

**NATIONAL CREDIT UNION ADMINISTRATION
OFFICE OF INSPECTOR GENERAL**

SEMIANNUAL REPORT
TO
THE CONGRESS

October 1, 2010 – March 31, 2011



TABLE OF CONTENTS

INSPECTOR GENERAL'S MESSAGE	i
THE NCUA AND OFFICE OF INSPECTOR GENERAL MISSIONS.....	1
INTRODUCTION.....	2
NCUA HIGHLIGHTS	5
FEDERALLY INSURED CREDIT UNION HIGHLIGHTS	8
LEGISLATIVE HIGHLIGHTS.....	9
OFFICE OF THE INSPECTOR GENERAL.....	11
AUDIT ACTIVITY	12
INVESTIGATIVE ACTIVITY.....	21
LEGISLATIVE AND REGULATORY REVIEWS	24
TABLE I: INSPECTOR GENERAL ISSUED REPORTS WITH QUESTIONED COSTS	26
TABLE II: INSPECTOR GENERAL ISSUED REPORTS WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE.....	27
TABLE III: SUMMARY OF OIG ACTIVITY OCTOBER 1, 2010 THROUGH MARCH 31, 2011...	28
INDEX OF REPORTING REQUIREMENTS.....	29
APPENDIX A: NCUA SYSTEM REVIEW REPORT (SEC OIG REPORT NO. 478).....	30



INSPECTOR GENERAL'S MESSAGE TO THE NCUA BOARD AND THE CONGRESS

On behalf of the Office of Inspector General (OIG) of the National Credit Union Administration (NCUA), I am pleased to present our *Semiannual Report to Congress* highlighting our accomplishments and ongoing work for the six-month period ending March 31, 2011. Challenges and opportunities stemming from the financial crisis remain our primary focus, from reviewing the supervision and regulation of failed corporate and natural person credit unions, to participating in comprehensive efforts—involving all of the Federal financial regulatory agencies and inspectors general—to ensure the future stability of the nation’s financial system. Since the passage of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*” (Dodd-Frank) last summer, the NCUA has worked diligently to enact reforms to empower consumers and investors, mitigate problems identified during the financial crisis, and improve accountability and transparency in the credit union system. The OIG, through its audit and Material Loss Review (MLR) work, has endeavored simultaneously to ensure that the NCUA understands where mistakes were made in the past and to recommend suitable corrective actions.

Of particular significance, during this reporting period the OIG issued a capping report that summarized significant findings from the first ten Material Loss Review (MLR) reports the OIG issued, as well as recommendations for avoiding similar mistakes and shortcomings in the future. The capping report identified eight areas that led to credit union failures and losses to the National Credit Union Share Insurance Fund (NCUSIF). The OIG made 12 specific recommendations to address these problem areas. Subsequent to the capping report’s issuance, the NCUA provided the OIG with a detailed chronology of corrective actions it has already taken to address each of the recommendations, as well as corrective actions in progress and anticipated, along with targeted completion dates.

Moreover, during this period the OIG completed and reported on MLRs of two failed corporate credit unions: U.S. Central Federal Credit Union (U.S. Central) of Lenexa, Kansas, and Western Corporate Federal Credit Union (WesCorp) of San Dimas, California. Drawing on the mistakes and shortcomings that the MLRs identified, the NCUA concurrently developed a Corporate Resolution System plan consisting of a comprehensive three phase Stabilize, Resolve, and Reform strategy. The Reform phase involved the agency’s implementation of a new regulatory framework for corporate credit unions that will, we believe, go far in addressing the deficiencies we noted during our MLR work on both corporates.

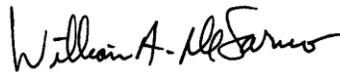
The OIG also conducted a MLR of one natural person credit union during the reporting period, St. Paul Croatian Federal Credit Union (St. Paul) of Eastlake, Ohio, where fraud was the direct cause of the credit union’s failure. In addition to the fraud, however, we found that St. Paul management failed to implement proper controls and oversight, and NCUA examiners failed to adequately address the risks to St. Paul operations. In response to the MLR report, the NCUA stated its commitment to improving its

existing supervision mechanisms and providing necessary staff training to enhance risk monitoring and supervision processes. Moreover, the agency took steps to increase the number of administrative actions on credit unions that were taking excessive risks.

The OIG staff has also expended much effort and time during this reporting period in making presentations and otherwise offering a forum for NCUA examiners, supervisors, state regulatory authorities, credit union industry representatives, and others to learn and engage in constructive dialogue about the MLR process, what lessons can be learned from the information set forth in the MLR reports, and emerging issues that will impact our collective and individual work and responsibilities.

Finally, Dodd-Frank created the Financial Stability Oversight Council (FSOC) to monitor emerging threats to financial stability, designate for supervision those non-bank financial firms and market utilities that could pose threats to financial stability, and identify gaps in the financial regulatory framework. The FSOC includes representatives from the key Federal financial regulatory agencies, including the NCUA. At the same time, Dodd-Frank established the Council of Inspectors General on Financial Oversight (CIGFO), which consists of IGs for the Federal agencies represented on the FSOC, as well as the IG for the Department of Housing and Urban Development and the Special IG for the Troubled Asset Relief Program. Under the leadership of the Treasury IG, the CIGFO meets at least quarterly to share information among the IGs and to discuss the ongoing work of each IG, with a focus on concerns that may apply to the broader financial sector and ways to improve financial oversight. In addition, the CIGFO is required to annually issue a report that highlights the IG's concerns and recommendations, as well as issues that may apply to the broader financial sector. I have participated in those meetings, and my staff and I are actively involved in drafting portions of the annual report.

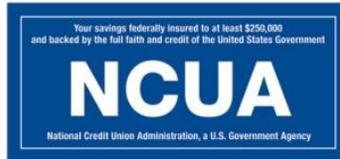
We look forward to working with the NCUA Board and Congress to accomplish the new requirements of Dodd-Frank and to enhance the economy, efficiency, and effectiveness of the NCUA so that it may better achieve its mission.



William A. DeSarno
Inspector General

THE NCUA MISSION

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



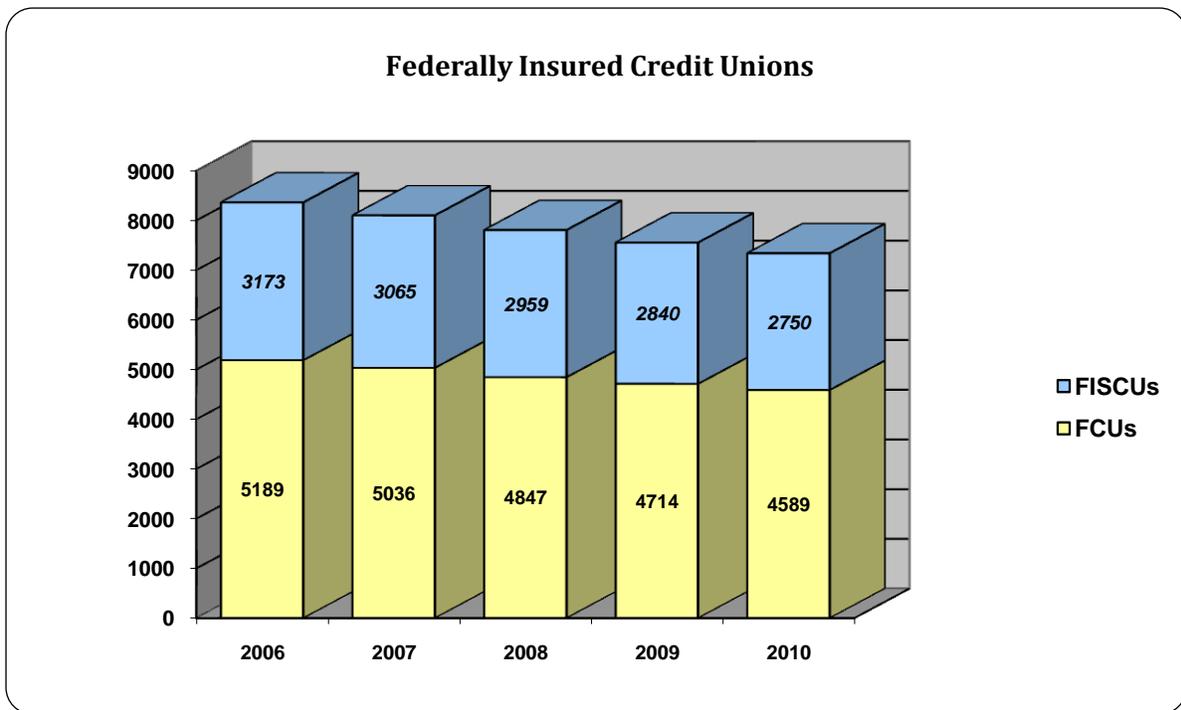
THE OFFICE OF INSPECTOR GENERAL MISSION

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

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

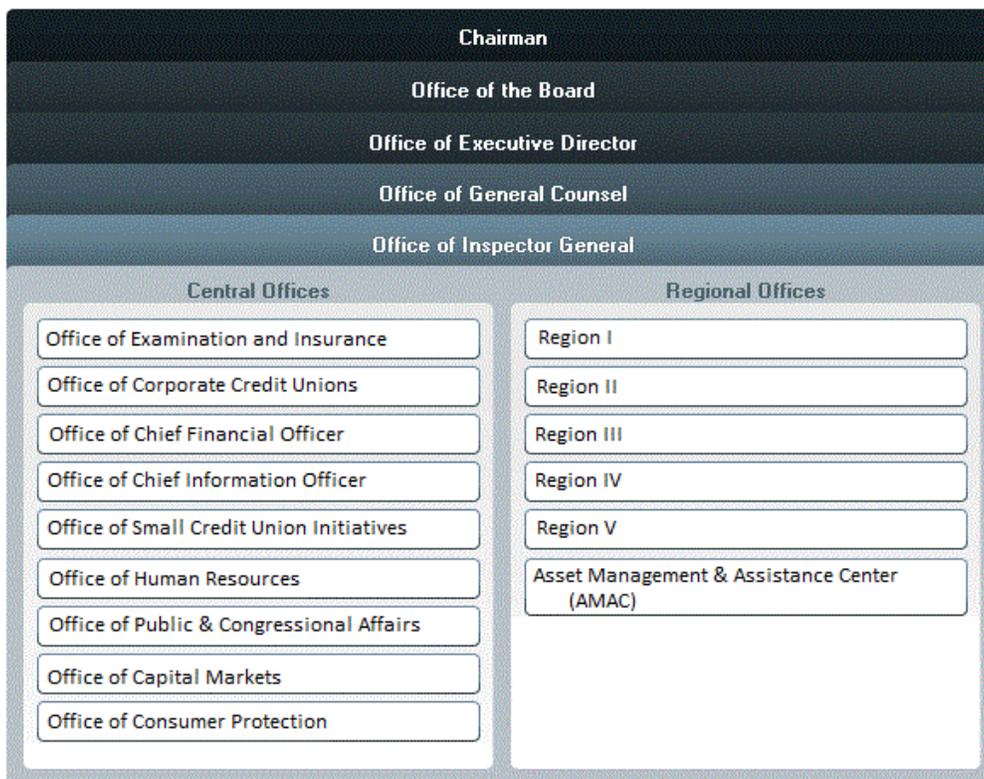
INTRODUCTION

The NCUA was established as an independent, federal regulatory agency on March 10, 1970. The agency is responsible for chartering, examining, supervising, and insuring federal credit unions. It also insures state-chartered credit unions that have applied for insurance and have met National Credit Union Share Insurance requirements. The NCUA is funded by the credit unions it supervises and insures. As of December 31, 2010, the NCUA was supervising and insuring 4,589 federal credit unions and insuring 2,750 state-chartered credit unions, a total of 7339 institutions. This represents a decline of 125 federal and 90 state-chartered institutions since December 31, 2009, for a total decline of 215 credit unions nationwide, primarily as a result of mergers and liquidations.

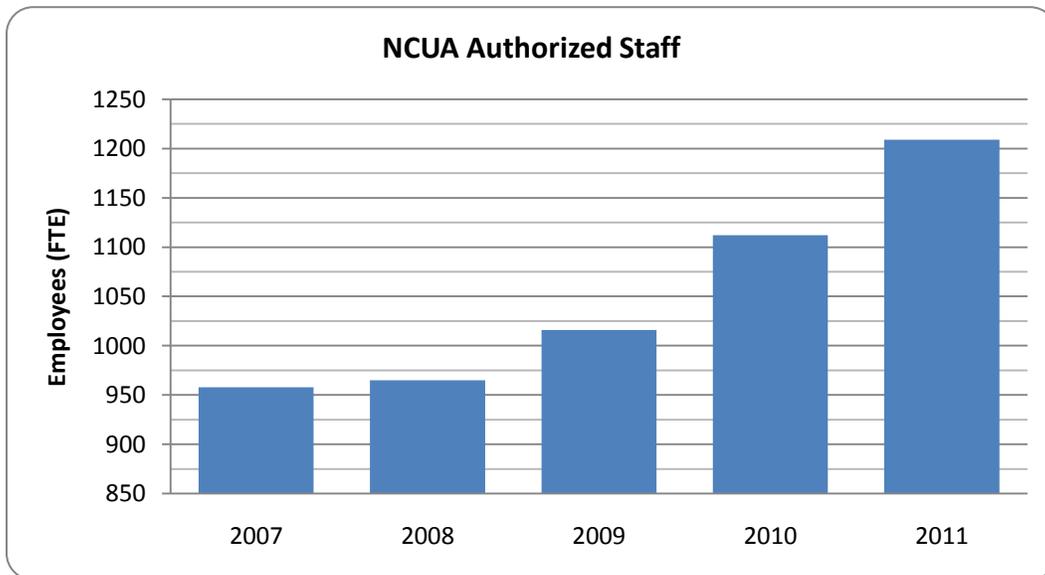
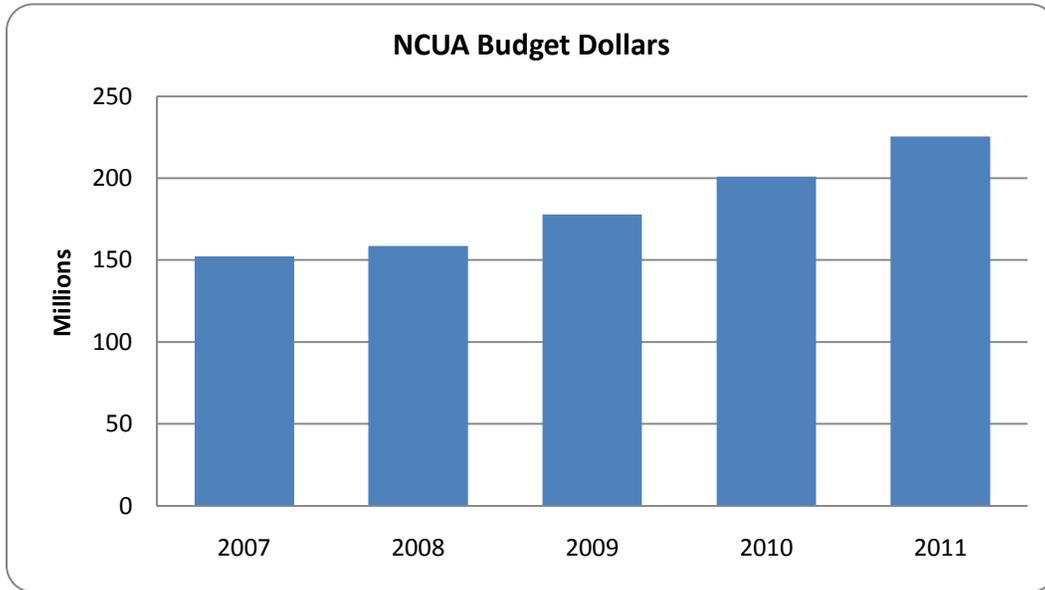


The NCUA operates under the direction of a Board composed of three members. Board members are appointed by the President and confirmed by the Senate. They serve six-year terms. Terms are staggered, so that one term expires every two years. The Board is responsible for the management of the NCUA, including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

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



The NCUA Board adopted its 2011 budget of \$225,403,988 on November 18, 2010. The Full-Time Equivalent (FTE) staffing authorization for 2011 is 1,209 representing an increase of 97 FTEs from 2010.



NCUA HIGHLIGHTS

NCUA Works to Implement Dodd-Frank Initiatives

This year NCUA, along with the other Federal financial regulatory agencies, has begun implementing the *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* (Dodd-Frank). The law aims to empower consumers and investors, mitigate problems identified during the financial crisis, and ensure the future stability of the nation's financial system. Like the other financial regulators, NCUA must issue new rules, revise some existing regulations, and take on additional duties. Recently, NCUA has focused on implementing the following changes:

- **Interchange Fee Caps:** Dodd-Frank requires the Board of Governors of the Federal Reserve (Federal Reserve) to consult with NCUA in crafting new rules governing fee caps on debit card interchange transactions. In order to protect the solvency of smaller credit unions, NCUA recently called for the adoption of a final rule containing meaningful exemptions for issuers with less than \$10 billion in assets.
- **Credit Ratings:** The inflated grades of credit rating agencies exacerbated the financial crisis. Dodd-Frank, therefore, requires all regulators to replace credit rating rule references with new creditworthiness standards that regulated entities must follow. In February, the NCUA Board approved a proposed rule implementing this mandate.
- **Share Insurance Protection:** Dodd-Frank permanently raised the maximum of share insurance protection to \$250,000 per account. NCUA satisfied this requirement with a rule revision last September. NCUA is working on final rules for unlimited coverage for noninterest-bearing accounts.
- **Incentive-Based Compensation:** Incentive-based compensation packages led many financial executives and professionals to favor short-term self gain over long-term financial stability. Dodd-Frank requires credit unions and other regulated entities with more than \$1 billion in assets to disclose the structures of their incentive-based compensation practices. Credit unions with more than \$10 billion in assets have additional obligations. In February 2011, NCUA proposed a new rule to implement these changes.
- **Financial Stability Oversight Council (FSOC):** FSOC works to monitor and ensure the stability of the U.S. financial system. As one of 10 voting members, NCUA has new responsibilities, not only to raise the distinctive perspective of credit unions within FSOC, but also to look more broadly at the threats facing the global financial system.
- **Office of Minority and Women Inclusion (OMWI):** Created in January 2011 in response to Dodd-Frank, OMWI will monitor diversity of employment at NCUA and in credit unions. OMWI will also promote the use of minority and women contractors at NCUA.

- **Consumer Financial Protection Bureau (CFPB):** Because too many American families suffered devastating losses in the last decade as a result of predatory financial products, Congress created CFPB. CFPB is charged with writing new consumer rules and supervising consumer compliance at financial institutions with more than \$10 billion in assets. NCUA has begun working with CFPB to transfer employees, share data, and plan for coordinated exams. By providing comments during the rulemaking process, credit unions are assisting NCUA in crafting rules that will result in many changes in the way credit unions operate.

Chairman Matz Renews Call for Supplemental Capital

In a January 14, 2011, letter to the Chairmen and Ranking Members of the House Financial Services and Senate Banking Committees, NCUA Chairman Debbie Matz called for changes to the net worth provisions of the Federal Credit Union Act that would enable financially strong credit unions to continue offering a full range of financial service products to consumers without inadvertently reducing net-worth and triggering Prompt Corrective Action (PCA). Chairman Matz pointed out that some financially healthy, well-capitalized credit unions that offer desirable products and services are discouraged from marketing them out of concern that attracting share deposits from new and existing members will inflate the credit union's asset base, thus diluting its net worth for purposes of PCA. Chairman Matz specifically proposed two reforms that would enable NCUA to reverse the disincentive for credit unions to accept deposits from their members:

- Allow qualifying credit unions to exclude assets that carry zero risk, such as short-term U.S. Treasury securities, from the definition of total assets. NCUA would set a minimum net worth requirement, and would also determine that share growth is the cause of declining net-worth, not poor management or unsafe practices, before a credit union would be allowed to exercise this exclusion; and
- Authorize qualifying credit unions to issue supplemental capital. The form of supplemental capital would be subject to strict regulatory prescriptions that address safety and soundness criteria, protect investors, and preserve the cooperative credit union governance model.

Chairman Matz indicated that Congress already permits low-income designated credit unions to offer uninsured supplemental capital accounts to non-members. Modifying the Federal Credit Union Act, to permit qualifying credit unions to offer uninsured alternative capital instruments subject to regulatory restrictions, and expanding the Act's definition of "net worth" to include those instruments would, Matz explained, allow well-managed credit unions to better manage net worth levels under varying economic conditions.

Chairman Matz's letter went on to state that one of the principal purposes of PCA was to control accelerated, unmanageable growth of credit union assets, and that NCUA's implementing regulations respected that goal. Moreover, she explained, it was "[f]or that reason that in the course of implementing PCA over the last 9 years, NCUA did not propose statutory remedies in response to occasional periods of reluctance by credit unions to grow assets. That reluctance in the present period of national economic distress has become acute, however, warranting a statutory remedy." Chairman Matz emphasized that it was never the objective of PCA to discourage manageable asset growth by financially healthy credit unions in times of economic distress. "To the extent PCA does so now," Matz asserted, "it does not contribute to the objective of resolving the problems of insured credit unions; it unintentionally creates a problem for them, which redounds to the detriment of consumers."

NCUA Sets Strategic Goals for 2011

At its January 13, 2011, board meeting, the NCUA Board approved the NCUA Annual Performance Budget (APB), which serves as the agency's annual plan. The plan outlines NCUA objectives, strategies, and initiatives for 2011. It also provides guidance and serves as a tool to illustrate how staff contributes to meeting agency goals and objectives. High priority goals include monitoring risks in federally insured credit unions and continuing to stabilize the corporate credit union system. A cross-agency working group developed the initial draft APB using input from all NCUA offices and regions. Regional and central office leadership provided concurrence. Some significant enhancements to NCUA's APB include: (1) a description of agency programs and offices that contribute to goals; (2) a clearer connection between annual objectives and strategic goals; and (3) the addition of annual measures for each objective in addition to strategic measures. Overall, the plan aims to serve as an improved management tool and offer the public and staff increased transparency.

Board Member Hyland Outlines Corporate Credit Union Resolution to AICPA

At the American Institute of Certified Public Accountants' (AICPA) annual "Conference on Credit Unions," held on October 25, 2010, NCUA Board Member Gigi Hyland told the AICPA that NCUA is working to assist the credit union industry in weathering its "most significant financial and structural challenge" presented by a "perfect storm of over-concentration in private-label, mortgage-backed securities held by several large corporate credit unions." Board Member Hyland characterized the steps the agency took in its resolution plan as a "comprehensive solution to the problems afflicting corporates." According to Hyland, the plan puts consumers first and ensures that there will be no loss to taxpayers. Hyland emphasized that the plan was not a bailout, stating that it was being paid for entirely by credit unions. Specifically, Hyland explained that credit unions would pay the bill, the NCUA had taken over the failed corporates, and the NCUA was in the process of phasing them out. Pointing to the future of the corporate credit union system, Board Member Hyland noted that "while credit unions do not have to make decisions immediately, they need to be engaged to begin thinking about the future and working on a transition strategy."

Board Member Fryzel Emphasizes Three Key Stages of Corporate Resolution Plan

In an address to the New Jersey Credit Union League on October 4, 2010, NCUA Board Member Michael Fryzel emphasized the three key stages of the NCUA's Corporate Resolution Plan. Board Member Fryzel explained to the annual gathering of over 860 credit union volunteers and professionals that with the Corporate Resolution Plan's three-stage process—stabilization, resolution, and reform—the NCUA envisioned the way toward a future of stronger corporate credit unions. Fryzel highlighted the NCUA's aim to fulfill four specific principles that the agency set forth at the beginning of the corporate crisis: (1) prevent any interruption in services to consumer credit unions; (2) preserve public confidence in the credit union system; (3) manage the situation to achieve the lowest long-term cost; and (4) make an orderly transition to a new regulatory regime, based on the principle that consumer credit unions should determine the new contours of the realigned corporate system. Board Member Fryzel concluded by stating his confidence that "the new resolution plan will strengthen the system's safeguards validating depositors' confidence in a well-regulated system that puts the interests of consumers first."

FEDERALLY INSURED CREDIT UNION HIGHLIGHTS

Credit unions submit quarterly call reports (financial and operational data) to the NCUA. An NCUA staff assessment of the December 31, 2010, quarterly call reports submitted by all federally insured credit unions found that key financial indicators show improvement.

Key Financial Indicators Showing Improvement

Looking at the December 31, 2010 quarterly statistics for major balance sheet items and key ratios shows the following for the nation's 7,339 federally insured credit unions: assets grew 3.4 percent; net worth to assets ratio increased from 9.89 to 10.06 percent; the loan to share ratio decreased from 76.06 percent to 71.82 percent. However, the delinquency ratio decreased from 1.84 to 1.74 percent; and credit union return on average assets increased from .18 percent to .51 percent.

Savings Shifting to Money Market Accounts

Total share accounts increased 4.49 percent. Money market shares increased 11.0 percent. Regular shares comprise 28.03 percent of total share accounts; share certificates comprise 27.14 percent; money market shares comprise 22.34 percent; share draft accounts comprise 11.45 percent; and all other share accounts comprise 11.04 percent.

Loans Decreased Slightly

Loan decline of 1.34 percent resulted in a decrease in total loans by \$7.68 billion. Total net loans of \$555 billion comprise 61 percent of credit union assets. First mortgage real estate loans are the largest single asset category with \$223.05 billion accounting for 39.49 percent of all loans. Other real estate loans of \$86.57 billion account for 15.33 percent of all loans. Used car loans of \$101.52 billion were 17.97 percent of all loans, while new car loans amounted to \$62.89 billion or 11.13 percent of total loans. Credit card loans totaled \$35.96 billion or 6.37 percent of total loans and other loans totaled \$54.84 billion for 9.71 percent of total loans.

LEGISLATIVE HIGHLIGHTS

NCUA Joins Federal Financial Regulatory Agencies in Seeking Comments on Proposed Rule on Incentive Compensation

On March 30, 2011, NCUA joined six other Federal financial regulatory agencies (Board of Governors of the Federal Reserve System; Federal Deposit Insurance Company; Federal Housing Finance Agency; Office of the Comptroller of the Currency; Office of Thrift Supervision; and the Securities and Exchange Commission) in requesting comment on a joint proposed rule to ensure that regulated financial institutions design their incentive compensation arrangements to take account of risk. The proposed rule, which is being issued pursuant to the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank), would apply to certain financial institutions with more than \$1 billion in assets. It also contains heightened standards for the largest of these institutions. In prohibiting incentive compensation arrangements that could encourage inappropriate risks, the proposal would require compensation practices at regulated financial institutions to be consistent with three key principles—that incentive compensation arrangements should appropriately balance risk and financial rewards, be compatible with effective controls and risk management, and be supported by strong corporate governance. The proposed rule complements guidance previously issued by the agencies, including guidance on sound incentive compensation policies issued by the banking agencies last year.

The agencies are proposing that financial institutions with \$1 billion or more in assets be required to have policies and procedures to ensure compliance with the requirements of the rule, and submit an annual report to their federal regulator describing the structure of the incentive compensation arrangements. The agencies are proposing that larger financial institutions defer at least 50 percent of the incentive compensation of certain officers for at least three years and that the amounts ultimately paid reflect losses or other aspects of performance over time. For credit unions, large financial institutions would be defined as those with \$10 billion or more in assets. In February 2011, NCUA proposed a new rule to implement these changes.

Senator Udall Introduces S. 509, Allowing MBL Cap Increase

On March 8, 2011, Sen. Mark Udall (D-Colo.) introduced S. 509, the *Small Business Lending Enhancement Act*. The Act would allow a gradual increase in eligible credit unions' Member Business Lending (MBL) cap from 12.25 percent of assets to 27.5 percent, in accordance with strict safety and soundness measures. It awaits the action of the Senate Banking Committee. The bill mirrors provisions proposed in 2010, which Congress failed to act on. In order for state and federally chartered credit unions to qualify for the 27.5 percent cap, they would have to, among other provisions:

- Be capitalized with at least a 7 percent net worth ratio;
- Have outstanding MBLs of at least 80 percent of the current cap for a year;
- Boast five or more years experience in MBLs and demonstrate sound loan underwriting and servicing; and
- Expand their MBL portfolios by no more than 30 percent in any given year.

NCUA Chairman Matz, in a letter dated February 24, 2011, to Treasury Secretary Timothy Geithner, assured him that if a statutory increase in the MBL cap should become law, NCUA is prepared to

enhance the regulation of business lending. Specifically, Chairman Matz advised Secretary Geithner that “[i]f legislative changes increase or eliminate the current aggregate MBL cap, NCUA would promptly revise [its] regulation to ensure that additional capacity in the credit union system would not result in unintended safety and soundness concerns.” The letter also outlined ongoing NCUA efforts to monitor MBL activities, and cited January 2011 guidance to credit unions that reiterated the importance of stringent risk management practices and appropriate staff expertise.

NCUA Issues Proposed Rule in Response to “Toolbox” Legislation

On January 4, 2011, President Obama signed into law (P.L. 111-382), the NCUA-recommended “toolbox” legislation. When implemented, the new law will provide the NCUA with new tools to address both troubled individual credit unions and the larger corporate credit union crisis. The legislation, which alters the Federal Credit Union Act by permitting the NCUA to make payments to the Temporary Corporate Credit Union Stabilization Fund (TCCUSF) without borrowing from the U.S. Treasury, was approved on the final day of the 111th Congress. The legislation also clarifies that the equity ratio of the National Credit Union Share Insurance Fund (NCUSIF) is based solely on unconsolidated financial statements of the NCUSIF and grant credit unions the ability to count Section 208 assistance as net worth for the purposes of Prompt Corrective Action (PCA).

To implement the new law, the NCUA, at its March 17, 2011 Board meeting, issued a proposed rule to amend the definition of “net worth” in the agency’s rule on Prompt Corrective Action (PCA). The proposed rule would allow for the inclusion of NCUA-provided Section 208 assistance that contains minimum elements of equity in a credit union’s net worth for PCA purposes. This change will facilitate NCUA’s ability to conduct assisted mergers of credit unions. The proposed rule also makes an additional technical change to the definition of net worth outside of the scope of the new law. This proposed fix would eliminate the double counting of net worth in a combination resulting in a bargain purchase gain. Finally, the proposal would revise the definition of “equity ratio” as it appears in NCUA’s regulation on insurance requirements. Under the proposed rule, NCUA would calculate the NCUSIF’s equity ratio using the financial statements of the NCUSIF alone, without consolidation or combination with the financial statements of any other fund or entity.

Chairman Matz Calls for Exemptions in Fed Interchange Rulemaking

In a February 16, 2011, letter to Federal Reserve Chairman Ben Bernanke, NCUA Chairman Matz called upon the Federal Reserve to craft a debit card interchange rule that reflects Dodd-Frank Act language addressing small institution pricing issues. Dodd-Frank requires the Federal Reserve to consult with NCUA and other financial institution regulators in formulating new rules governing debit card interchange transactions. Chairman Matz called for the regulation implementing the statutory interchange provision to contain “meaningful exemptions for smaller card issuers.” Chairman Matz added, “The [Dodd-Frank] Act explicitly exempts card issuers with total assets under \$10 billion from any interchange fee regulation. In addition to exempting small issuers from the fee limits, I believe it is important that small issuers be exempted from requirements related to network exclusivity and routing restrictions. Such action would be consistent with the exemption from the interchange transaction fee rulemaking, which is intended to shield smaller institutions from the costs of the Act.” Chairman Matz also noted that “[s]eventeen percent or nearly 1,000 federally insured credit unions offering ATM/Debit card services possess total assets of less than \$10 million, and more than 3,000 (59%) possess total assets less than \$50 million. The current rule’s prohibitions against network exclusivity and merchant routing restrictions could significantly increase both fixed and variable costs for these small institutions, resulting in an inability to remain competitive with larger card issuers.” The new rule will take effect in July 2011.

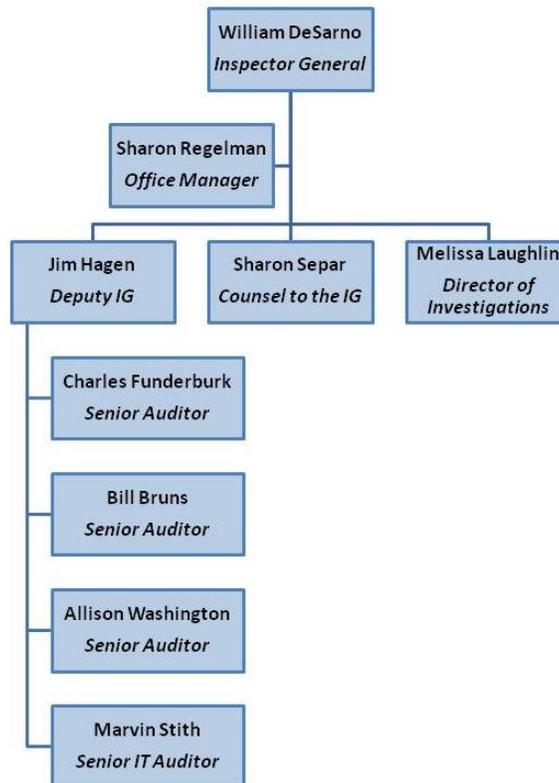
OFFICE OF THE INSPECTOR GENERAL

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

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

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

NCUA OIG ORGANIZATIONAL CHART



AUDIT ACTIVITY

Audit Reports Issued

OIG-10-16 – October 7, 2010

Material Loss Review of St. Paul Croatian Federal Credit Union

The National Credit Union Administration (NCUA) Office of Inspector General (OIG) conducted a Material Loss Review (MLR) of St. Paul Croatian Federal Credit Union (St. Paul).

We determined a suspected fraud was the direct cause of St. Paul's failure. As of December 31, 2009, the credit union had approximately \$238.8 million in total assets. St. Paul had a substantial majority of its assets in loans that were supposedly secured by members' shares. During the December 31, 2009, examination, NCUA found the majority of the loans were not actually share secured and a number of them were allegedly fraudulent. NCUA also found that St. Paul's chief executive officer (CEO) allegedly manipulated loan records and masked the suspected loan fraud by constantly refinancing certain loans or making advance payment on those loans. NCUA projected an estimated loss of \$170 million to NCUSIF.

We also determined that credit union management failed to meet their required obligations to implement proper internal controls and oversight. Specifically, management did not (1) ensure adequate internal controls were in place; (2) ensure adequate policies were in place and adhered to; and (3) resolve prior examiner findings in a timely fashion.

We further determined NCUA examiners did not adequately evaluate the risks to St. Paul operations. Specifically, examiners did not (1) thoroughly evaluate the credit union's internal controls when assessing transaction risk; (2) ensure credit union management took corrective action on repetitive Document of Resolution issues; and (3) expand examination procedures when red flags indicated higher risks to the credit union.

This report does not contain recommendations, but provides observations and suggestions. However, the OIG issued a Material Loss Review Capping Report with recommendations based on issues raised in this report as well as the other nine Material Loss Reviews conducted by the OIG.

OIG-10-17 – October 18, 2010

Material Loss Review of U.S. Central Federal Credit Union

The National Credit Union Administration (NCUA) Office of Inspector General (OIG) contracted with Crowe Horwath LLP (Crowe) to conduct a Material Loss Review (MLR) of U.S. Central Corporate Credit Union (U.S. Central), a federally chartered credit union.

Our review determined U.S. Central's management and Board of Directors (Board) contributed to the conservatorship of U.S. Central and resulting material loss to the NCUA's Temporary Corporate Credit Union Stabilization Fund (TCCUSF). Specifically, management and the Board's inadequate oversight resulted in U.S. Central purchasing significant holdings of private label subprime and ALT-A mortgage-backed securities that exposed the credit union to excessive amounts of financial risk.

U.S. Central's management and Board failed to identify and manage this risk exposure prior to the mortgage-backed securities market dislocation that occurred in mid-2007.

U.S. Central's aggressive growth strategy placed increased pressure on the credit union to produce higher levels of revenue in order to increase or maintain sufficient capital. In an effort to maintain or increase net income and continue to grow its retained earnings, U.S. Central management increased its offerings of higher yielding investments for its members to invest in, such as mortgage-backed securities. U.S. Central, in turn, significantly expanded its investments in higher yielding, higher risk subprime mortgage-backed securities, to support this growth strategy. We believe this growth strategy and accompanying investment decisions to purchase higher yielding securities to such extraordinary levels was contradictory to U.S. Central's fundamental purpose as a wholesale corporate credit union, which was serving as a secure investment option and a source of liquidity for retail corporate credit unions, and support for the not for profit credit union structure.

We determined U.S. Central's management and Board failed to recognize the substantial risk they undertook with significant investments in complex mortgage-backed securities collateralized by subprime assets. We also determined management allowed the investments in mortgage-backed products to represent a significant concentration compared to net worth and failed to impose prudent limits in these securities.

We believe stronger and timelier supervisory action regarding U.S. Central's concentration in mortgage-backed securities could have resulted in a reduced loss to the NCUSIF. Although NCUA does not provide specific guidance regarding sector concentration limits, we believe NCUA staff should have recognized the risk exposure that U.S. Central's significant concentration in mortgage-backed securities represented earlier than 2007 and 2008.

OIG-10-18 – November 15, 2010

Independent Evaluation of NCUA's Compliance with the FISMA 2010

The Office of Inspector General (OIG) for the National Credit Union Administration (NCUA) engaged Richard S. Carson and Associates, Inc (Carson Associates), to independently evaluate its information systems and security program and controls for compliance with the Federal Information Security Management Act (FISMA), Title III of the E-Government Act of 2002.

Carson Associates evaluated NCUA's security program through interviews, documentation reviews, technical configuration reviews, and sample testing. We evaluated NCUA against standards and requirements for federal government agencies such as those provided through FISMA, the Government Accountability Office's *Federal Information System Controls Audit Manual (FISCAM)*, National Institute of Standards and Technology (NIST) Special Publications (SPs), and Office of Management and Budget (OMB) memoranda.

The NCUA has worked to further strengthen its information technology (IT) security program during Fiscal Year (FY) 2010. NCUA's accomplishments during this period include:

- Enhanced change control management system, adding security impact analysis for its IT systems.
- Use of an SCAP-validated scanner to verify its workstation configurations.
- Enhanced policies and procedures.
- Completed e-Authentication risk assessments for its two e-Authentication systems.
- Completed security control assessments for five of its six FISMA systems.
- Signed Authorizations To Operate for all six Certification and Accreditation packages.

- Improved Plan of Action and Milestones process.
- Updated Privacy Policy on NCUA.gov to describe use of third-party Web sites and applications.

We identified five areas remaining from last year's FISMA evaluation that NCUA officials need to address:

- Improve its security configuration program.
- Improve its contingency planning program for its FISMA systems.
- Enhance its procedures for ensuring terminated users and inactive user accounts are removed from its systems.
- Update the Service Level Agreement for its Intrusion Detection System.
- Implement continuing education requirements for its information technology employees.

In addition, we identified six new findings this year where NCUA could improve IT security controls. Specifically, NCUA needs to:

- Perform a security control assessment for its General Support System.
- Complete an overall Business Impact Assessment of its FISMA systems.
- Improve its oversight of external service providers.
- Improve its remote access controls.
- Improve its Plan of Action and Milestone process.
- Review its use of Personally Identifiable Information and Social Security Numbers.

OIG-10-19 – November 16, 2010

Material Loss Review of Western Corporate (WesCorp) Federal Credit Union

The National Credit Union Administration (NCUA) Office of Inspector General (OIG) conducted a Material Loss Review of Western Corporate Federal Credit Union (WesCorp).

We determined WesCorp's management and Board of Directors (management) did not implement appropriate risk management practices to adequately limit or control significant risks in its investment strategy. Specifically, although management invested in high investment grade securities (AAA and AA), management implemented an aggressive investment strategy with unreasonable limits in place that allowed for excessive investments in privately issued residential mortgage backed securities (RMBS). Management's actions allowed a substantial investment portfolio of privately issued RMBS, resulting in a significant concentration risk, and left WesCorp increasingly vulnerable to significant credit risk, market risk, and liquidity risk through the portfolio's exposure to economic conditions in the residential real estate sector. WesCorp management's actions contributed directly to conditions that resulted in NCUA placing the corporate under federal conservatorship on March 20, 2009 and an expected loss to the Temporary Corporate Credit Union Stabilization Fund (Stabilization Fund) of \$5.59 billion.

In addition, we determined Office of Corporate Credit Unions' examiners (OCCU examiners) did not adequately and aggressively address WesCorp's increasing concentration of privately-issued RMBS and the increasing exposure of WesCorp's balance sheet to credit, market, and liquidity risks. Specifically, we determined OCCU examiners did not critique or respond in a timely manner to WesCorp's growing concentrations of privately-issued RMBS in general and in particular RMBS: (1) backed by higher risk mortgage collateral; (2) concentrated in California; and (3) issued,

originated, and serviced by Countrywide. This occurred because NCUA did not have appropriate regulatory support in place--in the form of more specific investment concentration limits--to address the growing and risky concentration. As a result, OCCU examiners did not have the regulatory leverage to limit or stop the growth of WesCorp's purchase of privately issued RMBS, which would have likely mitigated WesCorp's severely distressed financial condition and expected loss as a result of the extended credit market dislocation, and thus averted NCUA's ultimate conservatorship of WesCorp.

OIG-10-20 –November 23, 2010

OIG Capping Report on Material Loss Reviews

The purpose of this report is to summarize significant findings from the first ten material loss reviews (MLRs) issued by the NCUA Office of Inspector General. The Federal Credit Union Act requires the OIG to conduct a MLR of an insured credit union if the loss to the National Credit Union Share Insurance Fund exceeds \$25 million and an amount equal to 10 percent of the total assets of the credit union at the time at which the NCUA Board initiated assistance or was appointed liquidating agent. We issued ten MLR reports during the period from November 2008 through November 2010. Based on similarities and trends found in the first ten MLRs completed by the OIG, we made 12 recommendations to NCUA management for corrective action. Management agreed with all recommendations and has either taken or is planning to take corrective action to address all recommendations.

AUDITS IN PROGRESS

NCUA Financial Statements 2010

Our current contracting audit firm, KPMG, is working on the 2010 financial statements of the NCUA Operating Fund, National Credit Union Share Insurance Fund, the Central Liquidity Facility, the Community Development Revolving Loan Fund and the Temporary Corporate Credit Union Stabilization Fund (TCCUSF).

The NCUA Operating Fund was established as a revolving fund managed by the NCUA Board for the purpose of providing administration and service to the federal credit union system. The National Credit Union Share Insurance Fund was established as a revolving fund managed by the NCUA Board to insure member share deposits in all Federal credit unions and qualifying state credit unions. The CLF was established as a mixed ownership government corporation managed by the NCUA Board to improve general financial stability by meeting the liquidity needs of credit unions. The Community Development Revolving Loan Fund's purpose is to stimulate economic activities in the communities served by low-income credit unions. This in turn will result in increased income, ownership and employment opportunities for low-wealth residents and other economic growth. The TCCUSF, established in 2009, allows NCUA to borrow money from the Treasury to pay for corporate credit union losses, and then pay back the Treasury over time with funds obtained from assessments on federally insured credit unions. We expect to issue our report in April 2011.

Material Loss Reviews of Constitution, Members United and Southwest Corporate Federal Credit Unions

The FCU Act requires the NCUA Office of Inspector General (OIG) to conduct a material loss review (MLR) of an insured credit union if the loss exceeds \$25 million and an amount equal to 10 percent of the total assets of the credit union at the time at which the Board initiated assistance or was appointed liquidating agent. In addition, the OIG may perform a material loss review on selected cases that caused a loss of less than \$25,000,000 at the discretion of the Inspector General. (See next section of this semiannual report titled "Report on Credit Union Losses Not Reaching Materiality Level of \$25 Million.")

The OIG was notified by NCUA that the losses incurred by these credit unions had exceeded the statutory requirements, triggering a material loss review by the OIG. NCUA determined that the Constitution, Members United and Southwest Corporate credit unions' portfolios were reasonably likely to sustain credit losses amounting to approximately \$145 million, \$400 million and \$980 million, respectively. The material loss review objectives were to (1) determine the cause(s) for the conservatorships of these corporate credit unions and the resulting losses to the Temporary Corporate Credit Union Stabilization Fund (TCCUSF), (2) assess supervision of the corporate credit unions, and (3) make appropriate recommendations to prevent future losses. We analyzed NCUA examination and supervision reports and related correspondence; interviewed management and staff from the NCUA Office of Corporate Credit Unions; and reviewed NCUA guides, policies and procedures, NCUA Call Reports, and NCUA Financial Performance Reports (FPRs). We expect to issue the final reports in July 2011.

Material Loss Review of Beehive and Certified Federal Credit Unions

The National Credit Union Administration (NCUA) Office of Inspector General (OIG) is conducting a Material Loss Review of Beehive and Certified Federal Credit Unions. We are reviewing both these losses to (1) determine the cause(s) of the credit union's failure and the resulting loss to the National Credit Union Share Insurance Fund (NCUSIF); and (2) assess NCUA's supervision of the credit union. To achieve these objectives, we analyzed NCUA examination and supervision reports and related correspondence; interviewed management and staff from NCUA Region; and reviewed NCUA guidance, policies and procedures, NCUA Call Reports, and Financial Performance Reports. We expect to issue the final reports in June 2011.

Review of Building Security at NCUA's Central Office

The objective of our review was to assess the adequacy of physical building security measures at NCUA's Central Office. Within this objective, we placed a particular emphasis upon reviewing building security access and controls, specifically related to: (1) facility entrance security; (2) interior security; (3) security systems; and (4) security operations and administration. We issued a draft report to NCUA management in April 2011 and anticipate issuing the final report to the NCUA Board in late April or early May 2011.

Review of Repeat Documents of Resolution

Recent material loss reviews indicated that requirements included in DORs issued by examiners to credit unions to correct significant deficiencies had not been timely addressed. For example, the same DOR issues were repeated over several examination contacts at the same credit union. We observed during material loss reviews that unaddressed DOR requirements were relevant to the issue(s) that led to the failure of credit unions. We therefore started this discretionary audit with the objectives to determine (1) the process for resolution/closure of DORs and (2) the effectiveness of the current resolution process. We anticipate issuing the final report in July 2011.

Significant Audit Recommendations on which Corrective Action Has Not Been Completed

As of September 30, 2010, there were no significant audit recommendations on reports issued over six months ago that have not been either fully implemented or are in the process of implementation.

Report On Credit Union Losses Under Materiality Level of \$25 Million

Section 988 of P.L. 111-203, the “Dodd-Frank Wall Street Reform and Consumer Protection Act” did two things relative to material loss reviews (MLR) of failed credit unions.

First, the threshold for a mandated material loss review was raised to \$25 million or greater loss to the National Credit Union Share Insurance Fund (NCUSIF or SIF) starting on the implementation date of the Act (July 21, 2010) and going forward.

Second, the NCUA OIG is now required to (1) perform limited reviews of all credit union failures under the threshold to assess whether an in-depth review (consistent with the scope of a material loss review) is warranted and (2) report to the National Credit Union Administration Board and the Congress every 6 months on the results of the limited reviews and the timeframe for performing any in-depth reviews we determine are necessary.

This report on losses not reaching \$25 million covers the six-month period from October 1, 2010 to March 31, 2011. For all losses to the SIF under the MLR threshold, we determined (1) why NCUA initiated assistance and (2) whether any unusual circumstances existed that might warrant an in-depth review of the loss.

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

We conducted limited reviews of seven failed credit unions that incurred losses to the SIF under \$25 million that occurred between October 1, 2010 and March 31, 2011. Based on those limited reviews, we determined that none of the losses warrants additional work. For the seven failed credit unions for which we do not intend to conduct additional work, we concluded that either 1) no unusual circumstances presented themselves in our review, or 2) we had already addressed the reasons identified for failure in recommendations to the agency in our Material Loss Review Capping report or other MLR reports.

The chart below provides details on the seven credit union losses to the NCUSIF of less than \$25 million. It provides details on the credit union, estimated loss to the SIF, grounds for conservatorship or merger, cause of the failure if one occurred, supervision, other factors, and our decision to proceed or not with an MLR of the credit union.

DECISIONS REGARDING LOSSES LESS THAN \$25 MILLION

Decision*	Credit Union	Region	Date of Failure	Est. Loss to SIF	Grounds for the NCUA Appointment
Terminate	Family First Federal Credit Union	V	2/15/2011	\$21.5 M	Insolvent; poor credit risk, high loan delinquency; high loan charge-offs poor loan underwriting, high concentration of unsecured loans
Terminate	Oakland Municipal Credit Union	II	1/31/2011	\$13.7 M	Weak management; low and declining net worth position; high loan losses high delinquency; high operating expenses; negative earnings
Terminate	The Union Credit Union	V	10/29/2010	\$2,479	Insolvent due to poor underwriting and collections
Terminate	NYC – OTB Federal Credit Union	I	2/23/2011	\$542,000	Insolvent due to understated delinquency; underfunded ALLL; underwriting deficiencies; weak management
Terminate	Phil-Pet Federal Credit Union	IV	9/30/2010	\$958,000	Poor management practices related to loan underwriting; high delinquency and loan losses
Terminate	Wisconsin Heights Credit Union	IV	3/04/2011	\$713,000	Insolvent due to weak management; critically undercapitalized; poor loan underwriting and control
Terminate	Land of Enchantment	V	3/07/2011	\$1.1M	Insolvent due to weak management; alleged fraud by VP/Loan Officer; poor loan underwriting and high delinquency and charge-offs

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

PEER REVIEWS

October 1, 2010, through March 31, 2011.

Audit organizations that perform audits and attestation engagements of federal government programs and operations are required by *Government Auditing Standards* to undergo an external peer review every three years. The objective of an external peer review is to determine whether, during the period under review, the audit organization's system of quality control was suitably designed and whether the audit organization was complying with its quality control system in order to provide the audit organization with reasonable assurance of conforming to applicable professional standards.

External Peer Review of NCUA OIG Office of Audit

Although we did not have an external Peer Review during the current semi-annual period, the U.S. Securities and Exchange Commission (SEC) OIG Office of Audits completed its external peer review of the NCUA OIG Office of Audit for the three-year period ending October 31, 2009. The SEC OIG issued its "NCUA System Review Report" on May 7, 2010. A copy of the report is included herein as Appendix A. In its report, the SEC OIG rendered the opinion that the system of quality control for the NCUA OIG audit organization was suitably designed and complied with, to provide the NCUA OIG with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Therefore, the NCUA OIG received a peer rating of pass. There are no outstanding recommendations from this external peer review.

External Peer Review of National Science Foundation OIG Office of Audit

The NCUA OIG did not conduct a peer review of another audit organization during this reporting period. However, on February 5, 2009, we issued an external peer review report for the audit function of the National Science Foundation (NSF) OIG for the three year period ended September 30, 2008. The NSF OIG reported to our office that it does not have any outstanding recommendations related to the peer review report.

INVESTIGATIVE ACTIVITY

In accordance with professional standards and guidelines established by the Department of Justice, the OIG conducts investigations of criminal, civil, and administrative wrongdoing involving agency programs, operations and personnel. Our investigative program focuses on activities designed to promote accountability, effectiveness, and efficiency, as well as fighting fraud, waste, and abuse in agency programs and operations. In addition to our efforts to deter misconduct and promote integrity awareness among agency employees, we investigate referrals and direct reports of employee misconduct. Investigations may involve possible violations of regulations regarding employee responsibilities and conduct, Federal criminal law, and other statutes and regulations pertaining to the activities of NCUA employees.

Moreover, we receive complaints from credit union members and officials that involve NCUA employee program responsibilities. We examine these complaints to determine whether there is any indication of NCUA employee wrongdoing or misconduct. If not, we refer the complaint to the appropriate regional office for response, or close the matter if contact with the regional office indicates that the complaint has already been appropriately handled.

OIG HOTLINE CONTACTS

The OIG maintains a toll free hotline to enable employees and citizens to call with information about suspected waste, fraud, abuse or mismanagement involving agency programs or operations. We also receive complaints through an off-site post office box, from electronic mail, and facsimile messages. All information received from any of these sources is referred to as a *hotline contact*. The OIG hotline program is handled by our Office Manager, under the direction of our Director of Investigations. The majority of hotline contacts are from consumers seeking help with a problem with a credit union. These contacts are referred to the appropriate NCUA regional offices for assistance. During this reporting period, we referred 127 consumer complaints to NCUA Office of Consumer Protection and regional offices. We referred three allegations of potential fraud at credit unions to the NCUA Office of General Counsel.

INVESTIGATIONS

Bank Fraud

During the previous reporting period, the OIG received an allegation that a NCUA employee may have committed bank fraud. The OIG's investigation is ongoing.

Unprofessional Behavior

During this reporting period, the OIG received an allegation that an NCUA examiner had displayed unprofessional behavior while conducting an examination. This investigation is ongoing.

Standards of Ethical Conduct for Employees of the Executive Branch

During this reporting period, the OIG received an allegation that an employee was seeking employment with a credit union while conducting an examination. This investigation is ongoing.

Standards of Ethical Conduct for Employees of the Executive Branch

During the previous reporting period, the OIG received an allegation that an employee was using his position as a Credit Union examiner for private gain. The OIG investigated the matter and found no corroborating evidence to support the allegation. The OIG closed the inquiry with an Investigative Memorandum to the file.

Fraud and Related Activity in Connection with Computers

During the previous reporting period, the OIG received an allegation that an employee had accessed the email of another employee without authorization. The OIG investigated the allegation, including a forensic analysis of the subject's computer, and found no evidence to support the allegation. The investigation was closed with an Investigative Memorandum to the file.

Misconduct

During the current reporting period, the OIG received an allegation of misconduct by two credit union examiners. The OIG conducted a preliminary inquiry into the matter and did not develop substantive information to warrant further investigation. The matter was referred to the Office of Consumer Protection.

Prohibited Hiring Practices

During the current reporting period, the OIG received an allegation that an employee was hired under a vacancy announcement where the duty station was not listed properly. The OIG's review of the matter did not support the allegation.

Misuse of Government-Issued Charge Card

During the current reporting period, the OIG received an allegation that an employee used his government-issued charge card for personal expenses in violation of agency policy. The OIG's investigation substantiated the allegation. The investigation also found that the employee had not accurately accounted for his transit subsidy reimbursement, an additional violation of agency policy. The OIG issued a report of investigation and forwarded it to agency management.

PEER REVIEWS

October 1, 2010, through March 31, 2011.

Section 6(e)(7) of the Inspector General Act of 1978, as amended, requires those OIGs that have been granted statutory law enforcement authorities pursuant to the Act, to be periodically reviewed by another OIG or a committee of OIGs (Peer Review). The purpose of the peer review is to ascertain whether adequate internal safeguards and management procedures exist to ensure that the law enforcement powers conferred by the 2002 amendments to the Act are properly exercised. The NCUA OIG does not have statutory law enforcement authority; therefore, our investigation organization is not required to have a peer review and, to date, has neither undergone a peer review nor conducted a peer review of another OIG. However, the NCUA Office of Investigations intends to participate in the peer review process in the future and is scheduled to undergo a peer review in the third quarter of 2013.

LEGISLATIVE AND REGULATORY REVIEWS

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

During the reporting period, the OIG reviewed 25 items, including proposed and final legislation, proposed and final regulations, NCUA Interpretive Ruling Policy Statements (IRPS) and Letters to Credit Unions.

SUMMARY OF STATUTES AND REGULATIONS REVIEWED	
Legislation	Title
P.L. 111-382	“An Act to Clarify the National Credit Union Administration Authority to Make Stabilization Fund Expenditures Without Borrowing From the Treasury”
S. 300	“Government Charge Card Abuse Prevention Act of 2011”
S. 413	“Cybersecurity and Internet Freedom Act of 2011”
H.R. 1136	“Executive Cyberspace Coordination Act of 2011”
Regulations/Rulings/IRPS	Title
12 CFR Parts 701, et al.	Fixed Assets, Member Business Loans, and Regulatory Flexibility Program
12 CFR Parts 702 et al.	Prompt Corrective Action; Amended Definition of Low-Risk Assets
12 CFR Part 704	Corporate Credit Unions; Technical Corrections
12 CFR Part 701	The Low-Income Definition
12 CFR Parts 701, 708a, 708b	Fiduciary Duties at FCUs; Mergers and Conversions of Insured Credit Unions
12 CFR Part 707	Truth in Savings
IRPS 11-1	Guidelines for the Supervisory Review Committee
IRPS 11-2	Chartering Corporate Credit Unions
12 CFR Part 740	Accuracy of Advertising and Notice of Insured Status
12 CFR Parts 703, 704, 709, 742	Removing References to Credit Ratings in Regulations; Proposing Alternatives to the Use of Credit Unions

12 CFR Part 745	Share Insurance and Appendix
12 CFR Parts 741 and 751	Incentive Based Compensation Arrangements
12 CFR Parts 700, 701, 702, 741	Net Worth and Equity Ratio
12 CFR Part 741	Interest Rate Risk

Letters to Credit Unions	Title
11-CU-0255 (03/2011)	Conflict of Interest of FCU Employee
11-CU-0204 (03/2011)	Conflict of Interest of FCU Director
11-CU-0344 (03/2011)	NCUA Rulemakings on Director Duties
11-CU-0152 (03/2011)	Training Reimbursement to CU Officials
10-CU-1169 (01/2011)	Request for Advisory Opinion—Correspondent Services
10-CU-0974 (10/2010)	FCU Compliance with 202.6(b)(6) of the Federal Reserve Board's Regulation B (Reg B)
10-CU-0984 (10/2010)	Disclosing Credit Life Insurance Conversion to Debt Cancellation Coverage

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

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

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

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

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

TABLE III: SUMMARY OF OIG ACTIVITY October 1 through March31, 2011		
PART I – AUDIT REPORTS ISSUED		
Report Number	Title	Date Issued
OIG-10-16	Material Loss Review of St. Paul Croatian FCU	10/07/2010
OIG-10-17	Material Loss Review of U.S. Central FCU	10/18/2010
OIG-10-18	Independent Evaluation of the NCUA’s Compliance with FISMA 2010	11/15/2010
OIG-10-19	Material Loss Review of Western Corporate (WesCorp) FCU	11/16/2010
OIG-10-20	OIG Capping Report on Material Loss Reviews	11/23/2010
PART II – AUDITS IN PROGRESS <i>(as of March 31, 2011)</i>		
NCUA Financial Statements Audit 2010		
Material Loss Review of Constitution Corporate FCU		
Material Loss Review of Members United Corporate		
Material Loss Review of Southwest Corporate FCU		
Material Loss Review of Beehive CU		
Material Loss Review of Certified FCU		
Review of Building Security At NCUA’s Central Office		
Review of Repeat Documents of Resolution		

INDEX OF REPORTING REQUIREMENTS		
Section	Data Required	Page Ref
4(a)(2)	Review of legislation and regulations	24
5(a)(1)	Significant problems, abuses, or deficiencies relating to the administration of programs and operations disclosed during the reporting period.	12
5(a)(3)	Recommendations with respect to significant problems, abuses or deficiencies	12
5(a)(3)	Significant recommendations described in previous semiannual reports on which corrective action has not been completed.	17
5(a)(4)	Summary of matters referred to prosecution authorities and prosecutions which have resulted.	None
5(a)(5)	Summary of each report to the Board detailing cases where access to all records was not provided or where information was refused.	None
5(a)(6)	List of audit reports issued during the reporting period.	28
5(a)(7)	Summary of particularly significant reports.	12
5(a)(8)	Statistical tables on audit reports with questioned costs.	26
5(a)(9)	Statistical tables on audit reports with recommendations that funds be put to better use.	27
5(a)(10)	Summary of each audit report issued before the start of the reporting period for which no management decision has been made by the end of the reporting period.	None
5(a)(11)	Description and explanation of reasons for any significant revised management decision made during the reporting period.	None
5(a)(12)	Information concerning significant management decisions with which the Inspector General is in disagreement.	None
5(a)(14)	An appendix containing the results of any peer review conducted by another OIG during the reporting period or, if no peer review was conducted within that reporting period, a statement identifying the date of the last peer review conducted by another OIG.	20
5(a)(15)	List of outstanding recommendations from any peer review conducted by another OIG that have not been fully implemented.	None
5(a)(16)	A list of any peer reviews conducted by the IG of another OIG during the reporting period, including a list of any outstanding recommendations made that remain outstanding or have not been fully implemented.	None

APPENDIX A: NCUA SYSTEM REVIEW REPORT (SEC OIG REPORT NO. 478)



U.S. Securities and Exchange Commission
Office of Inspector General
Office of Audits

**National Credit Union Administration
System Review Report**



May 7, 2010
Report No. 478

System Review Report

May 7, 2010

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

Dear Mr. DeSarno,

We have reviewed the system of quality control for the audit organization of the National Credit Union Administration (NCUA), Office of Inspector General (OIG) in effect for the period ended October 30, 2009. A system of quality control encompasses NCUA OIG's organizational structure and the policies adopted and procedures established to provide it with reasonable assurance of conforming with *Government Auditing Standards*. The elements of quality control are described in the *Government Auditing Standards*. NCUA OIG is responsible for designing a system of quality control and complying with it to provide NCUA OIG with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and NCUA OIG's compliance therewith based on our review.

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

In performing our review, we obtained an understanding of the system of quality control for NCUA OIG's audit organization. In addition, we tested compliance with NCUA OIG's quality control policies and procedures to the extent we considered appropriate. These tests covered the application of NCUA OIG's policies and procedures on selected engagements. Our review was based on selected tests;

therefore, it would not necessarily detect all weaknesses in the system of quality control or all instances of noncompliance with it.

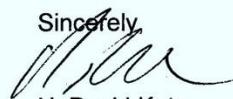
There are inherent limitations in the effectiveness of any system of quality control, and therefore noncompliance with the system of quality control may occur and not be detected. Projection of any evaluation of a system of quality control to future periods is subject to the risk that the system of quality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

Enclosure 1 to this report identifies the audit engagements that we reviewed.

In our opinion, the system of quality control for the audit organization of NCUA OIG in effect for the period ended October 30, 2009 has been suitably designed and complied with to provide NCUA OIG with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Federal audit organizations can receive a rating of *pass*; *pass with deficiencies*, or *fail*. The NCUA OIG has received a peer review rating of *pass*. As is customary, we issued a letter dated May 7, 2010, that sets forth findings that were not considered to be of sufficient significance to affect our opinion expressed in this report.

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

Sincerely,



H. David Kotz
Inspector General

Enclosures (2)

Enclosure 1**SCOPE AND METHODOLOGY**

We tested compliance with the NCUA OIG audit organization's system of quality control to the extent we considered appropriate. These tests included a review of 1 of 2 audit reports issued during the period April 1, 2008, through October 30, 2009. We also reviewed the internal quality control review performed by NCUA OIG.

In addition, we reviewed the NCUA OIG's monitoring of an engagement performed by an IPA, where the IPA served as the principal auditor. NCUA OIG contracted for the audit of its agency's Fiscal Year 2008 Financial Statements. Due to problems related to a major accounting issue that has not been resolved, the financial statement audit has not been completed and a final report has not been issued. We reviewed this audit to determine whether it was adequately monitored.

Reviewed Engagements Performed by NCUA OIG

<u>Report No.</u>	<u>Report Date</u>	<u>Report Title</u>
OIG-09-03	Oct 23, 2009	Material Loss Review – New London Security Federal Credit Union
OIG-08-06	June 4, 2008	Review of the Implementation of Homeland Security Presidential Directive 12

Reviewed Monitoring Files of NCUA OIG for Contracted Engagements

<u>Report No.</u>	<u>Report Date</u>	<u>Report Title</u>
Pending	Pending	NCUA Financial Statements

Enclosure 2



National Credit Union Administration

Office of Inspector General

The Honorable H. David Kotz
Inspector General
Office of the Inspector General
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Date: April 22, 2010

Subject: Report on the External Quality Control Review of the National Credit Union Administration Inspector General Audit Organization

Dear Mr. Kotz

We appreciate the work conducted by your staff in reviewing the quality control process for the audit function at the National Credit Union Administration (NCUA) OIG. We agree with your opinion that the system of quality control for the audit function meets the requirements established by the Comptroller General of the United States for a General Government audit organization. We have no additional comments on the final System Review draft report provided. Thank you for the professionalism shown and your efforts in completing this review.

Sincerely,

A handwritten signature in black ink, appearing to read 'William A. DeSarno'.

William A. DeSarno
Inspector General

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