;
- Reallocating regional resources and coordinating with the Assistant Regional Director, Operations (ARDO)/ARDPs/RD to secure assistance when group resources are not sufficient; and
- Ensuring all workload budgets are reconciled by the 10th of each month.

¹⁹ Specialized expertise at the regional and central offices can include Subject Matter Examiners (SME) in such examination areas as: Capital Markets, Consumer Compliance, Electronic Payment Systems, Information Systems and Technology, and Specialized Lending.

Regional Directors are responsible and accountable for:

- Providing quarterly reports to E&I²⁰ noting the region's examination program, workload budget, and the status of any shortfalls and/or the identification of any assistance needed.

E&I is responsible and accountable for:

- Monitoring the successful completion of the national examination and supervision program;
- Reviewing the status of regional and national program completion and emerging needs;
- Assisting with resource needs where necessary;
- Establishing national priorities, when conditions warrant, ensuring completion of national program goals; and
- Monitoring appropriate MARS reports, specialized reports, and evaluating quarterly regional workload reports, to identify national trends and resource priorities.

We believe NCUA's tiered approach to budgeting resource hours and scheduling examinations and supervision contacts is working as operationally intended. Our review of the process showed the average number of hours to complete examinations and supervision contacts appears reasonable compared to the average number of days. Therefore, we are making no recommendations at this time.

Improvements to MARS Would Enhance Compliance Monitoring

We determined NCUA uses several quality control methods such as Quality Control Reviews (QCR), Monthly Management Reports, SE Evaluations, and ARDP Reviews to help achieve the above results and ensure examinations consistently meet established timeframe standards. However, we determined that NCUA's MARS cannot produce a report that would provide Regional officials with the exact number of days all outstanding contacts have been open. As a result, SEs and other regional officials must rely on other reports inside of MARS to estimate the number of days an outstanding contact has been open.

NCUA's Examiner's Guide states that regional office Division of Supervision (DOS) analysts review reports to identify existing or emerging trends, common or frequently occurring findings, and systemic risk factors including trends in the examination process. To monitor the duration of examinations, regional offices told the OIG they rely

²⁰ E&I officials periodically and routinely request these reports from the regions.

on their DOS analysts to perform QCRs, which includes, in part, whether examiners adhered to timeliness aspects covered in:

- Instruction 5000.15 (Rev. 3) – *Annual Examination Scheduling*;
- The Examiner's Guide; and
- Examination workpapers for evidence to explain why an examination may have exceeded established timeframes.

Regional offices also noted the use of monthly management reports to measure compliance with established timeframes including use of an aging report – *Days Since Last Contact*. In addition, regional offices told the OIG that SEs use the MARS report – *FCU Contact Completion* – to track completion timeframes to determine whether a waiver from the ARDP is necessary and that ARDPs use the DOS QCRs, SE Evaluations, and DOS monthly management reports to spot check completion timeframes throughout the year.

During our review, we learned that SEs and regional officials monitor outstanding examinations and supervision contacts and roughly estimate the length of time outstanding contacts are open with *Time Work in Progress (WIP)* and *Contact Time* reports. NCUA officials also advised the OIG that the *WIP Exception Report* shows time charged for which examiners did not upload a contact report to AIREs. However, we determined none of these reports allows SEs to determine the exact number of days outstanding contacts, not yet uploaded to AIREs, have been open.

Additionally, NCUA officials indicated the Reporting Services Reports section of NCUA Central²¹ contains a report – *Examinations Open Greater than No. of Days* – that reflects the number of days examinations (WCC 10 and 11) and onsite supervision contacts (WCC 22 and 23)²² uploaded in AIREs, remained open. We determined users could enter any number of days to filter the results. For example, if users enter the number “60”, the report will capture all examination and onsite supervision contacts open for more than 60 days. Therefore, by entering the number “1”, users can capture virtually all examination and onsite supervision contacts and see the number of days they remained open. However, we believe having regional officials review examinations and supervision contacts in this manner is inefficient.

Although the tools/reports described above do exist inside and outside of MARS, we believe regional offices would benefit from the development of an additional report inside MARS to track the exact number of days all outstanding contacts have been open. Although we determined that, on average, NCUA meets or exceeds established timeframes for completing examinations and supervisory contacts, we believe such a report could provide useful information and significantly improve an SE's ability to precisely monitor outstanding work assignments for compliance with the NSPM as well

²¹ NCUA Central is NCUA's internal web site where management officials access MARS reports.

²² WCC 22 and WCC 23 are on-site supervision contacts of FCUs and FISCUs, respectively.

as ensure nationwide consistency in the length of time examinations and supervision contacts remain open. Therefore, we are making the following recommendation:

Recommendation

We recommend NCUA management:

1. Develop a Management Automated Resource System report to provide an exact number of days all outstanding examinations and supervision contacts have been open, organized by Supervisory Examiner group. This additional tool would allow Supervisory Examiners and regional officials to better manage the examination process to ensure timeframes for completion stay within established guidelines.

Management Response

Management agreed with the recommendation. Management indicated they plan to address the issue by directing the Office of Examination and Insurance to coordinate with the Office of the Chief Information Officer to develop the recommended report and integrate the report into the Management Automated Resource System.

OIG Response

We concur with management's planned actions.

Examiners Work Assignments are Commensurate with Experience and Expertise

NCUA has established national guidance to ensure consistency in the examination process by requiring regional offices to assign examiners to work on credit unions that are commensurate with their experience and expertise. We believe this work-allocation guidance, along with NCUA guidance on Examiner-in-Charge (EIC) rotation, as well as through a national training program for newer and seasoned examiners, delivers a consistent national message to all examiners.

Due to scope limitations, we did not perform tests designed to determine the five regional offices' adherence to NCUA's national guidance on this issue. However, all five RDs informed the OIG that SEs adhere to NCUA Instruction No. 1220.03 *Examiner Work Allocation*²³ for assigning work to Grade CU-11 examiners and below, which limits Non-Principal Examiners (PE) from spending no more than 25 percent of total work time per calendar year in charge of "large, complex, difficult, or sensitive" credit union work.

²³ NCUA revised NCUA Instruction No. 1220.03 on October 25, 2011.

NCUA Instruction No. 1220.03 also states in part:

Only grade CU-9 or higher examiners may EIC or have credit unions assigned to their district that meet the criteria for "large, complex, difficult, or sensitive" credit union work. Examiners with grades lower than CU-9 may participate on examinations and supervision contacts for credit unions that meet the criteria for "large, complex, difficult, or sensitive" credit union work, but may not EIC or be assigned district responsibility for them.

The five RDs also confirmed they adhere to NCUA Instruction No. 5000.19 *Examiner-in-Charge Rotation*. This instruction states in part:

Examiners may serve as EIC for the following examination related work.²⁴

- *The EIC may be the same examiner for consecutive examinations completed within a four calendar year time period. This includes federal and state examinations as well as the off-site review of state examination reports.*
- *The EIC will be rotated at the conclusion of the fourth calendar year and will not serve in that role until another examination or review of a state examination report is completed by a different examiner. The rotation time period starts with the calendar year in which an examiner first serves as EIC.*

In addition, NCUA ensures examiners receive national training based on an annual IDP prepared by the examiner and SE to identify and address employee-specific training and development needs, as well as the use of webinars, conferences, and instructional documents to disseminate examination related policies and practices nationally. Also, regional offices acknowledged the use of MARS reports related to workload allocation and monitoring to ensure adherence to the national instructions.

Perceived Inconsistencies in the Examination Process

Senator Johnson's request to the OIG noted a concern that examiners are conducting examinations with unclear standards or with inconsistent application of agency policies and procedures. We asked NCUA management officials to comment on the Senate Committee's concerns regarding this important topic. We learned that NCUA officials believe any perception by credit unions that examination standards are inconsistently applied could be due to:

²⁴ Work Classification Code types 10, 11, and 26.

- The use of a RFE process which focuses attention and resources on areas of elevated risk where the level of risk may differ among credit unions of the same size and complexity;
- The level of risk in a specific credit union may differ from examination period to examination period;
- Although NCUA Instruction 5000.20 (Rev. 4) *Risk-Focused Examinations – Minimum Scope Requirements* prescribes minimum scope requirements for all examinations, examiners must apply reasonable discretion and judgment in developing the remainder of the examination scope to address areas of existing or emerging risk, which may result in reasonably different examination scopes for credit unions of the same size and complexity and/or different scopes from one examination period to another;
- The use of the CAMEL Rating System, which established a framework for assigning CAMEL ratings and assessing risk using both quantitative and qualitative information, could result in reasonably different conclusions based on interpretations of qualitative information; and
- A lack of knowledge among credit unions about other credit unions' situations (unique challenges, operational differences, risk characteristics).

We agree with NCUA officials that these examples provide some explanation for any perceived inconsistencies by credit unions regarding the examination process. We note that the examples of perceived inconsistencies reported have one consistent item, i.e. the human element in the form of examiner judgment and discretion. However, we also believe a contributing factor to perceived inconsistencies from credit unions, and specifically those referred to in the Senator's letter to the OIG, could be attributed to the fact that previously, each regional office had its own supervision manual to guide examiners when performing examinations and supervision contacts. As noted above, with the issuance of the NSPM, we believe NCUA officials have rectified this shortcoming.

B. Complaint Process

NCUA has an Appeals Process in Place

We determined that NCUA has an appeals process where credit unions can question examination results through informal and formal channels. Specifically, NCUA has in place a two-tiered appeal process which encourages that disputes over examiner determinations get resolved at the regional office level and at the Central Office level through the SRC. We also determined that NCUA executive management would benefit from a new reporting requirement on regional determinations. In addition, we determined the SRC needs an electronic system of record to document decisions made by the Committee; and that the Ombudsman position does not organizationally report directly to either the agency's highest-ranking official or the NCUA Board, as required by the criteria which originally established the position.

Appeals Process

During our review, we determined NCUA does not keep statistical information on informal examination complaints because the process takes place during report development. NCUA guidance encourages examiners to maintain ongoing communication with credit union officials and management. NCUA officials indicated that open communication is important when working through examination findings and potential DOR issues. NCUA officials further indicated that during the report development phase, the "give and take" between examiners and credit union officials is where both parties work through any controversial examination issues.

Regional Director Appeals

If, after receiving an examiner's final determination and disagreement persists, FCUs and FISCUs can elevate the dispute and request a meeting with the RD. NCUA considers these regional determinations slightly more formal, as evidenced by the establishment of guidelines which require credit unions to contact the regional office within 30 days of the examiner's final determination with their intent to have the RD review their case. Only after receiving the credit union's request and verifying that an NCUA examiner made the determination, will the RD review the dispute.²⁵

We found no written guidance indicating that NCUA requires its five regional offices to keep statistics on each regional determination. However, because each region keeps correspondence logs, we were able to have each region review their logs for the five-year scope period of our review and provide us with the number of complaints elevated to the RD for a regional determination, the average response time (days), and the outcome of the regional determination. Although we did not perform tests to determine the reliability of the data, we determined NCUA's five regional offices handle, on

²⁵ If a state examiner made the examination determination, the region will turn the appeal over to the state for appropriate action.

average, six examination-related complaints annually, with an overall average of 85 percent of the outcomes decided in favor of the NCUA. Table 3 (below) provides details on the number of complaints, the timeliness of resolution, and the outcome for each regional office from January 2007 through December 2011.

Table 3

Regional Office Complaints – FCU Examinations January 1, 2007 through December 31, 2011						
	Region I	Region II	Region III	Region IV	Region V	Overall Average
Total Complaints (5-Yr Period)	30	31	45	19	24	6 (Yearly Avg)
Average Resolution Time (Days)	55	28	48	26	60	43
Shortest Resolution Time (Days)	3	1	1	9	12	
Longest Resolution Time (Days)	197	80	321	63	464	
Complaints Resolved in Agency Favor	25 (83%)	31 (100%)	38 (84%)	15 (79%)	18 (75%)	85%

Source: NCUA Regional Offices' Correspondence Logs

During our review, we determined that currently, NCUA executive management does not know the number, types, and outcomes of regional determinations, but advised the OIG that having such information would be a benefit in order to be aware of the types of disputed examination issues that credit unions elevate for a regional determination. Although we determined that, on average, RDs make approximately six regional determinations per year, we agree with executive management and believe requiring the regions to regularly provide this information to E&I would prove useful in allowing E&I to know the types of examination issues on which examiners and credit union management are unable to reach agreement. Therefore, we are making the following recommendation.

Recommendation

We recommend NCUA management:

2. Establish a national reporting requirement requiring each regional office to regularly provide to the Office of Examination and Insurance specific details on disputed examination issues elevated by credit unions to the Regional Director for a regional determination. The requirement could include providing information on the number of elevated disputed examination issues, details about the disputed issue and the level of effort needed to resolve it at the examiner level, the outcome of the regional determination, and the length of time it took to close the disputed issue.

Management Response

Management agreed with the recommendation. Management indicated they plan to address the issue by directing the Office of Examination and Insurance to establish a tracking procedure to facilitate the collection and consolidation of relevant complaint information from each region.

OIG Response

We concur with management's planned actions.

Supervisory Review Committee

Enactment of the Riegle Act in 1994 led the NCUA Board to establish an independent intra-agency appellate process to review material supervisory determinations. NCUA created the SRC, an independent appellate committee, through Interpretive Ruling and Policy Statement (IRPS 95-1²⁶). The SRC consists of three senior staff members to hear appeals of disputed examination issues. After receiving the RD's determination on a disputed examination issue at the regional level, a credit union may file a formal appeal to the SRC either 30 days after the regional determination, or 60 days after contacting the regional office if the region has yet to make a determination.

In all cases, credit unions must submit their written appeal to the SRC chairperson and include the name of the appellant credit union, the determination or denial being appealed, and the reason(s) for the appeal. The Board of Directors of the appealing credit union must also authorize the appeal. Appeals heard by the SRC are limited to: (1) CAMEL composite ratings of 3, 4, and 5 and all component ratings of those composite ratings; (2) adequacy of loan loss reserve provisions; and (3) loan classifications on loans that are significant as determined by the appealing credit union.²⁷

The SRC may request additional information from the appellant and/or the regional office within 15 days of its receipt of the appeal, and the appellant must provide the additional information to the SRC within 15 days of receipt of the SRC request. The SRC must make a determination on the appeal within 30 days from the date of the receipt of an appeal by the SRC or of its receipt of any requested additional information.

We determined the SRC received two appeals during the scope period of our review, one in 2009, and the other in 2010. Both appeals involved disputed CAMEL ratings and in both cases the SRC upheld the changes to the CAMEL ratings proposed by NCUA examiners.

²⁶ On August 29, 2012, NCUA issued IRPS 12-1 to amend IRPS 11-1, which removed all references to the RegFlex program.

²⁷ Subject to requirements, credit unions may also appeal to the SRC a decision of the Director of the Office of Small Credit Union Initiatives to deny Technical Assistance Grant reimbursements.

Although we were able to determine that the SRC heard two cases within the scope period of our review, we determined the SRC's record keeping is in need of significant improvement. Specifically, we determined the SRC keeps all of its records in hard-copy format in a cardboard box. During a change in SRC chairpersons in late 2011, the outgoing chairperson passed the cardboard box of files to the newly appointed chairperson. When we questioned the new chairperson on the number of appeals the SRC had decided on from 2007 to 2011, she could not readily tell us. However, we were able to piece together the number of SRC cases and their outcomes from the box of documents and interviews with present and past SRC members. In addition, from regional offices, we confirmed the number of examination complaints, which included the two previously mentioned SRC appeal cases. We believe best business practices dictate that a Central Office-level appeals committee should have in place an electronic system of records to house and organize all documents including the final decisions handed down by the SRC on appeals cases. Therefore, we are making the following recommendation:

Recommendation

We recommend NCUA management:

3. Develop an electronic system of records for all Supervisory Review Committee related activities to document the decisions and supporting information associated with appeals cases brought before the Committee.

Management Response

Management agreed with the recommendation. Management indicated they have already taken steps to address this recommendation by automating the storage and organization of Supervisory Review Committee cases and are in the process of working on enhancing central case tracking.

OIG Response

We concur with management's actions taken and planned.

Ombudsman

The Riegle Act also led to the appointment of an Ombudsman through a BAM approved by the NCUA Board on March 13, 1995. As previously mentioned, the BAM established the Ombudsman position and provided that an existing NCUA employee, appointed by the Chairman, would carry out the functions of the position collateral to the appointee's existing duties. In addition, the Ombudsman would report to the NCUA Board, act independently of NCUA program functions, and have access to agency records. The Board further authorized the Ombudsman to keep confidential any information and material he/she obtained as a result of investigating complaints.

The BAM prescribed six principal duties of the Ombudsman position:

1. Receive, review and investigate external complaints of a regulatory nature (with certain exceptions) unresolved at the operational level;
2. Recommend solutions to the parties to resolve individual complaints. The BAM specified here that the Ombudsman would not, however, have independent decision-making authority;
3. Refer complaints outside the Ombudsman's jurisdiction to appropriate agency officials;
4. Follow up on SRC decisions to ensure that no retaliation had taken place and report instances of retaliation to the appropriate agency officials.
5. Recommend systemic changes to respond to recurring problems revealed through the Ombudsman's investigations; and
6. Report semiannually to the NCUA Board regarding the complaints the Ombudsman has considered, the recommended solutions and actions taken, and any follow-up on SRC decisions.

At the time the NCUA initially staffed the Ombudsman position, the Board did not set a term of service for each Ombudsman appointee. NCUA filled the first Ombudsman position with the agency's Chief Financial Officer. Subsequently, NCUA filled the position with employees in the Office of the Chief Financial Officer, the Office of Human Resources and, since 2010, the Office of Consumer Protection.

The position description for the Ombudsman, initially created in 1996, identified it as a collateral duty position and listed, under duties and responsibilities, the six principle duties, listed above. In addition, the position description stated the Ombudsman *"shall be independent of NCUA program functions . . . and report to the NCUA Board."*

In a BAM dated November 19, 2009, the NCUA Chief Financial Officer, in seeking Board approval of the fiscal year 2010 and 2011 operating and capital budgets, requested funding to establish an OCP as of January 1, 2010. The BAM provided that OCP would *"assume the activities of the agency's Ombudsman,"* and stated that the Ombudsman *"investigates complaints and recommends solutions on regulatory issues that cannot be resolved at the regional level."* The BAM also referenced an attachment, which provided additional information concerning OCP. The attachment contained one reference to the Ombudsman position, stating that one of the objectives in creating the OCP was to *"elevate the role of the Ombudsman and provide dedicated resources to this function."*

Other than the brief references to the Ombudsman in the 2009 operating and capital budget request, the NCUA Board did not, when the Ombudsman position transferred into OCP in January 2010, issue a new BAM to revise or supersede the 1995 BAM.

When the NCUA Board established the OCP in January 2010, it sought, among other important goals, to centralize the member complaint process in a new division, the Division of Consumer Compliance and Outreach (DCCO). DCCO eventually assumed from the five NCUA regional offices the responsibility of responding to member complaints. The Board further transferred the Ombudsman responsibilities to the Director, DCCO.

The position description²⁸ developed for the DCCO Director provided that the Ombudsman is responsible for *“investigating external complaints relating to regulatory issues, recommending solutions and proposing systemic changes to deal with recurring problems to appropriate agency officials.”*²⁹ According to this position description, the Director, DCCO reported directly to the OCP Director in carrying out both her director and Ombudsman responsibilities. The OCP Director also prepared the DCCO Director/Ombudsman's performance appraisal.

The NCUA website (www.ncua.gov) identifies the Ombudsman and describes this individual's responsibilities. Specifically, the website states the following:

NCUA's Ombudsman investigates complaints and recommends solutions. These complaints must relate to regulatory issues that cannot be resolved at the operational (regional) level.

The Ombudsman assists in resolving problems by helping the complainant to define options and by recommending actions to the parties involved, but the Ombudsman cannot at any time decide on matters in dispute or advocate the position of the complainant, NCUA or other parties.

The Ombudsman does not handle any matter:

- *subject to formal review as set forth in NCUA Regulations or IRPSs;*
- *involving an enforcement action where a notice of charges has been filed;*
- *in litigation;*
- *involving a conservatorship or liquidation; or*
- *within the Inspector General's jurisdiction.*

²⁸ Position Description Number 1397 dated February 3, 2010.

²⁹ The position description limits the Ombudsman to reviewing only consumer (member) related complaints of a regulatory nature; the Ombudsman is not involved in the NCUA's formal appeals process for examination-related complaints from credit unions.

All information and materials obtained as a result of a complainant's interview and any confidential records gathered during an investigation will be used only for purposes of the investigation and will not be disclosed outside of the Ombudsman's Office.

*The Ombudsman will make recommendations to appropriate agency officials for systemic changes to deal with recurring problems revealed through investigations. **The Ombudsman reports to the NCUA Board** and is independent from operational programs.”*

(Emphasis added.)

In March 2011, NCUA launched a new website, www.mycreditunion.gov. NCUA describes the new website as a toolbox to provide educational information and personal finance tips designed to help individuals in making smart financial decisions and better choices for their money. The webpage identifies the NCUA Ombudsman, provides contact information for her office, and describes her duties similarly to the main NCUA website, with the exception that it omits the statement “*the Ombudsman reports to the NCUA Board.*” There is no mention of who the Ombudsman reports to.

As described above, the Ombudsman's current position description sets forth her responsibilities as:

[i]Investigating external complaints relating to regulatory issues, recommending solutions and proposing systemic changes to deal with recurring problems to appropriate agency officials.

It further states:

[t]he incumbent reports directly to the OCP director on all matters, both technical and administrative.

The Ombudsman described the scope of her responsibilities as follows:

- Acts as an objective mediator between consumers and NCUA, and credit unions and NCUA;
- Lacks authority to make final decisions or overturn agency decisions;
- Makes recommendations limited to only identifying inefficiencies and breakdowns in procedures and policies between NCUA and outside parties; and
- May ask RDs, Office Directors, and/or the NCUA Board to reconsider their respective decisions, but cannot influence final decisions.

The NCUA Ombudsman stated that, with regard to member complaints she reviews in her Ombudsman capacity, she reports statistical, administrative, and procedural

information to the OCP Director who, in turn, reports to the Board. She also provides statistical information for inclusion in NCUA Management Reports, which are issued monthly, as well as in semiannual reports to the NCUA Board. The Ombudsman also stated that all of the cases to which she has responded have been appeals of routine member complaints, not complaints from credit unions related to examinations.

Table 4 (below) provides details on the number and timeliness to resolve the member complaint cases opened and responded to by the Ombudsman during 2010 and 2011:

Table 4

Member Complaints Handled by the Ombudsman			
	2010	2011	Total
Complaints	4	38	42
Average Resolution Time (Days)	32	173	
Shortest Resolution Time (Days)	3	1	
Longest Resolution Time (Days)	82	335	
How Resolved	Unknown*	Unknown*	

**No statistics kept on the outcome of Ombudsman member complaint cases*

Ombudsman Reporting

Although the Ombudsman organizationally reports to the Director, OCP, should substantive consumer complaint issues arise, she has the authority to report such issues directly to the NCUA Chairman. However, we determined the Ombudsman has not met with the Chairman to discuss any such complaints since she assumed the Ombudsman function in 2010, as none of those received rose to the level of “substantive.”

We determined further that the current Ombudsman position description does not agree with either the information posted on NCUA’s main website or the guidelines set forth in the 1995 BAM. Specifically, the current position description lacks both the detailed delineation of duties and responsibilities and the paragraph concerning Ombudsman independence and reporting, which the 1995 position description included. All three of these sources—the main NCUA website, the 1995 BAM, and the 1996 position description—indicate that the Ombudsman reports directly to the NCUA Board. However, as mentioned above, the current position description for the DCCO Director/Ombudsman position states that *[t]he incumbent reports directly to the OCP Director on all matters.*”

Both the Ombudsman and the Director, OCP, acknowledged that while section 309(d) of the FCU Act is silent regarding to whom the Ombudsman reports, current Federal

employee Ombudsman guidance³⁰ advises that the Ombudsman should, if possible, report and have direct access to the highest agency official. The Director, OCP, recommended to the NCUA Board, in a White Paper dated July 2011 (White Paper), that the NCUA Office of Human Resources conduct a renewed review of all aspects of the Ombudsman position and update both the position description and the performance plan for the position. The White Paper also specifically recommended that the NCUA Board revisit who the Ombudsman reports to and consider the independence, impartiality, and confidentiality required of the position when making its determination.

We believe that the NCUA's original determination that the Ombudsman position should report to the highest agency official—an approach also proposed by the Director, OCP and endorsed by the Ombudsman Steering Committee—represents the optimal reporting structure. Therefore, we are making the following recommendation.

Recommendation

We recommend NCUA management:

4. Revisit the current Ombudsman reporting structure to ensure the position reports either directly to the highest agency official as recommended by the Ombudsman Steering Committee, or to the NCUA Board as set forth in the 1995 Board Action Memorandum.

Management Response

Management agreed with the recommendation and indicated they plan to reevaluate the current Ombudsman reporting structure.

OIG Response

We concur with management's planned actions.

Member Complaint Process

At the time we initiated this audit, DCCO was responsible for processing and facilitating the resolution of member complaints. Prior to the formation of OCP in 2010, NCUA regional offices responded to complaints against credit unions. In 2010, NCUA centralized this responsibility within DCCO. Table 5 (below) provides the number of closed member complaints received by DCCO against FCUs and FISCUs, for 2011 and 2012.³¹

³⁰ *A Guide for Federal Employee Ombuds*, developed by the Coalition of Federal Ombudsman and the Federal Interagency Alternative Dispute Resolution Working Group Steering Committee (Ombudsman Steering Committee); 1 C.F.R. § 305.90-2.

³¹ OCP began using Parature software to capture complaint data on June 6, 2011. Data for 2012 is current through May 31, 2012.

Table 5

Closed Member Complaints Against Credit Unions			
	June - December 2011	January – May 2012	Total
Federal Credit Unions	383	1,173	1,556
Federally Insured State-Chartered Credit Unions	324	341	665
Total	707	1,514	2,221

Initially, DCCO analysts routinely responded by letter to member complaints and reported violations of compliance regulations. All of the letter responses bore the signature line “Ombudsman,” although they were not hand-signed by the Ombudsman herself. Because OCP recognized that this arrangement could result in a potential conflict if the complainant sought Ombudsman review of a DCCO complaint response, OCP decided to reorganize internally to avoid this scenario.

In June 2012, OCP reorganized internally, creating a new, third division – the Division of Consumer Affairs (DCA). OCP changed the name of DCCO to the Division of Consumer Compliance Policy and Outreach (DCCPO). The DCA assumed responsibility for investigating and responding to member complaints. The Ombudsman function remained within the newly titled DCCPO, continuing to reside in the Director position. With the creation of DCA, OCP ensured a separation of functions between NCUA responses to member complaints and potential Ombudsman review of such responses.³² As a result, NCUA member complaint responses no longer bear the signature line “Ombudsman,” but rather, are now signed by the Director, DCA.

³² Although NCUA created a new position description for the DCCO Director position as a result of the reorganization, the language for the DCCO Director’s ombudsman responsibilities were not changed. Consequently, we reiterate our recommendation above that NCUA revisit the current ombudsman reporting structure to ensure the position reports either to the highest agency official or to the NCUA Board.

Appendix A:

Small Credit Union Examination Program FCU Examinations – Minimum Scope Requirements
Complete a review of loans granted during the prior six months including a sample from identified loan concentrations, loan types that present higher levels of risk (e.g. real estate, MBLs, participations, indirect), insider loans, extensions, and share secured loans.
Review file maintenance reports generated by the credit union for at least three consecutive months.
Review and test the most recent three months' bank and/or corporate account statements and associated reconciliations, using original documents.
Review the Allowance for Loan and Lease Losses (ALLL) Account for Full and Fair Disclosure Requirements.
Review of audit, internal audit, and/or Supervisory Committee activities including work papers.
Review AIREs share and loan download and queries.
Review prior DOR items to determine if resolved, unresolved, or no longer applicable, and appropriately document results within DOR module.
Review surety bond coverage to ensure credit union has adequate coverage in accordance with NCUA Rules and Regulations Part 713.
Review compliance with any new regulations, or changes to existing regulations, since the last examination.

Small Credit Union Examination Program FCU Examinations – Minimum Required Questionnaires
BSA – Bank Secrecy Act
Flood Act
5300 Review
Audit Verification Review
Red Flag Questionnaire

Appendix B: NCUA Management Comments



National Credit Union Administration

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VIA E-Mail

TO: William DeSarno, Inspector General
Office of Inspector General (OIG)

FROM: David M. Marquis, Executive Director

SUBJ: Comments on "Review of NCUA's Examination and Complaint Processes for Small Credit Unions"

DATE: August 27, 2012

This memorandum responds to your request for review and comment on the OIG draft report titled *Review of NCUA's Examination and Complaint Processes for Small Credit Unions*.

Examination Process

The report finds NCUA's examination process for small credit unions has clear standards and policies to conduct examinations. However, you determined inconsistencies exist in the manner we implement the policies. Because we recently implemented a National Supervision Policy Manual (NSPM) that addresses the issue of inconsistency, you are not making recommendations to the examination process.

Although you did not make any recommendations about the examination process, you made the following recommendation to enhance procedures for monitoring compliance with the NSPM:

Recommendation #1: *Develop a Management Automated Resource System (MARS) report to provide an exact number of days all outstanding examinations and supervision contacts have been open, organized by Supervisory Examiner (SE) group. This additional tool would allow SEs and regional officials to better manage the examination process to ensure timeframes for completion stay within established guidelines.*

Management Response: We agree this recommendation will help us monitor compliance with the NSPM and ensure national consistency in the length of time examinations and supervision contacts remain open.

Our current systems already contain several relevant control reports including:

- Time Work in Progress,
- Contact Time,
- Work in Progress Exception Report, and
- Exams Open Greater than Number of Days.

These reports allow us to monitor and measure progress on examinations and the number of days an exam remained open after it is completed and uploaded. However, we do not have a report that captures overdue reports that are still open and where an exam upload has not yet occurred. To address this issue, the Office of Examination and Insurance (E&I) will:

1. Coordinate with the Office of the Chief Information Officer (OCIO) to develop the suggested report and add it to MARS, and
2. Work with OCIO to integrate the various reports into MARS.

Complaint Process

You determined our appeals process provides an adequate forum for credit unions to question examination results. But, there are operational and organizational deficiencies that we can improve related to the regional determination process, the Supervisory Review Committee (SRC), and the Ombudsman position. As a result, you made the following three recommendations to correct identified deficiencies:

Recommendation #2: *Establish a national reporting requirement requiring each regional office to regularly provide to E&I, specific details on disputed examination issues that credit unions elevate to the Regional Director for a regional determination. The requirement could include such information as the number of elevated disputed examination issues, details about the disputed issue and the level of effort to resolve it at the examiner level, the outcome of the regional determination, and the length of time it took to close the disputed issue.*

Management Response: We agree with the recommendation. E&I will establish a tracking procedure facilitating collection and consolidation of relevant complaint information from each region.

Recommendation #3: *Develop an electronic system of record for all Supervisory Review Committee related activities to document the decisions and supporting information associated with appeals cases brought before the Committee.*

Management Response: We agree with the need to enhance our case management, recordkeeping and reporting processes around SRC complaints. We have already taken steps to address this recommendation. We have automated the storage and organization of cases, so it is centrally accessible by assigned staff. We are in process of enhancing central case tracking, as well.

Recommendation #4: *Revisit the current Ombudsman reporting structure to ensure the position reports either directly to the highest agency official as recommended by the Ombudsman Steering Committee, or to the NCUA Board as approved in the 1995 BAM.*

Management Response: We agree with your recommendation and will reevaluate the current Ombudsman reporting structure as outlined in your recommendation.

Thank you for the opportunity to comment.