OVERHEAD TRANSFER RATE PROPOSAL

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EXECUTIVE SUMMARY

Introduction

NCUA reviews and sets the Overhead Transfer Rate (OTR) every two years, with 2003 a year for reassessment. A five member Task Force (TF) of specialists from the related areas explored possible alternative methodologies to calculate and administer the OTR. This report recommends an alternative method for calculating the OTR. The target audience for this report is Executive Director Skiles and E&I Director Marquis, with possible further distribution to NCUA Board members and other key internal staff at Executive Director Skiles' direction. The TF consists of the following members:

- Larry Fazio, Director of Risk Management
- Dan Gordon, Senior Investment Officer
- Brenda Martell, Risk Management Analyst
- Michael McNeill, Budget Analyst
- Steve Sherrod, Senior Investment Officer

The **key goals and guiding principles** of the TF were:

- Develop a methodology that allocates NCUA's costs as fairly as possible between federal credit unions and federally insured state-chartered credit unions.
- Consider all feasible alternatives, developing a methodology that balances simplicity with accuracy and comprehensiveness, and that is feasible based on the capabilities of NCUA's current systems and resources.
- Provide for complete transparency in what the task force considers, concludes, and proposes.

Recommendation

The Task Force recommends adoption of a new method for determining the Overhead Transfer Rate. Based on current data:

- The proposed new method would result in an Overhead Transfer Rate of 61.4%.
- The current method would result in an Overhead Transfer Rate between 74 and 77%.

Based on the current method, the Overhead Transfer Rate was last set at 62%. The substantial increase in the projected Overhead Transfer Rate based on the current method is due to significant increases in the amount of time examiners are reporting spent on insurance-related activities, consistent with the Risk-Focused Examination Program. The proposed new method differs from the current method in the following key respects:

- Takes into consideration the value to the NCUSIF of the insurance-related work performed by state supervisory authorities.
- Takes into consideration the cost of NCUA resources and programs with different allocation factors from the examination and supervision program.
- Factors in operational costs charged directly to the NCUSIF.

The key benefits of the proposed new method are:

- More comprehensively allocates the NCUSIF operational costs between federal credit unions and federally insured state-chartered credit unions.
- Addresses a long standing criticism from several interested parties in a fair and practical manner.
- Balances comprehensiveness and accuracy with simplicity and practicality.
- Incorporates features within the methodology to provide flexibility in accommodating changes in NCUA and state supervisory authority examination and supervision programs.

The Task Force recommends adoption of the proposed new Overhead Transfer Rate method, and that NCUA continue to set the Overhead Transfer Rate every two years based on two full cycles worth of survey results (starting with the 2006 budget cycle).

Overview of New Method

	Result	**Comments**
Step 1 – Apply Exam Time Survey to Workload Budget.		This step, and the result, is the same as for the current OTR Method.
Exam Survey – Regulatory	28.8%	Applies to FCU Exam and Supervision only.
Adjusted Based on Workload Budget – Regulatory	24.5%	Takes into consideration other workload, including time spent on FISCUs.
Step 2 – Apply Regulatory % to Dollar Budget.	26.6% or $38.8M	This is a minor refinement to the current method, taking into consideration special cost centers like AMAC, OCCU, OCUD, etc.
Step 3 – Determine Insurance Costs to be Paid from NCUSIF.	$109.5M	This is a minor refinement to the current method. Equals NCUA Budget minus Regulatory Cost from Step 2, plus $2.1M in direct charges.
Step 4 – Factor in Value of SSA Work and Allocate Insurance Costs.		Taking into consideration the value of the SSA work is the only major difference between the methods.
Imputed Value of SSA Work	$16.8M	Applies NCUA's actual exam and supervision programs, staffing patterns, and costs to FISCUs. This is what it would cost for NCUA to do all of the FISCU insurance work.
Allocated to FISCUs	$41.1M	Allocation based on insured assets, per mutual nature of NCUSIF. Net of imputed value.
Step 5 – Calculate OTR.	**61.4%**	Given FISCUs are responsible for $41.4M, this equates to an OTR dollar amount of $89.6M, which is 61.4% of the NCUA budget.

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DETAILED ANALYSIS OF STEP 1
CALCULATION OF REGULATORY COST DRIVER

NCUA is both a regulator and an insurer[1]. To properly and fairly separate and allocate the costs associated with these roles, the TF needed to determine a cost driver for regulatory and non-regulatory activities. NCUA spends resources via its Core and Special Programs conducted by field staff. These programs enable NCUA to fulfill both its regulatory and NCUSIF due diligence related responsibilities. The TF identified three components needed to calculate the cost driver for NCUA's regulatory role. These components are:

1. The regulatory (non-insurance) related percentage of time spent on federal examination and supervision contacts is based upon the **Examination Time Survey results**. The Examination Time Survey process and results are described in detail in Appendix 6.

2. The regulatory related percentage of time applied to **other[2] Core**[3] **and Special**[4] **programs** is based on the characteristics of each program and assumptions made by the TF.

3. The percentages from components 1 and 2 are then applied to the **Workload Budget Hours** (in this case for 2003), which represents examiner and specialized examiner time spent on various programs. This results in a weighted percentage of program hours devoted to NCUA's regulatory role.

Component 1: Examination Time Survey Results

NCUA automated the Examination Time Survey collection process in 2002. The Office of Examination and Insurance (E&I) randomly selects one Supervisory Examiner (SE) group from each region to participate in the survey process. The regions select three experienced examiners from the selected SE groups to complete surveys for all examination and supervision contacts made in federally chartered credit unions. Collection of the current survey began in June 2002 and concludes in May 2003. The full year's worth of survey results will be applied to the new formula to arrive at the Overhead Transfer Rate used for budget purposes. As of March 31, 2003, the Examination Time survey results were as follows:

Contact Type	Total Surveys Collected	Non-insurance Related % (Regulatory)
Examination (code 10)	135	29.6%
Supervision (code 22)	87	25.2%

[1] In its 2001 review, Deloitte and Touche characterized NCUA's dual role as similar to a "multi-product company."
[2] That is, not federal examination or supervision program time (e.g., 5300 time, state exam time, etc.).
[3] Core programs include hours budgeted for field examiners to complete federal and state examination/supervision, state exam review, and the 5300 program.
[4] Special programs include hours budgeted for field examiners to complete fair lending exams, subject matter examiner work, agricultural lending reviews, FOM and chartering activity, capital market specialist contacts, small credit union programs, and CUSO exams.

Component 2: Percentage of Regulatory Time Spent on Other Core and Special Programs

The TF applied regulatory related percentages to other Core and Special Programs based on the characteristics of each program and assumptions made by the Task Force. The following chart shows the regulatory percent the TF determined for other Core and Special Programs, the associated rationale for the determination, and applicable sensitivity analysis[5] for regulatory percent determinations.

Other Core Programs	Regulatory %	Sensitivity	Rationale for Regulatory %
State Exam and Supervision (codes 11,23,28)	0%	-1.0	NCUA has limited regulatory responsibility for FISCUs, almost all of which is handled by state supervisory authorities. Thus, all of NCUA's activities related to examining and supervising FISCUs is non-regulatory, motivated by NCUA's management of the NCUSIF.
State Exam Review (code 26)	0%	-0.1	NCUA's review of state examinations is to assess and monitor insurance risk, motivated by NCUA's management of the NCUSIF. Thus, all of this activity is non-regulatory.
5300 Program (codes 20 - FCU)	29.6%	-0.5	This function fulfills mixed roles. Thus, the TF applied the regulatory percent for FCU examinations, as determined by the survey. The TF lacks a more specific driver. Developing a specific driver would not be cost effective. Therefore, the TF used the assumption that the mixture is similar to that for examinations.
5300 Program (code 21 – FISCU)	0%	-0.4	NCUA collects and reviews call reports for FISCUs to assess and monitor insurance risk, motivated by NCUA's management of the NCUSIF. Thus, all of this activity is non-regulatory.
Special Programs	**Regulatory %**	**Sensitivity**	**Rationale for Regulatory %**
Fair Lending Exams (code 03)	100%	0.0	NCUA's motivation for conducting these exams is to fulfill its regulatory role. The insurance benefit derived from this program is not material, and not a motivation for the program.
Subject Matter Examiner (code 04)	29.6%	0.0	This function fulfills mixed roles. NCUA has SMEs for both consumer compliance (regulatory) and safety and soundness (insurance) disciplines. Thus, the TF applied the regulatory percent for FCU examinations, as determined by the survey. The TF lacks a more specific driver, developing a specific driver would not be cost effective, and the mixture of safety & soundness and consumer compliance SMEs approximates the time survey.

[5] The sensitivity number represents how the OTR percent would change for a 10% increase in the regulatory percent assigned.

Special Programs (cont.)	Regulatory %	Sensitivity	Rationale for Regulatory %
Agricultural Lending (code 05)	0%	0.0	NCUA's review of agricultural lending is to assess and monitor insurance risk, motivated by NCUA's management of the NCUSIF. Thus, all of this activity is non-regulatory.
FOM & Chartering (code 06)	100%	0.0	NCUA's motivation for conducting these reviews is to fulfill its regulatory role. The insurance benefit derived from this program is not material, and not a motivation for the program.
RCMS (Code 07)	0%	0.0	NCUA's review of capital markets issues is to assess and monitor insurance risk, motivated by NCUA's management of the NCUSIF. Thus, all of this activity is non-regulatory.
Small Credit Unions (codes 02,08,14)	100%	-0.1	NCUA's motivation for conducting these reviews is to fulfill its regulatory role. There is an insurance benefit derived from this program, but is not the primary motivation for the program. The low level of hours for this program in relation to the total, and thus low sensitivity (a 100% change would only increase the OTR by 0.8), makes developing a more specific driver not cost effective.
CUSO Exams (code 29)	0%	0.0	NCUA's has no direct regulatory authority related to CUSOs, and its review of CUSOs is to assess and monitor insurance risk, motivated by NCUA's management of the NCUSIF. Thus, all of this activity is non-regulatory.

Total special program hours are relatively immaterial to the final analysis. To illustrate, if all special program hours were set at 100% regulatory, the Overhead Transfer Rate percent would only decline 0.8 percent.

Component 3: 2003 Workload Budget

The task force applied the respective results of components 1 and 2 to the Workload Budget Hours (using the 2003 budget) for Core and Special Programs to calculate the weighted percent of program hours devoted to NCUA's regulatory role. Core and Special Programs make up total "productive" hours for examiner and specialized examiner staff. A total 1,027,195 hours are budgeted for productive hours in 2003. These hours account for 59.6 percent of total 2003 program hours.[6] The regulatory percentages discussed in components 1 and 2 are applied to the specific time categories for Core and Special Programs to determine the total regulatory hours for each category. After applying the appropriate regulatory factors for each time category, total regulatory hours equal 150,417. This represents 24.5 percent of total core and special program hours, the weighted percent of program hours devoted to NCUA's regulatory role.

[6] The remaining time (40.4 percent) includes examiner development, training, meetings, administrative, and leave (i.e., overhead costs of conducting the core and special programs).

Core Programs	2003 Budget Hours	Regulatory %	Regulatory Hours
Federal Examination	346,586	29.6%	102,555
Federal Supervision	106,231	25.2%	26,781
State Exam & Supv	70,391	0.0%	0
State Exam Review	10,566	0.0%	0
5300 Program – FCU	33,721	29.6%	9,978
5300 Program – FISCU	28,610	0.0%	0
Total Core Program	**596,105**	**n/a**	**139,303**
Special Programs	**2003 Budget Hours**	**Regulatory %**	**Regulatory Hours**
Fair Lending Exams	3,001	100.0%	3,001
Subject Matter Examiners	3,116	29.6%	922
Agricultural Lending	2,160	0.0%	0
FOM & Chartering	1,638	100.0%	1,638
RCMS	0	0.0%	0
Small Credit Unions	5,553	100.0%	5,553
CUSO Exams	1,148	0.0%	0
Total Special Program	**16,616**	**n/a**	**11,114**
Total Core & Special Programs	**612,721**	**n/a**	**150,417**
Percent of NCUA's Field Program devoted to NCUA's Regulatory Role			**24.5%**[7]

[7] Please note that the figures presented within this report are calculated within an Excel workbook, and rounded typically to one decimal place. Thus, there may be some instances where the "math" shown here is off by a decimal point due to rounding.

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DETAILED ANALYSIS OF STEP 2
APPLICATION OF COST DRIVERS TO NCUA BUDGET

In Step1, we calculated the regulatory cost driver (24.5%) based on the weighted level of examination and supervision (core and special program) hours budgeted to fulfill NCUA's dual role as regulator and insurer. In Step 2, we apply this cost driver, along with other cost drivers, to the NCUA dollar budget. The TF determined that the regulatory cost driver calculated in Step 1 was the appropriate driver for most of NCUA's cost centers, with the exception of the following areas:

- **Asset Management and Assistance Center (AMAC) Costs**. The TF used a 0% regulatory cost driver for AMAC's portion of the NCUA budget since its role is solely related to NCUA's role as insurer. AMAC's role is to "handle liquidation payouts, manage assets acquired from liquidations and assistance programs, and manage recoveries for the National Credit Union Share Insurance Fund. AMAC also provides assistance and advice pertaining to conservatorships, real estate and consumer loans, appraisals, bond claim analysis, and reconstructing accounting records."
- **Office of Credit Union Development (OCUD) Costs**. The TF used a 100% regulatory cost driver for OCUD's portion of the NCUA budget. OCUD's role is to "foster business development of credit unions by providing the guidance and education needed for the delivery of financial services, facilitate the expansion of credit union services through the chartering of new credit unions and field of membership expansions, and coordinate efforts with third-party organizations to improve the … successful operation of credit unions." Though there is some insurance benefit derived from the programs of this office, it is not its primary purpose and not material enough to warrant further refinement of the cost driver.
- **Office of Corporate Credit Unions (OCCU) Costs**: The TF used a 0% regulatory cost driver for OCCU's portion of the NCUA budget. OCCU supervises all corporate credit unions, including non-federally insured state-chartered corporate credit unions due to the systemic risk these institutions pose. The only regulation applicable solely to corporate credit unions, Part 704 of NCUA Rules and Regulations, is designed to address insurance risk.
- **Regional Divisions of Insurance (DOI) Costs:** The TF used a 100% regulatory cost driver for the DOI portions of the NCUA budget. Each of NCUA's six regions has a Division of Insurance devoted to overseeing chartering, mergers, purchase and assumptions, fields of membership, credit union member complaints, account insurance, bylaw questions, credit union low income designations, and administration of the region's small credit union program. DOI's role is principally regulatory. Though there is some insurance benefit derived from the programs of these Divisions, it is not their primary purpose and not material enough to warrant further refinement of the cost driver.

When we apply the cost drivers to the respective portions of the NCUA budget, we arrive at the amount ($38.8 million) of the NCUA dollar budget for 2003 ($146.1 million) that represents NCUA's cost of fulfilling its regulatory role. This regulatory cost equals 26.6% of NCUA's total budget, calculated as follows:

Area	**Portion of Dollar Budget (millions)**	**Cost Driver - Regulatory Percent**	**Regulatory Cost (millions)**
Divisions of Insurance	$5.9	100.0%	$5.9
AMAC	$2.2	0.0%	$0.0
OCUD	$0.8	100.0%	$0.8
OCCU	$6.5	0.0%	$0.0
All Other Costs	$130.7	24.5%	$32.1
Total 2003 NCUA Budget	$146.1		**$38.8**
		Pct. of Budget	26.6%

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DETAILED ANALYSIS OF STEP 3
CALCULATION OF CURRENT NCUSIF INSURANCE COSTS

From Step 2, we arrived at the portion of NCUA's budget that applies to its regulatory role. When the regulatory portion of the budget is subtracted from the total NCUA budget, the result is the portion of the NCUA budget applicable to NCUA fulfilling its role in managing the NCUSIF. However, in addition to NCUA budget costs, there are some operational costs charged directly to the NCUSIF.[8] These insurance costs must be factored into the total operational costs of providing NCUSIF deposit insurance, which need to be absorbed by federally insured credit unions. The TF did not include credit union failure related costs (payouts to failed institution members) in the calculation since these losses are already allocated based on the mutual nature of the NCUSIF deposit insurance product and are not costs of operating the NCUSIF.

This calculation results in total insurance costs to be absorbed by FICUs of $109.5 million, calculated as follows:

	Millions
2003 NCUA Dollar Budget	$146.1
Regulatory Costs (see Step 2)	- $38.8
Direct Operational Charges to NCUSIF	+ $2.1
Total NCUSIF Operational Costs	= $**109.5**

[8] Direct charges include costs associated with providing state examiners computers and training.

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DETAILED ANALYSIS OF STEP 4
ALLOCATION OF INSURANCE COSTS TO FCUS AND FISCUS

Overview

Step 4 is designed to calculate the "total" cost of providing the NCUSIF federal share insurance, including work performed by state supervisory authorities (SSAs), and then allocate these costs on an insured asset basis between FCUs and FISCUs. Through Steps 1, 2, and 3, we determined the total cost applicable to NCUA's role as insurer to be absorbed by FICUs. The TF concluded it is appropriate to recognize NCUA relies to the fullest extent possible on state supervisory authorities to perform much of the insurance related supervision of these institutions. The costs NCUA/NCUSIF avoids[9] should be taken into account when determining and allocating the "total" costs of providing the NCUSIF's federal share insurance.

The TF also concluded the most fair and appropriate basis to allocate NCUSIF costs between FCUs and FISCUs is the asset distribution of these insured credit unions. This is consistent with the mutual nature of the deposit insurance provided by the NCUSIF, and the allocation method for premiums and dividends.

Step 4 Calculations

In Step 3, we calculated $109.5 million is the total NCUA cost in fulfilling its role as insurer. However, the value provided by NCUA's reliance on SSA work should be factored in to determine the total cost to the federally insured credit union system of providing NCUSIF share insurance. To do this, we calculate the imputed value of the insurance related work performed by SSAs[10] and add this to the total NCUA insurance cost, calculated as follows;

	Millions
Total NCUSIF Operational Costs	$109.5
SSA Insurance Work Imputed Value	+ $16.8
Total Cost of Providing NCUSIF Insurance	**= $126.3**

Now we must allocate the total cost to FICUs of providing the NCUSIF insurance between FCUs and FISCUs. The allocation is based on the proportional basis of insured assets. As of December 31, 2002, FCUs and FISCUs represented 54.1% and 45.9% of insured assets respectively. Thus, the distribution of costs would be:

	FCU (Millions)	FISCU (Millions)
Total Cost of Providing NCUSIF Insurance	$126.3	$126.3
Proportional Allocation Basis	x 54.1%	x 45.9%
Total Allocated Insurance Costs	= $68.3	**= $58.0**

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[9] NCUA relies on state supervisory authority examination work. Different SSAs are funded by various means, such as fees paid by state-chartered credit unions, through general state tax revenues, etc.

[10] The calculation of the imputed SSA value is a four step process detailed in the following sections of this report.

However, state supervisory authorities are already providing $16.8 million worth of imputed value to the NCUSIF. Therefore, FISCUs are only responsible for absorbing $41.1 million through the OTR ($58.0 million minus $16.8 million).

	Millions
Total Allocated Insurance Costs - FISCUs	$58.0
SSA Insurance Work Imputed Value	- $16.8
Net Cost of NCUSIF Insurance – FISCUs	**= $41.1**

(See pages 15 through 21 for a detailed review of how the SSA Insurance Work Imputed Value is calculated.)

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DETAILED ANALYSIS OF STEP 5
CALCULATE OTR

Step 5 computes the overhead transfer rate as a percentage of the NCUA dollar budget. In Step 4, we determined the dollar cost to be absorbed by FISCUs through the OTR. This amount divided by the percentage of total insured shares and deposits held by FISCUs (their proportional cost basis) results in the total dollar cost to be absorbed by all insured credit unions through the OTR. To state it another way, if FISCUs are responsible for 45.9% of the cost of providing NCUSIF insurance, and this represents $41.1 million, then the dollar amount of NCUA costs to be absorbed by the OTR must equal $89.6 million.[11]

FISCU Portion of NCUA Insurance Cost	$41.1m
Divided by FISCU Proportional Allocation Basis	45.9%
Equals Dollar Amount of OTR	$89.6m

Or

Dollar Amount of OTR	$89.6m
Times FISCU Proportional Allocation Basis	45.9%
Equals FISCU Portion of NCUA Insurance Cost	$41.1m

Now that we have calculated the dollar amount of the NCUA budget to be covered by the overhead transfer, we can calculate the overhead transfer rate as a percentage of the budget. The dollar amount of the OTR divided by the NCUA Budget results in the OTR as a percentage, which is what has long been called the Overhead Transfer Rate (OTR).

	Millions
Dollar Amount of OTR	$89.6
Divided by NCUA Budget	$146.1
Equals OTR	61.4%

The remainder of the NCUA budget must be funded by other sources, primarily the federal credit union operating fee.[12] Subtracting the total dollar cost to be absorbed by the OTR from the NCUA budget results in the following costs to be funded by other sources:

	Millions
NCUA Budget	$146.1
Minus Dollar Amount of OTR	$89.6
Equals Cost to be Funded by Other Sources (primarily federal credit union operating fees)	$56.5

[11] Mathematically, the first computation must be used to arrive at the OTR dollar amount, since this amount is the unknown we are solving for.

[12] Other funding sources, in addition to the federal credit union operating fee, include fees collected for various services and publications, corporate credit union operating fees, etc.

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DETAILED ANALYSIS OF SSA IMPUTED VALUE STEP 1

Overview

To develop an overhead transfer rate that properly reflects the "total" cost to insured credit unions of providing NCUSIF insurance, it is necessary to factor in the value to the NCUSIF of the insurance related supervision provided by state examination programs and relied upon by NCUA in managing the NCUSIF. The TF developed a four step process to calculate (impute) the value of the insurance work performed by SSAs that NCUA relies upon. The imputed value derived from these calculations is factored into the calculation of the overhead transfer rate.

The TF determined the best measure available of the value of state examination programs to the NCUSIF is what it would cost NCUA to perform this work.[13] The only separate measure of the value of this work is the actual cost of SSA supervision programs. However, these do not necessarily reflect the value to NCUA in managing the NCUSIF[14] and were not readily available to the TF (see Appendix 5).

Imputed SSA Value Step 1 Calculation

To impute the value derived from NCUA's reliance on insurance related state examination and supervision programs, we must calculate what NCUA would need to do to meet its due diligence requirements if the SSAs were not performing this work. The first step in this process is to determine, using the identical criteria for FCUs, what level of examination time would be required to examine all federally insured state-chartered credit unions. To do this, we first look at the examination hours NCUA actually expended on FCUs in 2002 by asset size and CAMEL rating. The results are as follows:

Table 1

FCU 2002 Average Exam Time (Hours)	Assets < $10M	$10M - $100M	$100M - $250M	$250M - $500M	> $500M
CAMEL 1	45	86	162	193	295
CAMEL 2	47	93	173	214	303
CAMEL 3	51	100	188	208	303
CAMEL 4	67	119	230	0	0
CAMEL 5	84	172	0	0	0

[13] The TF realizes that the imputed value may be higher or lower than what SSAs actually spend to conduct insurance related supervision programs NCUA relies upon. Nonetheless, the relevant factor for purposes of computing the OTR is the value to the NCUSIF derived from this work.

[14] Another consideration is the fact SSA programs may not represent cost effective insurance related supervision of institutions based on each state's unique program and cost structure, necessitating separate regulatory and insurance cost drivers be calculated for each state. Such an endeavor would not only be costly, but raise a host of other potential problems.

The next step is to determine how many FISCUs fall into each CAMEL/Asset category to arrive at an estimate of the total time needed. The table below provides the breakdown, as of December 31, 2002, of FISCUs by CAMEL and Asset category.

Table 2

FISCUs (#) in Each Category	Assets < $10M	$10M - $100M	$100M - $250M	$250M - $500M	> $500M
CAMEL 1	249	312	91	55	41
CAMEL 2	952	746	108	29	24
CAMEL 3	499	238	18	4	1
CAMEL 4	93	35	4	0	0
CAMEL 5	9	6	0	0	0

Multiplying the respective cells from Table 1 and Table 2 and summing the results provides the total exam hours it would take, using the same criteria as for FCUs, for NCUA to conduct exams of all FISCUs. This provides an estimate of the exam time needed if NCUA were to conduct all of the state examination work on the same basis employed for FCUs.[15]

Table 3

	Assets < $10M	$10M - $100M	$100M - $250M	$250M - $500M	> $500M
CAMEL 1	11,205	26,832	14,742	10,615	12,095
CAMEL 2	44,744	69,378	18,684	6,206	7,272
CAMEL 3	25,449	23,800	3,384	832	303
CAMEL 4	6,231	4,165	920	0	0
CAMEL 5	756	1,032	0	0	0
Total	88,385	125,207	37,730	17,653	19,670
				Total Additional Exam Hours	**288,645**

Thus, the TF estimates it would take 288,645 hours if NCUA were to conduct examinations in all FISCUs.

[15] NCUA determines exam time using a bottoms-up approach where examiners, in collaboration with management, determine how much time is needed on an individual credit union basis. However, in the aggregate the use of averages will closely approximate the total hours needed. The average time method was tested against applying exam time to each individual FISCU. The calculated total hours were nearly identical, within 2%, so the TF choose to use the simpler, less labor intensive approach.

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DETAILED ANALYSIS OF SSA IMPUTED VALUE STEP 2

In Step 1 of computing the SSA imputed value, we calculated that it would take 288,645 hours if NCUA were to conduct examinations in all FISCUs. However, not all examination time is used to meet NCUA's role as insurer. Federal credit union examination survey results indicate that 70.4 percent of examination time is used to meet NCUA's needs in managing risks to the NCUSIF. For consistency and fairness purposes, we apply this same distribution to FISCUs when determining the total time it would take NCUA to supervise FISCUs to meet its role as insurer.

	Hours
Gross FISCU Exam Hours	288,645
x Insurance Factor Based on Exam Survey	70.4%
= Total Insurance Hours w/out Deferred Program	203,235

However, well run, financially healthy FCUs are eligible for a deferred examination program. The deferred examination program results in a reduction of the total hours needed annually to exam FCUs, and the same standard would be applicable to FISCUs if examined by NCUA. Making an adjustment for the deferred examination program (a.k.a. risk-based scheduling) results in the following:

FISCUs	**Hours**
Total Insurance Hours w/out Deferred Program	203,235
- Not Eligible for Deferral Hours[16]	94,080
= Eligible for Deferral	109,155
x Adjustment for Deferred Program (one-third deferral)	66.7%
= Annual Deferred Program Hours	72,770
Not Eligible for Deferral Hours	94,080
+ Annual Deferred Program Hours	72,770
+ Adjustment for Additional Supervision[17]	9,096
= Total FISCU Hours with Deferred Program	175,946
+ Current Budgeted Supervision Hours	23,351
- Current Budgeted Exam Insurance Hours	47,040
Total Additional FISCU Insurance Hours Needed	**152,257**

[16] Equals 2 times the current NCUA insurance review hours of 47,040 to reflect that almost all of this work is conducted jointly with SSAs. Current NCUA insurance review hours are primarily for credit unions with specific risks, and thus would not be eligible for deferral.

[17] FCUs on a deferred exam program receive some supervision in the year they do not receive an examination. NCUA applies a formula based on the size of the institution, which in the aggregate equates to about 25% of the deferred hours. Thus, this figure is calculated on the same basis by subtracting the annual deferred program hours (72,770) from the eligible hours (109,155), and multiplying the result (36,385) by 25%.

Since NCUA is already contributing 47,040 hours to examining FISCUs in 2003, the calculated additional FISCU hours needed if NCUA were to do all of the work equals 152,257 hours. This also includes an adjustment for needed additional supervision. NCUA currently budgets 23,251 supervision hours for FISCUs. Since this supervision is typically performed jointly with SSAs, if NCUA were to conduct all of the needed supervision, it would take an estimated additional 23,251 hours.

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DETAILED ANALYSIS OF SSA IMPUTED VALUE STEP 3

In Step 2 of computing the SSA imputed value, we calculated that it would take an additional 152,257 hours (gross) if NCUA were to examine and supervise, from an insurance perspective only, all FISCUs using the same insurance-based criteria applied to FCUs.[18] The next step is to convert these hours to the number of examiners this would require.

Since NCUA would be conducting all of the insurance work, there would be no need to conduct reviews of state examination reports as is currently done. There are 10,566 hours budgeted for this task. Thus, the net number of hours needed to fulfill NCUA's role in managing the insurance fund under the scenario where all the FISCU insurance work was conducted by NCUA is:

	Hours
Gross Additional FISCU Hours Needed	152,257
- Budgeted State Examination Review Hours	10,566
= Net Additional FISCU Hours Needed	141,691

After adjusting for various benefits, training, and administrative time[19], NCUA's workload budget is based on each examiner contributing 1,245 hours annually to the examination and supervision program (a.k.a. productive time). This productivity ratio and the resulting productive hours are calculated as follows:

Budgeted Core and Special Program Hours	612,721
/ Total Budgeted Workload Hours	1,027,195
= Productivity Ratio	59.6%
Total Work Hours in a Year Per Full Time Equivalent (FTE)	2,087
x Productivity Ratio	59.6%
= Productive Hours per FTE Examiner	1,245

Thus, to accomplish 141,691 hours worth of additional FISCU work, it would take 113.8 FTE Examiners calculated as follows:

Net Additional FISCU Hours Needed	141,691
/ Productive Hours per FTE Examiner	1,245
= Number of Additional FTE Examiners Needed	**113.8**

[18] If NCUA were to perform the insurance related examination and supervision work for FISCUs, state examinations would only consist of regulatory reviews.

[19] For example, examiners (and all employees in one form or another for that matter) receive training each year, are entitled to sick and annual leave, incur travel time, have holidays off, etc.

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DETAILED ANALYSIS OF SSA IMPUTED VALUE STEP 4

Overview

In Step 3 we determined that it would take an additional 113.8 FTE Examiners if NCUA were to conduct all of the insurance related work in FISCUs. However, to arrive at the total cost (and thus value-added) of such an endeavor would necessitate additional staffing and other resources (overhead) to manage and administer 113.8 examiners. For example, additional Supervisory Examiners, Regional Office Analysts, Human Resource Personnel, facilities, etc. would be required. In this Step, we not only account for the additional staffing and resources needed to support such a program, but establish the dollar cost associated with this program.

Imputed SSA Value Step 4 Calculation

Our first task is to determine what additional staffing would be needed to manage this program and the related staff. The TF reviewed NCUA's staffing patterns and organizational structure and developed ratios of examiners to other positions based on ratios that are actually employed in running the agency. We excluded the following positions/offices:

- Divisions of Insurance: NCUA has no regulatory responsibility (chartering, FOM management, etc.) related to FISCUs. Any FISCU related Division of Insurance work is already handled by existing staff and would not increase with the implementation of this program.
- Divisions of Special Actions: Any FISCU related Special Actions work, i.e., supervising problem FISCUs posing risk to the NCUSIF, is already handled by existing staff and would not increase materially with the implementation of this program.
- Central Office: With the exception of the Office of Human Resources (OHR), all other central offices are currently sufficiently scalable, and/or removed from any direct impact on workload, to absorb the additional work associated with this program. Especially in lieu of the pending reduction of an NCUA region, which is about the size of this theoretical FISCU program, the TF saw no need for additional central office staffing with the exception of OHR.

The TF identified the following positions and ratios for use in computing the total additional staff needed for such a FISCU program.

Additional Staff Needed	Ratio Examiners to Position	FTEs Per Position
Examiners	1/1	113.8
Supervisory Examiners	1/9	12.6
Regional Office Analysts	1/20	5.7
Regional Office Directors	1/20	5.7
Other Regional Support Staff	1/15	7.6
= Number of Additional FTEs Needed		**145.4**

Now that we know how many additional FTE staff members would be needed, we must apply the average cost per FTE to arrive at the cost of this additional staffing. The average cost we used is based on the actual budget for regional offices and field staff and includes all costs, such as travel, training, facilities, consumables (e.g., supplies), in addition to salary and benefits, necessary to run a field program.

Total Cost of Regions	$90,280,212
/ FTEs in Regions	727.6
= Per Regional FTE Cost	$124,079
Per Regional FTE Cost	$124,079
x Number of Additional FTEs Needed	145.4
= Cost of Additional Regional Positions	$18,045,370[20]

With this additional staffing, there would be an impact on the workload of the Office of Human Resources (which includes the Division of Training and Development). Adding 145.4 additional staff members to NCUA would represent a 15.0 percent increase in staffing (current staffing is 971). Thus, we projected a 15.0 percent increase in OHR's budget.

In addition to increases in certain costs, there would be some areas of savings to NCUA if it conducted all of the insurance related FISCU work. There would be no need to pay for the training of state examiners, or providing SSAs with computers and other equipment. Adjusting for these costs and savings results in the imputed SSA value of $16.8 million.

Cost of Additional Regional Positions	$18,045,370
+ Additional OHR Costs (15.0% of $6.1 million budget)	$911,357
- SSA Training and Equipment Cost	$2,141,388
= Imputed SSA Value	**$16,815,339**

[20] The Excel workbook calculates these figure automatically based on various inputs. There is a minor rounding difference here.

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BENEFITS AND IMPLICATIONS OF PROPOSED METHOD

Benefits of the Proposed Method

- The framework allocates costs between FCUs and FISCUs based upon insured dollars. This is a mutual insurance allocation that is not biased based on charter type or field of membership.

- The proposed method allocates costs in a transparent framework, in part relying on examiner time survey results. The bases for other allocation assumptions are explicitly documented.

- The proposed method recognizes the value of insurance work conducted by SSAs that NCUA relies upon in lieu of performing the work itself. The imputed value of insurance work conducted by SSAs is computed on NCUA's actual time, program methodology, and cost basis. This provides for a level playing field.

- The framework is not unduly complex. Thus, no additional costs should be incurred by the NCUA to administer the framework. The simplicity of the framework also should facilitate understanding, debate, and recommendations for improvement.

- The proposed new OTR methodology is designed to accommodate changes in the distribution of insurance-related work between NCUA and SSAs. In a scenario where NCUA conducted additional FISCU work, the operating fund budget would increase to accommodate the newly required staffing and these costs would flow through the new formula resulting in a fair distribution between the operating and insurance funds.

Implications of the Proposed Method

- NCUA could be faced with increasing its involvement in conducting insurance work in FISCUs in particular states if necessary due to variations in a state's program, such as state budget problems, unacceptable quality or frequency of the state's supervision of credit unions, or at the request of the state regulator. Significant variations in the level of NCUA involvement in conducting insurance related FISCU work in individual states would unbalance the fair distribution of insurance costs for FICUs. Thus, NCUA will need to monitor the level of effort expended in individual states in relation to the respective FICU populations, and would need to assess fees to absorb additional work above the current, normal operating range. The cost per hour, which represents the marginal cost of conducting this work, is calculated as follows:

Imputed SSA Value	$16,815,339
/ Additional FISCU Program Hours	141,691
= Marginal Cost Per Hour	$119[21]

- The proposed new OTR method would increase the Federal Operating Fee. For 2003, the operating fee declined by 2.2% based on an OTR of 62%. Under the proposed method, the operating fee would have decreased by 0.6%. However, given the significant increase in the results of the survey, the OTR under the current method would increase to 74%.[22] This would result in a substantial decline in the federal operating fee of 30.4%.[23]

- The proposed new OTR method is affected by the insured asset distribution of FCUs and FISCUs. Large swings in this distribution could affect the OTR, and thus the federal operating fee, to the extent that NCUA expenses (e.g., staffing) were not adjusted commensurate with the changes.

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[21] For comparison, the cost per core and special program hour of NCUA's regional office and field program is $147 (which includes overhead costs associated with regulatory-related activities). The cost per core and special program hour for all of the NCUA's costs $238.

[22] The NCUA Board sets the rate. Thus, the board could choose a different rate.

[23] Some SSAs base their fees paid by state-chartered credit unions on the federal operating fee. A large reduction could create competitive pressures for the dual-chartering system, especially in light of budget problems currently in many states.

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APPENDIX 1
LEGAL AND PHILISOPHICAL BASIS FOR OTR

The TF recognizes there is a distinct overlap between the historical role of a regulator (concerned with enforcing laws and implementing public policy) and that of an insurer. Though not motivated by the associated financial liability that comes with the role of insurer, regulators address threats to the viability of their financial institutions to protect consumers and their jurisdiction's economy. This focus on viability benefits the insurer.

The definition of regulatory versus insurance related is open to legitimate debate. Traditionally, even before the advent of federal deposit insurance, regulators have been concerned with protecting the success of the financial industry by "regulating" it (not to be confused with enforcing laws, i.e., rules and regulations) much as one would regulate a nuclear reactor, setting bounds and controlling the reactions to prevent a meltdown. Thus, financial institution exams focused on (1) ensuring laws/regulations were being followed to protect consumers, and (2) ensuring institutions were viable to protect consumers, access to the financial services, and preserve the stability of and confidence in the banking system.[24]

Even today, the OCC (a regulator) indicates it is "committed to bank supervision policies and procedures that support prompt detection and mitigation of problems before they affect a bank's viability." OCC stated one of its motives "is so that a bank's ability to serve its customers is not adversely affected." The OCC, OTS, and FRB conduct exams as regulators, and address safety and soundness issues, even though they have no direct responsibility as an insurer. Similarly, state supervisory authorities examine state-chartered institutions for the same reason.[25]

NCUA has a unique dual role in that it serves as both the regulator of federal credit unions and the insurer of federal credit unions and federally insured state-chartered credit unions. The TF concluded that it is appropriate to allocate examination and supervision related costs between the NCUSIF and NCUA due to the following two lines of reasoning:

<u>Congressional Intent</u>

In Title II of the Federal Credit Union Act, Congress established the NCUSIF and housed it within NCUA for administration by the NCUA Board. Congress envisioned efficiencies from this arrangement, as well as NCUA's partnership with state regulators, by prescribing the following:

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[24] The stability of, and consumers' confidence in, the banking system is essential to the interests of the US economy. If people are stuffing money in mattresses, it isn't being put into the system to promote spending, investment in companies and R&D, etc.

[25] There is a fundamental difference, though, between federal regulators and state regulators. The OCC, OTS, and FRB have a mandate as federal agencies to help protect the financial interests of the federal government (i.e., the FDIC insurance fund) and avoid duplication of efforts and costs by partnering with the FDIC. The SSAs have no such direct mandate. Their state governments choose to be involved in safety and soundness and partnering with insurers given the various benefits they perceive for themselves.

> *"**1782(a)(5)** Reports required under title I of this Act shall be so prepared that they can be used for share insurance purposes. To the maximum extent feasible, the Board shall use for insurance purposes reports submitted to State regulatory agencies by State-chartered credit unions." - Title II*

Congress also recognized that, in addition to losses related to credit union failures, the NCUSIF would incur expenses related to its administration, including examination staff and other employees. In fact, Title I was adjusted to recognize this in addition to the related Title II provisions. The NCUA Board is empowered with determining the "proper" allocation of "administrative and other expenses incurred in carrying out the purposes of this title."

> *"**1766(j)(3)** Funding – The salaries and expenses of the Board and employees of the Board shall be paid from fees and assessments (<u>including interest earned on insurance deposits)</u> levied on <u>insured</u> credit unions under this Act." - **Title I***
>
> *"**1783(a)** There is hereby created in the Treasury of the United States a National Credit Union Share Insurance Fund which shall be used by the Board as a revolving fund for carrying out the purposes of this title. Money in the fund shall be available upon requisition by the Board, without fiscal year limitation, for making payments of insurance under section 207 of this title, for providing assistance and making expenditures under section 208 of this title in connection with the liquidation or threatened liquidation of insured credit unions, <u>and for such administrative and other expenses incurred in carrying out the purposes of this title as it may determine to be proper</u>." - Title II*
>
> ***"1784(a)** The Board shall appoint examiners who shall have power, on its behalf, to examine any insured credit union, any credit union making application for insurance of its member accounts, or any closed insured credit union whenever in the judgment of the Board an examination is necessary to determine the condition of any such credit union for insurance purposes." - Title II*
>
> *"**1789(a)** … (4) to appoint such officers and employees as are not otherwise provided for in this Act, to define their duties, fix their compensation, require bonds of them and fix the penalty thereof, and to dismiss at pleasure such officers or employees. Nothing in this chapter or any other Act shall be construed to prevent the appointment and compensation as an officer or employee of the Administration of any officer or employee of the United States in any board, commission, independent establishment, or executive department thereof; (5) employ experts and consultants or organizations thereof, as authorized by section 15 of the Administrative Expenses Act of 1946 (5 U.S.C. 55a); (6) prescribe the manner in which its general business may be conducted and the privileges granted to it by law may be exercised and enjoyed; (7) exercise all powers specifically granted by the provisions of this title and such incidental powers as shall be necessary to carry out the powers so granted; (8) make examinations of and require information and reports from insured credit unions, as provided in this title; and may be employed as fiscal agent of the United States." - Title II*

NCUA Board's Emphasis on Managing Risk to the NCUSIF

Under its Title II authority, the NCUA Board places priority on managing risk to the NCUSIF by using NCUA resources. The Board recognizes that NCUA's role as insurer must be proactive (involved in preventative maintenance), and not merely reactive (addressing claims). To do otherwise would be to fail to meet the Board's fiduciary responsibility.[26]

Prior to federal share insurance, NCUA's examination of credit unions primarily revolved around determining compliance with established rules and regulations and verifying the institution was solvent. Since the implementation of federal share insurance, the NCUA Board has instituted a much more proactive examination and supervision program geared toward safety and soundness, insurance related issues. As recently as 2002, the NCUA Board further strengthened its commitment to fulfilling NCUA's role as insurer by implementing the Risk-Focused Examination Program. This program bases examination scope and timing to a large extent on the risks an institution poses to the NCUSIF.

In addition, there are other related insurance organizations that engage in proactive risk management. American Share Insurance (ASI), MISC, and CUNA Mutual Insurance Group (CUMIS) all engage in proactive forms of risk management, though have minimal or no regulatory roles. ASI and CUMIS[27] are private for profit entities with no public policy responsibilities (unlike the FDIC which has at least indirect public policy responsibilities as a government entity). Yet, in order to "maximize profits," they spend money on preventative maintenance exam programs. The FDIC also engages in proactive risk management, even though its role is primarily that of insurer.

[26] Also, moral hazard concerns related to federal deposit insurance must be mitigated.

[27] CUMIS is able to rely to some extent on NCUA, SSA, and ASI exam programs as a form of risk management. Thus, the on-site portion of their risk management program is less extensive and not a fair comparison in terms of "cost effectiveness."

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APPENDIX 2
HISTORY OF THE OVERHEAD TRANSFER RATE (OTR)

Background

NCUA supervises all federal credit unions and insures all federal and most state-chartered credit unions. Consistent with the principle of "dual chartering," NCUA only incurs "insurance-related" expenses when interacting with state credit unions. However, when interacting with federal credit unions, the agency incurs expenses for both regulatory-related and "insurance-related" activities.

The NCUA Operating Fund, a revolving fund in the United States Treasury under the management of the NCUA Board, funds the agency's costs associated with federal credit union supervision. The NCUA Operating Fund also funds the cost of administrative services to the National Credit Union Share Insurance Fund (NCUSIF).

To appropriately distribute the costs associated with NCUA's mission as the regulator for FCUs, and the insurer for FICUs, the *Federal Credit Union Act* authorizes the NCUA Board to expend funds from the NCUSIF for the "administrative and other expenses" related to federal share insurance (12 U.S.C. §1783). The NCUA Board exercises this authority by annually transferring a portion of the agency's total operating expenses from the NCUA Operating Fund to the NCUSIF.

The percentage of the agency's operating expense transferred to the NCUSIF is called the Overhead Transfer Rate (OTR). The remainder of NCUA's operating budget is funded primarily by Operating Fees collected from Federal Credit Unions. All NCUSIF insured credit unions hold a 1% deposit in the NCUSIF. Depending upon the performance of the NCUSIF, all insured credit unions are eligible for dividends on their deposit.

NCUA's Dual Role as Regulator and Insurer

NCUA has a dual role. NCUA serves as both supervisory/regulator of federally chartered credit unions and insurer for all federally insured credit unions (including state charters). Rather than employing a separate staff for the NCUSIF, including examiners, the Board uses NCUA staff to carry out both functions. This is a cost-effective structure from which all insured credit unions and their members benefit. The OTR funds the portion of NCUA's expenses that are related to the management and oversight of the NCUSIF (i.e., insurance-related). The federal operating fee covers the cost of supervising/regulating federally chartered credit unions.

Some critics suggest these functions should be separated. However, having two separate organizations would result in additional costs to FICUs due to redundant overhead and overlapping responsibilities. The NCUA's current funding structure has resulted in a strong, healthy credit union industry and a model insurance fund that has never cost the American taxpayer.

Activities Funded by the OTR

All federally insured credit unions and their members derive economic and public trust benefits from NCUA's efforts to mitigate risks and protect the NCUSIF. NCUA spends a material amount of time addressing safety and soundness issues. NCUA recently transitioned into a Risk-Focused Examination (RFE) program. This new examination program, along with ongoing regulatory relief efforts, reflects NCUA's increasing emphasis on its role as insurer. Examples of some of NCUA's efforts that help fulfill fiduciary responsibility in managing the NCUSIF are:

- Research and policy analysis.
- Data collection.
- Offsite monitoring.
- Hotline support.
- Special programs.
- Training and development.
- Examination program development and support.
- Policies and standards set forth in Letters, IRPS, white papers, articles, speeches, presentations, meetings and various other outreach initiatives.

Overview of OTR History

- 1970: NCUSIF was established.
- 1972 – GAO audit recommends NCUA adopt method of allocating costs between NCUA and newly formed NCUSIF.
- 1973-1980: Various allocation methods were employed, including direct charges to the NCUSIF for insurance expenses (cost of closing institutions, liquidation and merger costs, etc.), and examiner time spent supervising (as opposed to examining) institutions.
- 1981-1984: The OTR ranged between 30 and 34%.
- 1985-1994: Annual examination surveys were conducted requiring the completion of 1,000 to 1,200 survey forms. Survey results varied between 50.1% and 60.4%; however, the OTR was maintained at 50%.
- 1994: Survey results of 55.96% insurance-related. OTR maintained at 50% rate for 1995 through 1997. The Board approved conducting surveys once every 3 years.
- 1997: Survey results of 50% insurance-related. OTR maintained at 50% rate for 1998 through 2000.
- 2000: Survey results of 66.72% resulted in an increase of the OTR to 66.72% for 2001 and the NCUAB's decision to hire an independent party to assess the process.
- 2001: Deloitte and Touche (D&T) auditors conducted a review of the OTR process, found the process to be reasonable, and made some minor recommendations to enhance the process.
- 2002: OTR set at 62%. An analysis based on surveys resulted in an OTR range of 62 to 70%. E&I implemented D&T's recommendations to automate the survey collection process, enhance guidance and training for examiners, collect surveys on an ongoing basis (beginning in June 2002), and establish a help-line and public folders to better communicate issues. Automated survey collection began in June 2002. At year end, examiners had uploaded 167 surveys.

- 2003: Survey collection continues. A total of 222 surveys have been collected since June 2002. E&I will provide training for the newly selected survey participants in May 2003. These participants will complete surveys for 12 months beginning in June 2003. A follow-up teleconference will be held for participants shortly following the training session to ensure understanding and enhance communication.

Expanded Detail Regarding OTR History and Method

NCUA surveys examination staff to determine the percentage of time spent on insurance-related activities while examining and supervising FCUs. The survey results serve as the basis for the recommendation for the OTR that is presented to the NCUAB. The survey process attempts to accurately and objectively measure the cost NCUA incurs managing the NCUSIF.

From 1985 through 1994, the Office of Examination and Insurance (E&I) coordinated annual studies to determine an appropriate factor for apportioning the agency's total operating expenses. E&I designed examiner survey forms to capture estimates about time devoted to regulatory-related and insurance-related issues. The breakdown of examination time served as a basis for allocating the agency's total operating expenses because of the following factors:

- NCUA primarily carries out its mission as an insurer and as a federal credit union supervisor through the examination process; and
- On-site examinations are the primary catalyst for other agency functions.

During this period (1985-1994), E&I gathered empirical data using the following process:

1. E&I had all NCUA examiners complete survey forms for each federal credit union examination completed during a certain time period.
2. The survey forms captured the examiners' estimates of the hours they spent completing various examination scope components.
3. The examiners submitted the survey forms, and E&I compiled the data and developed a recommendation to the NCUA Board.

In 1994, E&I conducted a study with a smaller sample of examiner survey forms (98 total responses). On-site interviews were conducted with examiners participating in the survey to ensure reasonableness of survey results. This study yielded results that were consistent with results obtained from the previous surveys of all NCUA examiner staff. As a result, E&I recommended the NCUA Board adopt a transfer rate of 50% for the succeeding three-year period, followed by a reevaluation of the rate in 1997. In view of the projected cost savings from the deferred study period (approximately $150,000 over three years), coupled with the long history of consistent results, the NCUA Board adopted this recommendation.

During 1997, E&I conducted a new study to determine if the overhead transfer rate of 50 percent was still appropriate. As with the 1994 study, E&I used a smaller sample of surveys during 1997. The 1997 study supported the continued use of a 50% overhead transfer rate and thus the NCUA Board voted to keep the 50 percent overhead transfer rate in effect for a new three-year period ending in 2000.

In 2000, data was gathered by surveying principal examiners, regional staff, and central office staff. The surveys resulted in insurance-related percentages for each group. These percentages were applied to the percentage of FTEs allocated to each group resulting in a weighted average OTR of 66.72 percent. The Board adopted the OTR of 66.72 percent and requested that an independent study be commissioned to analyze the process.

In 2001, auditors from Deloitte and Touche completed a study that determined the process was reasonable. The study included recommendations for improvement that were implemented beginning in 2002. These recommendations included improving communication of the survey process and results, improving the survey process by automating and varying the frequency/timing, and updating the survey definitions and purpose.

In 2001, the NCUA Board adopted a 62 percent OTR for 2002 and 2003 based on an analysis of three scenarios resulting from the application of various factors to 2002 budgeted workload hours. Previous year exam time survey results[28] were applied to productive time, and three factors were applied to non-productive time[29], resulting in an OTR ranging from 62 to 70 percent.

In 2002, E&I implemented an automated survey process and collected 167 surveys. As of yearend, the cumulative percentage of time spent by examiners on insurance-related activities for federal credit union examinations and supervision contacts were 68 percent and 74 percent respectively.

In 2003, E&I is developing a recommendation to the NCUA Board derived in part from the Examination Time Survey results. To date, 222 surveys have been collected on a flow basis since June 2002. As expected with the implementation of the risk-focused examination program, the cumulative percentage of time spent by examiners on insurance-related activities for federal credit union examination and supervision contacts increased, to 70 and 75 percent respectively.

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[28] Federal Examination hours were allocated at 63.22% insurance-related, Federal Supervision hours were allocated at 86.40% insurance-related, and State Exam Review and 5300 program hours were allocated at 100%.
[29] Non-productive time (non-program) allocations varied based upon 3 scenarios – 50% (past OTR), 63.22% (reflecting Federal Examination insurance-related time based upon the survey), and 70.85% (weighted average core for federal examination and supervision hours).

Ramifications of the OTR

- A higher OTR results in a lower federal operating fee. Since the OTR funds a portion of NCUA's budget, when the OTR increases the amount of NCUA's budget funded by operating fees paid by FCUs falls.

- The OTR is an expense that reduces the NCUSIF's income, which in turn reduces the amount of funds available for dividends (or to offset premiums).

- Some state regulators base their operating fees on NCUA's operating fee structure. Thus, a higher OTR, resulting in a lower federal operating fee, may result in a decrease in the examination fees paid to state regulators by federally insured state credit unions (FISCUS). This in turn may cause a potential decrease in funding for the state regulator's examination program.

Legal Authority for the OTR[30]

Section 1781(a) of the FCU Act, authorizes the NCUA Board to insure member accounts of all FCUs and member accounts of FISCUs the Board has approved to insure.

Section 1783(a) of the Act establishes the NCUSIF as a "revolving fund" for carrying out the purposes of Title II of the Act.

Section 1789(a)(6)-(7) of the Act allows the Board to prescribe the manner in which it conducts its general business and to exercise all powers specifically granted under Title II or incidental to carrying out such powers. Therefore the Board may transfer money from the NCUSIF to cover expenses (such as personnel and other examination-related costs) paid from the operating fund.

[30] Based on the January 9, 2001, legal opinion from NCUA's Office of General Counsel.

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APPENDIX 3
COMPARISON OF CURRENT OTR METHOD TO PROPOSED METHOD

Current OTR Methodology

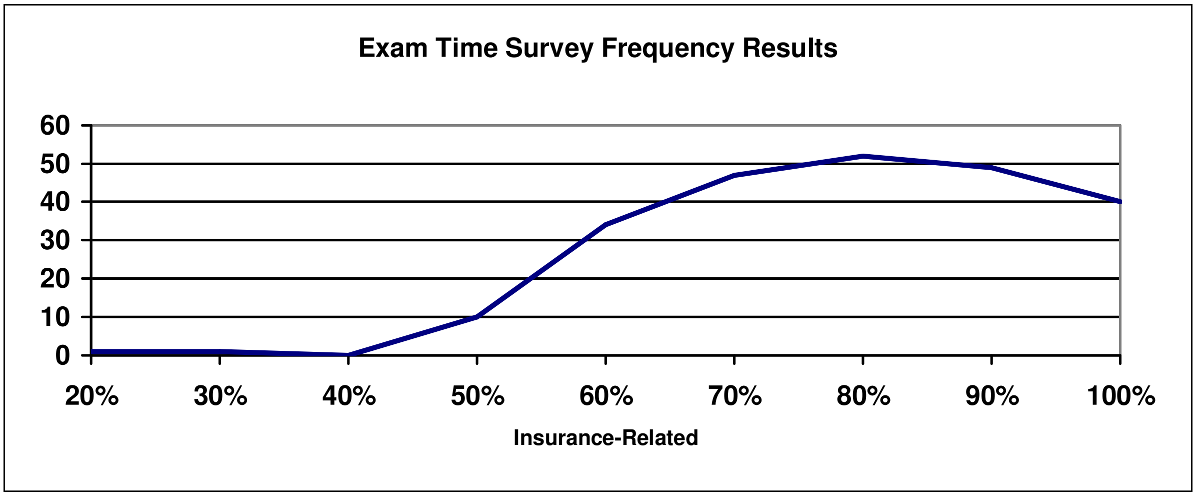
If we were to use the current methodology, which applies the survey results-to-date and other assumptions to the 2003 workload budget to produce three scenarios, the OTR would range from 66.18 to 77.12 percent. The following details the current methodology for comparison purposes.

Survey Results

Examiners uploaded 221 time surveys from June 2002 to March 2003. The weighted (based on each contact's hours) percent of time spent on insurance-related areas is 71.3%.

Contact Type	Number of Surveys	Total Hours	% Insurance Related Hours	% Non-Insurance Related Hours
Exam (10)	134	9,242	70.5%	29.5%
On-site Supervision (22)	87	2,146	74.8%	25.2%
Totals	221	11,388	71.2%	28.8%

The non-weighted mean time spent on insurance-related areas is 74.1%. A range of one standard deviation (half a standard deviation to either side of the mean) encompasses surveys with insurance-related percentages from 66.1% to 82.1%.



Current Methodology Assumptions

The current methodology bases all three scenarios on the same assumptions related to core examination and special programs (productive time). The current methodology applies the following assumptions and insurance factors to the 2003 Workload Budget productive time:

- The exam time survey accurately reflects time spent on insurance-related activities for federal examination (70.48 %) and supervision (74.79%). These factors are applied to the hours budgeted for federal exam and supervision time.
- Time spent on state examination, supervision, and report review is 100% insurance-related.
- Time spent on agricultural lending and CUSO exams is 100% insurance-related.
- Time spent by subject matter examiners mirrors the survey results for federal examinations, i.e., examiners spend 70.48% of their time on insurance-related activities during examination contacts.
- Time spent on fair lending, chartering/FOM, and small credit unions is 0% insurance-related.

After applying these factors to core examination and special program hours budgeted for 2003, the current method concludes that examiners spend 77.1 percent of their productive time on insurance-related activities.

CORE & SPECIAL PROGRAMS	2003 Budget Hours	% of Productive Time	% Insurance-Related	Time Weighted Average Transfer Rate
Federal Examination	346,586	56.6%	70.5%	39.9%
Federal Supervision	106,231	17.3%	74.8%	13.0%
State Exam & Supervision	70,391	11.5%	100.0%	11.5%
State Exam Review	10,566	1.7%	100.0%	1.7%
5300 Program	62,331	10.2%	100.0%	10.2%
Fair Lending Exams	3,001	0.5%	0.0%	0.0%
Subject Matter Examiner	3,116	0.5%	70.5%	0.4%
Agricultural Lending	2,160	0.4%	100.0%	0.4%
Chartering/FOM Activities	1,638	0.3%	0.0%	0.0%
Capital Market Specialists	0	0.0%	100.0%	0.0%
Small Credit Unions	5,553	0.9%	0.0%	0.0%
CUSO Exams	1,148	0.2%	100.0%	0.2%
Total Productive Hours	**612,721**	**100.0%**	N/A	**77.1%**

Current OTR Method – Three Scenarios

The current methodology calculates three scenarios which result in an OTR range. The scenarios differ in the factors applied to non-productive hours (training, meetings, travel, leave, etc.). The three scenarios are as follows:

- Scenario 1 assumes that non-productive hours support core program activities and time should mirror the time examiners spend on insurance related activities. Accordingly, we applied the percent of examiner's time spent on insurance-related activities – 77.12% to non-productive hours.

- Scenario 2 assumes that non-productive hours mirror the federal examination program rate for time spent on insurance-related activities of 70.48% (derived from the survey).

- Scenario 3 applies 50% to non-productive hours. This assumes an equal split between insurance and non-insurance related activities for non-productive hours.[31]

Under each scenario, we multiplied the percentage of total hours for each category by the insurance percentages, which results in an insurance factor for that category. We total the factors for each scenario to determine resulting in a range of possible OTRs. The following table outlines the details and results of the current methodology.

[31] This scenario is provided for historical comparison. The TF concluded there is no supportable basis for the assumption for non-productive time in this scenario, and suggests this scenario be excluded from serious consideration.

			Insurance % Applied to Non-productive Time					
			Scenario 1: Time-Weighted % of Productive Time **77.12%**		**Scenario 2:** Federal Examination Survey Results **70.48%**		**Scenario 3:** Prior Standard **50%**	
PRODUCTIVE TIME	**2003 Budgeted Hours**	**% of Total Hours**	**% Ins**	**Factor**	**% Ins**	**Factor**	**% Ins**	**Factor**
Core Programs:								
FEDERAL EXAMINATION	346,586	**33.74**	70.48%	**23.78**	70.48%	**23.78**	70.48%	**23.78**
FEDERAL SUPERVISION	106,231	**10.34**	74.79%	**7.73**	74.79%	**7.73**	74.79%	**7.73**
STATE EXAM & SUPV	70,391	**6.85**	100.00%	**6.85**	100.00%	**6.85**	100.00%	**6.85**
STATE EXAM REVIEW	10,566	**1.03**	100.00%	**1.03**	100.00%	**1.03**	100.00%	**1.03**
5300 PROGRAM	62,331	**6.07**	100.00%	**6.07**	100.00%	**6.07**	100.00%	**6.07**
Special Programs:								
FAIR LENDING EXAMS	3,001	**0.29**	0.00%	**0.00**	0.00%	**0.00**	0.00%	**0.00**
SUBJECT MATTER EXAMINER	3,116	**0.30**	70.48%	**0.21**	70.48%	**0.21**	70.48%	**0.21**
AGRICULTURAL LENDING	2,160	**0.21**	100.00%	**0.21**	100.00%	**0.21**	100.00%	**0.21**
CHARTERING FOM ACTIVITIES	1,638	**0.16**	0.00%	**0.00**	0.00%	**0.00**	0.00%	**0.00**
CAPITAL MARKET SPECIALIST	0	**0.00**	100.00%	**0.00**	100.00%	**0.00**	100.00%	**0.00**
SMALL CREDIT UNIONS	5,553	**0.54**	0.00%	**0.00**	0.00%	**0.00**	0.00%	**0.00**
CUSO EXAMS	1,148	**0.11**	100.00%	**0.11**	100.00%	**0.11**	100.00%	**0.11**
NON-PRODUCTIVE TIME	**2003 Budgeted Hours**	**TOTAL**	**% Ins**	**Factor**	**% Ins**	**Factor**	**% Ins**	**Factor**
Examiner Development and Reference Management:								
OFFICE	76,362	**7.43**	77.12%	**5.73**	70.48%	**5.24**	50.00%	**3.72**
COMPUTER/ADMIN	5,848	**0.57**	77.12%	**0.44**	70.48%	**0.40**	50.00%	**0.28**
SE MGT DETAILS	6,560	**0.64**	77.12%	**0.49**	70.48%	**0.45**	50.00%	**0.32**
PC AND AIRES	3,520	**0.34**	77.12%	**0.26**	70.48%	**0.24**	50.00%	**0.17**
MEETING/EXT/INT	33,154	**3.23**	77.12%	**2.49**	70.48%	**2.27**	50.00%	**1.61**
TRAINING/CLASSROOM	44,612	**4.34**	77.12%	**3.35**	70.48%	**3.06**	50.00%	**2.17**
TRAINING OJT	10,068	**0.98**	77.12%	**0.76**	70.48%	**0.69**	50.00%	**0.49**
TRAINING SPEC	7,200	**0.70**	77.12%	**0.54**	70.48%	**0.49**	50.00%	**0.35**
DETAILS CO	6,000	**0.58**	77.12%	**0.45**	70.48%	**0.41**	50.00%	**0.29**
DETATILS RO	7,852	**0.76**	77.12%	**0.59**	70.48%	**0.54**	50.00%	**0.38**
MGT DEV DETAILS	5,710	**0.56**	77.12%	**0.43**	70.48%	**0.39**	50.00%	**0.28**
Administrative Time:								
TRAVEL	44,853	**4.37**	77.12%	**3.37**	70.48%	**3.08**	50.00%	**2.18**
TRAINING TRAVEL	13,852	**1.35**	77.12%	**1.04**	70.48%	**0.95**	50.00%	**0.67**
HOLIDAY	39,160	**3.81**	77.12%	**2.94**	70.48%	**2.69**	50.00%	**1.91**
LEAVE	109,723	**10.68**	77.12%	**8.24**	70.48%	**7.53**	50.00%	**5.34**
TOTALS	**1,027,195**	**100.00**	**Scenario 1:**		**Scenario 2:**		**Scenario 3:**	
			OTR RESULTS	**77.12**		**74.44**		**66.18**

Proposed OTR Methodology

Based upon the current results of the examination time survey and the proposed new methodology described in this report, the recommended OTR would be 61.4 percent. Two key similarities exist between the current and proposed methodology. Both methodologies:

1. Rely upon the results of the Examination Time Survey as a key driver to allocate NCUA's insurance-related versus regulatory costs; and

2. Apply the survey results to the Workload Budget Hours to calculate the OTR.

We enhanced and improved the proposed OTR methodology by considering additional information to ensure equitable treatment for all federally insured credit unions. The key differences are that the proposed methodology will:

1. Apply the results of the Examination Time Survey to NCUA's dollar budget and add back direct NCUSIF charges to determine the total cost of insurance-related activities for all federally insured credit unions.

2. More fairly allocate the total insurance costs to FCUs and FISCUs based upon the current breakdown of assets. Currently, FCUs represent for 55 percent of total NCUSIF-insured assets, and FISCUs are 45 percent.

3. Recognize the value of the work done by SSAs. We calculate the imputed value of the SSAs' work by applying the results of the time survey and average FCU examination hours (based upon asset size and CAMEL code) to the FISCUs that we do not already examine. We considered the impact of deferred examinations (risk-based scheduling) and joint exams to ensure that we fairly estimated the imputed value.

4. Reduce NCUA's total insurance costs by the SSA imputed value prior to calculating the OTR. This step, which ultimately lowers the OTR, recognizes the value of the work done by the SSAs that benefits the NCUSIF.

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APPENDIX 4
OTR UNDER VARIOUS SCENARIOS

No FISCU Work Conducted by NCUA

In the scenario where NCUA relied completely upon SSAs to conduct all of the on-site insurance-related examination and supervision of FISCUs, NCUA's Core and Special Programs workload budget would decline by 70,391 hours.[32] The total workload budget would decline to 909,000 hours based on the same 59.7% productivity ratio.

Step 1: The Percent of NCUA's Field Program devoted to NCUA's Regulatory Role would increase to 27.7% based on current survey results.

Steps 2 & 3: Field and Regional Office costs would decline by approximately $9 million based on the same cost estimation employed for the proposed new method. This would result in NCUSIF costs of:

	Millions
2003 NCUA Dollar Budget	$137.1
Regulatory Costs (see Step 2)	- $40.5
Direct Operational Charges to NCUSIF	+ $2.1
Total NCUSIF Operational Costs	= $**98.8**

Step 4: Based on the SSAs picking up all of the FISCU work, the SSA imputed value would increase to $26.2 million. This results in a net cost to FISCUs of $31.2 million.

	Millions
Total NCUSIF Operational Costs	$98.8
SSA Insurance Work Imputed Value	+ $26.2
Total Cost of Providing NCUSIF Insurance	= **$125.0**

	FCU (Millions)	FISCU (Millions)
Total Cost of Providing NCUSIF Insurance	$125.0	$125.0
Proportional Allocation Basis	x 54.1%	x 45.9%
Total Allocated Insurance Costs	= $67.6	= **$57.4**

	Millions
Total Allocated Insurance Costs - FISCUs	$57.4
SSA Insurance Work Imputed Value	- $26.2
Net Cost of NCUSIF Insurance – FISCUs	= **$31.2**

[32] This scenario assumes NCUA would still conduct reviews of state examination reports. There are 10,566 hours within the workload budget for this task.

Step 5: With FISCUs responsible for $31.2 million through the OTR, this results in an OTR of 49.5%.

	Millions
FISCU Portion of NCUA Insurance Cost	$31.2
Divided by FISCU Proportional Allocation Basis	45.9%
Equals Dollar Amount of OTR	$67.9
Dollar Amount of OTR	$67.9
Divided by NCUA Budget	$137.1
Equals OTR	49.5%

Thus, even if NCUA relied completely on SSAs for on-site state examination and supervision time, FISCUs would still be responsible for their share of the other costs associated with providing the NCUSIF insurance. Theses cost provide the following benefits and services.

- NCUA's overall due diligence and risk management procedures related to the NCUSIF.
- Administration of the NCUSIF operations, such as processing claims, investing funds, administrative personnel and paperwork, etc.
- Costs related to the operation of the NCUA Board in relation to NCUSIF duties.
- Research and policy analysis.
- Data collection.
- Offsite monitoring.
- Hotline support.
- Special programs.
- Training and development.
- Examination program development and support.
- Policies and standards set forth in Letters, IRPS, white papers, articles, speeches, presentations, meetings and various other outreach initiatives.
- SSA equipment and state examiner training.

FCU Exam Survey Increases to 100%

The survey results for the percent of FCU examination and supervision insurance related time have increased from a range of 60 to 67 percent historically to well over 70 percent currently due in large part to the implementation of the risk-focused examination program. Though it is very unlikely this level would reach 100%, this scenario is presented for information purposes.

Step 1: The Percent of NCUA's Field Program devoted to NCUA's regulatory role would decrease to 1.7%. Some Special Programs are still regulatory in nature.

Steps 2 & 3: Regulatory costs would decline to $8.9 million, mostly involving special cost centers devoted to regulatory roles. This would result in NCUSIF costs of:

	Millions
2003 NCUA Dollar Budget	$146.1
Regulatory Costs	- $8.9
Direct Operational Charges to NCUSIF	+ $2.1
Total NCUSIF Operational Costs	= $**139.4**

Step 4: The SSA imputed value would increase to $25.4 million since we would apply the same survey results (100%) to the imputed value as for the FCU program. This results in a net cost to FISCUs of $50.2 million.

	Millions
Total NCUSIF Operational Costs	$139.4
SSA Insurance Work Imputed Value	+ $25.4
Total Cost of Providing NCUSIF Insurance	**= $164.8**

	FCU (Millions)	FISCU (Millions)
Total Cost of Providing NCUSIF Insurance	$164.8	$164.8
Proportional Allocation Basis	x 54.1%	x 45.9%
Total Allocated Insurance Costs	= $89.1	**= $75.6**

	Millions
Total Allocated Insurance Costs - FISCUs	$75.6
SSA Insurance Work Imputed Value	- $25.4
Net Cost of NCUSIF Insurance – FISCUs	**= $50.2**

Step 5: With FISCUs responsible for $50.2 million through the OTR, this results in an OTR of 74.9%.

	Millions
FISCU Portion of NCUA Insurance Cost	$50.2
Divided by FISCU Proportional Allocation Basis	45.9%
Equals Dollar Amount of OTR	$109.4

	Millions
Dollar Amount of OTR	$109.4
Divided by NCUA Budget	$146.1
Equals OTR	74.9%

The new formula takes into consideration other regulatory programs and costs within NCUA, as well as provides an imputed SSA value based on the same survey results applied to FCU work. Thus, even with the extreme of a survey reflecting 100% insurance-related exam and supervision work, the OTR only increases to 74.9%.

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APPENDIX 5
ALTERNATIVES CONSIDERED

The TF considered a number of alternatives to the recommended framework. Each alternative is addressed briefly below.

Payments Directly to SSAs or FISCUs in Lieu of Reducing the OTR

The TF considered and recommends against paying SSAs for the imputed value of their work. We believe the decision to establish a payment by the Federal government to the states is more appropriately a role for Congress. Also, direct payments to FISCUs may have the unintended consequence of inviting SSAs to charge FISCUs an amount equal to these payments, accomplishing indirectly what we recommend against above. Further, the TF does not wish to involve FISCUs in the event the adequacy of an SSA's examination program was called into question.

Although a remote possibility, direct payment to SSAs or credit unions could result in an inappropriate reward for engaging in directly unproductive profit seeking (DUPS) activities. For example, an SSA or credit union could attempt to decrease a CAMEL rating, resulting in increased imputed time and value for SSA examination and supervision and, therefore, an increased payment. By utilizing the OTR, the linkage between CAMEL ratings and an individual SSA or credit union is fully diluted. Further, since the computation of imputed value is based on credit union size as well as CAMEL code, the imputed value for a set of many small credit unions may be higher than that for a set of fewer large credit unions, even if each set aggregates to the same total size. We do not intend to provide SSAs or credit unions with an incentive against consolidation, in order to increase payments based on imputed value.

Retaining the Current Method

We recommend against retaining the current method since the proposed new method may be implemented at little cost, recognizes the value of SSA examinations, and makes a number of other minor refinements and improvements to the current method.

Use Actual SSA Costs in Lieu of Imputing a Value

The TF considered using actual SSA costs. However, using actual SSA costs would necessitate a thorough review of each SSA's budget and examination program. This may be perceived as an unwarranted intrusion into the operation of the SSAs, would be very labor intensive, and related conclusions and assumptions would no doubt be the source of significant debate. Further, there may be efficiency differences among the SSAs, resulting in potential subsidies for inefficient states reporting higher hours and, thus, higher costs. Because the relevant cost the NCUSIF avoids by relying upon SSAs is the cost of NCUA conducting the work, the alternative of using actual SSA costs was dismissed.

Use of Full Cost Accounting

The TF considered advising adoption of a full cost accounting system by NCUA. The TF is cognizant NCUA may improve its ability to track costs to further the purposes of the Government Performance Results Act of 1993. However, because the TF is of the opinion the recommended framework is reasonably fair and accurate based on various tests conducted against the assumptions and calculations, we do not advise spending significant additional resources to refine allocations. As NCUA's cost accounting systems mature, it may be cost effective in the future to explore additional refinements to the OTR methodology.

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APPENDIX 6
EXAMINATION TIME SURVEY BACKGROUND, RESULTS, AND DETAILS

Examination Time Survey Background

Since its inception in 1985, the examination time survey evolved from a manually completed form to the automated form used now. From 1985 to 1994, NCUA collected 1,000 to 1,200 manually completed survey forms annually. Since survey results were consistent, we reduced the sample size considerably and instead of annual collection, moved to a 3-year cycle. In 1994, 1997, and 2000, the sample size ranged from 60 to 100 survey forms. There were no surveys completed in 2001.

In 2001 Deloitte and Touche (D&T) completed a study and concluded the time survey process was reasonable and appropriate for use in allocating NCUA's costs between insurance-related and regulatory-related activities. The study did include some recommendations to enhance the survey process, such as automating the survey form, improving communications, and varying the period of collection, but did not recommend any changes to the survey's content. These recommendations have been implemented.

In 2002, E&I randomly selected one SE group (via lottery draw) from each region to participate in the survey process. The regions selected three experienced examiners from these SE groups to complete surveys for all examination and supervision contacts made in federally chartered credit unions. NCUA began collection automated exam time surveys in June 2002.

In the past, examiners completed time surveys during a set period, often occurring near the end of the exam program year. As of 2002, examiners complete surveys for all examination and supervision contacts they conduct during a 12-month period that starts in June. In June 2003, a new set of participants will be completing time surveys for the next 12-month period. The new process allows us to collect data for a variety of credit unions, completion dates, and geographic locations that provides a sample that better represents the entire population.

Prior to introducing the automated form, NCUA did not provide formal training to survey participants. As of 2002, E&I held a training session and a subsequent teleconference for the selected participants, their supervisors, and a regional office analyst from each region. We also dedicated an email address for examiners to use to request help with the survey. In addition, we set up a public folder to store information such as Frequently Asked Questions (FAQs), summary reports, and training information. In general, communications regarding the survey process have improved, which helps to ensure consistent application and reliable results.

Results of the Examination Time Survey

We will use a full year's worth of survey results when determining the OTR. The current yearly cycle will conclude in May 2003. As of March 31, 2003, the cumulative results of the time survey process were as follows:

Contact Type (WCC)	**Total Surveys Collected**	**Insurance Related %**	**Non-insurance Related % (Regulatory)**
Examination (code 10)	135	70.4%	29.6%
Supervision (code 22)	87	74.8%	25.2%
Total	**222**	**71.2%**	**28.8%**

Time Category Results June 2002 – March 2003	**Exam - Insurance**	**Supervision - Insurance**
Planning / Scope Development	73.2%	80.0%
Call Report Review	60.4%	55.0%
Supervisory Committee	61.2%	59.3%
Financial Analysis	65.8%	76.1%
Loan Analysis	77.0%	78.8%
Investment Analysis	66.8%	65.5%
Liquidity Analysis	87.6%	82.2%
Asset Liability Management	82.4%	80.8%
Compliance	27.9%	25.0%
Information Systems Technology	71.5%	69.0%
Management	68.6%	75.3%
Examination Report/JC/Follow-Up	81.4%	82.7%
Total	**70.4%**	**74.8%**

Content of Time Survey Form

The TF carefully reviewed the survey form and concurs with D&T's assessment (conducted in 2001) that the survey is properly designed to differentiate between regulatory and insurance related activities. Further, the survey is carefully administered to ensure the integrity of the information. A copy of the survey form and instructions follows:

General Information about Examination:

Name:	**__________________ FEDERAL Credit Union**
Charter Number:	**#__________**
Assets (no decimal places):	**$____________________**
Effective Date of Contact:	**____/____/200x**
Contact Type (WCC):	**_______**
CAMEL Rating:	**COMPOSITE RATING ____**
	Capital Adequacy ___
	Asset Quality ___
	Management ___
	Earnings ___
	Liquidity ___

Survey Form Time Detail

Time Categories	Total Hours	Insurance Related	Non-Insurance Related
Planning / Scope Development			
Call Report Review			
Supervisory Committee			
Financial Analysis			
Loan Analysis			
Investment Analysis			
Liquidity Analysis			
Asset Liability Management			
Compliance			
Information Systems Technology			
Management			
Examination Report/JC/Follow-Up			
Total Exam Hours			

<u>Survey Form Instructions/Guidelines</u>: The survey is an excel workbook that includes pop-up guidance along with the complete set of general definitions and specific instructions for the users. The following is a copy of what is included in the form:

GENERAL DEFINITIONS

<u>Insurance Related Examination Procedures</u>:

Insurance Related examination or supervision contact procedures address safety and soundness issues. On the time survey forms, respondents should classify the time used to evaluate safety and soundness as “Insurance Related.” “Insurance Related” time involves efforts to review, report, or document areas that include, but are not limited to, the following:

- Evaluating financial trends and Call Report data.
- Determining the credit union’s solvency position.
- Evaluating risks, and potential costs, the credit union presents to the NCUSIF (when appropriate).
- Assessing management’s efforts to protect earnings and net worth by identifying, evaluating, controlling, and monitoring internal and external risks.
- Assessing management’s abilities to develop strong policies and a reliable internal control structure.

<u>Non-Insurance Related Examination Procedures</u>:

Non-Insurance Related examination or supervision contact procedures address compliance with the laws and regulations that NCUA enforces. On the survey forms, respondents should classify the time used to evaluate issues not related to safety and soundness as “Non-Insurance Related.” “Non-Insurance Related” time involves efforts to review, report, or document areas that include, but are not limited to, the following:

- Compliance with consumer protection laws, NCUA Rules and Regulations, the FCU Act, and Bylaws
- Review of previously cited regulatory violations, areas of concern, and corrective actions taken
- Call report accuracy and timeliness

SPECIFIC INSTRUCTIONS ABOUT INDIVIDUAL SCOPE CATEGORIES

<u>NOTE</u>: The procedures referenced within each time category of the survey are <u>not</u> all encompassing. These guidelines merely provide *examples* respondents should consider when estimating the allocation of their time.

A. Planning / Scope Development

1) Time related to Insurance Issues includes the time required for tasks such as:

- Reviewing prior contact reports to identify historical safety and soundness concerns;
- Reviewing scope workbook to become familiar with potential safety and soundness concerns;
- Reviewing correspondence between contacts that address safety and soundness issues;
- Reviewing recent financial trends;
- Evaluating changes to the credit union's product and service mix that could present new safety and soundness concerns;
- Determining whether a Subject Matter Examiner could assist during the supervision process in addressing safety and soundness concerns;
- Considering whether additional resources (i.e., grants, technical assistance, low-income designation) are available to assist management in addressing safety and soundness concerns;
- Evaluating prevailing economic conditions;
- Reviewing risk management reports;
- Interviewing key officials to learn status of action taken to correct previously identified safety and soundness concerns;
- Developing on-site procedures for evaluating safety and soundness concerns;
- Completing portions of scope workbook that pertain to safety and soundness concerns; and
- Updating scope workbook to document new information about safety and soundness issues.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Reviewing prior contact reports for previously cited noncompliance issues and regulatory violations;
- Reviewing scope workbook to become familiar with potential regulatory concerns;
- Reviewing correspondence between contacts that address compliance and regulatory concerns;
- Determining the potential applicability of new regulatory requirements;
- Determining whether a Subject Matter Examiner could assist during the supervision process in addressing compliance and regulatory concerns;
- Considering whether additional resources (i.e., grants, technical assistance, low-income designation) are available to assist management in addressing regulatory and compliance concerns;
- Evaluating changes to the credit union's product and service mix that could require an expanded review of regulatory compliance;
- Interviewing key officials to determine management's level of expertise regarding, and attitude toward, regulatory compliance;
- Developing on-site procedures for evaluating regulatory concerns;
- Completing portions of scope workbook that pertain to regulatory concerns; and
- Updating scope workbook to document new information about regulatory issues.

B. Call Report Review

1) Time related to Insurance Issues includes the time required for tasks such as:

- Determining if factors causing inaccuracies in Call Reports are symptoms of internal control weaknesses.
- Reviewing Call Report trends for potential risk indicators.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Verifying the accuracy and timeliness of Call Reports filed by management.

C. Supervisory Committee Review

1) Time related to Insurance Issues includes the time required for tasks such as:

- Reviewing general internal controls and segregation of duties;
- Evaluating if the supervisory committee serves as a legitimate "check" upon management activity; and
- Determining whether supervisory committee is effective in correcting identified internal control weaknesses.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Ensuring the supervisory committee is carrying out its fiduciary responsibility to ensure member account verifications and annual audits are complete and timely and meeting the supervisory committee's regulatory requirements.
- Reviewing the actual documentation from the supervisory committee audit and member account verification.

D. Financial Analysis

1) Time related to Insurance Issues includes the time required for tasks such as:

- Reviewing the current financial trends; and
- Determining whether management has adequate controls and risk management systems in place.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Reviewing general accounting procedures to ensure compliance with the *Accounting Manual for Federal Credit Unions*;
- Verifying that current financial statements reflect the balances in the general ledger;
- Determining that management is maintaining adequate subsidiary ledgers; and
- Testing the validity of delinquency computation and income accrual procedures.

E. Loan Analysis

1) Time related to Insurance Issues includes the time required for tasks such as:

- Reviewing loan underwriting procedures;
- Determining the risk associated with the product mix;
- Evaluating loan policies to determine if sound practices exist;
- Reviewing collection efforts for timeliness;
- Evaluating whether the level of the credit union's reserves is consistent with the loan products offered by the credit union.
- Assessing the controls management has over loan losses.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Evaluating compliance with the limitations promulgated within the Federal Credit Union Act, NCUA Rules and Regulations, and consumer compliance laws and regulations;
- Ensuring the written policies comply with all applicable lending regulations; and
- Evaluating the accuracy and funding methodology of the allowance for loan loss account.

F. Investment Analysis

1) Time related to Insurance Issues includes the time required for tasks such as:

- Reviewing appropriateness of the investment portfolio and overall practices;
- Determining the adequacy of the internal controls related to investments;
- Assessing investment trends;
- Ensuring adequate safekeeping procedures are in place; and
- Evaluating management's effectiveness in addressing investment risks.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Reviewing the permissibility of the investments included in the portfolio; and
- Reviewing the written investment policy to ensure the policy includes all elements discussed in the regulations.

G. Liquidity Analysis

1) Time related to Insurance Issues includes the time required for tasks such as:

- Determining whether the credit union has sufficient liquidity to cash needs for loan and share transactions;
- Evaluating whether management has sound contingency plans for addressing unanticipated liquidity needs; and
- Ensuring risk management processes (measuring, monitoring, controlling, and reporting) are appropriate for credit union.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Ensuring management is complying with statutory borrowing limitations.

H. Asset Liability Management

1) Time related to Insurance Issues includes the time required for tasks such as:

- Determining if management has adequate controls in place and assigns clear responsibilities to address the credit union's overall exposure to interest rate risk;
- Reviewing the adequacy of the credit union's modeling and risk monitoring procedures; and
- Ensuring that management initiates corrective action when internal analysis identifies concerns relative to interest rate risk.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Ensuring written asset liability management policies do not contain provisions that are inconsistent with regulations that apply to loans, investments, or shares.

I. Compliance

1) Time related to Insurance Issues includes the time required for tasks such as:

- Determining whether any identified regulatory violations could cause the credit union to have financial risk exposure.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Assessing management's compliance with the Bank Secrecy Act;
- Reviewing compliance with consumer regulations that pertain to lending and savings programs; and
- Evaluating other regulatory compliance issues such as records preservation, security devices, regulatory fees, membership eligibility, and other applicable state and federal laws and regulations.

J. Information Systems Technology

1) Time related to Insurance Issues includes the time required for tasks such as:

- Ensuring that the credit union's written policies contribute toward the establishment and maintenance of a system of sound internal controls; and
- Determining if weaknesses in the control structure presents any exposure to financial risks.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Ensuring that all agreements with outside parties meet applicable legal requirements; and
- Evaluating controls the credit union has in place to ensure compliance with Privacy Act requirements.

K. Management Analysis

1) Time related to Insurance Issues includes the time required for tasks such as:

- Reviewing planning and general business practices for overall soundness;
- Reviewing income/expense budget process and controls; and
- Assessing management's capabilities in implementing strategies to address risks.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Reviewing compliance with Federal Credit Union Bylaws;
- Reviewing Board minutes to ensure meetings take place in accordance with the Federal Credit Union Act and Bylaws; and
- Ensuring that all written policies are consistent with applicable laws and regulations.

L. Contact Report / Joint Conference / Follow-Up Procedures

1) Time related to Insurance Issues includes the time required for tasks such as:

- Communicating safety and soundness or risk management issues to credit union officials and employees during the exit interview process;
- Documenting supervision plans for monitoring safety and soundness concerns noted during an on-site contact;
- Discussing safety and soundness or risk management concerns with management during the joint conference;
- Preparing written reports that provide guidelines for correcting safety and soundness concerns;
- Drafting correspondence for the Regional Director's signature that discuss safety and soundness concerns;
- Preparing internal monitoring reports that assess management's progress in addressing safety and soundness or risk management issues;
- Assisting management in obtaining outside mentor assistance to address safety and soundness concerns; and
- Implementing administrative remedies designed to correct safety and soundness or risk management concerns.

2) Time related to Non-Insurance Issues includes the time for tasks such as:

- Communicating regulatory violations that do not present safety and soundness concerns to credit union officials and employees during the exit interview process;
- Documenting supervision plans for monitoring regulatory violations noted during an on-site contact;
- Discussing regulatory concerns with management during the joint conference;
- Preparing written reports that provide guidelines for complying with regulations that do not specifically pertain to insurance-related concerns;
- Assisting management in obtaining outside mentor assistance to address regulatory and compliance issues; and
- Drafting correspondence for the Regional Director's signature that discusses regulatory concerns.

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APPENDIX 7
POTENTIAL CRITICISMS AND RESPONSES

The OTR is Driven by the NCUA Budget.
Neither the current nor the proposed methods are driven by the NCUA budget. The NCUA budget is set without respect to the OTR. Both methods for calculating the OTR factor in the impact of expenditures in areas related to NCUA's regulatory and insurance roles, but do not drive the budgets in these areas.

Proposal of the New Method Indicates the Past Method Was Flawed. Since the Major Change is the Imputed SSA Value, Shouldn't FISCUs be Reimbursed for Being Overcharged in the Past?
The proposed new method is an improvement of the current method in several respects, primarily in its consideration of the value provided by SSAs. However, the current method was the best one available at the time. In regard to addressing past charges, it would be an extremely complicated matter, subject to various assumptions, to determine what would have been charged for the OTR in the past. Considering historical OTRs in relation to credit union trends, and the time value of money, it is actually more likely that FISCUs would owe FCUs on a present value basis.

The Only Reason NCUA is Adopting this New Method is Because of the Risk-Focused Exam's Effect on the Time Survey.
Admittedly, given the increase in the time survey results and that 2003 was the year to reevaluate the OTR, the timing of this new method was opportune. Fortunately, NCUA assigned some very talented and innovative individuals to fully explore alternatives to the OTR methodology. Out of this team came the proposed new method, an innovative approach to dealing with this issue.

The Proposed New OTR Method Imputes A Value For SSAs' Work At State-Chartered Natural Person Credit Unions, But Does Not Include Corporate Credit Unions.
The TF reviewed reports of SSA hours for corporate credit unions and determined the aggregate of all state examination hours was immaterial to the OTR calculation. In part, this is because OCCU conducts a robust insurance review program for both Federally-chartered and State-chartered corporate credit unions.

The Proposed New Method Is Subject To Year-To-Year Variation. The Framework Will Tilt Cost Towards Insurance As Examiners Shift Focus To Insurance Issues During Economic Recessions.
The proposed new method is quite properly designed to capture increased insurance expenses when insurance concerns rise. The TF recommends the OTR be set every two years to smooth out year-to-year fluctuations.

The OTR Method Is Survey Driven. As Experienced Is Gained With Risk Focused Examinations, Or As A Form Of "Self-Preservation" To Increase The OTR, Examiners May Over-Report Insurance Hours And Under-Report Regulatory Hours.

The survey process has been reviewed independently by Deloitte and Touche. We continue to refine the survey process to ensure the regulatory compliance role is distinguished from the insurance role. We provide careful, thorough training for all examiners participating in the survey, conduct periodic teleconferences with survey participants to address questions, and have established an e-mail folder to foster understanding and provide clarifying information. NCUA makes it clear examiners should report how they actually spend time, without any predetermined agenda such as arriving at a particular percentage. NCUA is committed to ensuring the integrity of the survey process.

The Survey Process Uses Only Experienced Examiners. Experienced Examiners Typically Handle The Riskier, More Complex, Larger Cases, Which Likely Translates Into More Insurance Time Than Regulatory Time. Thus The Process Is Set Up To Be Skewed Toward Insurance-Related Results.

The TF analyzed the CAMEL and Asset ranges for the credit union examinations and supervision contacts that have received a survey. The distribution of the survey sample is similar to the credit union population. Thus, the sample that is derived from the use of experienced examiners will not inherently skew the results.

If NCUA Could Absorb All Of The Additional FISCU Work With The Only Impact To Central Office Staffing And Costs In OHR, Then There Should Be Ample Room For Cost And Staff Reductions In The Central Office.

There is a certain, core level of infrastructure necessary to support any organization, and in particular any government agency. This core infrastructure is independent within a certain range from the size of the programs administered. Some examples in NCUA's case include:

- The NCUA Board and related staffing is necessary to represent the Executive Branch of the government and oversee NCUA's operations. This is largely independent of the size of the exam program.
- Infrastructure necessary to support GAO, Congressional, and Public (e.g., FOIA) requests for information and to implement law affecting the operation of federal agencies, such as GISRA, GPRA, etc.
- Policy and procedure setting offices, such as OSPSP and E&I, which are largely independent of the size (though not complexity) of the exam program. For example, there is a fixed level of effort involved in determining an appropriate examination procedure for a particular area, such as member business lending. Once set, from an E&I resource standpoint the policy is just as easily applied to a population of 1,000 examined credit unions as it is to 10,000.

In addition, other offices (such as OCIO) currently already provide support to both federal and state examiners. Thus, there is net wash in terms of the impact of additional NCUA staffing that would result in a reduction of support to state examiners.

The Imputed SSA Value Assumes All SSA Costs Are Equal. The Method Should Take Into Consideration Geographic Cost Differences, And Evaluate Differences In The Quality Or Efficiency Of SSA Programs.

Geographic differences (cost of labor) are already reflected in NCUA staff costs, and thus in the imputed SSA value. Just as NCUA does not charge a higher examination fee to FCUs in a higher cost area than we do for those in a lower cost area, we have not based the imputed value on a state or geographic specific basis. This is based on the mutual nature of the NCUSIF, as well as ease of administration.

In terms of the quality of SSA programs, short-term "assistance" provided by NCUA to an SSA to bolster or supplement their program should simply be distributed throughout the system based on the mutual nature of the NCUSIF. This is conceptually similar to a regional specialized examiner providing assistance to a number of different supervisory examiner's groups, or one federal supervisory examiner's group with seasoned examiners providing assistance to another group with less experienced examiners. However, if NCUA were to experience chronic problems with a particular state's examination reports, requiring NCUA to perpetually spend an inordinate amount of time in that state, NCUA would need to consider charging those FISCUs a fee to offset these costs and thus re-establish the "fair" distribution of costs to the system.

For example, NCUA could set an operating trigger, based on examiner time spent in a particular state on a recurring basis, beyond which NCUA would charge FISCUs for time spent. In terms of a complete SSA withdrawal from providing examination reports, or a partnership between NCUA and an SSA conducting alternating exams, NCUA would need to charge the FISCUs in these states for the work conducted at an hourly rate of $119. This revenue would offset the additional costs of conducting this work, and restore the fair distribution of insurance-related costs amongst FICUs.

Imputed SSA Value	$16,815,339
/ Additional FISCU Program Hours	141,691
= Marginal Cost Per Hour	$119

The amount of time it would take NCUA to conduct the insurance work in a FISCU, based on the time spent in an equivalent FCU and with a time survey insurance-related factor of 70.5% is:

FISCU Insurance Hours Based on Average FCU Exam Time

FCU 2002 Average Exam Time (Hours)	Assets < $10M	$10M - $100M	$100M - $250M	$250M - $500M	> $500M
CAMEL 1	32	61	114	136	208
CAMEL 2	33	66	122	151	214
CAMEL 3	36	71	133	147	214
CAMEL 4	47	84	162	NA	NA
CAMEL 5	59	121	NA	NA	NA

Average Cost Per NCUA Insurance Review

FISCU Exam Cost ($)	Assets < $10M	$10M - $100M	$100M - $250M	$250M - $500M	> $500M
CAMEL 1	3,808	7,259	13,566	16,184	24,752
CAMEL 2	3,927	7,854	14,518	17,969	25,466
CAMEL 3	4,284	8,449	15,827	17,493	25,466
CAMEL 4	5,593	9,996	19,278	NA	NA
CAMEL 5	7,021	14,399	NA	NA	NA

The Task Force Did Not Consider All Alternatives, Such As (1) Separating NCUA And The NCUSIF, (2) Reducing NCUA's Exam Program Or Increasing Reliance On SSA Work, Or (3) Reducing The NCUA Dollar Budget.

These issues are outside the scope of the work performed by the Task Force. Separation of the NCUSIF from NCUA is something that would need to be determined by Congress. NCUA Management has developed, and the NCUA Board approved, carefully crafted programs regarding NCUA's exam program and due diligence related to SSA work. Further, the NCUA dollar budget is set in as efficient a manner as possible based on these approved programs. Though these programs have an impact on the data inputs to the OTR formula, the OTR formula itself is independent of the structure of these programs.

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APPENDIX 8
CAMEL AND ASSET BREAKDOWN COMPARISON BETWEEN FCUS AND FISCUS

Relevance of CAMEL and Asset Breakdown

The proposed new OTR method uses an imputed value for state supervisory authority (SSA) work. This calculation, in part, is affected by the CAMEL and asset distribution of FISCUs. The TF believes it appropriate to factor in both CAMEL and asset size when determining the value SSAs provide NCUA. We observed the CAMEL/asset distribution for the respective populations (FCUs and FISCUs) were similar, as follows:

CAMEL	<$10M FCU / FISCU (%)	$10 – 100M FCU / FISCU (%)	$100 - 250M FCU / FISCU (%)	$250-500M FCU / FISCU (%)	>$500M FCU / FISCU (%)
1	13% / 15%	26% / 23%	49% / 42%	71% / 63%	81% / 65%
2	57% / 57%	60% / 58%	48% / 49%	28% / 34%	19% / 31%
3	27% / 25%	12% / 17%	3% / 8%	1% / 3%	0% / 4%
4	3% / 3%	1% / 2%	0% / 1%	0% / 0%	0% / 1%
5	0% / 0%	0% / 0%	0% / 0%	0% / 0%	0% / 0%

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APPENDIX 9
2002 NCUA INSURANCE REVIEW TIME DETAIL

In 2002, NCUA completed on-site examination or supervision contacts in 22 percent of all FISCUs. These contacts accounted for 41 percent of total FISCU assets. Since 1999, the percentage of FISCU assets with on-site contacts has grown from 20 to 41 percent, due in part to conversions of some larger credit unions. During the same timeframe, the number of FISCUs with on-site contacts grew from 12 to 22 percent, hovering around the 20 percent mark for the past 3 years. However, as a portion of the total NCUA Workload budget, FISCU review time remains below 12%. The following chart breaks down the on-site contact time by state:

	On-site Contacts			Total FISCUs		On-site Stats	
State	# FISCUs with On-site Contacts	FISCU On-site Contact Hours	Assets with On-site Contacts	All FISCUs	Total assets	% Assets On-site/Total Assets	% On-site versus total # FISCUs
AK	2	369	429,860,626	2	429,860,626	100%	100%
AL	34	1,679	1,351,811,554	75	3,392,970,633	40%	45%
AR	0	-	-	-	-	n/a	n/a
AZ	11	1,514	2,152,532,100	29	3,457,764,017	62%	38%
CA	39	5,025	19,318,521,564	201	45,110,842,427	43%	19%
CO	11	557	308,043,478	74	6,005,838,573	5%	15%
CT	11	535	1,229,945,253	50	2,451,106,149	50%	22%
FL	45	3,949	7,280,966,777	108	13,713,194,478	53%	42%
GA	13	602	2,226,324,956	75	6,429,980,233	35%	17%
HI	1	60	83,511,393	3	165,066,797	51%	33%
IA	20	954	399,479,267	176	4,463,840,279	9%	11%
ID	3	205	158,424,159	25	929,455,111	17%	12%
IL	79	3,722	10,952,529,004	375	15,144,615,295	72%	21%
IN	6	163	1,508,972,594	33	3,887,676,099	39%	18%
KS	17	1,272	582,019,256	100	2,385,296,776	24%	17%
KY	15	453	893,578,755	37	1,157,171,468	77%	41%
LA	16	766	224,146,215	57	826,881,294	27%	28%
MA	42	4,114	3,043,626,547	111	10,015,596,151	30%	38%
MD	3	232	571,473,807	6	2,559,809,609	22%	50%
ME	9	455	549,116,929	15	861,493,561	64%	60%
MI	45	3,870	3,261,157,700	277	16,439,966,006	20%	16%
MN	24	737	1,012,086,348	107	3,285,641,875	31%	22%

State	On-site Contacts			Total FISCUs		On-site Stats	
	# FISCUs with On-site Contacts	FISCU On-site Contact Hours	Assets with On-site Contacts	All FISCUs	Total assets	% Assets On-site/Total Assets	% On-site versus total # FISCUs
MO	25	1,410	2,269,961,778	164	6,737,320,674	34%	15%
MS	9	304	294,773,626	32	419,848,172	70%	28%
MT	9	1,006	739,222,594	14	816,307,104	91%	64%
NC	12	965	10,037,078,943	103	11,908,617,490	84%	12%
ND	6	354	345,486,422	39	1,048,296,266	33%	15%
NE	6	375	49,255,954	28	574,483,926	9%	21%
NH	11	733	1,234,768,649	24	2,641,351,813	47%	46%
NJ	6	142	161,027,069	21	375,253,429	43%	29%
NM	12	714	499,213,956	26	950,005,821	53%	46%
NV	2	439	840,506,342	4	1,096,530,641	77%	50%
NY	16	1,033	1,570,446,132	37	3,242,052,009	48%	43%
OH	38	2,145	1,148,769,277	161	6,263,055,621	18%	24%
OK	5	199	139,827,752	28	2,496,458,412	6%	18%
OR	7	436	537,886,670	25	6,175,000,681	9%	28%
PA	35	3,278	4,701,847,086	81	5,457,595,237	86%	43%
RI	7	640	1,506,852,530	14	2,783,883,077	54%	50%
SC	4	288	348,587,560	19	644,844,062	54%	21%
TN	26	1,100	2,449,041,167	135	5,053,590,907	48%	19%
TX	47	3,100	3,279,082,498	248	16,773,094,079	20%	19%
UT	16	1,760	3,882,510,597	85	6,279,835,923	62%	19%
VA	8	603	21,285,133	70	3,496,469,354	1%	11%
VT	8	351	380,517,122	32	715,336,970	53%	25%
WA	20	1,548	6,071,358,598	93	15,109,867,985	40%	22%
WI	44	1,543	4,187,842,752	308	11,665,602,066	36%	14%
WV	3	42	12,098,052	9	91,874,595	13%	33%
All FISCUs	828	55,741	104,247,376,541	3,736	255,930,643,771	41%	22%

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APPENDIX 10
DETAIL OF NCUA'S 2003 BUDGET

BUDGET BY OFFICE

Divisions of Insurance

	Pay	Benefits	DOI
Region I	680,481.29	148,328.10	828,809.39
Region II	963,142.79	232,269.75	1,195,412.54
Region III	797,964.33	231,164.47	1,029,128.80
Region IV	934,759.36	244,395.80	1,179,155.16
Region V	834,392.96	240,165.81	1,074,558.77
Region VI	459,627.63	127,734.19	587,361.82
Total	4,670,368.36	1,224,058.12	**5,894,426.48**

Regional Offices

	Offices	DOI	Offices (Net)
Region I	3,441,453.16	828,809.39	2,612,643.77
Region II	4,923,424.71	1,195,412.54	3,728,012.17
Region III	3,913,574.23	1,029,128.80	2,884,445.43
Region IV	4,676,638.60	1,179,155.16	3,497,483.44
Region V	5,316,868.04	1,074,558.77	4,242,309.27
Region VI	3,630,708.84	587,361.82	3,043,347.02
Total	25,902,667.58	5,894,426.48	**20,008,241.10**

Regional Field & Total

	Field	Total
Region I	10,413,246.93	13,854,700.09
Region II	11,448,668.32	16,372,093.03
Region III	11,110,957.79	15,024,532.02
Region IV	10,153,767.99	14,830,406.59
Region V	9,466,055.83	14,782,923.87
Region VI	11,784,847.24	15,415,556.08
Total	**64,377,544.10**	**90,280,211.68**

Other Offices

Asset Management & Assistance Center	2,184,995.25
Office of Credit Union Development	835,904.50
Office of Corporate Credit Unions	6,447,575.33
Office of the Board	1,854,105
Office of the Chief Financial Officer	16,396,648
Office of the Chief Information Officer	9,313,530
Office of Examination & Insurance	3,064,498
Office of the Executive Director	695,979
Equal Opportunity Programs	572,006
Office of General Counsel	4,206,127
Office of Human Resources	6,084,735
Office of Inspector General	1,386,333
Office of Public & Congressional Affairs	947,530
Office of Strategic Program Support & Planning	1,809,534
All Other Central Offices	46,331,024.63

Summary

Divisions of Insurance	5,894,426.48	5.9
Regional Offices	20,008,241.10	20.0
Field	64,377,544.10	64.4
Total Regions	90,280,211.68	90.3
AMAC	2,184,995.25	2.2
OCUD	835,904.50	0.8
OCCU	6,447,575.33	6.4
All Other Central Offices	46,331,024.63	46.3
Total Central Offices	55,799,499.71	55.8
Total NCUA Budget	146,079,711.39	146.1

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APPENDIX 11
CALCULATION AND COMPARISON OF FEDERAL OPERATING FEE

Federal Operating Fee

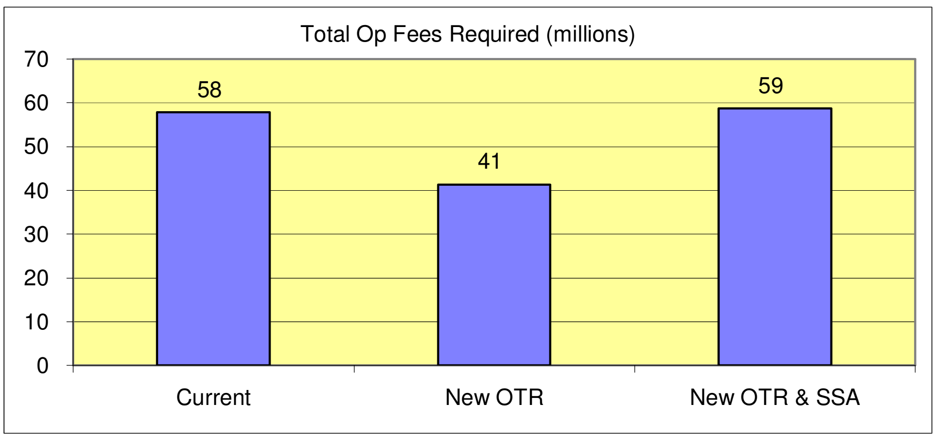
The data shown below compares the current overhead transfer rate (OTR) method with the proposed method, using the 2003 operating fee schedule.

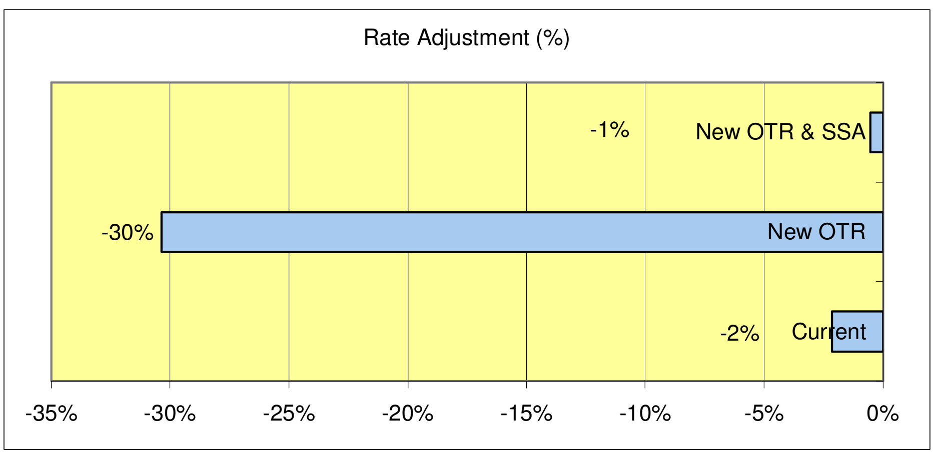
PROJECTED 2003 OPERATING FEE REQUIREMENTS

Comparison of Proposed Versus Current OTR Method

(amounts in millions)

	Current OTR & No SSA Value	Proposed OTR & No SSA Value	Proposed OTR with SSA Value
Overhead Transfer Rate	62.00%	73.45%	61.35%
Corporate Op Fees	0.91	0.91	0.91
Natural Person Op Fees	56.84	40.44	57.77
Total Op Fees Required	57.75	41.35	58.68
Rate Adjustment ($)	(1.24)	(17.64)	(0.31)
Rate Adjustment (%)	-2.13%	-30.36%	-0.54%





State Operating Fees Based on Call Report Data

The information below is taken from the December 31, 2002, Call Reports for FISCUs. The totals per state or territory in aggregate are derived from Account 320, "Total Operating Fees," on the Call Report.

STATE	Operating Fees ($)
AK	49,085
AL	639,462
AZ	384,903
CA	4,265,422
CO	951,805
CT	175,719
FL	2,741,708
GA	816,724
HI	16,997
IA	1,179,877
ID	212,852
IL	3,088,601
IN	403,878
KS	903,815
KY	183,644
LA	337,639
MA	1,260,560
MD	216,220
ME	253,406
MI	4,606,691
MN	773,310
MO	1,079,473
MS	286,346
MT	106,660
NC	1,141,017
ND	312,269
NE	165,963
NH	257,131
NJ	34,769

STATE	Operating Fees ($)
NM	296,551
NV	107,602
NY	319,732
OH	1,663,366
OK	483,159
OR	697,490
PA	1,000,528
RI	191,669
SC	74,711
TN	1,646,704
TX	2,653,103
UT	1,090,784
VA	795,166
VT	91,367
WA	2,296,478
WI	2,226,684
WV	22,658
46 States[33]	**42,503,698**

[33] Not all states have federally insured state-chartered credit unions.