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April 22, 2016

Mr. Gerard Poliquin  
Secretary of the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, VA 22314

**RE: Comments on the Overhead Transfer Rate Methodology**

Dear Mr. Poliquin:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only national trade association focusing exclusively on federal issues affecting the nation's federally insured credit unions, I am writing to you regarding the National Credit Union Administration's (NCUA) Overhead Transfer Rate (OTR) methodology. NAFCU appreciates this opportunity to provide comments on the methodology by which NCUA transfers funds from the National Credit Union Share Insurance Fund (NCUSIF) to the agency's operating budget to cover insurance-related activities. NAFCU strongly believes that a full and transparent system is the only way to produce an objective mechanism for funding agency operations.

**Background**

Until now, the NCUA Board has never used notice and comment rulemaking to establish either an individual determination of OTR or the general methodology used to calculate OTR. For the past year, NCUA has promised to solicit public comment on the OTR, as recommended in a 2011 study of the rate by PricewaterhouseCoopers. As the agency has made clear, in response to feedback from the credit union community and to obtain more frequent public input on the OTR going forward, NCUA will solicit comments on the OTR methodology every three years in conjunction with the public review of the agency's strategic plan.

Since the OTR was first implemented, the Board has repeatedly examined the OTR methodology and considered ways to improve it, most recently in 2013. Currently, FCUs pay for 65 percent of NCUA's operating budget, yet make up only 50 percent of the shares insured by the NCUSIF (see figure 1).

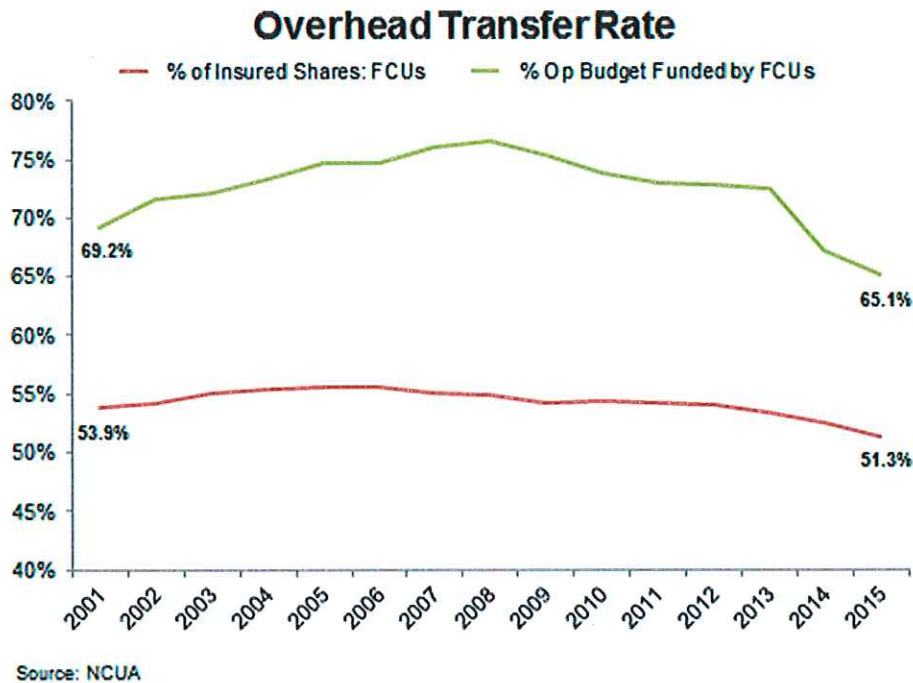


Figure 1

### General Comments

Although the agency is soliciting comments solely related to the underlying OTR methodology, NAFCU would like to take this opportunity to provide NCUA with general comments about its ever increasing operating budget. Particularly, NAFCU believes that stakeholder discontent regarding the OTR methodology stems directly from the agency's operating budget increases and, consequently, the perception that the OTR is being used to offset those increases.

NAFCU believes this perception is not entirely unjustified. NAFCU and other industry stakeholders have repeatedly questioned why the agency's budget has increased despite the fact that the entire financial services industry is performing well. For example, the Federal Deposit Insurance Corporation, the insurer of banks, reduced its budget by 4.7 percent from FY 2015, citing increased improvement in the industry and a decline in the number of bank failures. NCUA, however, has increased its budget for nine years in a row, despite similar improvements in the credit union industry.

While NAFCU and our member credit unions support budget allocations that make the agency more advanced and productive, such as hiring specialized staff and developing technology upgrades, we urge the agency to state rationales behind each budget allocation increase. NAFCU believes this effort will help mitigate concern about the OTR and will be the most prudent way forward in gaining stakeholder contentment.

### **Improved Examiner Efficiency**

NAFCU believes the agency can offset the need for operating budget increases, and thus decrease the impact of the OTR, by focusing examination and supervision activities on credit unions that present high risks to the NCUSIF. However, under the agency's current policy, NCUA examines all federally insured state-chartered credit unions (FISCUs) with \$250 million or more in assets every year, without regard to risk. This is costly to both the agency and FISCUs.

Instead of conducting redundant examinations on an annual basis at FISCUs, NAFCU has heard from our members that the agency should conduct on-site follow-ups based on a review of the State Supervisory Authority (SSA) exam rather than automatically defaulting to examining the FISCU every year.

Additionally, NAFCU restates our earlier calls for the agency to move to an 18-month examination cycle for well-run, low-risk credit unions, which will reduce costs related to examinations. To that end, NAFCU supports the agency's plans to develop and adopt the use of more technology, which should reduce on-site examination time, further reducing costs to be covered by the NCUSIF. NAFCU strongly encourages NCUA to continue developing similar measures that will increase agency efficiency.

### **Increased Transparency**

NAFCU believes that NCUA needs to be fully overt in all actions related to the budget and the OTR. To do this, NAFCU urges the agency to provide stated rationales for every budget allocation increase. NAFCU believes that the agency's OTR preamble is a good example of providing a rationale behind recent OTR increases. As stated in the preamble, the agency notes that recent increased emphasis on risk focused examinations should be attributed to the increased amount of time examiners are spending on insurance-related activities.

While this is a positive step forward as compared to the previous level of opaqueness, NAFCU believes the agency must do a better job of telegraphing agency focus, and whether insurance related examination and supervisory activities will increase depending on agency focus. A relatively low-cost way for the agency to begin doing this is through the rule-making process for new regulations.

For example, as NCUA promulgates new regulations, agency staff conducts an analysis to determine whether the rule will be applied to FISCUs under Title II. Under section 203, the Board has broad discretion to charge the insurance fund directly for matters related to the purposes of carrying out Title II. Therefore, in order to increase transparency under its Title II authority, NAFCU strongly urges the agency to state whether new rules are insurance or non-insurance related as new regulations are promulgated. Not only will this provide more adequate notice of the agency's application of the rule, but it will also

provide the industry with an opportunity to voice comments on the agency's interpretation of whether it's insurance related or not.

### **Increased Implementation and Accuracy of Examination Time Surveys**

Although NAFCU appreciates the agency's implementation of the Examination Time Survey (ETS), especially as it helps set out objective cost allocations and determine a cost driver for regulatory and non-regulatory activities, we firmly believe the agency can do more to increase the accuracy of the ETS. Specifically, we believe that agency-wide adoption of the ETS, or a similarly designed time capture tool, will help refine the OTR.

The methodology is also intended to take into consideration the cost of NCUA resources and programs with different allocation factors from the examination and supervision program. However, NAFCU strongly believes that consideration of other resources and program under the current methodology is not precise, and therefore is open to non-objective cost allocation methods. NAFCU believes that any effort to allocate costs not based on objective and measurable criteria opens the agency to criticism about conflicts of interest, perceived or real.

Therefore, NAFCU asks the agency to provide further breakdown of NCUA cost centers since several NCUA offices do not track time as being insurance or non-insurance related. For example, despite having a \$10 million budget, the Office of National Examinations and Supervision (ONES) examiners aren't required to complete the ETS. Additionally, the Office of Consumer Protection currently does not utilize the ETS or some version of time tracking. Instead, these offices only estimate how much time is spent on insurance related activities. This lack of information is especially disconcerting considering that several of these offices have historically had 0 percent of time allocated toward insurance related activity, but have recently begun estimating more time being spent on insurance related matters.

The industry should be assured that these increased allocations toward insurance related activities are based on objective criteria, and therefore, the bases for these allocations need to be explicitly documented. As NCUA's cost accounting systems mature, NAFCU believes it may be cost effective in the future to explore such additional refinements to the OTR methodology. Therefore, NAFCU encourages the agency to develop best practices that would require all offices to conduct a more scientific accounting of time allotted toward varying insurance and non-insurance related activities.

Finally, as Figure 2 shows, the results from the ETS are the largest reason behind some of the recent spikes in the OTR. Accordingly, improved transparency and accuracy regarding ETS implementation would help explain variations in the OTR. Without increased transparency and documented justifications, steady increases in OTR over the last decade give the appearance that the agency is favoring federal charters over state charters.

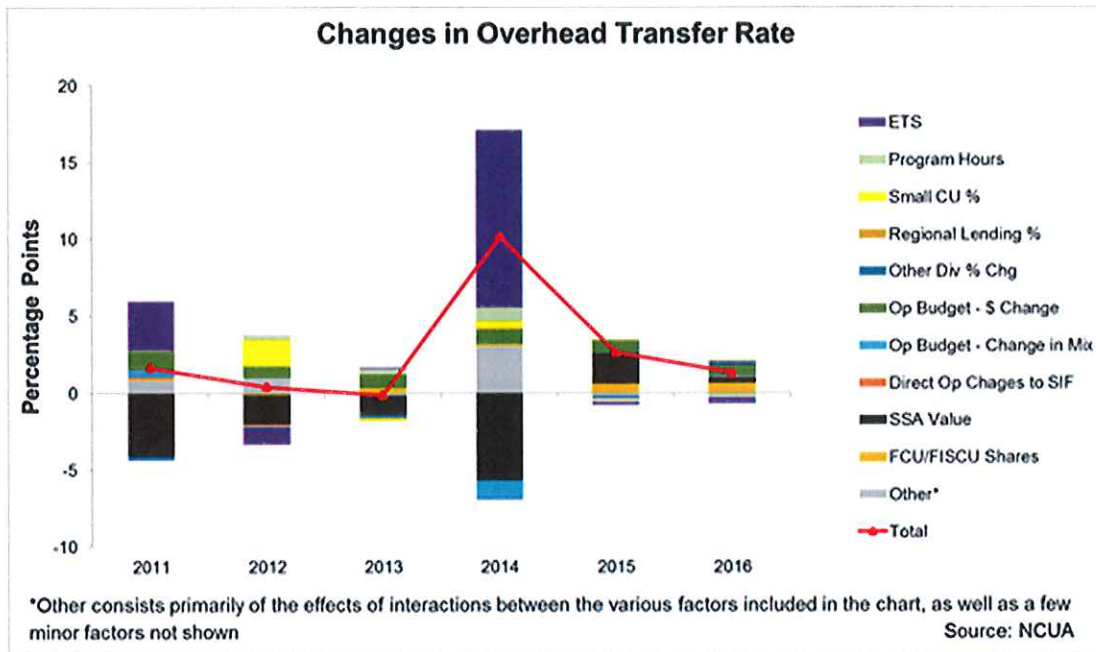


Figure 2

NAFCU believes that the creation of the ETS was a large step forward in increasing objective cost allocation, and as such, we urge the agency to continue refining the ETS and ensuring that all offices have an objective way to allocate time.

### Assumption of Rules as Solely Insurance-Related

NAFCU agrees that allocation of overhead costs should be based on a pro-rata basis, as it is the best way to objectively allocate costs to different functions of the agency. To further improve transparency, NAFCU urges the agency to publish the results and rationales behind the allocation of costs based on insurance and non-insurance activities. For example, according to the 2013 ETS Analysis Report, NCUA has 252 total examination related rules and regulations. Of the 252 rules, 64 percent have been classified as being insurance related, and the remaining 36 percent are non-insurance and consumer regulatory related. However, the Analysis Report simply made conclusory statements about which rules are insurance or non-insurance related. A better approach would have been to explain why.

Additionally, some industry stakeholders have questioned whether there are some rules that could be bifurcated between insurance related and non-insurance related. Although agency staff informed the Board during the November 2014 Board Meeting that there weren't many, if any, rules that could be bifurcated, NAFCU believes documentation supporting this assertion is needed if the agency is committed to transparency.

While the ETS Analysis Report is useful in understanding which rules the agency has deemed insurance or non-insurance related, NAFCU requests that during the next comment

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period on the OTR methodology, the agency identify which of those rules could be potentially bifurcated, and specifically ask for stakeholder comment on whether the agency's classification of those rules is appropriate.

### **Agency Should Not Delegate Approval of OTR to Staff**

Finally, while NAFCU and our member credit unions believe that a formula-based policy facilitates more objective cost allocation measures, any formula still needs general oversight to protect against any unintentional misalignment. Allowing for annual Board oversight of the OTR enables the Board to consider and evaluate trends that might have greater implications. Although NAFCU urges the agency to continue basing the OTR on a published and transparent methodology, we believe the Board should continue to use its judgement and perspective when reviewing the OTR, especially as there are still components of the OTR that are not entirely objective or transparent.

In conclusion, NAFCU appreciates the opportunity to comment on the OTR methodology. We and our member credit unions look forward to working with the agency as it continues to refine its OTR methodology and implement the ETS across all agency offices. Should you have any questions or would like to discuss these issues further, please contact me, or Carrie Hunt, NAFCU's Executive Vice President of Government Affairs and General Counsel, at (703) 842-2234 or [chunt@nafcu.org](mailto:chunt@nafcu.org).

Sincerely,



B. Dan Berger  
President & Chief Executive Officer