

NATIONAL CREDIT UNION ADMINISTRATION
OFFICE OF INSPECTOR GENERAL



**NCUA 2015
FINANCIAL STATEMENT AUDITS
FOR
SHARE INSURANCE FUND
OPERATING FUND
CENTRAL LIQUIDITY FACILITY
COMMUNITY DEVELOPMENT REVOLVING LOAN FUND**



For the year ended December 31, 2015

Audited Financial Statements	Audit Report Number
Share Insurance Fund	OIG-16-02
Operating Fund	OIG-16-03
Central Liquidity Facility	OIG-16-04
Community Development Revolving Loan Fund	OIG-16-05

February 12, 2016

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

James W. Hagen
Inspector General



Office of Inspector General

February 12, 2016

The Honorable Debbie Matz, Chairman
The Honorable Rick Metsger, Vice Chairman
The Honorable J. Mark McWatters, Board Member
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314

Dear Chairman Matz and NCUA Board Members:

I am pleased to transmit KPMG LLP's (KPMG) report on its financial statement audit of the National Credit Union Administration's (NCUA) financial statements, which includes the Share Insurance Fund, the Operating Fund, the Central Liquidity Facility, and the Community Development Revolving Loan Fund, as of and for the years ending December 31, 2015 and 2014. The NCUA prepared financial statements in accordance with the Office of Management and Budget (OMB) Circular No. A-136 Revised, *Financial Reporting Requirements*, and subjected them to audit.

Under a contract monitored by NCUA OIG, KPMG, an independent certified public accounting firm, performed an audit of NCUA's financial statements as of December 31, 2015. The contract required that the audit be performed in accordance with generally accepted government auditing standards issued by the Comptroller General of the United States, Office of Management and Budget audit guidance, and the *Government Accountability Office/President's Council on Integrity and Efficiency Financial Audit Manual*.

KPMG's audit report for 2015 includes: (1) an opinion on the financial statements, (2) conclusions on internal control over financial reporting, and (3) a section addressing compliance and other matters. In its audit of NCUA, KPMG found:

- The financial statements were fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles;
- There were no material weaknesses in internal controls;¹
- There were no significant deficiencies related to internal controls;² and
- No instances of reportable noncompliance with laws and regulations it tested or other matters that are required to be reported under Government Auditing Standards or OMB guidance.

¹ A material weakness is defined as a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

² A significant deficiency is defined as a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

To ensure the quality of the audit work performed, we reviewed KPMG's approach and planning of the audit, evaluated the qualifications and independence of the auditors, monitored the progress of the audit at key points, and reviewed and accepted KPMG's reports and related documentation and inquired of its representatives. Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards, was not intended to enable us to express, and we do not express, opinions on NCUA's financial statements or conclusions about the effectiveness of internal control or conclusions on compliance with laws and regulations. KPMG is responsible for the attached auditor's reports dated February 12, 2016, and the conclusions expressed in the reports. However, our review disclosed no instances where KPMG did not comply, in all material respects, with generally accepted government auditing standards.

We would like to extend our thanks to NCUA management and staff involved in issuing the financial statements within the established milestones. In addition, we appreciate the professionalism, courtesies, and cooperation extended to KPMG throughout the audit and our oversight of the audit process.

Management and Performance Challenges

The Inspector General is required by law to provide a summary statement on management and performance challenges facing the Agency. Below we provide a brief overview of NCUA's organizational structure, its mission, and vision, as well as what we believe are the key challenges to agency management in the coming year.

Organizational Structure

Created by Congress, NCUA is an independent federal agency with the unique role of insuring deposits at all federal and most state-chartered credit unions, protecting the members who own credit unions, and regulating federally chartered credit unions. A three member politically appointed Board oversees NCUA's operations by setting policy, approving budgets, and adopting rules. As of September 30, 2015, over 102.1 million members have \$992.5 billion in deposits at 6,090 federally insured credit unions. These credit unions have \$1.2 trillion in assets.

Agency Mission and Vision

Throughout 2016 and 2017, NCUA will implement initiatives to continue meeting its mission to "provide, through regulation and supervision, a safe and sound credit union system which promotes confidence in the national system of cooperative credit," and its vision to ensure that "NCUA will protect consumer rights and member deposits."

Agency Challenges

In 2016, NCUA will face several risks that continue to threaten the safety and soundness of the credit union system, as well as several emerging risks that the agency must confront. As I noted last year, interest rate risk (IRR) and cybersecurity remain significant agency challenges where NCUA must continue to build on the positive steps already taken in its supervisory efforts.

Similarly, three emerging risks – aging membership, disparities in performance between large and small credit unions, and vendor authority – will also provide unique challenges to the agency that could potentially affect the safety and soundness of the credit union system and the Share Insurance Fund if not adequately managed.

Interest Rate Risk — A rising rate environment may prove challenging for those credit unions that hold either high concentrations of long-term assets funded with short-term liabilities, or have rate-sensitive deposits and fixed-rate assets. The latter is especially true if fixed-rate assets lose value, which can cause deposit rates to rise, liquidity to decrease, and earnings to compress by lowering net interest margins. Although a large amount of uncertainty remains regarding interest rates, because they have begun to rise, NCUA must continue to keep IRR a priority for its supervisory examinations and communications in 2016.

Cybersecurity — As I noted last year, cyber threats continue to pose significant dangers to the stability and soundness of the credit union industry and are expected to increase in frequency and severity as the capabilities to conduct cyberattacks become more sophisticated and easier for criminals or terrorists to perform. Further, because consumers continue to interact with financial institutions through online and mobile transactions, the risk of hacking and fraud will continue to grow. Credit unions will need to enhance the security of their systems to protect themselves and their members. Of particular concern are attacks to credit union service organizations, which could potentially compromise a large number of credit unions at once. Because of these risks, NCUA will need to continue its efforts to evaluate credit unions' cybersecurity risk management. One such effort, the recently released Cybersecurity Assessment Tool for credit unions, gives credit unions a structured methodology to manage information security and protect member information more effectively.

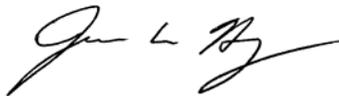
Aging Membership — An emerging challenge that NCUA and credit unions face is that of an aging demographic. The average age of adult credit union members is 46.7. Peak borrowing age is 25–44. Given this, the average credit union member is already past their prime borrowing years. Because nearly 26 percent of the U.S. population is under the age of 20, NCUA must continue to help credit unions take action to attract younger members to address this concern. NCUA has taken or plans to take actions that will allow for continued growth, including for example, providing technical assistance and grants to help low-income credit unions expand the products and services they offer, as well as updating and modernizing the field-of-membership rules. NCUA must continue to help decrease the average members' age by attracting younger members.

Disparities in Performance between Large and Small Credit Unions — Other emerging challenges facing NCUA is the lack of asset growth in credit unions with assets less than \$10 million and the overall decline in membership. Although credit unions overall performed well in 2015, much of the system's growth can be attributed mainly to the largest institutions. Smaller credit unions have seen less loan and net worth growth than larger credit unions. Smaller credit unions are vital to their communities and NCUA must continue to provide them with needed technical assistance and create new opportunities for growth through reduced regulatory burdens,

increased access to supplemental capital, and enhanced chartering and field-of-membership options.

Vendor Authority — Finally, the challenge of obtaining the same legal authority that other federal financial institutions regulators have to oversee third-party vendors is a significant concern facing NCUA from both a systemic and cybersecurity risk. As credit unions increasingly use credit union service organizations or other third parties to achieve economies of scale to remain competitive, this regulatory blind spot prevents the agency from having a full understanding of all potential risks within the credit union system. Significant problems with a key technology service vendor, for example, such as inadequate security measures or weak internal controls, or perhaps the failure of a key vendor, could result in significant losses to the Share Insurance Fund.

Respectfully,



James W. Hagen
Inspector General

cc: Executive Director, Mark Treichel
General Counsel, Michael McKenna
Director, PACA, Todd Harper
Deputy Executive Director (Audit Follow-up Official), John Kutchev
Chief Financial Officer, Rendell Jones
Deputy Chief Financial Officer, Peggy Sherry
Chief Information Officer, Ed Dorris
Director, OSCUI, William Myers
President, AMAC, Mike Barton
Director, E&I, Larry Fazio
Director, E&I, Division of Capital and Credit Markets, J. Owen Cole, Jr.

Report #OIG-16-02

National Credit Union Share Insurance Fund

Financial Statements as of and for the Years Ended
December 31, 2015 and 2014, and
Independent Auditors' Report

NATIONAL CREDIT UNION SHARE INSURANCE FUND

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Overview

I. Mission and Organizational Structure

NCUSIF Mission

The National Credit Union Administration (NCUA) administers the National Credit Union Share Insurance Fund (NCUSIF or Fund).¹ Congress created the NCUSIF in 1970 to insure members' shares (deposits) in credit unions. The NCUSIF is backed by the full faith and credit of the United States. As of December 2015, the NCUSIF insures an estimated \$961.3 billion in member shares in over 6,000 credit unions.

The NCUSIF protects members' accounts in insured credit unions in the event of a credit union failure. The NCUSIF insures the balance of each members' account, dollar-for-dollar, up to the standard maximum share insurance amount of \$250,000, including principal and posted dividends through the date of a failure, subject to various rules on account types, rights, and capacities. The Fund insures all types of member shares received by a credit union in its usual course of business.

The NCUSIF also provides funding when the NCUA Board determines that some form of financial assistance to troubled credit unions will result in the least resolution cost. Examples of financial assistance include but are not limited to the following:

- a waiver of statutory reserve requirements;
- a guaranteed line of credit, cash assistance, including subordinated notes or other forms; and
- cash assistance to arrange a merger or purchase and assumption.

When a credit union is no longer able to continue operating and assistance alternatives are not practical, the credit union will be liquidated and the NCUSIF will pay members' shares up to the standard maximum insurance amount.

Organizational Structure

NCUA's Director of the Office of Examination and Insurance (E&I) is responsible for overseeing the agency's examination and supervision program. NCUA's E&I Director is also the President of the NCUSIF and responsible for risk management of the NCUSIF. Regional offices and the Office of National Examinations and Supervision conduct examinations and other NCUA offices provide operational and administrative services to the NCUSIF. The Asset Management and Assistance Center (AMAC) conducts credit union liquidations. AMAC establishes an Asset Management Estate (AME) to collect the obligations due to the liquidated credit union, monetizes assets and distributes amounts to claimants, including the NCUSIF, according to their respective regulatory payout priorities.

¹ The NCUSIF is one of five funds established in the U.S. Treasury and administered by the NCUA Board. The four permanent funds include the NCUSIF, the Operating Fund, the Central Liquidity Facility (CLF) and the Community Development Revolving Loan Fund. In addition, the NCUA Board administers the Temporary Corporate Credit Union Stabilization Fund (TCCUSF) that was established in 2009 to accrue the losses of corporate credit unions during the credit crisis and to recover such losses over time. All five funds report under separate financial statements.

II. Performance Goals, Objectives and Results

Consistent with the *NCUA Strategic Plan 2014 through 2017*, which emphasizes ensuring a “sustainable credit union system,” the agency prepared the *NCUA 2015-2016 Annual Performance Plan*. Performance goals include maintaining strong levels of credit union system-wide net worth and corporate credit union leverage ratios, examining all federal credit unions annually, examining all federally insured, state-chartered credit unions with assets above \$250 million annually, maintaining yearly NCUSIF losses for current year failures as a percentage of insured shares at less than 0.03%, and minimizing total assets in CAMEL² Code 4 or 5 rated credit unions. For 2015, NCUSIF losses for current year failures ratio was 0.002%, as compared to 0.005% for 2014. Total assets in CAMEL Code 4/5 credit unions decreased to \$8.6 billion in 2015, as compared to \$11.5 billion in 2014.

In measuring the performance of the NCUSIF for 2015 and 2014, the following additional measures should be considered.

2015 and 2014 Performance Measures		
	December 31, 2015	December 31, 2014
Equity Ratio	1.26%	1.29%
Insurance and Guarantee Program Liabilities (Contingent Liability)	\$164.9 million	\$178.3 million
Net Position	\$12.2 billion	\$11.8 billion
Insured Shares	\$961.3 billion	\$903.0 billion
Credit Union Involuntary Liquidations and Assisted Mergers	16	15
Assets in CAMEL 3, 4 and 5 rated Credit Unions	\$98.3 billion	\$106.9 billion

The equity ratio and contingent liability are significant financial performance measures in assessing the ongoing operations of the NCUSIF. The equity ratio serves as a mechanism to balance funding from capitalization deposits and premium assessments in response to changes in insured share growth, insurance losses, interest income from U.S. Treasury security investments, as well as other revenues and expenses.

Equity Ratio and Normal Operating Level

The financial performance of the NCUSIF revolves around the equity ratio and the Normal Operating Level (NOL). The equity ratio is calculated as the ratio of the contributed one percent (1.00%) deposit plus cumulative results of operations, excluding net cumulative unrealized gains and losses on investments, to the aggregate amount of the insured shares in all insured credit unions. The NOL is the desired long-term target equity level for the NCUSIF. The NCUA Board sets the NOL between 1.20% and 1.50%. The NCUA Board set the current NOL at 1.30%.

By statute, when the equity ratio falls below 1.20%, the NCUA Board must establish and implement a restoration plan to rebuild the equity ratio, which may include a premium assessment to each insured credit union. The NCUSIF pays a distribution when the equity ratio exceeds the NOL at year-end. When the NCUSIF or the Temporary Corporate Credit Union

² CAMEL is the acronym for Capital, the quality of Assets, the capability of Management, the quality and level of Earnings, and the adequacy of Liquidity.

Stabilization Fund (TCCUSF) does not have an outstanding borrowing from the U.S. Treasury, the distribution is paid to insured credit unions.

The equity ratio was 1.26%, which is below the NOL as of December 2015. As a result, no distribution was payable to the TCCUSF for 2015. For 2014, the NCUSIF ended the year with an equity ratio of 1.29%, which resulted in no distribution to TCCUSF. In 2015 and 2014, the NCUA Board did not assess a premium charge to insured credit unions for the NCUSIF. We expect that the NCUSIF will receive additional capitalization deposits of approximately \$259.6 million from insured credit unions in early 2016 when NCUA invoices for its biannual contributed capital adjustment. The additional capitalization deposits will result in a projected equity ratio of approximately 1.29%.

Insurance Losses (Contingent Liabilities)

Through its supervision process, NCUA applies a supervisory rating system to assess each insured credit union's relative health in the adequacy of Capital, the quality of Assets, the capability of Management, the quality and level of Earnings, and the adequacy of Liquidity (CAMEL), applying a rating to the credit union ranging from "1" (strongest) to "5" (weakest). The CAMEL rating system is a tool to measure risk and allocate resources for supervisory purposes. NCUA periodically reviews the CAMEL rating system to respond to continuing economic and regulatory changes in the credit union industry.

The NCUSIF's year-end contingent liability is derived by using an internal econometric model that applies estimated failure and loss rates and takes into account the historical loss history, CAMEL ratings, credit union level financial ratios, and other conditions. In addition, specific analysis is performed on those insured credit unions where failure is imminent or where additional information is available that may affect the estimate of losses.

NCUA identifies credit unions at risk of failure through the supervisory and examination process, and estimates losses based upon economic trends and credit unions' financial condition and operations. NCUA also evaluates overall credit union economic trends and monitors potential system-wide risk factors, such as increasing levels of consumer debt, bankruptcies, and delinquencies.

The credit union industry continued to improve during 2015 as reflected by the reduction in assets in CAMEL 3, 4 and 5 rated credit unions as compared to 2014. Assets in CAMEL 3, 4 and 5 rated credit unions dropped to \$98.3 billion at the end of 2015, versus \$106.9 billion at the end of 2014. Although the system-wide net worth ratio decreased slightly from 11.0% to 10.9% during 2015, the ratio has shown improvement since 2011. These factors, as well as other trends, helped contribute to a reduction in amounts for the Insurance and Guarantee Program Liabilities on the NCUSIF Balance Sheets. The NCUSIF ended 2015 with Insurance and Guarantee Program Liabilities of \$164.9 million to cover potential losses as compared with \$178.3 million for the previous year-end, a reduction of \$13.4 million.

Due to uncertain economic risks and the possibility of variances from historical data, actual losses could differ materially from the contingent liabilities recorded by the NCUSIF.

Performance measures are designed to enable management and our stakeholders to assess programs and financial performance and to use this information to make improvements. Performance measures have inherent limitations including the change over time in the correlation

of cause and effect. A strong correlation between cause and effect in one period may not continue into the next. In addition, performance measures may not address systemic risks, which can have a significant determination on future results.

III. Financial Statement Analysis

The NCUSIF ended 2015 with the Balance Sheets showing an increase in Total Assets and its Total Net Position, and a reduction in Insurance and Guarantee Program Liabilities from the prior year. With the Statements of Net Cost, net cost increased to \$157.2 million, primarily as a result in increases in Operating Expenses. These changes are explained in further detail below.

Summarized Financial Information (in thousands)		
	December 31, 2015	December 31, 2014
Total Assets	\$12,328,652	\$11,957,607
Investments, Net	12,079,490	11,611,538
Notes Receivable, Net	108,568	174,213
Receivables from Asset Management Estates, Net	65,779	87,785
Insurance and Guarantee Program Liabilities	164,857	178,318
Contributed Capital	9,353,113	8,944,099
Net Position	12,156,161	11,775,355
Operating Expenses	197,752	179,818
Provision for Insurance Losses, Reserve Expense (Reduction)	(250)	3,298
Provision for Insurance Losses, AME Receivable Bad Debt Expense	(35,161)	(45,138)
Total Net Cost of Operations	157,154	132,345
Cumulative Results of Operations	2,803,048	2,831,256
Interest Revenue – Investments	218,526	208,259

Balance Sheet Highlights

Total Assets increased by \$371.0 million in 2015. The increase came primarily from net collections of capital deposits of \$409.0 million and Interest Revenue – Investments of \$218.5 million, partially offset by Total Net Cost of Operations of \$157.2 million and net unrealized losses on Investments of \$89.6 million.

Balances of Investments increased by \$468.0 million during 2015, primarily driven by investing net additions to Contributed Capital. During 2015, U.S. Treasury yields increased, particularly in the second half of 2015. The increase in market interest rate yields resulted in an overall decrease in the market value of U.S. Treasury securities.

Notes Receivable, Net declined \$65.6 million and Receivables from Asset Management Estates, Net declined \$22.0 million. The decreases in the balances of Notes Receivable is primarily attributable to the repayment of two outstanding capital notes during 2015. Receivables from Asset Management Estates, Net include the collection of principal on outstanding loans, mortgages and other debt instruments. Also, Receivables from Asset Management Estates, Net include various transactions that are explained in Note 7 to the financial statements.

Insurance and Guarantee Program Liabilities, referred to as contingent liabilities, were \$164.9 million and \$178.3 million as of December 31, 2015 and 2014, respectively. In general,

the decrease reflects improved financial strength in the credit union industry and strengthening macroeconomic conditions, such as housing indicators.

Contributed Capital increased by \$409.0 million during 2015 due to the growth of insured shares in credit unions. Each insured credit union deposits one percent of its insured shares as Contributed Capital. In 2015, credit union membership grew by 3.5% to approximately 103 million members.

Net Position increased \$380.8 million during 2015 and is a combination of other increases and decreases. Increases include interest revenue on Investments of \$218.5 million and net additions of Contributed Capital of \$409.0 million. Decreases include Net Cost of Operations of \$157.2 million and net unrealized losses on Investments of \$89.6 million.

Statements of Net Cost Highlights

Total Net Cost of Operations was \$157.2 million for 2015, as compared to \$132.3 million for 2014. The primary increase in Net Cost of Operations is attributable to the increase in Operating Expenses of \$17.9 million. As explained in Note 10, Operating Expenses include expenses from the NCUA Operating Fund based on an allocation factor (Overhead Transfer Rate) that increased from 69.2% to 71.8% for 2015. Also, the Provision for Insurance Losses is an expense reduction of \$35.4 million and \$41.8 million for both 2015 and 2014, respectively; the net change between years is a decrease of \$6.4 million. Within the Provision of Insurance Loss for 2015, the Reserve Expense was a \$250 thousand reduction, reflecting a net decrease in the cost of credit union failures over the year, while the AME Receivable Bad Debt Expense was a \$35.2 million expense reduction, reflecting recoveries and increases in net realizable values of assets managed.

Statements of Changes in Net Position Highlights

Cumulative results of operations decreased by \$28.2 million in 2015. This decrease was primarily driven by net unrealized losses on Investments of \$89.6 million and Net Cost of Operations of \$157.2 million, partially offset by Interest Revenue of \$218.5 million. Interest Revenue was the primary source of funds to partially offset expenses and obligations.

Statements of Budgetary Resources Highlights

Activity impacting budget totals of the overall Federal Government is recorded in the NCUSIF's Statements of Budgetary Resources. The NCUSIF's net outlays were negative, meaning that the NCUSIF had net cash inflows of \$579.4 million and \$435.3 million for 2015 and 2014, respectively. This increase is primarily the result of the growth of credit union insured shares and the corresponding 1.00% contributed capital deposit adjustment received.

Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the NCUSIF. While the statements have been prepared from the books and records of the NCUSIF in accordance with U.S. generally accepted accounting principles (GAAP) for Federal entities and the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records. The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

Liquidity Risk and Capital Resources

For liquidity, the NCUSIF maintains cash in its Fund Balance with Treasury (FBWT) account as well as investments in U.S. Treasury securities. Investments in U.S. Treasury securities include overnight investments, which are available to meet urgent liquidity needs of the NCUSIF.

2015 and 2014 Fund Balance with Treasury and Investments		
	December 31, 2015	December 31, 2014
Fund Balance with Treasury	\$ 2.4 million	\$ 10.5 million
U.S. Treasury Securities		
Overnight	141.2 million	173.6 million
Available-for-Sale	11,938.3 million	11,437.9 million

During 2015, the FBWT account was primarily increased by maturing investments in U.S. Treasury securities and Interest Revenue collected. The FBWT account was decreased by purchases of U.S. Treasury securities and amounts expended for the purposes of the share insurance program.

The NCUSIF has multiple other sources of funding including:

- capitalization deposits contributed by insured credit unions, as provided by the *Federal Credit Union Act*, Public Law 73-467, as amended (FCU Act);
- cumulative results of operations retained by the NCUSIF;
- assessments on insured credit unions, as necessary;
- borrowings from the U.S. Treasury; and
- borrowings from the Central Liquidity Facility (CLF).

The NCUSIF is a revolving fund in the U.S. Treasury and has access to sufficient funds to meet its obligations, including its Insurance and Guarantee Program Liabilities.

Contributed Capital

Each insured credit union must deposit and maintain in the NCUSIF 1.00% of its insured shares. For the years ended December 31, 2015 and 2014, the NCUSIF's contributed capital from insured credit unions increased by \$409.0 million and \$282.9 million, respectively. Total insured shares were estimated at \$961.3 billion and \$903.0 billion as of December 31, 2015 and 2014, respectively.

At December 31, 2015, NCUA estimated the total insured shares to be approximately \$961.3 billion, subject to certified reporting of insured share amounts. We expect that the NCUSIF will receive additional capitalization deposits of approximately \$259.6 million from insured credit unions in early 2016 when NCUA invoices for its biannual contributed capital adjustment. The additional capitalization deposits will result in a projected equity ratio of approximately 1.29%.

Cumulative Results of Operations

The NCUSIF ended 2015 and 2014 with a total of \$2.8 billion and \$2.8 billion in cumulative results of operations, respectively. Interest Revenue is currently the primary source of funds for operations.

Assessments

The NCUA Board may also assess premium charges to all insured credit unions, as provided by the FCU Act. During the years ended December 31, 2015 and 2014, the NCUA Board did not assess any premium charges to insured credit unions for the NCUSIF.

Borrowing Authority from the U.S. Treasury

The NCUSIF has \$6.0 billion in maximum statutory borrowing authority, shared with the TCCUSF, from the U.S. Treasury. As of December 31, 2015 and 2014, the TCCUSF had \$1.7 billion and \$2.6 billion in borrowing outstanding from the U.S. Treasury, respectively; the NCUSIF had no borrowings outstanding. As a result, the NCUSIF had \$4.3 billion and \$3.4 billion, respectively, in available borrowing authority shared with the TCCUSF. The estimated losses and liquidity needs of the TCCUSF are based on NCUA's expectations and assumptions about the resolution of failed corporate credit unions, including the disposition and recovery value of their assets. Actual losses of the TCCUSF, including the TCCUSF's funding needs, could differ from those estimates. Any additional borrowing for the TCCUSF reduces funds available for the NCUSIF from this source.

Borrowing Authority from the CLF

The NCUSIF also has the ability to borrow from the CLF as provided in the FCU Act. At December 31, 2015 and 2014, the NCUSIF did not have any outstanding borrowing from the CLF. The CLF is authorized by statute to borrow, from any source, an amount not to exceed twelve times its subscribed capital stock and surplus. The CLF had statutory borrowing authority of \$5.6 billion as of December 31, 2015. NCUA maintains a note purchase agreement with Federal Financing Bank (FFB) on behalf of CLF with a maximum principal amount of \$2.0 billion. Under the terms of its agreement, CLF borrows from FFB as needed. Under terms prescribed by the note purchase agreement, CLF executes promissory notes in amounts as necessary and renews them annually. Advances under the current promissory note can be made no later than March 31, 2016.

IV. Systems, Controls, and Legal Compliance

The NCUSIF was created by Title II of the FCU Act, 12 U.S.C. §1781 *et seq.*, as amended. In January 2011, the *National Credit Union Authority Clarification Act*, Public Law 111-382, amended the FCU Act in part by amending the definitions of “equity ratio” and “net worth.” NCUA, including the NCUSIF, is exempt from requirements under the *Federal Credit Reform Act of 1990* (2 U.S.C. § 661 *et seq.*).

Internal controls should be designed to provide reasonable assurance regarding prevention or prompt detection of unauthorized acquisition, use, or disposition of assets. The *Federal Managers' Financial Integrity Act*, Public Law 97-255 (FMFIA), requires agencies to establish management controls over their programs and financial systems. Accordingly, NCUA management is responsible for establishing and maintaining effective internal controls and financial management systems that meet the objectives of FMFIA, which include safeguarding assets and compliance with applicable laws and regulations. NCUA managers monitor and assess their relevant internal controls and report on their assessment. This allows NCUA management to provide reasonable assurance that internal controls are operating effectively. NCUA is in compliance with FMFIA as well as all applicable laws such as the *Prompt Payment Act*, Public Law 97-177, and the *Debt Collection Improvement Act*, Public Law 104-134. As required by the *Improper Payments Elimination and Recovery Act*, Public Law 111-204, as

amended, we have determined that the NCUSIF's programs are not susceptible to a high risk of significant improper payments.

As required by the *Federal Information Security Management Act*, Public Law 107-347, as amended (FISMA), NCUA develops, documents, and implements an agency-wide program to provide information privacy and security (management, operational, and technical security controls) for the information and information systems that support the operations of the agency, including those provided or managed by another agency, contractor, or other source.



KPMG LLP
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Independent Auditors' Report

Inspector General, National Credit Union Administration and
the National Credit Union Administration Board:

Report on the Financial Statements

We have audited the accompanying financial statements of the National Credit Union Share Insurance Fund (NCUSIF), which comprise the balance sheets as of December 31, 2015 and 2014, and the related statements of net cost, changes in net position, and statements of budgetary resources for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 15-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Credit Union Share Insurance Fund as of December 31, 2015 and 2014, and its net



costs, changes in net position, and budgetary resources for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the information in the Overview and Required Supplementary Information sections be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended December 31, 2015, we considered the NCUSIF's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the NCUSIF's internal control. Accordingly, we do not express an opinion on the effectiveness of the NCUSIF's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the NCUSIF's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of compliance disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 15-02.



Purpose of the Other Reporting Required by Government Auditing Standards

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the NCUSIF's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

February 12, 2016

NATIONAL CREDIT UNION SHARE INSURANCE FUND

BALANCE SHEETS

As of December 31, 2015 and 2014

(Dollars in thousands)

	<u>2015</u>	<u>2014</u>
ASSETS		
INTRAGOVERNMENTAL		
Fund Balance with Treasury (Note 2)	\$ 2,411	\$ 10,493
Investments, Net - U.S. Treasury Securities (Note 3)	12,079,490	11,611,538
Accounts Receivable - Other	106	-
Accrued Interest Receivable (Note 3)	59,867	59,700
Note Receivable - Note due from the National Credit Union Administration Operating Fund (Note 5)	<u>10,392</u>	<u>11,733</u>
Total Intragovernmental Assets	<u>12,152,266</u>	<u>11,693,464</u>
PUBLIC		
Notes Receivable, Net (Note 5)	108,568	174,213
Accounts Receivable - Due from Insured Credit Unions, Net (Note 4)	2	1,586
Accrued Interest Receivable - Notes (Note 5)	253	396
General Property, Plant and Equipment, Net (Note 6)	1,784	128
Other - Receivables from Asset Management Estates (AMEs), Net (Note 7)	65,779	87,785
Other Assets	<u>-</u>	<u>35</u>
Total Public Assets	<u>176,386</u>	<u>264,143</u>
TOTAL ASSETS	<u>\$ 12,328,652</u>	<u>\$ 11,957,607</u>
LIABILITIES		
INTRAGOVERNMENTAL		
Accounts Payable - Due to the National Credit Union Administration Operating Fund (Note 10)	<u>\$ 3,944</u>	<u>\$ 3,509</u>
Total Intragovernmental Liabilities	3,944	3,509
PUBLIC		
Accounts Payable	3,372	425
Other - Insurance and Guarantee Program Liabilities (Note 8)	164,857	178,318
Other Liabilities	<u>318</u>	<u>-</u>
Total Public Liabilities	<u>168,547</u>	<u>178,743</u>
TOTAL LIABILITIES	<u>172,491</u>	<u>182,252</u>
Commitments and Contingencies (Note 8)		
NET POSITION		
Contributed Capital (Note 13)	9,353,113	8,944,099
Cumulative Result of Operations	<u>2,803,048</u>	<u>2,831,256</u>
Total Net Position	<u>12,156,161</u>	<u>11,775,355</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 12,328,652</u>	<u>\$ 11,957,607</u>

The accompanying notes are an integral part of these financial statements.

NATIONAL CREDIT UNION SHARE INSURANCE FUND

STATEMENTS OF NET COST

For the Years Ended December 31, 2015 and 2014

(Dollars in thousands)

	<u>2015</u>	<u>2014</u>
GROSS COSTS		
Operating Expenses	\$ 197,752	\$ 179,818
Provision for Insurance Losses		
Reserve Expense (Reduction) (Note 8)	(250)	3,298
AME Receivable Bad Debt Expense (Reduction) (Note 7)	<u>(35,161)</u>	<u>(45,138)</u>
Total Gross Costs	<u>162,341</u>	<u>137,978</u>
 LESS EARNED REVENUES		
Interest Revenue on Note Receivable from the National Credit Union Administration Operating Fund (Note 5)	(206)	(229)
Interest Revenue on Notes (Note 5)	(3,527)	(3,142)
Insurance and Guarantee Premium Revenue and Other Revenue	<u>(1,454)</u>	<u>(2,262)</u>
Total Earned Revenues	<u>(5,187)</u>	<u>(5,633)</u>
 TOTAL NET COST OF OPERATIONS	 <u>\$ 157,154</u>	 <u>\$ 132,345</u>

The accompanying notes are an integral part of these financial statements.

NATIONAL CREDIT UNION SHARE INSURANCE FUND**STATEMENTS OF CHANGES IN NET POSITION****For the Years Ended December 31, 2015 and 2014****(Dollars in thousands)**

	<u>2015</u>	<u>2014</u>
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 2,831,256	\$ 2,619,929
BUDGETARY FINANCING SOURCES		
Non-Exchange Revenue		
Interest Revenue - Investments	218,526	208,259
OTHER FINANCING SOURCES		
Non-Exchange Revenue		
Net Unrealized Gain/(Loss) - Investments (Note 3)	<u>(89,580)</u>	<u>135,413</u>
Total Financing Sources	128,946	343,672
Net Cost of Operations	<u>(157,154)</u>	<u>(132,345)</u>
Net Change	<u>(28,208)</u>	<u>211,327</u>
CUMULATIVE RESULTS OF OPERATIONS	<u>2,803,048</u>	<u>2,831,256</u>
CONTRIBUTED CAPITAL (Note 13)		
Beginning Balances	8,944,099	8,661,174
Change in Contributed Capital	<u>409,014</u>	<u>282,925</u>
CONTRIBUTED CAPITAL	<u>9,353,113</u>	<u>8,944,099</u>
NET POSITION	<u>\$ 12,156,161</u>	<u>\$ 11,775,355</u>

The accompanying notes are an integral part of these financial statements.

NATIONAL CREDIT UNION SHARE INSURANCE FUND

STATEMENTS OF BUDGETARY RESOURCES

For the Years Ended December 31, 2015 and 2014

(Dollars in thousands)

	<u>2015</u>	<u>2014</u>
BUDGETARY RESOURCES (Notes 12 and 15)		
Unobligated balance, brought forward, January 1	\$ 11,333,233	\$ 10,895,555
Spending authority from offsetting collections (mandatory)		
Collected	882,031	804,885
Change in receivables from federal sources	273	103
Anticipated nonexpenditure transfer	-	-
TOTAL BUDGETARY RESOURCES	<u>\$ 12,215,537</u>	<u>\$ 11,700,543</u>
STATUS OF BUDGETARY RESOURCES		
Obligations incurred	\$ 304,828	\$ 367,310
Unobligated balance, end of year:		
Exempt from apportionment	<u>11,910,709</u>	<u>11,333,233</u>
Total unobligated balance, end of year	<u>11,910,709</u>	<u>11,333,233</u>
TOTAL STATUS OF BUDGETARY RESOURCES	<u>\$ 12,215,537</u>	<u>\$ 11,700,543</u>
CHANGE IN OBLIGATED BALANCE		
Unpaid Obligations:		
Unpaid obligations, brought forward, January 1	\$ 8,054	\$ 10,377
Obligations incurred	304,828	367,310
Outlays (gross)	<u>(302,616)</u>	<u>(369,633)</u>
Unpaid obligations, end of year	<u>\$ 10,266</u>	<u>\$ 8,054</u>
Uncollected payments:		
Uncollected customer payments from federal sources, brought forward, January 1	\$ (59,700)	\$ (59,597)
Change in uncollected customer payments from Federal sources	<u>(273)</u>	<u>(103)</u>
Uncollected customer payments from Federal sources, end of year	<u>\$ (59,973)</u>	<u>\$ (59,700)</u>
Obligated balance, start of year (net)	<u>\$ (51,646)</u>	<u>\$ (49,220)</u>
Obligated balance, end of year (net)	<u>\$ (49,707)</u>	<u>\$ (51,646)</u>
BUDGET AUTHORITY AND OUTLAYS, NET		
Budget authority, gross (mandatory)	\$ 882,304	\$ 804,988
Actual offsetting collections (mandatory)	(882,031)	(804,885)
Change in uncollected customer payments from Federal sources (mandatory)	(273)	(103)
Anticipated offsetting collections (mandatory)	-	-
BUDGET AUTHORITY, NET (MANDATORY)	<u>\$ -</u>	<u>\$ -</u>
Outlays, gross (mandatory)	\$ 302,616	\$ 369,633
Actual offsetting collections (mandatory)	<u>(882,031)</u>	<u>(804,885)</u>
Outlays, net (discretionary and mandatory)	<u>(579,415)</u>	<u>(435,252)</u>
AGENCY OUTLAYS, NET (MANDATORY)	<u>\$ (579,415)</u>	<u>\$ (435,252)</u>

The accompanying notes are an integral part of these financial statements.

NATIONAL CREDIT UNION SHARE INSURANCE FUND

NOTES TO FINANCIAL STATEMENTS

For the Years Ended December 31, 2015 and 2014

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The National Credit Union Share Insurance Fund (NCUSIF) was created by Title II of the *Federal Credit Union Act*, Public Law 73-467, as amended (FCU Act), 12 U.S.C. § 1781 *et seq.* The NCUSIF was established as a revolving fund in the Treasury of the United States (U.S. Treasury), under management of the National Credit Union Administration (NCUA) Board (NCUA Board) for the purpose of insuring member share deposits in all Federal Credit Unions (FCUs) and in qualifying state-chartered credit unions requesting insurance.

The NCUA exercises direct supervisory authority over FCUs and coordinates required supervisory involvement with the state chartering authorities for state-chartered credit unions insured by the NCUSIF. Federally insured (insured) credit unions are required to report certain financial and statistical information to NCUA on a quarterly basis and are subject to periodic examination by the NCUA. Information derived through the supervision and examination process provides the NCUA with the ability to identify insured credit unions experiencing financial difficulties that may require assistance from the NCUSIF.

Assistance from the NCUSIF may be in the form of a waiver of statutory reserve requirements, liquidity assistance in the form of a guaranteed line of credit pursuant to Section 208 of the FCU Act, cash assistance in the form of a subordinated note pursuant to Section 208 of the FCU Act, or other such form. In some cases, a merger partner for the credit union may be sought. Mergers between financially troubled credit unions and stronger credit unions may also require NCUSIF assistance. Merger assistance may be in the form of cash assistance, purchase of certain assets by the NCUSIF, and/or guarantees of the values of certain assets (e.g., primarily loans). When a credit union is no longer able to continue operating and the merger and assistance alternatives are not practical, the NCUSIF or the appropriate state supervisory authority may liquidate the credit union. In the event of a credit union liquidation, the NCUSIF pays members' shares up to the maximum insured amount and monetizes the credit union's assets.

Fiduciary Responsibilities

Fiduciary activities are the collection or receipt, management, protection, accounting, investment, or disposition by the Federal Government of cash or other assets, in which non-federal individuals or entities have an ownership interest that the Federal Government must uphold. NCUA's Asset Management and Assistance Center (AMAC) conducts liquidations and performs management and recovery of assets for failed credit unions. Assets and liabilities of liquidated credit unions reside in Asset Management Estates (AMEs). These assets and liabilities are held in part, for the primary benefit of non-federal parties and therefore are considered fiduciary in accordance with Federal Accounting Standards Advisory Board (FASAB) Statement of Federal Financial Accounting Standards (SFFAS) No. 31, *Accounting*

for Fiduciary Activities. Fiduciary assets are not assets of the Federal Government and therefore are not recognized on the Balance Sheet. Additionally, NCUA entity assets are non-fiduciary.

Sources of Funding

Deposits insured by the NCUSIF are backed by the full faith and credit of the United States. The NCUSIF has multiple sources of funding. Each insured credit union is required to deposit and maintain in the NCUSIF 1.00% of its insured shares. The NCUA Board may also assess premiums to all insured credit unions, as provided by the FCU Act.

In addition, the NCUSIF has borrowing authority, shared with the Temporary Corporate Credit Union Stabilization Fund (TCCUSF), from the U.S. Treasury and the ability to borrow from NCUA's Central Liquidity Facility (CLF).

Basis of Presentation

The NCUSIF's financial statements have been prepared from its accounting records in accordance with the FASAB's SFFAS. The American Institute of Certified Public Accountants recognizes FASAB as the official accounting standards-setting body of the Federal Government. The format of the financial statements and notes is in accordance with the form and content guidance provided in Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*, revised August 4, 2015.

Consistent with SFFAS No. 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*, NCUA considers and where appropriate, applies Financial Accounting Standards Board (FASB) guidance for those instances where no applicable FASAB guidance is available. Any such significant instances are identified herein.

Basis of Accounting

In its accounting structure, the NCUSIF records both proprietary and budgetary accounting transactions. Following the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to the actual collection or payment of cash.

Federal budgetary accounting recognizes the obligation, borrowing authorities, and other fund resources upon the establishment of a properly documented legal liability, which may be different from the recording of an accrual-based transaction. The recognition of budgetary accounting transactions is essential for compliance with legal controls over the use of federal funds and compliance with budgetary laws.

NCUA, including the NCUSIF, is exempt from requirements under the *Federal Credit Reform Act of 1990* (2 U.S.C. § 661 et seq.).

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) for the Federal Government requires management to make estimates and assumptions that affect the following:

- reported amounts of assets and liabilities;
- disclosure of contingent assets and liabilities at the date of the financial statements; and
- the amounts of revenues and expenses reported during that period.

Actual results could differ from estimates. Significant items subject to those estimates and assumptions include (i) reserves for probable losses and contingencies related to Insurance and Guarantee Program Liabilities; (ii) the amount and timing of recoveries, if any, related to any claims paid and settlement of the guarantee liabilities; (iii) allowance amounts established for loan loss related to cash assistance provided to insured credit unions; and (iv) allowance amounts for losses on the receivables from AMEs.

Fund Balance with Treasury

Fund Balance with Treasury (FBWT) is the aggregate amount of the NCUSIF's accounts with the Federal Government's central accounts, from which the NCUSIF is authorized to make expenditures and pay liabilities. The entire FBWT is a revolving fund type.

Investments

Investment securities primarily consist of marketable U.S. Treasury securities of varying maturities (debt securities). The NCUSIF also holds non-marketable U.S. Treasury overnight securities purchased and reported at par value, which are classified as held to maturity. All marketable securities are carried as available-for-sale, in accordance with FASB Accounting Standards Codification (ASC) 320, *Investments – Debt and Equity Securities*.

Interest earned and unrealized holding gains and losses on U.S. Treasury securities are excluded from net costs and reported as components of non-exchange revenue. Realized gains and losses from the sale of available-for-sale securities are determined on a specific identification basis.

All U.S. Treasury securities that are in an unrealized loss position are reviewed for other-than-temporary impairment (OTTI). The NCUSIF evaluates its U.S. Treasury securities on a monthly basis. An investment security is deemed impaired if the fair value of the investment is less than its amortized cost. Amortized cost includes adjustments (if any) made to the cost basis of an investment for accretion, amortization, and previous OTTI. To determine whether impairment is an OTTI, the NCUA takes into consideration whether it has the intent to sell the security. The NCUA also considers available evidence to assess whether it is more likely than not that it will be required to sell the debt security before the recovery of its amortized cost basis. If the NCUA intends to sell, or more likely than not will be required to sell the security before recovery of its amortized cost basis, an OTTI shall be considered to have occurred.

Premiums and discounts are amortized or accreted over the life of the related available-for-sale security as an adjustment to yield using the effective interest method.

Accounts Receivable

Accounts receivable represent the NCUSIF's claims for payment from other entities. Gross receivables are reduced to net realizable value by an allowance for doubtful accounts as further discussed below. Public accounts receivable represent accounts receivable between the NCUSIF and a non-federal entity.

Capitalization Deposits from Insured Credit Unions

Each insured credit union pays to and maintains with the NCUSIF a capitalization deposit amount equal to 1.00% of its insured shares. Receivables and associated non-exchange revenue are recognized upon invoicing.

Premium Assessments from Insured Credit Unions

The NCUA Board has the statutory authority according to the FCU Act Section 202, *Administration of the Insurance Fund*, to assess insured credit unions for a premium charge. The NCUA Board may assess each insured credit union a premium charge for insurance in an amount stated as a percentage of insured shares outstanding as of the most recently ended reporting period if the NCUSIF's equity ratio, as defined, is less than 1.30%. When the NCUA Board projects that the equity ratio will, within six months, fall below 1.20%, the NCUA Board must establish and implement a restoration plan within 90 days, which meets the statutory requirements and any further conditions that the NCUA Board determines appropriate. In order to meet statutory requirements, the plan must provide that the equity ratio will meet or exceed the minimum amount specified of 1.20% before the end of the 8-year period beginning upon the implementation of the plan (or such longer period as the NCUA Board may determine to be necessary due to extraordinary circumstances).

The NCUA Board did not assess premiums for 2015 and 2014.

Allowance for Doubtful Accounts

An allowance for doubtful accounts is the NCUA's best estimate of the amount of losses in an existing NCUSIF receivable. Based on an assessment of collectability, the NCUSIF calculates an allowance on an individual account basis for public accounts receivable. An account may be impaired or written off if it is probable that the NCUSIF will not collect all principal and interest contractually due. No allowance is calculated for intragovernmental accounts receivable, as these are deemed to be fully collectible.

Accrued Interest Receivable

The NCUSIF recognizes accrued interest receivable for amounts of interest contractually earned but not yet received.

Notes Receivable, Net

Notes Receivable, Net represent loans to insured credit unions as authorized by the NCUA Board, including assistance under Section 208 of the FCU Act. Any related allowance for loss represents the difference between the funds disbursed and the expected repayment from the insured credit unions.

General Property, Plant and Equipment, Net

General Property, Plant and Equipment consists of internal-use software and assets under capital lease, and is recognized and measured in accordance with SFFAS No. 6, *Accounting for Property, Plant, and Equipment*, as amended by SFFAS Nos. 10, 23, 35 and 44.

In 2015, NCUSIF adopted SFFAS No. 44, *Accounting For Impairment Of General Property, Plant, And Equipment Remaining In Use*.

Incurred costs for internal use software during the software development phase are capitalized in accordance with SFFAS No. 10, *Accounting for Internal Use Software*. General Property, Plant and Equipment is subject to depreciation and carried at net cost once placed into service. Depreciation and amortization are recognized over the useful life of the asset.

Other - Receivables from Asset Management Estates, Net

Receivables from AMEs, Net include claims to recover payments made by the NCUSIF to satisfy obligations to insured shareholders and to recoup administrative expenses paid on behalf of AMEs. A related allowance for loss represents the difference between the funds disbursed and obligations incurred and the expected repayment, when recognized, from the AMEs pursuant to the liquidation payment priorities set forth in 12 C.F.R. § 709.5(b). Assets held by the AMEs are the main source of repayment of the NCUSIF's receivables from the AMEs. The recoveries from these AME assets are paid to the NCUSIF as AME assets are monetized and to the extent a receivable is due for share payout obligations and administrative expenses.

The allowance for loss on receivables from AMEs is based on expected asset recovery rates, and come from several sources including:

- actual or pending AME asset disposition data;
- asset valuation data based upon the performance, quality, and type of the assets in the portfolio;
- estimated liquidation costs based on information from similar recently failed credit unions; and
- estimated AME specific administrative expenses based upon complexity and expected duration of the AME.

Expected asset recovery rates are evaluated during the year, but remain subject to uncertainties because of potential changes in economic and market conditions.

Distribution Payable

In accordance with SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, the NCUSIF records a non-exchange liability, per Section 202(c)(3) of the FCU Act, *Distributions from Fund Required*, for unpaid amounts due as of the reporting date, as discussed herein.

Per Section 202(c)(3) of the FCU Act, *Distributions from Fund Required*, the NCUA Board shall effect a pro rata distribution to insured credit unions after each calendar year, if:

- (i) any loans to the NCUSIF from the Federal Government, and any interest on those loans, have been repaid;
- (ii) the NCUSIF's equity ratio exceeds the normal operating level of 1.30%; and

- (iii) the NCUSIF's available assets ratio exceeds 1.00%.

The amount of share distribution should equal the maximum possible amount that does not reduce the NCUSIF's equity ratio below the normal operating level of 1.30%, and does not reduce the NCUSIF's available assets ratio below 1.00%.

At the end of any calendar year in which the TCCUSF or the NCUSIF has an outstanding advance from the U.S. Treasury, the NCUSIF is prohibited from making the distribution to insured credit unions described under Section 202 of the FCU Act. As of December 31, 2015 and 2014, the TCCUSF had an outstanding advance from the U.S. Treasury. Where the TCCUSF has an outstanding advance from the U.S. Treasury, Section 217(e) of the FCU Act requires the NCUSIF to make a distribution to the TCCUSF of the maximum amount possible that does not reduce the NCUSIF's equity ratio below the normal operating level of 1.30% and does not reduce the NCUSIF's available assets ratio below 1.00%.

Capital Leases

In accordance with SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, and SFFAS No. 6, *Accounting for Property, Plant, and Equipment*, the NCUSIF records a depreciable asset and liability for all capital leases at the present value of the rental and other minimum lease payments during the lease term.

Insurance and Guarantee Program Liabilities

In accordance with SFFAS No. 5, all federal insurance and guarantee programs, except social insurance and loan guarantee programs, should recognize a liability for:

- unpaid claims incurred, resulting from insured events that have occurred as of the reporting date;
- a contingent liability when an existing condition, situation, or set of circumstances involving uncertainty as to possible loss exists, and the uncertainty will ultimately be resolved when one or more probable future events occur or fail to occur; and
- a future outflow or other sacrifice of resources that is probable.

The NCUSIF records a contingent liability for probable losses relating to insured credit unions. Through NCUA's supervision process, NCUA applies a supervisory rating system to assess each credit union's relative health in the adequacy of Capital, the quality of Assets, the capability of Management, the quality and level of Earnings, and the adequacy of Liquidity (CAMEL), applying a rating ranging from "1" (strongest) to "5" (weakest). The year-end contingent liability is derived by using an internal econometric model that applies estimated failure and loss rates and takes into account the historical loss history, CAMEL ratings, credit union level financial ratios, and other conditions. In addition, credit union specific analysis is performed on those credit unions where failure is imminent or where additional information is available that may affect the estimate of losses. In such cases, specific reserves are established.

Liabilities for loss contingencies also arise from claims, assessments, litigation, fines, penalties, and other sources. These loss contingencies are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred for any contingencies.

Net Position and Contributed Capital

Each insured credit union pays and maintains with the NCUSIF a capitalization deposit in the amount equal to 1.00% of its insured shares. The NCUSIF reports the capitalization deposits from member credit unions as contributed capital. This amount is included in the NCUSIF's Balance Sheets and Statements of Changes in Net Position.

Revenue Recognition

Exchange Revenue

Exchange revenues arise and are recognized when a Federal Government entity provides goods and services to the public or to another Federal Government entity for a price. Exchange revenue primarily consists of premium assessments, the purpose of which is to recover the losses of the credit union system.

Non-Exchange Revenue

Non-exchange revenues are inflows of resources that the Federal Government demands or receives by donation. Such revenues are recognized when a specifically identifiable, legally enforceable claim to resources arises, to the extent that collection is probable (more likely than not) and the amount is reasonably estimable. NCUSIF recognizes non-exchange revenue as described below.

Each insured credit union pays to and maintains with the NCUSIF a capitalization deposit amount equal to 1.00% of its insured shares. This amount is recognized as non-exchange revenue upon receipt. In accordance with SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, interest revenue on investments in U.S. Treasury securities is recognized as non-exchange revenue because the main source of funds for investments comes from capital deposits. Additionally, the related unrealized holding gains and losses on investments in U.S. Treasury securities are excluded from net costs and reported as a component of non-exchange revenue.

Tax-Exempt Status

NCUA, as a government entity, is not subject to federal, state, or local income taxes and accordingly, no provision for income taxes is recorded for the NCUSIF.

Reclassification

Certain prior year amounts have been reclassified to conform to the current year presentation.

2. FUND BALANCE WITH TREASURY

FBWT balances and status at December 31, 2015 and 2014, consisted of the following (in thousands):

	<u>2015</u>	<u>2014</u>
Total Fund Balance with Treasury: Revolving Funds	\$ <u>2,411</u>	\$ <u>10,493</u>
Status of Fund Balance with Treasury:		
Unobligated Balance - Available	\$ 11,910,709	\$ 11,333,233
Obligated Balances Not Yet Disbursed	10,266	8,054
Non-Budgetary Investment Accounts	(11,858,591)	(11,271,094)
Non-FBWT Budgetary Accounts	<u>(59,973)</u>	<u>(59,700)</u>
Total	\$ <u>2,411</u>	\$ <u>10,493</u>

As a revolving fund, the FBWT is used for continuing business-like activities. The NCUSIF collects premiums and capitalization deposits, which in turn are invested in U.S. Treasury securities. The proceeds are primarily held to cover insurance losses and are also used for merger assistance, liquidations, and other administrative expenses, without requirement for annual appropriations. FBWT contains monies available for future obligations as well as monies obligated for current activities. Non-budgetary Investment accounts, which consist of U.S. Treasury investments, reduce the status of fund balance. Non-FBWT Budgetary Accounts consist of budgetary receivables and nonexpenditure transfers.

As of December 31, 2015 and 2014, there were no unreconciled differences between U.S. Treasury records and balances reported on the NCUSIF's general ledger.

3. INVESTMENTS

The FCU Act, Section 203(c), as amended, provides guidance regarding U.S. Treasury security investments. All investments at the NCUSIF pertain to marketable (available-for-sale) U.S. Treasury securities of varying maturities and non-marketable (held to maturity) U.S. Treasury daily overnight securities. Premiums or discounts on available-for-sale securities are amortized using the effective interest method.

As of December 31, 2015 and 2014, the carrying amount, gross unrealized holding gains, gross unrealized holding losses, and fair value of U.S. Treasury securities were as follows (in thousands):

	Cost	Amortized (Premium) Discount	Interest Receivable	Investments, Net (Par)	Net Unrealized Gain (Loss)	Carrying/ Fair Value
As of December 31, 2015:						
U.S. Treasury Securities						
Available-for-Sale	\$ 12,040,813	\$ (163,233)	\$ 59,867	\$ 11,800,000	\$ 60,733	\$ 11,938,313
Held to Maturity	141,177	-	-	141,177	-	141,177
Total	<u>\$ 12,181,990</u>	<u>\$ (163,233)</u>	<u>\$ 59,867</u>	<u>\$ 11,941,177</u>	<u>\$ 60,733</u>	<u>\$ 12,079,490</u>
As of December 31, 2014:						
U.S. Treasury Securities						
Available-for-Sale	\$ 11,496,631	\$ (209,040)	\$ 59,700	\$ 11,170,000	\$ 150,312	\$ 11,437,903
Held to Maturity	173,635	-	-	173,635	-	173,635
Total	<u>\$ 11,670,266</u>	<u>\$ (209,040)</u>	<u>\$ 59,700</u>	<u>\$ 11,343,635</u>	<u>\$ 150,312</u>	<u>\$ 11,611,538</u>

Maturities of U.S. Treasury securities as of December 31, 2015 and 2014 were as follows (in thousands):

	2015 Fair Value	2014 Fair Value
Held to Maturity (Overnights)	\$ 141,177	\$ 173,635
Available-for-Sale:		
Due in one year or less	2,070,703	2,095,075
Due after one year through five years	4,087,657	4,536,594
Due after five years through ten years	<u>5,779,953</u>	<u>4,806,234</u>
	<u>\$ 12,079,490</u>	<u>\$ 11,611,538</u>

There were no realized gains or losses for the years ended December 31, 2015 and 2014.

The following table includes gross unrealized losses on investment securities, for which OTTI has not been recognized, in addition to the fair values of those securities, aggregated by investment classification and length of time the investments have been in a loss position, at December 31, 2015 and 2014 (in thousands):

	Losses		Losses		Total	
	Less than 12 months		12 months or more			
	Unrealized Losses	Fair Value	Unrealized losses	Fair value	Unrealized losses	Fair value
As of December 31, 2015:						
Available-for-Sale:						
U.S. Treasury Securities	<u>\$ (58,077)</u>	<u>\$ 4,484,500</u>	<u>\$ (15,025)</u>	<u>\$ 959,781</u>	<u>\$ (73,102)</u>	<u>\$ 5,444,281</u>
As of December 31, 2014:						
Available-for-Sale:						
U.S. Treasury Securities	<u>\$ (2,378)</u>	<u>\$ 755,516</u>	<u>\$ (49,055)</u>	<u>\$ 2,213,719</u>	<u>\$ (51,433)</u>	<u>\$ 2,969,235</u>

4. ACCOUNTS RECEIVABLE

Public – Accounts Receivable

Accounts Receivable Due from Insured Credit Unions

As of December 31, 2015 and 2014, accounts receivable due from insured credit unions were \$2.0 thousand and \$1.6 million, respectively. As none of these amounts were deemed uncollectible, the allowance for doubtful accounts on public accounts receivable as of December 31, 2015 and 2014 was \$0.

5. NOTES RECEIVABLE

Intragovernmental – Notes Receivable

Note Due from the NCUA Operating Fund

In 1992, the NCUSIF lent \$42.0 million to the NCUA Operating Fund, pursuant to a 30-year note secured by the NCUA premises in Alexandria, Virginia. Interest income recognized was approximately \$206.0 thousand and \$228.6 thousand for the years ended December 31, 2015 and 2014, respectively. The note receivable balance as of December 31, 2015 and 2014 was approximately \$10.4 million and \$11.7 million, respectively.

The variable rate on the note is equal to the NCUSIF's prior-month yield on investments. The average interest rate for the years ended December 31, 2015 and 2014 was 1.87% and 1.85%, respectively. The interest rate as of December 31, 2015 and 2014 was 1.90% and 1.87%, respectively.

As of December 31, 2015, the above note requires principal repayments as follows (in thousands):

<u>Years Ending December 31</u>	<u>Secured Term Note</u>
2016	\$ 1,341
2017	1,341
2018	1,341
2019	1,341
2020	1,341
Thereafter	<u>3,687</u>
Total	<u>\$ 10,392</u>

Public – Notes Receivable

As of December 31, 2015, the NCUSIF did not have any outstanding capital notes due from insured credit unions. At December 31, 2014, the NCUSIF held two outstanding capital notes due from insured credit unions. Both outstanding capital notes were repaid during 2015. The capital notes receivable totaled \$0 and \$54.6 million and the related allowance for loss was \$0 and \$7.1 million, for a net capital note receivable of \$0 and \$47.5 million as of December 31, 2015 and 2014, respectively. These capital notes were subordinated to all shareholders, creditors, and any other such financial obligations. Accrued interest on the notes was due on a semi-annual basis. Interest on these notes had fixed and variable terms.

The NCUSIF had an outstanding collateralized senior note due from an insured credit union for \$108.6 million and \$126.7 million as of December 31, 2015 and 2014, respectively. There was no related allowance for loss as of December 31, 2015 and 2014. Accrued interest on the notes is due on a monthly basis. Interest on this note had variable terms through December 2014. In December 2014, the outstanding collateralized senior note was modified to mutually benefit the NCUSIF and the insured credit union. The resulting modification resulted in changing the interest rate from variable to a fixed term over the remaining life of the senior note.

As of December 31, 2015 and 2014, the accrued interest receivable for the notes totaled \$252.8 thousand and \$395.8 thousand, respectively.

6. GENERAL PROPERTY, PLANT AND EQUIPMENT, NET

The components of General Property, Plant and Equipment as of December 31, 2015 and 2014 were as follows (in thousands):

	<u>Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>
As of December 31, 2015:			
Assets under Capital Lease	\$ 473	\$ (145)	\$ 328
Internal-Use Software	561	(561)	-
Internal-Use Software under Development	<u>1,456</u>	<u>-</u>	<u>1,456</u>
Total General Property, Plant and Equipment	<u>\$ 2,490</u>	<u>\$ (706)</u>	<u>\$ 1,784</u>
As of December 31, 2014:			
Assets under Capital Lease	\$ -	\$ -	\$ -
Internal-Use Software	561	(561)	-
Internal-Use Software under Development	<u>128</u>	<u>-</u>	<u>128</u>
Total General Property, Plant and Equipment	<u>\$ 689</u>	<u>\$ (561)</u>	<u>\$ 128</u>

Assets under capital lease are depreciable over 39 months, which corresponds with the life of the underlying capital lease. Current internal use software under development is expected to have a useful life of 5 years when placed into service.

As of December 31, 2015 and 2014, the NCUSIF included \$97.9 thousand and \$20.9 thousand, respectively, in internal labor costs attributable to internal use software during its software development stage. NCUSIF reimburses the Operating Fund for these internal labor costs since these costs are incurred by the Operating Fund.

7. OTHER – RECEIVABLES FROM ASSET MANAGEMENT ESTATES

As of December 31, 2015 and 2014, the receivable from AMEs was \$988.0 million and \$1.0 billion, and the related allowance for loss was \$922.2 million and \$953.0 million, for a net receivable from AMEs of \$65.8 million and \$87.8 million, respectively (in thousands).

	<u>2015</u>	<u>2014</u>
Gross Receivable from AME	\$ 987,963	\$ 1,040,764
Allowance for Loss, beginning balance	952,979	963,424
AME Receivable Bad Debt		
Expense (Reduction)	(35,161)	(45,138)
Increase in Allowance	11,776	43,888
Write-off of Cancelled Charters	(7,410)	(9,195)
Allowance for Loss, ending balance	<u>922,184</u>	<u>952,979</u>
Receivable from AME, Net	<u>\$ 65,779</u>	<u>\$ 87,785</u>

AME Receivable Bad Debt Reduction represents overall increases in expected asset recovery rates and related repayments. The Increase in Allowance primarily represents the net loss on payments made during liquidation. Write-off of Cancelled Charters represent recognizing the final loss or recovery upon closing the AME.

8. OTHER LIABILITIES – INSURANCE AND GUARANTEE PROGRAM LIABILITIES

NCUA identifies insured credit unions experiencing financial difficulty through NCUA's supervisory and examination process. On both a general and specific case basis, management determines the estimated losses from these credit unions. NCUA also evaluates overall economic trends and monitors potential system-wide risk factors, such as increasing levels of consumer debt, bankruptcies, and delinquencies. NCUA applies the CAMEL rating system to assess an insured credit union's financial condition and operations. The CAMEL rating system is a tool to measure risk and allocate resources for supervisory purposes. NCUA periodically reviews the CAMEL rating system to respond to continuing economic and regulatory changes in the credit union industry. The general reserve at year-end is derived by using an internal econometric model that applies estimated failure and loss rates and takes into account the historical loss history, CAMEL ratings, credit union level financial ratios, and other conditions. The anticipated losses are net of estimated recoveries from the disposition of the assets of failed credit unions. The total reserves for both identified and anticipated losses resulting from insured credit union failures were \$164.9 million and \$178.3 million as of December 31, 2015 and 2014, respectively.

In exercising its supervisory function, the NCUSIF will occasionally extend guarantees of assets (primarily loans) to third-party purchasers or existing insured credit unions in order to facilitate mergers. The NCUSIF would be obligated upon borrower nonperformance. There were no guarantees outstanding during 2015 or as of December 31, 2015. There were no guarantees outstanding during 2014 or as of December 31, 2014.

In addition, the NCUSIF may grant a guaranteed line-of-credit to a third-party lender, such as a corporate credit union or bank, if a particular insured credit union were to have a current or

immediate liquidity concern and the third-party lender refuses to extend credit without a guarantee. The NCUSIF would thereby be obligated if the insured credit union failed to perform. Total line-of-credit guarantees of credit unions as of December 31, 2015 and 2014 were approximately \$35.0 million and \$2.2 million, respectively. The insured credit unions borrowed \$0 and \$463.2 thousand from the third-party lender under these lines-of-credit guarantees as of December 31, 2015 and 2014, respectively. As of December 31, 2015 and 2014, the NCUSIF reserved \$707.5 thousand and \$41.8 thousand, respectively, for these guaranteed lines-of-credit. The guarantees expire in March 2016 and March 2015, respectively.

On rare occasions, the NCUSIF may provide indemnifications as part of a merger assistance or purchase and assumption agreement to acquiring credit unions. Such indemnifications make the NCUSIF contingently liable based on the outcome of any legal actions. There were no such indemnification contingencies as of December 31, 2015 and 2014, respectively.

The activity in the Insurance and Guarantee Program Liabilities from insured credit unions and AMEs was as follows (in thousands):

	<u>2015</u>	<u>2014</u>
Beginning balance	\$ 178,318	\$ 220,651
Reserve Expense (Reduction)	(250)	3,298
Insurance losses claims paid	(39,990)	(97,621)
Net Estimated Recovery/Claim on AMEs	<u>26,779</u>	<u>51,990</u>
Ending balance	<u>\$ 164,857</u>	<u>\$ 178,318</u>

The Insurance and Guarantee Program Liabilities at December 31, 2015 and December 31, 2014 were comprised of the following:

- Specific reserves were \$10.0 million and \$5.7 million, respectively. Specific reserves are identified for those credit unions where failure is imminent or where additional information is available that may affect the estimate of losses.
- General reserves were \$154.9 million and \$172.6 million, respectively.

In addition to these recorded contingent liabilities, additional adverse performance in the financial services industry could result in additional losses to the NCUSIF. The ultimate losses for insured credit unions will largely depend upon future economic and market conditions and, accordingly, could differ significantly from these estimates.

9. OTHER LIABILITIES

(a) Capital Lease Liability

NCUSIF leases laptops for state credit union examiners under a capital lease agreement that will run through 2018. Amounts presented in the table below include \$8.4 thousand of imputed interest.

The future minimum lease payments to be paid over the remaining life as of December 31, 2015, are as follows (in thousands):

<u>Years Ending December 31</u>	<u>Minimum Lease Payments</u>
2016	\$ 162
2017	162
2018	41
Total	<u>\$ 365</u>

(b) Distribution Payable

As of December 31, 2015 and 2014, the NCUSIF-calculated equity ratio of 1.26% and 1.29%, respectively, was below its normal operating level of 1.30%; therefore, the NCUSIF did not record or make a distribution to the TCCUSF. As of December 31, 2015 and 2014, the NCUSIF's available assets ratio was 1.24% and 1.27%, respectively. The equity ratio and available assets ratio calculations are discussed in Note 13.

10. INTRAGOVERNMENTAL COSTS AND EXCHANGE REVENUE

Program costs and revenues are separated between intragovernmental and public to facilitate government-wide financial reporting. Intragovernmental revenue and expenses arise from transactions with other federal entities. Public revenue and expenses arise from transactions with domestic and foreign persons and organizations outside of the Federal Government. Intragovernmental costs and exchange revenue as of December 31, 2015 and 2014 were as follows (in thousands):

<u>Intragovernmental Costs and Exchange Revenue</u>	<u>2015</u>	<u>2014</u>
Intragovernmental Costs	\$ 192,301	\$ 175,592
Public Costs/(Cost Reduction)	<u>(29,961)</u>	<u>(37,614)</u>
Total	<u>162,340</u>	<u>137,978</u>
Intragovernmental Exchange Revenue	(206)	(229)
Public Exchange Revenue	<u>(4,980)</u>	<u>(5,404)</u>
Total	<u>(5,186)</u>	<u>(5,633)</u>
Net Cost	<u>\$ 157,154</u>	<u>\$ 132,345</u>

Certain administrative services are provided to the NCUSIF by the NCUA Operating Fund. The NCUSIF is charged by the NCUA Operating Fund for these services based upon an annual allocation factor (Overhead Transfer Rate) approved by the NCUA Board and derived from a study of actual usage. In 2015 and 2014, the allocation to the NCUSIF was 71.8% and 69.2% of NCUA Operating Fund expenses, respectively. The cost of the services allocated to the NCUSIF, which totaled approximately \$192.3 million and \$175.6 million for the years ended December 31, 2015 and 2014, respectively, is reflected as an expense in the Statements of Net Cost and above in Intragovernmental Costs. These transactions are settled monthly. As of

December 31, 2015 and 2014, amounts due to the NCUA Operating Fund for allocated administrative expenses were \$3.9 million and \$3.5 million, respectively. The following table provides a breakdown of the administrative services provided to the NCUSIF by the NCUA Operating Fund (in thousands):

<u>Administrative Services Reimbursed to the NCUA Operating Fund</u>	<u>2015</u>	<u>2014</u>
Employee Salaries	\$ 103,348	\$ 93,858
Employee Benefits	38,917	34,868
Employee Travel	19,567	18,473
Contracted Services	17,484	15,240
Administrative Costs	9,731	9,743
Rent, Communications, and Utilities	<u>3,254</u>	<u>3,410</u>
 Total Services Provided by the NCUA Operating Fund	 <u>\$ 192,301</u>	 <u>\$ 175,592</u>

11. AVAILABLE BORROWING AUTHORITY, END OF PERIOD

The NCUSIF shares \$6.0 billion in borrowing authority from the U.S. Treasury with the TCCUSF. As of December 31, 2015 and 2014, the TCCUSF had \$1.7 billion and \$2.6 billion in borrowing outstanding from the U.S. Treasury, respectively. As a result, as of December 31, 2015 and 2014, the NCUSIF had \$4.3 billion and \$3.4 billion, respectively, in available borrowing authority shared with the TCCUSF.

Under the FCU Act, the NCUSIF also has the ability to borrow from the CLF. The NCUSIF is authorized to borrow from the CLF up to the amount of the CLF's unused borrowing authority. As of December 31, 2015 and 2014, the CLF had statutory borrowing authority of \$5.6 billion and \$5.1 billion, respectively. As of December 31, 2015 and 2014, the CLF had a note purchase agreement with the Federal Financing Bank with a maximum principal of \$2.0 billion and \$2.0 billion, respectively, all of which was unused. Advances made under the current promissory note can be made no later than March 31, 2016.

At December 31, 2015 and 2014, the NCUSIF had \$6.3 billion and \$5.4 billion, respectively, in total available borrowing capacity.

12. DISCLOSURES RELATED TO THE STATEMENTS OF BUDGETARY RESOURCES

The Statements of Budgetary Resources discloses total budgetary resources available to the NCUSIF, and the status of resources as of December 31, 2015 and 2014. Activity impacting budget totals of the overall Federal Government budget is recorded in the NCUSIF's Statements of Budgetary Resources budgetary accounts. As of December 31, 2015 and 2014, the NCUSIF's resources in budgetary accounts were \$12.2 billion and \$11.7 billion, and undelivered orders were \$2.6 million and \$4.2 million, respectively. All liabilities are covered by budgetary resources, excluding the Insurance and Guarantee Program Liabilities because they are contingent liabilities and do not require budgetary resources until the liabilities are no

longer contingent. All obligations incurred by the NCUSIF are reimbursable. The NCUSIF is exempt from OMB apportionment control.

Budgetary resources listed on the NCUSIF's statements and the budgetary resources found in the budget of the Federal Government differ because the NCUSIF's statements are prepared as of December 31, calendar year, rather than as of September 30, the Federal Government's fiscal year end.

13. CONTRIBUTED CAPITAL

The *Credit Union Membership Access Act of 1998*, Public Law 105–219 (CUMAA), mandated changes to the NCUSIF's capitalization provisions effective January 1, 2000. Under Section 202(c) of the FCU Act, each insured credit union must pay to and maintain with the NCUSIF a deposit in an amount equaling 1.00% of the credit union's insured shares. The CUMAA added provisions mandating that the amount of each insured credit union's deposit is adjusted as follows, in accordance with procedures determined by the NCUA Board, to reflect changes in the credit union's insured shares: (i) annually, in the case of an insured credit union with total assets of not more than \$50.0 million; and (ii) semi-annually, in the case of an insured credit union with total assets of \$50.0 million or more. The annual and semi-annual adjustments are based on insured member share deposits outstanding as of December 31 of the preceding year and June 30 of the current year, respectively. The 1.00% contribution is returned to the insured credit union in the event that its insurance coverage is terminated, or is obtained from another source, or the operations of the NCUSIF are transferred from the NCUA Board. As of December 31, 2015 and 2014, contributed capital owed to the NCUSIF totaled \$2.0 thousand and \$649.0 thousand, respectively. As of December 31, 2015 and 2014, contributed capital due to insured credit unions was \$490.4 thousand and \$0, respectively.

Beginning in 2000, the CUMAA mandated that distributions to insured credit unions are determined from specific ratios, which are based upon year-end reports of insured shares. Accordingly, distributions associated with insured shares at year-end are declared and paid in the subsequent year. This was updated with the passage of the *Helping Families Save Their Homes Act of 2009*, Public Law 111-22, which states that at the end of any calendar year in which the TCCUSF has an outstanding advance from the U.S. Treasury, the NCUSIF is prohibited from making the distribution to insured credit unions as described above. In lieu of the distribution, the NCUSIF shall make a distribution to the TCCUSF for the maximum amount possible that does not reduce the NCUSIF's equity ratio below the normal operating level of 1.30% and does not reduce the current available assets ratio below 1.00%.

Pursuant to the FCU Act, the NCUSIF-calculated equity ratio of 1.26% and 1.29% as of December 31, 2015 and 2014, respectively, was below the normal operating level of 1.30%; therefore, the NCUSIF did not estimate or record a distribution as of December 31, 2015 and 2014. Total contributed capital as of December 31, 2015 and 2014 was \$9.4 billion and \$8.9 billion, respectively.

The NCUSIF equity ratio is calculated as the ratio of contributed capital plus cumulative results of operations excluding net cumulative unrealized gains and losses on investments, to the aggregate amount of the insured shares in all insured credit unions.

The NCUSIF's available assets ratio as of December 31, 2015 and 2014 was 1.24% and 1.27%, based on total estimated insured shares as of December 31, 2015 and 2014 of \$961.3 billion and \$903.0 billion, respectively. The NCUSIF available assets ratio, as defined by the FCU Act, is calculated as the ratio of (A) the amount determined by subtracting (i) direct liabilities of the NCUSIF (including the distribution payable to the TCCUSF) and contingent liabilities for which no provision for losses has been made, from (ii) the sum of cash and the market value of unencumbered investments authorized under Section 203(c) of the FCU Act, to (B) the aggregate amount of the insured shares in all insured credit unions.

14. FIDUCIARY ACTIVITIES

Fiduciary activities are the collection or receipt, management, protection, accounting, investment, and disposition by an AME of cash and other assets, in which non-federal individuals or entities have an ownership interest. Fiduciary assets are not assets of the Federal Government. Fiduciary activities are not recognized on the basic financial statements, but are reported on schedules in the notes to the financial statements in accordance with SFFAS No. 31, *Accounting for Fiduciary Activities*. The NCUA Board, as liquidating agent of the AMEs, disburses obligations owed by and collects money due to the liquidating credit unions through AMAC. Following is the Schedule of Fiduciary Activity as of December 31, 2015 and 2014 (in thousands):

<u>Schedule of Fiduciary Activity</u>	<u>2015</u>	<u>2014</u>
Fiduciary Net Liabilities, beginning of year	\$ (958,508)	\$ (973,044)
Net Realized Losses upon Liquidation	(13,391)	(40,188)
Revenues		
Interest on Loans	9,104	11,124
Other Fiduciary Revenues	895	1,338
Expenses		
Professional & Outside Services Expenses	(4,840)	(7,354)
Compensation and Benefits	(1,611)	(1,760)
Other Expenses	(1,385)	(2,287)
Net Change in Recovery Value of Assets and Liabilities		
Net Gain/(Loss) on Loans	28,734	56,354
Net Gain/(Loss) on Real Estate Owned	(1,770)	3,416
Other, Net Gain/(Loss)	6,304	(15,302)
Decrease in Fiduciary Net Liabilities	<u>22,040</u>	<u>5,341</u>
Write off of Fiduciary Liabilities for Cancelled Charters	7,408	9,195
Fiduciary Net Liabilities, end of year	<u>\$ (929,060)</u>	<u>\$ (958,508)</u>

Comparing 2015 activity in the schedule of fiduciary activity with 2014, fiduciary net liabilities improved by \$29.4 million overall, including a decrease in fiduciary net liabilities of \$22.0 million and cancelled charters write-offs of \$7.4 million. The primary drivers were an improvement in net realized losses upon liquidation, improvement in the recovery value of assets and liabilities, and cancelled charters. The net realized losses upon liquidation decreased by \$26.8 million due, in part, to lower average cost of failure per credit union for liquidations in 2015. The net change in recovery value of assets and liabilities line-items decreased by

\$11.2 million due to rising net realizable values of assets managed. Charter cancellations write-offs decreased by \$1.8 million, corresponding with fewer credit union charter cancellations in 2015.

Revenues consist of cash collected during the liquidation of assets held within the AME. Gains and losses include the revaluation of assets based upon expected asset recovery rates, as well as the disposition of assets and adjustments to liabilities, which contribute to the change in fiduciary net assets/liabilities. Following is the Schedule of Fiduciary Net Assets/Liabilities as of December 31, 2015 and 2014 (in thousands):

<u>Schedule of Fiduciary Net Assets/Liabilities</u>	<u>2015</u>	<u>2014</u>
Fiduciary Assets		
Loans	\$ 72,383	\$ 97,780
Real Estate Owned	9,155	8,387
Other Fiduciary Assets	<u>10,134</u>	<u>7,773</u>
Total Fiduciary Assets	<u>91,672</u>	<u>113,940</u>
Fiduciary Liabilities		
Insured Shares	8,411	9,315
Accrued Liquidation Expenses	17,660	16,551
Unsecured Claims	3,111	1,561
Uninsured Shares	3,587	4,257
Due to NCUSIF (Note 7)	<u>987,963</u>	<u>1,040,764</u>
Total Fiduciary Liabilities	<u>1,020,732</u>	<u>1,072,448</u>
Total Fiduciary Net Assets/(Liabilities)	<u><u>\$ (929,060)</u></u>	<u><u>\$ (958,508)</u></u>

15. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

The Reconciliation of Net Cost of Operations to Budget explains the difference between the budgetary net obligations and the proprietary net cost of operations. The Reconciliation of Net Cost of Operations to Budget consisted of the following (in thousands):

<u>Reconciliation of Net Cost of Operations to Budget</u>	<u>2015</u>	<u>2014</u>
Resources Provided to Finance Activities:		
Budgetary Resources Obligated		
Budgetary Obligations Incurred	\$ 304,828	\$ 367,310
Less: Spending Authority from Offsetting Collections and Change in Receivables from Federal Sources	<u>(882,304)</u>	<u>(804,988)</u>
Net Obligations	(577,476)	(437,678)
Other Resources:		
Net Unrealized (Gain)/Loss	<u>89,580</u>	<u>(135,413)</u>
Total Resources Provided to Finance Activities	<u>(487,896)</u>	<u>(573,091)</u>
Resources Provided to Fund Items Not Part of the Net Cost of Operations:		
Change in Budgetary Resources Obligated for Goods and		
Services Not Yet Received	1,522	(3,306)
Resources that Fund Expenses Recognized in Prior Periods	-	5
Costs Capitalized on the Balance Sheet	558,549	417,917
Other Resources or Adjustments to Net Obligated Resources that do not Affect Net Cost of Operations	<u>120,102</u>	<u>332,732</u>
Total Resources Provided to Fund Items Not Part of the Net Cost of Operations	<u>680,173</u>	<u>747,348</u>
Resources Generated to Finance the Net Cost of Operations	<u>192,277</u>	<u>174,257</u>
Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period		
Provision for Insurance Losses		
Reserve Expense (Reduction)	(250)	3,298
AME Receivable Bad Debt Expense (Reduction)	(35,161)	(45,138)
Increase in Exchange Revenue	143	(67)
Components not Requiring or Generating Resources		
Depreciation Expense	145	-
Other Expenses	<u>-</u>	<u>(5)</u>
Total Components of Net Cost of Operations That Do Not Require or Generate Resources During the Reporting Period	<u>(35,123)</u>	<u>(41,912)</u>
Net Cost of Operations	<u>\$ 157,154</u>	<u>\$ 132,345</u>

Other Resources or Adjustments to Net Obligated Resources that do not Affect Net Cost of Operations consists largely of unrealized losses on investments net of investment revenue and increases to the receivable from AME Allowance due to transfers, net of AME receivable bad debt expense.

16. SUBSEQUENT EVENTS

Subsequent events have been evaluated through February 12, 2016, which is the date the financial statements were available to be issued and management determined that there were no items to disclose.

REQUIRED SUPPLEMENTARY INFORMATION (UNAUDITED)

Risk Assumed Information

Insurance and Guarantee Program Liabilities

As of December 31, 2015 and 2014, the aggregate outstanding insured shares of the insured credit unions were estimated at \$961.3 billion and \$903.0 billion, respectively. This amount represents the maximum potential future guarantee payments that the NCUSIF could be required to make under the share insurance program, without consideration of any possible recoveries. Additionally, to the extent the TCCUSF's obligations exceed the funds available in the TCCUSF, the NCUSIF will provide the necessary funds. These amounts bear no direct relationship to the NCUSIF's anticipated losses.

As discussed previously herein, NCUA identifies credit unions at risk of failure through the supervisory and examination process, and estimates losses based upon economic trends and credit unions' financial condition and operations. NCUA also evaluates overall economic trends and monitors potential credit union system-wide risk factors, such as increasing levels of consumer debt, bankruptcies, and delinquencies. NCUA applies the CAMEL rating system to assess a credit union's financial condition and operations. The CAMEL rating system is a tool to measure risk and allocate resources for supervisory purposes. NCUA periodically reviews the CAMEL rating system to respond to continuing economic and regulatory changes in the credit union industry. The aggregate amount of reserves recognized for credit unions at risk of failure was \$164.9 million and \$178.3 million as of December 31, 2015 and 2014, respectively. At December 31, 2015 and 2014, the general reserves were \$154.9 million and \$172.6 million, respectively. At December 31, 2015 and 2014, the specific reserves resulting from insured credit unions' expected failures were \$10.0 million and \$5.7 million, respectively.

The NCUSIF's contingent liability decreased by \$13.4 million from 2014 to 2015, and decreased by \$42.4 million from 2013 to 2014. The credit union industry improved during 2015 as reflected by the reduction in assets in CAMEL 3, 4 and 5 rated credit unions as compared to 2014. Assets in CAMEL 3, 4 and 5 rated credit unions dropped to \$98.3 billion at the end of 2015, versus \$106.9 billion at the end of 2014. Although the system-wide net worth ratio decreased slightly from 11.0% to 10.9% during 2015, the ratio has shown improvement since 2011. These factors, as well as other trends, helped contribute to a reduction in amounts for the Insurance and Guarantee Program Liabilities on the NCUSIF Balance Sheets.

Fees and Premiums

During 2015 and 2014, the NCUA Board did not assess premiums to insured credit unions from the NCUSIF.

Sensitivity, Risks and Uncertainties of the Assumptions

During 2013, NCUA implemented the use of the econometric reserve model to improve the precision of the future loss forecast. As discussed previously herein, the NCUA estimates the anticipated losses resulting from insured credit union failures by evaluating imminent failures and using an internal econometric model that applies estimated failure and loss rates and takes into account the historical loss history, CAMEL ratings, credit union level financial ratios, and

other conditions. The effectiveness of the reserving methodology is evaluated by applying analytical techniques to review variances between projected losses and actual losses and adjustments are made accordingly. Actual losses will largely depend on future economic and market conditions and could differ materially from the anticipated losses recorded by the NCUSIF as of December 31, 2015.

The development of assumptions for certain key input variables of our estimation model is a highly subjective process that involves significant judgment and will change over time. Future values are difficult to estimate, especially over longer timeframes. Key assumptions in the modeling include failure and loss rates. The failure rate is developed based on actual failures and historical migration trends in the CAMEL ratings, and incorporates actual data on macroeconomic trends such the consumer price index and geographic housing prices, as well as credit union system-wide factors such as delinquencies and charge-offs. The loss rate is partly subjective and is developed based on historical loss experience from actual failures, and incorporates the NCUA's expectations and assumptions about anticipated recoveries. The assumptions developed for the estimation model are periodically evaluated by the NCUA to determine the reasonableness of those assumptions over time.

The internal model provides a range of losses. Per current policy, the minimum in the range of losses is the 75 percent confidence level forecast and the upper bound is the 90 percent confidence level forecast. The NCUSIF general reserve is sensitive to assumptions made about the loss rates under various scenarios. For example, changing the assumptions to exclude statistical outliers for calculating loss rates results in a change in the range of losses. Additionally, management's judgment is used to select a point in the range of projected losses to record probable contingent liabilities in compliance with SFFAS No. 5, which was \$154.9 million in anticipated losses recognized on the NCUSIF's balance sheet at December 31, 2015. In selecting the point in the range of the forecasts, management considers overall credit union economic trends and system-wide risk factors, such as increasing levels of consumer debt, bankruptcies and delinquencies.

Consistent with accounting standards, the assumptions and method used to estimate the anticipated losses will require continued calibration and refinement as circumstances change.

Report #OIG-16-03

National Credit Union Administration Operating Fund

Financial Statements as of and for the Years Ended
December 31, 2015 and 2014, and
Independent Auditors' Report

**NATIONAL CREDIT UNION ADMINISTRATION
OPERATING FUND**

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KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report

Inspector General, National Credit Union Administration and
the National Credit Union Administration Board:

Report on the Financial Statements

We have audited the accompanying financial statements of the National Credit Union Administration Operating Fund (OF), which comprise the balance sheets as of December 31, 2015 and 2014, and the related statements of revenues, expenses and changes in fund balance, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 15-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Credit Union Administration Operating Fund as of December 31, 2015 and 2014, and the results of its operations, changes in fund balance, and cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Reporting Required by Government Auditing Standards

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended December 31, 2015, we considered the OF's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the OF's internal control. Accordingly, we do not express an opinion on the effectiveness of the OF's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the OF's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of compliance disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 15-02.

Purpose of the Other Reporting Required by Government Auditing Standards

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the OF's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

February 12, 2016

**NATIONAL CREDIT UNION ADMINISTRATION
OPERATING FUND**

**BALANCE SHEETS
As of December 31, 2015 and 2014
(Dollars in thousands)**

	<u>2015</u>	<u>2014</u>
ASSETS		
CASH AND CASH EQUIVALENTS (Note 3)	\$ 40,528	\$ 40,940
DUE FROM NATIONAL CREDIT UNION SHARE INSURANCE FUND (Note 7)	3,944	3,509
EMPLOYEE ADVANCES	38	62
OTHER ACCOUNTS RECEIVABLE, Net (Notes 7 and 10)	332	322
PREPAID EXPENSES AND OTHER ASSETS	1,732	2,145
ASSETS HELD FOR SALE (Note 6)	377	644
FIXED ASSETS — Net of accumulated depreciation of \$31,083 and \$28,210 as of December 31, 2015 and December 31, 2014, respectively (Note 4)	31,106	30,279
INTANGIBLE ASSETS — Net of accumulated amortization of \$16,279 and \$15,844 as of December 31, 2015 and December 31, 2014, respectively (Note 5)	<u>2,354</u>	<u>2,904</u>
TOTAL ASSETS	<u>\$ 80,411</u>	<u>\$ 80,805</u>
LIABILITIES AND FUND BALANCE		
LIABILITIES		
Accounts payable and accrued other liabilities	\$ 5,644	\$ 6,598
Obligations under capital leases (Note 8)	1,515	213
Accrued wages and benefits	7,176	12,873
Accrued annual leave	17,243	15,469
Accrued employee travel	646	491
Notes payable to National Credit Union Share Insurance Fund (Note 7)	<u>10,392</u>	<u>11,733</u>
Total liabilities	42,616	47,377
COMMITMENTS AND CONTINGENCIES (Notes 7, 8, 11 & 12)		
FUND BALANCE	<u>37,795</u>	<u>33,428</u>
TOTAL LIABILITIES AND FUND BALANCE	<u>\$ 80,411</u>	<u>\$ 80,805</u>

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
OPERATING FUND**

**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND BALANCE
For the years ended December 31, 2015 and 2014
(Dollars in thousands)**

	<u>2015</u>	<u>2014</u>
REVENUES		
Operating fees	\$ 78,773	\$ 77,875
Interest	22	16
Other	<u>1,100</u>	<u>1,213</u>
Total Revenues	79,895	79,104
EXPENSES, NET (Note 7)		
Employee wages and benefits	55,876	57,294
Travel	7,685	8,222
Rent, communications, and utilities	1,278	1,518
Contracted services	6,867	6,783
Depreciation and amortization	5,533	5,878
Administrative	<u>(1,711)</u>	<u>(1,542)</u>
Total Expenses, Net	<u>75,528</u>	<u>78,153</u>
EXCESS OF REVENUES OVER EXPENSES	4,367	951
FUND BALANCE—Beginning of year	<u>33,428</u>	<u>32,477</u>
FUND BALANCE—End of year	<u>\$ 37,795</u>	<u>\$ 33,428</u>

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
OPERATING FUND**

**STATEMENTS OF CASH FLOWS
For the years ended December 31, 2015 and 2014
(Dollars in thousands)**

	<u>2015</u>	<u>2014</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Excess of revenues over expenses	\$ 4,367	\$ 951
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities:		
Depreciation and amortization	5,533	5,878
Provision for loss on disposal of employee residences held for sale	114	122
Loss on fixed asset and intangible asset retirements	1,184	13
(Increase) decrease in assets:		
Due from National Credit Union Share Insurance Fund	(435)	(196)
Employee advances	24	(24)
Other accounts receivable, net	(10)	(119)
Prepaid expenses and other assets	413	(767)
(Decrease) increase in liabilities:		
Accounts payable	(216)	1,431
Accrued wages and benefits	(5,697)	1,517
Accrued annual leave	1,774	898
Accrued employee travel	155	(577)
Net Cash Provided by Operating Activities	<u>7,206</u>	<u>9,127</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of fixed assets and intangible assets	(5,702)	(3,969)
Proceeds from sale of employee residences held for sale	596	359
Purchases of employee residences held for sale	<u>(443)</u>	<u>(1,125)</u>
Net Cash Used in Investing Activities	<u>(5,549)</u>	<u>(4,735)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayments of notes payable to National Credit Union Share Insurance Fund	(1,341)	(1,341)
Principal payments under capital lease obligations	<u>(728)</u>	<u>(24)</u>
Net Cash Used in Financing Activities	<u>(2,069)</u>	<u>(1,365)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(412)	3,027
CASH AND CASH EQUIVALENTS—Beginning of year	<u>40,940</u>	<u>37,913</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 40,528</u>	<u>\$ 40,940</u>
SUPPLEMENTAL DISCLOSURE OF NONCASH ACTIVITIES		
Acquisition of equipment under capital lease	<u>\$ 2,030</u>	<u>\$ 177</u>
CASH PAYMENTS FOR INTEREST	<u>\$ 206</u>	<u>\$ 229</u>

See accompanying notes to the financial statements.

NATIONAL CREDIT UNION ADMINISTRATION OPERATING FUND

NOTES TO FINANCIAL STATEMENTS For the Years Ended December 31, 2015 and 2014

1. ORGANIZATION AND PURPOSE

The National Credit Union Administration Operating Fund (the “Fund”) was created by the Federal Credit Union Act of 1934. The Fund was established as a revolving fund in the United States Treasury under the management of the National Credit Union Administration (NCUA) Board for the purpose of providing administration and service to the Federal credit union system.

A significant majority of the Fund’s revenue is comprised of operating fees paid by Federal credit unions. Each Federal credit union is required to pay this fee based on its prior year asset balances and rates set by the NCUA Board.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation – The Fund prepares its financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP), based on standards issued by the Financial Accounting Standards Board (FASB), the private sector standards setting body. The Federal Accounting Standards Advisory Board (FASAB) is the standards setting body for the establishment of GAAP with respect to the financial statements of Federal Government entities. FASAB has indicated that financial statements prepared based upon standards promulgated by FASB may also be regarded as in accordance with GAAP for Federal entities that have issued financial statements based upon FASB standards in the past.

Basis of Accounting – The Fund maintains its accounting records in accordance with the accrual basis of accounting. As such, the Fund recognizes income when earned and expenses when incurred. In addition, the Fund records investment transactions when they are executed and recognizes interest on investments when it is earned.

Related Parties – The Fund exists within NCUA and is one of five funds managed by the NCUA Board. The other funds managed by the Board, deemed related parties, are:

- a) The National Credit Union Share Insurance Fund (NCUSIF),
- b) The National Credit Union Administration Temporary Corporate Credit Union Stabilization Fund (TCCUSF),
- c) The National Credit Union Administration Central Liquidity Facility (CLF), and
- d) The National Credit Union Administration Community Development Revolving Loan Fund (CDRLF).

The Fund supports these related parties by providing office space, information technology services, and supplies, as well as paying employees’ salaries and benefits. Certain types of support are reimbursed to the Fund by NCUSIF, TCCUSF, and CLF, while support of the

CDRLF is not reimbursed. Expenses included on the Statement of Revenues, Expenses, and Changes in Fund Balance are shown net of reimbursements from related parties. This may result in credit balances if expense activity for the Operating Fund is less than the reimbursements from related parties.

Additional related parties are described in Note 7.

Cash Equivalents – Cash equivalents are highly liquid investments with original maturities of three months or less. The Federal Credit Union Act permits the Fund to invest in United States Government securities or securities with both principal and interest guaranteed by the United States Government. All investments in 2015 and 2014 were cash equivalents and are stated at cost, which approximates fair value.

Fixed and Intangible Assets – Buildings, furniture, equipment, computer software, and leasehold improvements are recorded at cost. Computer software includes the cost of labor incurred by both external and internal software developers and other personnel in the development of the software. Capital leases are recorded at the lower of the present value of the future minimum lease payments or the fair market value of the leased asset. Depreciation and amortization are computed by the straight-line method over the estimated useful lives of buildings, furniture, equipment, and computer software, and the shorter of either the estimated useful life or lease term for leasehold improvements and capital leases. Estimated useful lives are 40 years for the buildings and two to ten years for the furniture, equipment, computer software, and leasehold improvements.

Long-lived Assets/Impairments – Fixed and intangible assets, subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the carrying value of the long-lived asset or asset group is not recoverable, an impairment is recognized to the extent that the carrying value exceeds its fair value. Fair value is determined through various valuation techniques, including discounted cash flow models, quoted market values, and third party independent appraisals, as considered necessary.

For impairments, the Fund's policy is to identify assets that are no longer in service, obsolete, or need to be written down, and perform an impairment analysis based on FASB Accounting Standards Codification (ASC) 360-10-35, *Property, Plant, and Equipment*, requirements. Subsequent adjustments to individual asset values are made to correspond with any identified changes in useful lives.

Assets Held for Sale – The Fund may hold certain real estate held for sale. Such held for sale assets are ready for immediate sale in their present condition. Real estate held for sale is recorded at the fair value less cost to sell. If an asset's fair value less cost to sell, based on a review of available financial information including but not limited to appraisals, markets analyses, etc., is less than its carrying amount, the carrying value of the asset is adjusted to its fair value less costs to sell.

Gains on disposition of real estate are recognized upon sale of the underlying asset. The Fund evaluates each real estate transaction to determine if it qualifies for gain recognition under the full accrual method. If the transaction does not meet the criteria for the full accrual method, the appropriate deferral method is used.

Accounts Receivable – Receivables include employee advances, amounts due from the NCUSIF, and other accounts receivable.

Accounts Payable and Accrued Other Liabilities – The Fund incurs administrative expenses and liabilities for programs pertaining to related parties that are controlled by the NCUA Board. Accruals are made as expenses are incurred. Accrued other liabilities include contingent liabilities, as described in Note 11.

Accrued Benefits – The Fund incurs expenses for retirement plans, employment taxes, workers compensation, transportation subsidies, and other benefits mandated by law. Corresponding liabilities recorded contain both short-term and long-term liabilities, including liabilities under the Federal Employees' Compensation Act (FECA). FECA provides income and medical cost protection to covered Federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease. The FECA program is administered by the U.S. Department of Labor (DOL), which pays valid claims and subsequently seeks reimbursement from NCUA for these paid claims. NCUA accrues a liability to recognize those payments, and NCUA subsequently reimburses DOL annually. The Fund records an estimate for the FECA actuarial liability using the DOL's FECA model. The model considers the average amount of benefit payments incurred by the agency for the past three fiscal years, multiplied by the medical and compensation liability to benefits paid ratio for the whole FECA program.

Operating Fees – Each Federal credit union is assessed an annual fee based on their assets as of the preceding 31st day of December. The fee is designed to cover the costs of providing administration and service to the Federal credit union system. The Fund recognizes this operating fee revenue ratably over the calendar year.

Revenue Recognition – Interest revenue and other revenue relating to Freedom of Information Act fees, sales of publications, parking income, and rental income is recognized when earned.

Income Taxes – NCUA, as a government entity, is not subject to federal, state, or local income taxes and, accordingly, no provision for income taxes is recorded for the Fund.

Leases – Operating leases are entered into for the acquisition of office space and equipment as part of administering NCUA's program. The cost of operating leases is recognized on the straight-line method over the life of the lease and includes, if applicable, any reductions resulting from incentives such as rent holidays. The same method is used to recognize income from operating leases. The Fund also has capital leases which are recorded at the lower of the present value of the future minimum lease payments or the fair market value of the leased asset. Certain office space for which NCUA is a lessee is subject to escalations in rent, as described in Note 8.

Fair Value Measurements – The following method and assumption was used in estimating the fair value disclosures:

Cash and cash equivalents, due from NCUSIF, employee advances, other accounts receivable (net), obligations under capital leases, and notes payable to NCUSIF are recorded at book values, which approximate their respective estimated fair values.

Use of Estimates – The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent liabilities at the date of the financial statements, and the reported amounts of revenues and expenses incurred during the reporting period. Significant estimates include the determination of the FECA liability, certain intangible asset values, and if there is any determination of a long-lived asset impairment, the related measurement of the impairment charges.

Commitments and Contingencies – Liabilities for loss contingencies arising from claims, assessments, litigation, fines and penalties, and other sources are recorded when it is probable that a liability has been incurred and the amount can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred.

3. CASH AND CASH EQUIVALENTS

The Fund's cash and cash equivalents as of December 31, 2015 and 2014 are as follows (in thousands):

	<u>2015</u>	<u>2014</u>
Deposits with U.S. Treasury	\$ 67	\$ 2,152
U.S. Treasury Overnight Investments	<u>40,461</u>	<u>38,788</u>
Total	<u>\$ 40,528</u>	<u>\$ 40,940</u>

The Operating Fund does not hold any cash or cash equivalents outside of the U.S. Department of the Treasury.

4. FIXED ASSETS

Fixed assets, including furniture and equipment, are comprised of the following as of December 31, 2015 and 2014 (in thousands):

	<u>2015</u>	<u>2014</u>
Office building and land	\$ 50,512	\$ 48,273
Furniture and equipment	8,898	8,850
Leasehold improvements	407	406
Equipment under capital leases	<u>2,309</u>	<u>279</u>
Total assets in-use	62,126	57,808
Less accumulated depreciation	<u>(31,083)</u>	<u>(28,210)</u>
Assets in-use, net	31,043	29,598
Construction in progress	<u>63</u>	<u>681</u>
Fixed assets, net	<u>\$ 31,106</u>	<u>\$ 30,279</u>

Depreciation expense for the years ended December 31, 2015 and 2014 totaled \$4.1 and \$3.1 million, respectively.

Construction in progress includes costs associated with improvements for NCUA headquarters that increase the future service potential of the capital asset (building) and does more than maintain the existing level of service.

5. INTANGIBLE ASSETS

Intangible assets are comprised of the following as of December 31, 2015 and 2014 (in thousands):

	<u>2015</u>	<u>2014</u>
Internal-use software	\$ 17,888	\$ 17,954
Less accumulated amortization	<u>(16,279)</u>	<u>(15,844)</u>
Total internal-use software, net	<u>1,609</u>	<u>2,110</u>
Internal-use software under development	1,751	794
Less impairment loss	<u>(1,006)</u>	<u>-</u>
Total software under development, net	<u>745</u>	<u>794</u>
Intangible assets, net	<u>\$ 2,354</u>	<u>\$ 2,904</u>

Internal-use software is computer software that is either acquired externally or developed internally. Amortization expense for the years ended December 31, 2015 and 2014 totaled \$1.4 and \$2.7 million, respectively.

Internal-use software that is in development represents costs incurred from the customization of software purchased from external vendors for internal use as well as the cost of software that is developed in-house.

An impairment loss of \$1.0 million and \$0 was recognized for the years ended December 31, 2015 and 2014, respectively, on internal-use software under development. Management determined that the internal-use software under development would not be completed and placed in service because it did not meet the required use specifications. Therefore, the software was fully impaired with a fair value of \$0. The amount of the loss is reported in administrative expenses on the Statements of Revenues, Expenses, and Changes in Fund Balance. Any recoveries offset the recognized impairment loss.

6. ASSETS HELD FOR SALE

The net balance of real estate available for sale as of December 31, 2015 and 2014 was \$377.0 and \$643.5 thousand, respectively, and includes impairment charges and costs to sell of \$66.5 and \$90.6 thousand as of December 31, 2015 and 2014, respectively. Real estate available for sale purchased by the Fund is from employees enrolled in the agency's home purchase program who are unable to sell their homes in a specified time period. It is the agency's intent to dispose of these properties as quickly as possible. Sales of homes are generally expected to occur within one year, pending market forces. Ongoing costs to maintain properties are expensed as incurred.

7. RELATED PARTY TRANSACTIONS

(a) Transactions with NCUSIF

Certain administrative services are provided by the Fund to NCUSIF. The Fund charges NCUSIF for these services based upon an annual allocation factor approved by the NCUA Board and derived from a study of actual usage. In 2015 and 2014, the allocation to NCUSIF was 71.8% and 69.2% of all expenses, respectively. The cost of the services allocated to NCUSIF, which totaled \$192.3 and \$175.6 million for 2015 and 2014, respectively, is reflected as a reduction of the expenses shown in the accompanying financial statements. These transactions are settled monthly.

In addition to the allocation described above, the Fund also charges NCUSIF for certain developmental costs related to development of internal-use intangible assets requiring the use of Operating Fund labor. As of December 31, 2015 and 2014, these amounts were \$97.9 and \$20.9 thousand, respectively.

As of December 31, 2015 and 2014, amounts due from NCUSIF totaled \$3.9 and \$3.5 million, respectively.

In 1992, the Fund entered into a commitment to borrow up to \$42.0 million in a 30-year secured term note with NCUSIF. The monies were drawn as needed to fund the costs of constructing a building in 1993. Interest costs incurred were \$206.0 and \$228.6 thousand for 2015 and 2014,

respectively. The notes payable balances as of December 31, 2015 and 2014 were \$10.4 and \$11.7 million, respectively. The current portion of the long-term debt is \$1.3 million as of December 31, 2015. The variable rate on the note is equal to NCUSIF's prior-month yield on investments. The average interest rates during 2015 and 2014 were 1.87% and 1.85%, respectively. The interest rates as of December 31, 2015 and 2014 were 1.90% and 1.87%, respectively.

The secured term note requires principal repayments as of December 31, 2015, as follows (in thousands):

Years ending December 31	Secured Term Note
2016	\$ 1,341
2017	1,341
2018	1,341
2019	1,341
2020	1,341
Thereafter	<u>3,687</u>
Total	<u>\$ 10,392</u>

(b) Transactions with CLF

Certain administrative services are provided by the Fund to CLF. The Fund pays CLF's employee salaries and related benefits, as well as CLF's portion of building and operating costs. Reimbursements of these expenses are determined by applying a ratio of CLF full-time equivalent employees to the NCUA total, with settlement and payment occurring quarterly. All other CLF reimbursement expenses are paid annually. The costs of the services provided to CLF were \$521.3 and \$505.5 thousand for the years ending December 31, 2015 and 2014, respectively, and are reflected as a reduction of the expenses shown in the accompanying financial statements.

Other accounts receivable include \$127.2 and \$118.7 thousand of amounts due from the CLF as of December 31, 2015 and 2014, respectively.

(c) Support of CDRLF

The Fund supports the administration of programs under CDRLF by paying related personnel costs such as pay and benefits and other associated costs which include but are not limited to telecommunications, supplies, printing, and postage.

For the years ending December 31, 2015 and 2014, unreimbursed administrative support to CDRLF is estimated at (in thousands):

	<u>2015</u>	<u>2014</u>
Personnel	\$ 321	\$ 307
Other	53	57
Total	<u>\$ 374</u>	<u>\$ 364</u>

(d) Support of TCCUSF

The Fund supports the administration of programs under TCCUSF by paying related personnel costs such as pay and benefits and other associated costs which include but are not limited to telecommunications, supplies, printing, and postage.

For the years ending December 31, 2015 and 2014, unreimbursed administrative support to TCCUSF is estimated at (in thousands):

	<u>2015</u>	<u>2014</u>
Personnel	\$ 1,204	\$ 921
Other	39	28
Total	<u>\$ 1,243</u>	<u>\$ 949</u>

In addition, the Fund initially paid for and was reimbursed \$1,083.7 and \$782.7 thousand for the salaries and related benefits of TCCUSF employees for the years ending December 31, 2015 and 2014, respectively. These reimbursements are reflected as a reduction of the corresponding expenses in the accompanying financial statements.

(e) Federal Financial Institutions Examination Council (FFIEC)

NCUA is one of the five Federal agencies that fund FFIEC operations. Under FFIEC's charter, NCUA's Chairman is appointed as a Member. FFIEC was established on March 10, 1979, as a formal inter-agency body empowered to prescribe uniform principles, standards, and report forms for the Federal examination of financial institutions by NCUA, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the Consumer Financial Protection Bureau, and the State Liaison Committee. FFIEC was also established to make recommendations to promote uniformity in the supervision of financial institutions. Additionally, FFIEC provides training to staff employed by Member agencies; the Member agencies are charged for these trainings based on use. For the years ended December 31, 2015 and 2014, FFIEC assessments totaled \$1.2 and \$1.1 million, respectively. FFIEC's 2016 budgeted assessments to NCUA total \$1.1 million (unaudited).

(f) Real Estate Available for Sale

The Fund purchases homes from employees enrolled in the agency's home purchase program who are unable to sell their homes in a specified time period, as mentioned in Note 6.

8. LEASE COMMITMENTS

Description of Leasing Agreements – The Fund has entered into lease agreements with vendors for the rental of office space and office equipment, which includes copiers, laptops, and mail equipment.

Operating Leases – The Fund leases a portion of NCUA’s office space under lease agreements that will continue through 2020. Office rental charges amounted to approximately \$971.9 thousand and \$1.1 million, of which approximately \$697.8 and \$765.0 thousand were reimbursed by NCUSIF for 2015 and 2014, respectively. In addition, the Fund leases laptops and other office equipment under operating leases with lease terms that continue through 2015.

Capital Leases – The Fund leases copiers, laptops, and mail equipment under lease agreements that run through 2019. Amounts presented in the table below include \$74.8 thousand of imputed interest.

The future minimum lease payments to be paid over the next five years as of December 31, 2015, before reimbursements, are as follows (in thousands):

Years ending December 31	Operating Leases	Capital Leases
2016	\$ 1,010	\$ 783
2017	1,170	774
2018	1,195	30
2019	1,222	3
2020	1,103	-
Total	<u>\$ 5,700</u>	<u>\$ 1,590</u>

Based on the allocation factor approved by the NCUA Board, NCUSIF is expected to reimburse the Fund for approximately 73.1% of the 2016 operating lease payments.

The Fund, as a lessor, currently holds operating lease agreements with one tenant, who rents a portion of the Fund’s building for retail space. The lease carries a five year term with escalating rent payments. The lease is set to expire in 2020.

The future minimum lease payments to be received from this non-cancelable operating lease at December 31, 2015 are as follows (in thousands):

Years ending December 31	Scheduled Rent Payments
2016	\$ 305
2017	312
2018	318
2019	324
2020	81
Total	<u>\$ 1,340</u>

9. RETIREMENT PLANS

Eligible employees of the Fund are covered by Federal Government retirement plans—either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Both plans include components that are defined benefit plans. FERS is comprised of a Social Security Benefits Plan, a Basic Benefits Plan, and the Thrift Savings Plan. Contributions to the plans are based on a percentage of an employee’s gross pay. Under the Thrift Savings Plan, employees may also elect additional contributions, the totals of which were not to exceed \$18.0 and \$17.5 thousand (\$24.0 and \$23.0 thousand for age 50 and above) in 2015 and 2014, respectively. In addition, the Fund matched up to 5% of the employee’s gross pay. In 2015 and 2014, the Fund’s contributions to the plans were approximately \$23.8 and \$21.5 million, respectively, of which approximately \$17.1 and \$14.9 million, respectively, was allocated to NCUSIF.

These defined benefit plans are administered by the U.S. Office of Personnel Management (OPM), which determines the required employer contribution level. The Fund does not account for the assets pertaining to the above plans, and does not have actuarial data with respect to accumulated plan benefits or the unfunded liability relative to eligible employees. These amounts are reported by OPM and are not allocated to individual employers.

The Fund established a voluntary defined contribution 401(k) Plan (NCUA Savings Plan), effective January 1, 2012. The NCUA Collective Bargaining Agreement (CBA) sets the rates of contribution required by the Fund, and the current agreement that became effective on July 7, 2015 is in effect for five years from its effective date and shall renew automatically for additional one year terms unless otherwise renegotiated by the parties. The Fund will maintain a voluntary 401(k) plan (NCUA Savings Plan) and will contribute, with no employee matching contribution, 3% of the employee’s compensation as defined in *Article 9 Compensation and Benefits* of the CBA. In 2015 and 2014, the Fund matched an employee’s voluntary contribution up to a maximum of 1.5% of the employee’s total pay. The Fund’s match will increase to 2.0% effective the first full pay period in January 2016 and remain in effect for the duration of this Agreement. NCUA’s contributions for 2015 and 2014 were \$5.8 and \$5.4 million, respectively. The operating expenses associated with the NCUA Savings Plan in 2015 and 2014 were

\$68.2 and \$64.1 thousand, respectively. A total of 71.8% and 69.2% of all costs of the NCUA Savings Plan was allocated to the NCUSIF in 2015 and 2014, respectively. Matching, vesting, and additional information is published and made available in a Summary Plan Description.

10. FAIR VALUE MEASUREMENTS

The following disclosures of the estimated fair values are made in accordance with the requirements of FASB ASC 820, *Fair Value Measurements and Disclosures*. Fair value is the amount that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Fund has no financial instruments that are subject to fair value measurement on a recurring basis.

The related impairment charges for 2015 and 2014 were \$113.5 and \$122.3 thousand, respectively. Impairment charges are recorded within the Statement of Revenues, Expenses, and Changes in Fund Balance and represent non-recurring fair value measures. The carrying amounts and established fair values of the Fund's assets held for sale as of December 31, 2015 and 2014 are as follows (in thousands):

Assets held for sale	Amortized Cost Basis	Fair Value	Impairment at Year-end
2015	\$ 377	\$ 377	\$ 66
2014	\$ 644	\$ 644	\$ 91

(a) Non-recurring Fair Value Measures

Assets held for sale represents residences from relocating employees and is presented at aggregate fair value less cost to sell. The fair value measurement recorded during the period includes pending purchase contracts, the lower of list prices or appraisals if less than six months old (if no pending purchase contracts exist), or recent market analyses (if no recent list prices or appraisals are readily available). Additionally, the fair value incorporates estimated reductions in the fair value to recognize costs to sell the properties. The Fund believes that these measurements fairly reflect the most current valuation of the assets.

(b) Summary Financial Instrument Fair Values

The carrying values approximate the fair values of certain financial instruments as of December 31, 2015 and 2014, were as follows (in thousands):

	2015		2014	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	\$ 40,528	\$ 40,528	\$ 40,940	\$ 40,940
Due from NCUSIF	3,944	3,944	3,509	3,509
Employee advances	38	38	62	62
Other accounts receivable, net	332	332	322	322
Obligations under capital lease	1,515	1,515	213	213
Notes payable to NCUSIF	10,392	10,392	11,733	11,733

Cash and Cash Equivalents – The carrying amounts for cash and cash equivalents financial instruments approximates fair value as the short-term nature of these instruments does not lead to significant fluctuations in value. Cash equivalents are U.S. Treasury overnight investments.

Due from NCUSIF – The carrying amounts for the due from NCUSIF financial instruments approximates fair value, as the amount is scheduled to be paid within the first quarter of fiscal year 2016.

Employee Advances – The carrying amounts for receivables from employees' financial instruments approximates fair value, as the amount is scheduled to be paid in fiscal year 2016.

Other Accounts Receivable, Net – The carrying amounts for other accounts receivable approximates fair value, as the original gross amounts together with a valuation allowance reflect the net amount that is deemed collectible. As of December 31, 2015 and 2014, the Fund's Other Accounts Receivable includes an allowance in the amount of \$5.7 and \$1.1 thousand, respectively.

Obligation under Capital Lease – The carrying amounts for the remaining obligations owed on capital leases financial instruments approximates fair value because the underlying interest rates approximate rates currently available to the Fund.

Notes Payable to NCUSIF – The carrying amounts for notes payable to NCUSIF financial instruments approximate fair value due to its variable rate nature.

11. CONTINGENCIES

NCUA recognizes contingent liabilities when a past event or transaction has occurred, a future outflow or other sacrifice of resources is probable, and the future outflow or sacrifice of resources is measurable. NCUA is party to various routine administrative proceedings, legal actions, and claims brought against it, which has or may ultimately result in settlements or

decisions against the agency. For those matters where an estimate is possible and the loss is probable, such amount has been accrued in other liabilities.

12. COLLECTIVE BARGAINING AGREEMENT

NCUA has a CBA with the National Treasury Employees Union (NTEU) that became effective on July 7, 2015. NTEU is the exclusive representative of approximately 79% of NCUA employees. This agreement will remain in effect for a period of five years from its effective date and shall renew automatically for additional one year terms unless otherwise renegotiated by the parties.

13. SUBSEQUENT EVENTS

Subsequent events have been evaluated through February 12, 2016, which is the date the financial statements were available to be issued, and management determined that there are no other items to disclose.

Report #OIG-16-04

National Credit Union Administration Central Liquidity Facility

Financial Statements as of and for the Years Ended
December 31, 2015 and 2014, and
Independent Auditors' Report

**NATIONAL CREDIT UNION ADMINISTRATION
CENTRAL LIQUIDITY FACILITY**

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KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report

Inspector General, National Credit Union Administration and
the National Credit Union Administration Board:

Report on the Financial Statements

We have audited the accompanying financial statements of the National Credit Union Administration Central Liquidity Facility (CLF), which comprise the balance sheets as of December 31, 2015 and 2014, and the related statements of operations, members' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 15-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Credit Union Administration Central Liquidity Facility as of December 31, 2015 and 2014, and its operations, members' equity, and cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Reporting Required by Government Auditing Standards

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended December 31, 2015, we considered the CLF's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the CLF's internal control. Accordingly, we do not express an opinion on the effectiveness of the CLF's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the CLF's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of compliance disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 15-02.



Purpose of the Other Reporting Required by Government Auditing Standards

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the CLF's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

February 12, 2016

**NATIONAL CREDIT UNION ADMINISTRATION
CENTRAL LIQUIDITY FACILITY**

BALANCE SHEETS

As of December 31, 2015 and 2014

(Dollars in thousands, except share data)

	<u>2015</u>	<u>2014</u>
ASSETS		
Cash and Cash Equivalents (Notes 3 and 5)	\$ 11,486	\$ 35,269
Investments Held to Maturity (Net of \$537 and \$266 unamortized premium, fair value of \$237,324 and \$193,788 as of 2015 and 2014, respectively) (Notes 4 and 5)	237,503	193,737
Accrued Interest Receivable (Note 5)	<u>710</u>	<u>514</u>
TOTAL ASSETS	<u>\$ 249,699</u>	<u>\$ 229,520</u>
LIABILITIES AND MEMBERS' EQUITY		
LIABILITIES		
Accounts Payable (Note 5)	\$ 160	\$ 179
Dividends Payable (Note 5)	138	125
Member Deposits (Notes 5 and 7)	<u>1,320</u>	<u>600</u>
Total Liabilities	<u>1,618</u>	<u>904</u>
MEMBERS' EQUITY		
Capital Stock – Required (\$50 per share par value authorized: 8,725,806 and 8,005,574 shares; issued and outstanding: 4,362,903 and 4,002,787 shares as of 2015 and 2014, respectively) (Note 6)	218,145	200,139
Retained Earnings	<u>29,936</u>	<u>28,477</u>
Total Members' Equity	<u>248,081</u>	<u>228,616</u>
TOTAL LIABILITIES AND MEMBERS' EQUITY	<u>\$ 249,699</u>	<u>\$ 229,520</u>

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
CENTRAL LIQUIDITY FACILITY**

**STATEMENTS OF OPERATIONS
For the Years Ended December 31, 2015 and 2014
(Dollars in thousands)**

	<u>2015</u>	<u>2014</u>
REVENUE		
Investment Income	\$ 2,486	\$ 1,735
Total Revenue	<u>2,486</u>	<u>1,735</u>
EXPENSES (Note 9)		
Personnel Services	325	338
Personnel Benefits	100	108
Other General and Administrative Expenses	<u>73</u>	<u>67</u>
Total Operating Expenses	<u>498</u>	<u>513</u>
Interest – Liquidity Reserve	<u>3</u>	<u>1</u>
Total Expenses	<u>501</u>	<u>514</u>
NET INCOME	<u>\$ 1,985</u>	<u>\$ 1,221</u>

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
CENTRAL LIQUIDITY FACILITY**

**STATEMENTS OF MEMBERS' EQUITY
For the Years Ended December 31, 2015 and 2014
(Dollars in thousands, except share data)**

	Capital Stock		Retained Earnings	Total
	Shares	Amount		
BALANCE – December 31, 2013	2,157,607	\$ 107,880	\$ 27,692	\$ 135,572
Issuance of Required Capital Stock	1,857,120	92,856		92,856
Redemption of Required Capital Stock	(11,940)	(597)		(597)
Dividends Declared (\$0.125/share) (Notes 6 and 7)			(436)	(436)
Net Income			1,221	1,221
BALANCE – December 31, 2014	4,002,787	\$ 200,139	\$ 28,477	\$ 228,616
Issuance of Required Capital Stock	380,319	19,016		19,016
Redemption of Required Capital Stock	(20,203)	(1,010)		(1,010)
Dividends Declared (\$0.125/share) (Notes 6 and 7)			(526)	(526)
Net Income			1,985	1,985
BALANCE – December 31, 2015	<u>4,362,903</u>	<u>\$ 218,145</u>	<u>\$ 29,936</u>	<u>\$ 248,081</u>

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
CENTRAL LIQUIDITY FACILITY**

STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2015 and 2014

(Dollars in thousands)

	<u>2015</u>	<u>2014</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	\$ 1,985	\$ 1,221
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Amortization of Investments	104	87
Interest - Liquidity Reserve	3	1
Changes in Assets and Liabilities:		
Increase in Accrued Interest Receivable	(196)	(201)
Increase/(Decrease) in Accounts Payable	(19)	91
Net Cash Provided by Operating Activities	<u>1,877</u>	<u>1,199</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of Investments	(67,876)	(93,519)
Proceeds from Maturing Investments	<u>24,006</u>	<u>8,000</u>
Net Cash Used in Investing Activities	<u>(43,870)</u>	<u>(85,519)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of Required Capital Stock	18,966	89,653
Redemption of Required Capital Stock	(595)	(502)
Withdrawal of Member Deposits	<u>(161)</u>	<u>(4)</u>
Net Cash Provided by Financing Activities	<u>18,210</u>	<u>89,147</u>
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	(23,783)	4,827
CASH AND CASH EQUIVALENTS—Beginning of Year	<u>35,269</u>	<u>30,442</u>
CASH AND CASH EQUIVALENTS—End of Year	<u>\$ 11,486</u>	<u>\$ 35,269</u>

See accompanying notes to the financial statements.

NATIONAL CREDIT UNION ADMINISTRATION CENTRAL LIQUIDITY FACILITY

NOTES TO FINANCIAL STATEMENTS For the Years Ended December 31, 2015 and 2014

1. ORGANIZATION AND PURPOSE

The National Credit Union Administration (NCUA) Central Liquidity Facility (CLF) was created by the National Credit Union Central Liquidity Facility Act (Act). CLF is designated as a mixed-ownership Government corporation under the Government Corporation Control Act. CLF exists within NCUA and is managed by the NCUA Board. CLF became operational on October 1, 1979.

CLF was created to improve the general financial stability of credit unions by serving as a liquidity lender to credit unions experiencing unusual or unexpected liquidity shortfalls. CLF accomplishes its purpose by lending funds, subject to certain statutory limitations, when a liquidity need arises.

CLF is subject to various Federal laws and regulations. CLF may not make loans to members for the purpose of expanding credit union loan portfolios. CLF's investments are restricted to obligations of the U.S. Government and its agencies, deposits in federally insured financial institutions, and shares and deposits in credit unions. Borrowing is limited by statute to 12 times the subscribed capital stock and surplus. See Notes 6 and 8 for further information about the capital stock and the CLF's borrowing authority.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation – CLF has historically prepared its financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP), based on standards issued by the Financial Accounting Standards Board (FASB), the private-sector standards-setting body. The Federal Accounting Standards Advisory Board (FASAB) is the standards-setting body for the establishment of GAAP with respect to the financial statements of Federal Government entities. FASAB has indicated that financial statements prepared based upon standards promulgated by FASB may also be regarded as in accordance with GAAP for those Federal entities, such as CLF, that have issued financial statements based upon FASB standards in the past.

Basis of Accounting – CLF maintains its accounting records in accordance with the accrual basis of accounting. As such, CLF recognizes interest income on loans and investments when earned, and recognizes interest expense on borrowings when incurred. CLF recognizes expenses when incurred. In addition, CLF accrues and records dividends on capital stock monthly and pays dividends quarterly.

Cash Equivalents – Cash equivalents are highly liquid investments with original maturities of three months or less.

Investments – By statute, CLF investments are restricted to obligations of the U.S. Government and its agencies, deposits in federally insured financial institutions, and shares and deposits in

credit unions. All investments are classified as held-to-maturity under FASB Accounting Standards Codification (ASC) topic 320-10-25-1, *Classification of Investment Securities*, as CLF has the intent and ability to hold these investments until maturity. Accordingly, CLF reports investments at amortized cost. Amortized cost is the face value of the securities plus the unamortized premium or less the unamortized discount.

CLF evaluates investment securities that are in an unrealized loss position for other-than-temporary impairment (OTTI). An investment security is deemed impaired if the fair value of the investment is less than its amortized cost. Amortized cost includes adjustments (if any) made to the cost basis of an investment for accretion, amortization, and previous OTTI. To determine whether impairment is other-than-temporary, CLF takes into consideration whether it has the intent to sell the security.

Premiums and discounts are amortized or accreted over the life of the related held-to-maturity investment as an adjustment to yield using the effective interest method. Such amortization and accretion is included in the “investment income” line item in the Statement of Operations.

CLF records investment transactions when they are made.

Loans and Allowance for Loan Losses – Loans, when made to members, are on a short-term or long-term basis. Loans are recorded at the amount disbursed and bear interest at the higher of the Federal Financing Bank Advance Rate or the Federal Reserve Bank Discount Window Primary Credit Rate. By regulation, Member *Liquidity Needs* Loans are made on a fully secured basis. CLF obtains a security interest in the assets of the member equal to at least 110% of all amounts due. CLF does not currently charge additional fees for its lending activities. There was no lending activity during 2015 and 2014.

Borrowings – CLF’s borrowings are recorded when they are received, do not hold premiums or discounts, and are carried at cost. Repayments are recorded when they are made.

Income Taxes – NCUA, as a government entity, is not subject to federal, state, or local income taxes and, accordingly, no provision for income taxes is recorded for CLF.

Use of Estimates – The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, as well as the disclosure of contingent assets and liabilities, if any, at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from management’s estimates.

Reclassifications – Certain prior year amounts have been reclassified to conform with the current year presentation.

Commitments and Contingencies – Liabilities for loss contingencies arising from claims, assessments, litigation, fines, and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred.

Related Parties – CLF exists within NCUA and is managed by the NCUA Board. NCUA Operating Fund (OF) provides CLF with information technology, support services, and supplies; in addition, NCUA OF pays CLF’s employees’ salaries and benefits, as well as CLF’s portion of monthly building operating costs. The allocation formula to calculate these expenses is based on

the number of full-time employees of the respective entities and the estimated amount of time CLF employees spend performing CLF functions.

3. CASH AND CASH EQUIVALENTS

CLF's cash and cash equivalents as of December 31, 2015 and 2014 are as follows (in thousands):

	<u>2015</u>	<u>2014</u>
U.S. Treasury Overnight Investments	\$ 11,300	\$ 35,107
Deposits with U.S. Treasury	180	160
SunTrust Bank	<u>6</u>	<u>2</u>
Total	<u>\$ 11,486</u>	<u>\$ 35,269</u>

U.S. Treasury securities had an initial term of less than three months when purchased.

4. INVESTMENTS

The carrying amount, gross unrealized holding gains, gross unrealized losses, and the fair value of held-to-maturity debt securities as of December 31, 2015 and 2014 were as follows (in thousands):

	<u>2015</u>	<u>2014</u>
Carrying Amount, December 31,	\$ 237,503	\$ 193,737
Gross Unrealized Holding Gains	782	933
Gross Unrealized Holding Losses	<u>(961)</u>	<u>(882)</u>
Fair Value	<u>\$ 237,324</u>	<u>\$ 193,788</u>

Maturities of debt securities classified as held-to-maturity were as follows:

(Dollars in thousands)	<u>2015</u>		<u>2014</u>	
	Net Carrying Amount	Fair Value	Net Carrying Amount	Fair Value
Due in one year or less	\$ 50,838	\$ 50,837	\$ 24,013	\$ 24,036
Due after one year through five years	155,949	155,853	140,877	140,910
Due after five years through ten years	<u>30,716</u>	<u>30,634</u>	<u>28,847</u>	<u>28,842</u>
Total	<u>\$ 237,503</u>	<u>\$ 237,324</u>	<u>\$ 193,737</u>	<u>\$ 193,788</u>

The following table includes gross unrealized losses on investment securities, for which OTTI has not been recognized, in addition to the fair values of those securities, aggregated by investment classification and length of time the investments have been in a loss position, at December 31, 2015 and 2014.

(Dollars in thousands)	Losses		Losses		Total	
	Less than 12 Months		More than 12 Months			
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
As of December 31, 2015						
U.S. Treasury Securities	\$ (624)	\$ 103,352	\$ (337)	\$ 20,796	\$ (961)	\$ 124,148
As of December 31, 2014						
U.S. Treasury Securities	\$ (107)	\$ 45,271	\$ (775)	\$ 40,104	\$ (882)	\$ 85,375

5. FAIR VALUE MEASUREMENTS

The fair value of an instrument is the amount that would be received to sell an asset or would be paid to transfer a liability in an orderly transaction between market participants by the measurement date. The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and cash equivalents – The carrying amounts for cash and cash equivalents approximate fair value.

Investments held-to-maturity – CLF's investments held-to-maturity are all comprised of U.S. Treasury Securities, for which a share price can be readily obtained. The fair value for investments is determined using the quoted market prices at the reporting date (observable inputs).

Member Deposits – Funds maintained with CLF in excess of required capital amounts are recorded as member deposits. These deposits are due upon demand; therefore, carrying amounts approximate the fair value.

Other – Accrued interest receivable, accounts payable, other liabilities, and dividends payable are recorded at book values, which approximate the respective fair values because of the short maturity of these instruments.

The following table presents the carrying amounts and established fair values of CLF’s financial instruments as of December 31, 2015 and 2014. The carrying values and approximate fair values of financial instruments are as follows:

(Dollars in thousands)	2015		2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	\$ 11,486	\$ 11,486	\$ 35,269	\$ 35,269
Investments held-to-maturity	237,503	237,324	193,737	193,788
Accrued interest receivable	710	710	514	514
Accounts payable	160	160	179	179
Dividends payable	138	138	125	125
Member deposits	1,320	1,320	600	600

6. CAPITAL STOCK

Membership in CLF is open to all credit unions that purchase a prescribed amount of capital stock. CLF capital stock is non-voting and shares have a par value of \$50. Currently, there is one subscribed form of membership—regular members which are natural person credit unions. Natural person credit unions may borrow from CLF directly as a regular member.

In October 2013, the NCUA Board issued a final rule 12 CFR Part 741, § 741.12 “Liquidity and Contingency Funding Plans,” which requires federally insured credit unions with assets of \$250 million or more to have access to a backup federal liquidity source for emergency situations. A credit union subject to this requirement may demonstrate access to a contingent federal liquidity source by maintaining membership in the CLF, or establishing borrowing access at the Federal Reserve Discount Window.

The capital stock account represents subscriptions remitted to CLF by member credit unions. Regular members’ required subscription amounts equal one-half of one percent of their paid-in and unimpaired capital and surplus, one-half of which is required to be remitted to CLF. Member credit unions are required to hold the remaining one-half in assets subject to call by the NCUA Board. These unremitted subscriptions are not reflected in CLF’s financial statements. Subscriptions are adjusted annually to reflect changes in the member credit unions’ paid-in and unimpaired capital and surplus. Dividends are non-cumulative, and are declared and paid on required capital stock.

A member of CLF whose capital stock account constitutes less than 5% of the total capital stock outstanding may withdraw from membership in CLF six months after notifying the NCUA Board of its intention. A member whose capital stock account constitutes 5% or more of the total capital stock outstanding may withdraw from membership in CLF two years after notifying the NCUA Board of its intention. As of December 31, 2015, CLF had no member withdrawal requests pending. As of December 31, 2014, CLF had no member withdrawal request pending.

The required capital stock is redeemable upon demand by the members, subject to certain conditions as set out in the Act and NCUA regulations; however, the stock is not deemed “mandatorily redeemable” as defined in FASB ASC 480-10-25-7, *Mandatorily Redeemable Financial Instruments*; therefore capital stock is classified in permanent equity.

CLF's capital stock accounts were composed of the following as of December 31, 2015 and 2014 (in thousands, except share data):

	<u>2015</u>		<u>2014</u>	
	<u>Shares</u>	<u>Amounts</u>	<u>Shares</u>	<u>Amounts</u>
Regular members	<u>4,362,903</u>	<u>\$ 218,145</u>	<u>4,002,787</u>	<u>\$ 200,139</u>

Dividends on capital stock are declared based on available earnings and the dividend policy set by the NCUA Board. Dividends are accrued monthly based on prior quarter-end balances and paid on the first business day after the quarter-end. The dividend rates paid on capital stock for regular members change quarterly.

7. MEMBER DEPOSITS

Member deposits represent amounts remitted by members over and above the amount required for membership. Interest is paid on member deposits at a rate equivalent to the dividend rate paid on required capital stock.

8. BORROWING AUTHORITY

CLF is authorized by statute to borrow, from any source, an amount not to exceed 12 times its subscribed capital stock and surplus. As of December 31, 2015 and 2014, CLF's statutory borrowing authority was \$5.6 billion and \$5.1 billion, respectively.

As described above, the borrowing authority amounts are referenced to subscribed capital stock and surplus of the CLF. The CLF borrowing arrangement is exclusively with the Federal Financing Bank (FFB). NCUA maintains a note purchase agreement with FFB on behalf of CLF with a current maximum principal amount of \$2.0 billion. Under the terms of its agreement, CLF borrows from FFB as needed. Under terms prescribed by the note purchase agreement, CLF executes promissory notes in amounts as necessary, the aggregate amount of which may not exceed its statutory borrowing authority, and renews them annually. Advances made under the current promissory notes can be made no later than March 31, 2016.

9. RELATED PARTY TRANSACTIONS

NCUA OF pays the salaries and related benefits of CLF's employees, as well as CLF's portion of building and operating costs. Reimbursements of these expenses are determined by applying a ratio of CLF full-time equivalent employees to the NCUA total, with settlement and payment occurring quarterly. All other CLF reimbursement expenses are paid annually. The total amount charged by NCUA was approximately \$521.3 and \$505.5 thousand, respectively, for December 31, 2015 and 2014. Accounts payable includes approximately \$127.2 and \$118.7 thousand, respectively, for December 31, 2015 and 2014, due to NCUA OF for services provided.

10. SUBSEQUENT EVENTS

Subsequent events have been evaluated through February 12, 2016, which is the date the financial statements were available to be issued, and management determined that there are no other items to disclose.

Report #OIG-16-05

National Credit Union
Administration
Community Development
Revolving Loan Fund

Financial Statements as of and for the Years Ended
December 31, 2015 and 2014, and
Independent Auditors' Report

**NATIONAL CREDIT UNION ADMINISTRATION
COMMUNITY DEVELOPMENT REVOLVING LOAN FUND**

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KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report

Inspector General, National Credit Union Administration and
the National Credit Union Administration Board:

Report on the Financial Statements

We have audited the accompanying financial statements of the National Credit Union Administration Community Development Revolving Loan Fund (CDRLF), which comprise the balance sheets as of December 31, 2015 and 2014, and the related statements of operations, changes in fund balance, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 15-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Credit Union Administration Community Development Revolving Loan Fund as of December 31, 2015 and 2014, and its operations, changes in fund balance, and cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Reporting Required by Government Auditing Standards

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended December 31, 2015, we considered the CDRLF's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the CDRLF's internal control. Accordingly, we do not express an opinion on the effectiveness of the CDRLF's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the CDRLF's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of compliance disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 15-02.



Purpose of the Other Reporting Required by Government Auditing Standards

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the CDRLF's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

February 12, 2016

**NATIONAL CREDIT UNION ADMINISTRATION
COMMUNITY DEVELOPMENT REVOLVING LOAN FUND**

BALANCE SHEETS

As of December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
ASSETS		
Cash and Cash Equivalents (Notes 3 and 8)	\$ 8,283,455	\$ 8,839,092
Loans Receivable (Notes 5, 7, and 8)	9,364,904	8,089,686
Interest Receivable (Note 8)	<u>9,495</u>	<u>5,208</u>
TOTAL ASSETS	<u><u>\$ 17,657,854</u></u>	<u><u>\$ 16,933,986</u></u>
LIABILITIES AND FUND BALANCE		
Liabilities - Accrued Technical Assistance Grants (Note 8)	\$ 1,954,448	\$ 1,028,047
Fund Balance		
Fund Capital (Note 4)	13,954,708	14,124,064
Accumulated Earnings	<u>1,748,698</u>	<u>1,781,875</u>
Total Fund Balance	<u>15,703,406</u>	<u>15,905,939</u>
TOTAL LIABILITIES AND FUND BALANCE	<u><u>\$ 17,657,854</u></u>	<u><u>\$ 16,933,986</u></u>

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
COMMUNITY DEVELOPMENT REVOLVING LOAN FUND**

**STATEMENTS OF OPERATIONS
For the Years Ended December 31, 2015 and 2014**

	<u>2015</u>	<u>2014</u>
SUPPORT AND REVENUES		
Interest on Cash Equivalents	\$ 1,988	\$ 2,034
Interest on Loans	37,649	28,850
Total Interest Income	<u>39,637</u>	<u>30,884</u>
Appropriation Revenue		
Appropriations Expended (Note 4)	2,528,386	1,569,740
Cancelled Technical Assistance Grants (Note 6)	<u>(518,444)</u>	<u>(253,093)</u>
Total Appropriation Revenue	<u>2,009,942</u>	<u>1,316,647</u>
Total Support and Revenues	<u>2,049,579</u>	<u>1,347,531</u>
EXPENSES		
Technical Assistance Grants	2,602,004	1,613,661
Cancelled Technical Assistance Grants (Note 6)	(519,248)	(254,959)
Bad Debt Expense	<u>-</u>	<u>3</u>
Total Expenses	<u>2,082,756</u>	<u>1,358,705</u>
NET LOSS	<u>\$ (33,177)</u>	<u>\$ (11,174)</u>

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
COMMUNITY DEVELOPMENT REVOLVING LOAN FUND**

**STATEMENTS OF CHANGES IN FUND BALANCE
For the Years Ended December 31, 2015 and 2014**

	Fund Capital			Accumulated Earnings	Total Fund Balance
	For Loans	For Technical Assistance	Total Fund Capital		
December 31, 2013	\$ 13,387,777	\$ 856,464	\$ 14,244,241	\$ 1,793,049	\$ 16,037,290
Appropriations Received (Note 4)	-	1,200,000	1,200,000	-	1,200,000
Appropriations Expended	-	(1,569,740)	(1,569,740)	-	(1,569,740)
Cancelled Appropriations - Remitted to Treasury (Note 4)	-	(3,530)	(3,530)	-	(3,530)
Cancelled Technical Assistance Grants (Note 6)	-	253,093	253,093	-	253,093
Net Loss	-	-	-	(11,174)	(11,174)
December 31, 2014	\$ 13,387,777	\$ 736,287	\$ 14,124,064	\$ 1,781,875	\$ 15,905,939
Appropriations Received (Note 4)	-	2,000,000	2,000,000	-	2,000,000
Appropriations Expended	-	(2,528,386)	(2,528,386)	-	(2,528,386)
Cancelled Appropriations - Remitted to Treasury (Note 4)	-	(159,414)	(159,414)	-	(159,414)
Cancelled Technical Assistance Grants (Note 6)	-	518,444	518,444	-	518,444
Net Loss	-	-	-	(33,177)	(33,177)
December 31, 2015	\$ 13,387,777	\$ 566,931	\$ 13,954,708	\$ 1,748,698	\$ 15,703,406

See accompanying notes to the financial statements.

**NATIONAL CREDIT UNION ADMINISTRATION
COMMUNITY DEVELOPMENT REVOLVING LOAN FUND**

**STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2015 and 2014**

	<u>2015</u>	<u>2014</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Loss	\$ (33,177)	\$ (11,174)
Adjustments to Reconcile Net Loss to Net Cash Used in Operating Activities		
Bad Debt Expense	-	3
Appropriations Expended	(2,528,386)	(1,569,740)
Cancelled Technical Assistance	518,444	253,093
Changes in Assets and Liabilities		
Increase in Interest Receivable	(4,287)	(1,326)
Increase in Accrued Technical Assistance	926,401	176,037
Net Cash Used in Operating Activities	<u>(1,121,005)</u>	<u>(1,153,107)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Loan Principal Repayments	224,782	858,220
Loan Disbursements	<u>(1,500,000)</u>	<u>(5,030,000)</u>
Net Cash Used In Investing Activities	<u>(1,275,218)</u>	<u>(4,171,780)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Appropriations Received 2015/2016	2,000,000	-
Appropriations Received 2014/2015	-	1,200,000
Cancelled Appropriations Remitted to Treasury 2009/2010	(159,414)	-
Cancelled Appropriations Remitted to Treasury 2008/2009	<u>-</u>	<u>(3,530)</u>
Net Cash Provided by Financing Activities	1,840,586	1,196,470
NET DECREASE IN CASH AND CASH EQUIVALENTS	(555,637)	(4,128,417)
CASH AND CASH EQUIVALENTS — Beginning of Year	<u>8,839,092</u>	<u>12,967,509</u>
CASH AND CASH EQUIVALENTS — End of Year	<u>\$ 8,283,455</u>	<u>\$ 8,839,092</u>

See accompanying notes to the financial statements.

NATIONAL CREDIT UNION ADMINISTRATION COMMUNITY DEVELOPMENT REVOLVING LOAN FUND

NOTES TO FINANCIAL STATEMENTS For the Years Ended December 31, 2015 and 2014

1. ORGANIZATION AND PURPOSE

The Community Development Revolving Loan Fund (CDRLF) for credit unions was established by an act of Congress (Public Law 96-123, November 20, 1979) to stimulate economic development in low-income communities. The National Credit Union Administration (NCUA) and the Community Services Association (CSA) jointly adopted Part 705 of NCUA Rules and Regulations, governing administration of CDRLF, on February 28, 1980.

Upon the dissolution of CSA in 1983, administration of CDRLF was transferred to the Department of Health and Human Services (HHS). From 1983 through 1990, CDRLF was dormant.

The Community Development Credit Union Transfer Act (Public Law 99-609, November 6, 1986) transferred CDRLF administration back to NCUA. The NCUA Board adopted amendments to Part 705 of NCUA Rules and Regulations on September 16, 1987, and began making loans/deposits to participating credit unions in 1990.

The purpose of CDRLF is to stimulate economic activities in the communities served by low-income credit unions, which is expected to result in increased income, ownership, and employment opportunities for low-income residents, and other economic growth. The policy of NCUA is to revolve the loans to qualifying credit unions as often as practical in order to gain maximum impact on as many participating credit unions as possible.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation – CDRLF has historically prepared its financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP), based on standards issued by the Financial Accounting Standards Board (FASB), the private sector standards setting body. The Federal Accounting Standards Advisory Board (FASAB) is the standards setting body for the establishment of GAAP with respect to the financial statements of Federal Government entities. FASAB has indicated that financial statements prepared based upon standards promulgated by FASB may also be regarded as in accordance with GAAP for Federal entities that have issued financial statements based upon FASB standards in the past.

Basis of Accounting – CDRLF maintains its accounting records in accordance with the accrual basis of accounting. As such, CDRLF recognizes income when earned and expenses when incurred. In addition, CDRLF records investment transactions when they are executed and recognizes interest on investments when it is earned.

Cash Equivalents – Cash equivalents are highly liquid investments with original maturities of three months or less. The Federal Credit Union Act permits CDRLF to make investments in United States Government Treasury securities. All investments in 2015 and 2014 were cash equivalents and were stated at cost, which approximates fair value.

Loans Receivable and Allowance for Loan Losses – Loans are generally limited to \$300,000 per credit union, however, NCUA may make loans that exceed this amount in certain circumstances. NCUA Rules and Regulations do not provide a maximum limit on loan applications. The maximum loan term is five (5) years. For loans issued on or after May 22, 2012, interest is to be paid on a semi-annual basis beginning six months after the initial distribution of the loan and every six months thereafter until maturity. Principal is to be repaid on the maturity date of the loan. The rate of interest on loans is governed by the CDRLF Loan Interest Rate Policy. CDRLF reviews the interest rate on an annual basis. Effective May 1, 2014, the interest rate was set to 0.60%, reflecting an increase of 0.20% from the previous period interest rate of 0.40%. In 2015, CDRLF opted to maintain the interest rate, which is set to 0.60%.

Loans are initially recognized at their disbursed amount, and subsequently at amortized cost, net of the allowance for loan losses, if any.

A provision for loans considered to be uncollectible is charged to the income statement when such losses are probable and reasonably estimable. Provisions for significant uncollectible amounts are credited to an allowance for loan losses, while de minimis amounts are directly charged-off. Management continually evaluates the adequacy of the allowance for loan losses based upon prevailing circumstances and an assessment of collectability risk of the total loan portfolio as well as historical loss experience. On the basis of this analysis, no allowance for loan losses was necessary as of December 31, 2015 and 2014. Accrual of interest is discontinued on nonperforming loans when management believes collectability is doubtful.

Accrued Technical Assistance Grants – CDRLF issues technical assistance grants to low-income designated credit unions. CDRLF utilizes multiyear appropriated funds and income generated from the revolving fund to issue technical assistance grants. Grant income and expense is recognized when CDRLF makes a formal commitment to the recipient credit union for technical assistance grants. CDRLF performs a review of long term unspent technical assistance grant awards (e.g. outstanding awards past the period of eligibility) and then formal steps are taken to cancel identified technical assistance grants. The cancelled technical assistance grant funds are credited back to the original appropriated fund from which they are awarded.

Related Party Transactions – NCUA, through the Operating Fund (OF), provides certain general and administrative support to CDRLF, including personnel costs such as pay and benefits as well as other costs which include but are not limited to telecommunications, supplies, printing, and postage. The value of these contributed services is not charged to CDRLF.

Revenue Recognition – Appropriation revenue is recognized as the related technical assistance grant expense is recognized. Total appropriation revenues will differ from total technical assistance grant expenses because not all technical assistance grants are funded by

appropriations. Interest income on cash and cash equivalents and on loans is recognized when earned.

Use of Estimates – The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, as well as the disclosure of contingent assets and liabilities, if any, at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from management’s estimates.

Income Taxes – NCUA, as a government entity, is not subject to federal, state, or local income taxes and, accordingly, no provision for income taxes is recorded for CDRLF.

Commitments and Contingencies – Liabilities for loss contingencies arising from claims, assessments, litigation, fines, and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred.

3. CASH AND CASH EQUIVALENTS

CDRLF’s cash and cash equivalents as of December 31, 2015 and 2014 are as follows:

	<u>2015</u>	<u>2014</u>
Deposits with U.S. Treasury	\$ 2,983,455	\$ 2,239,092
U.S. Treasury Overnight Securities	<u>5,300,000</u>	<u>6,600,000</u>
	<u>\$ 8,283,455</u>	<u>\$ 8,839,092</u>

4. GOVERNMENT REGULATIONS

CDRLF is subject to various Federal laws and regulations. Assistance, which includes lending and technical assistance grants, is limited to the amount appropriated by Congress to date for CDRLF, which includes accumulated earnings. Federally-chartered and state-chartered credit unions with a low-income designation are eligible to participate in CDRLF’s loan and technical assistance grant program.

Since inception, Congress has appropriated \$13,387,777 for the revolving loan component of the program, and this component is governed by Part 705 of NCUA Rules and Regulations.

During the year ended December 31, 2015, CDRLF received an appropriation for technical assistance grants in the amount of \$2,000,000 for the Federal fiscal year (FY) 2015. This is a multiyear appropriation that is available for obligation through September 30, 2016. Of this amount, \$1,651,056 was expended for the year ended December 31, 2015. An additional \$877,330 was expended from the FY 2014 appropriation.

During the year ended December 31, 2014, CDRLF received an appropriation for technical assistance grants in the amount of \$1,200,000 for FY 2014. This was a multiyear appropriation that was available for obligation through September 30, 2015. Of this amount, \$848,948 was

expended for the year ended December 31, 2014. An additional \$720,792 was expended from the FY 2013 appropriation.

Appropriated funds in the amount of \$159,414 from the FY 2009 appropriation were remitted to the U.S. Treasury in 2015 upon cancellation. Appropriated funds in the amount of \$3,530 from the FY 2008 appropriation were remitted to the U.S. Treasury in 2014 upon cancellation.

These appropriations were designated to be used for technical assistance grants, and no amounts were designated to be used as revolving loans.

5. LOANS RECEIVABLE

Loans receivable as of December 31, 2015 and 2014 consisted of the following:

	<u>2015</u>	<u>2014</u>
Balance as of the Beginning of the Year	\$ 8,089,686	\$ 3,917,909
Loans Disbursed	1,500,000	5,030,000
Loan Repayments	(224,782)	(858,220)
Bad Debt Expense	<u>-</u>	<u>(3)</u>
Loans Receivable as of the End of the Year	<u>9,364,904</u>	<u>8,089,686</u>
Changes in the Allowance for Loan Losses Consisted of the Following:		
Balance as of the Beginning of the Year	-	-
Decrease (increase) in the Allowance	<u>-</u>	<u>-</u>
Allowance for Loan Losses as of the End of the Year	<u>-</u>	<u>-</u>
Loans Receivable, Net, as of the End of the Year	<u>\$ 9,364,904</u>	<u>\$ 8,089,686</u>

Loans outstanding as of December 31, 2015, are scheduled to be repaid during the following subsequent years:

	<u>2015</u>
2016	\$ -
2017	2,524,905
2018	309,999
2019	5,030,000
2020	<u>1,500,000</u>
Total Loans Receivable	<u>\$ 9,364,904</u>

CDRLF has the intent and ability to hold its loans to maturity. CDRLF anticipates realizing the carrying amount in full.

6. CANCELLED TECHNICAL ASSISTANCE GRANTS

During 2015, CDRLF cancelled \$804 of technical assistance grants awarded from the revolving fund and \$518,444 of technical assistance grants awarded from multiyear funds. These amounts were recognized as Cancelled Technical Assistance Grants, decreasing expenses.

Cancelled technical assistance grants from the revolving fund are credited back to accumulated earnings. Cancelled technical assistance grants from previously expended multiyear funds are credited back to the original appropriated fund from which they are awarded. As a result, the \$518,444 was also recognized as Cancelled Technical Assistance Grants, decreasing revenue, and resulting in no change to net income.

For the year ended December 31, 2014, CDRLF cancelled \$1,866 of technical assistance grants awarded from the revolving fund and \$253,093 of technical assistance grants awarded from multiyear funds.

Cancelled technical assistance grants awarded from appropriations from FY 2010 through 2014 will be remitted to the U.S. Treasury upon cancellation of the related appropriation.

7. CONCENTRATION OF CREDIT RISK

As discussed in Note 1, CDRLF provides loans to credit unions that serve predominantly low-income communities.

NCUA Rules and Regulations Section 705.5 permit the classification of the loan in the participating credit union's accounting records as a non-member deposit. As a non-member deposit, \$250,000 per credit union is insured by the National Credit Union Share Insurance Fund (NCUSIF). The aggregate amount of uninsured loans totaled \$3,549,723 and \$3,049,723 as of December 31, 2015 and 2014, respectively. The increase in FY 2015 is due to the issuance of two loans over \$250,000.

8. FAIR VALUE MEASUREMENTS

The fair value of an instrument is the amount that would be received to sell an asset or would be paid to transfer a liability in an orderly transaction between market participants by the measurement date. The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Loans Receivable – Fair value is estimated using an income approach by separately discounting each individual loan's projected future cash flow. CDRLF believes that the discount rate reflects the pricing and is commensurate with the risk of the loans to CDRLF. Loans are valued annually on December 31.

Other – The carrying amounts for cash and cash equivalents, interest receivable, and accrued technical assistance grants approximate fair value.

The following table presents the carrying value amounts and established fair values of CDRLF's financial instruments as of December 31, 2015 and 2014.

	2015		2014	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets				
Cash and Cash Equivalents	\$ 8,283,455	\$ 8,283,455	\$ 8,839,092	\$ 8,839,092
Loans Receivable	9,364,904	9,374,039	8,089,686	8,095,057
Interest Receivable	9,495	9,495	5,208	5,208
Liabilities				
Accrued Technical Assistance Grants	1,954,448	1,954,448	1,028,047	1,028,047

9. RELATED PARTY TRANSACTIONS

NCUA, through the OF, supports the administration of programs under CDRLF by paying related personnel costs such as pay and benefits as well as other costs which include but are not limited to telecommunications, supplies, printing, and postage.

For the years ending December 31, 2015 and 2014, NCUA, through the OF, provided the following unreimbursed administrative support to CDRLF:

	2015	2014
Employee	\$ 321,027	\$ 306,760
Other	53,364	56,789
Total	\$ 374,391	\$ 363,549

10. SUBSEQUENT EVENTS

Subsequent events have been evaluated through February 12, 2016, which is the date the financial statements were available to be issued, and management determined that there are no other items to disclose.