

and authorized the Office of the Chief Financial Officer to transfer resources from the Share Insurance Fund to the Operating Fund to account for insurance-related expenses.

At the end of the calendar year, NCUA's financial transactions are subject to audit in accordance with Generally Accepted Accounting Principles.⁶

SUMMARY:

The 2019 – 2020 Budget Justification, which is included as Attachment 1, has been updated to respond to relevant comments submitted by NCUA Offices and collected from the public. The staff draft was posted to the NCUA website on September 26, 2018, and an identical version was published in the *Federal Register* on October 2, 2018. The funding levels in the document are unchanged. However, a number of revisions were made to the staff draft to provide more information about the NCUA's programs and to support the agency's multi-year effort to improve the transparency of its budgets and programs. These revisions are described in more detail, below.

As required by the Economic Growth, Regulatory Relief, and Consumer Protection Act (P.L. 115-174), the NCUA held a hearing on October 17, 2018 to discuss the draft budget, which was open to the public and streamed live on the NCUA website. At that meeting, three independent national associations presented their views on the draft budget. Written statements from six organizations, including two from associations that presented at the budget hearing, were collected and posted to the NCUA website (see: <https://www.ncua.gov/About/Pages/budget-strategic-planning/budget-comments-2019.aspx>). In total, the NCUA received and reviewed comments from eight individuals representing seven different organizations.

The updated Budget Justification includes information about the NCUA's Operating Budget, Share Insurance Fund Administrative Budget, and Capital Budget. Total funding presented in these three budgets increases 1.1 percent from the 2019 levels approved by the Board in November 2017. The combined budgets are \$334.8 million. The 2019 Operating Budget is \$304.4 million with 1,173 full-time equivalents (FTEs). The 2019 Capital Budget is \$22.0 million. The 2019 Share Insurance Fund Administrative Budget is \$8.4 million with five FTEs. Total FTEs decrease in 2019 by 10 positions.

In nominal terms, the 2019 Operating Budget, which represents more than 80 percent of the agency's funding, increases \$6.3 million, or 2.1 percent, compared to the 2018 Board-approved levels. After adjusting for inflation, the Operating Budget decreases 0.2 percent in real dollar terms when compared to the 2018 Board-approved levels.

Recommendations from the NCUA Reform Plan are integrated in the budget estimates. As discussed in the Budget Justification, "costs associated with the NCUA reorganization are being funded by reprioritizing unspent balances from the 2017 and 2018 budgets." Such costs for 2019

⁶ See 12 U.S.C. 1783(b) and 12 U.S.C. 1789.

and 2020 are projected to total \$9,500,000. If the budget is approved, beginning in January 2019, NCUA will finalize the mission improvements outlined in the Reform Plan, including:

- Consolidating from five regions to three, and eliminating regional office staff;
- Reducing leased office space by 80 percent in future years;
- Modernizing the examination process with enhanced technology to reduce the burden on credit unions and improve coordination with state supervisory authorities; and
- Implementing plans and policies for offsite examinations to contain travel costs.

Comments from the Public

A majority of the comments received from the public about the 2019 – 2020 Budget relate to NCUA operations and program execution. The Office of the Chief Financial Officer has provided these comments directly to the appropriate NCUA senior executives responsible for the relevant offices discussed. Several other comments noted improvements in the draft budget compared to previous years, including better justifications for the agency’s information technology capital projects. Commenters were also generally supportive of staffing reductions made by the NCUA since 2015, and of the anticipated cost avoidance that will be achieved by terminating office leases after the NCUA reorganization is completed.

One commenter asked for more specific information about the ten positions proposed for elimination in 2019, while another asked for specific information about the location of staff in the Office of National Examinations and Supervision (ONES). Other commenters encouraged the agency to increase its use of specialists for field examinations. In response to these comments, the revised budget justification includes on page 27 a more detailed discussion of the positions eliminated by the NCUA reform plan and an additional explanation of the locations for ONES staff.

Other comments expressed continued interest and support for improvements in how the NCUA measures program and technology investment performance. The agency shares this interest and is committed to continuing to improve operational transparency and accountability. We will continue to seek improvement in our performance indicators and Annual Performance Plans.

One commenter suggested that the NCUA include actual expenditures within the budgetary tables. On the Budget and Strategy page of the NCUA website, the Office of the Chief Financial Officer already publishes monthly reports on actual expenses from the NCUA Operating Fund, which is a more timely and accurate presentation of the agency’s spending and financial position. Within these monthly reports, expenses are generally presented in the same cost categories as the Budget Justification. In addition, the Chief Financial Officer makes an annual presentation at the July open meeting of the NCUA Board, providing an analysis of expenses incurred through the first half of the year and updating budgetary projections for the remainder of the year.

One commenter recommended that the NCUA extend the two-year display in the Budget Justification to show a three year budget projection. Given the detailed approach the NCUA uses when formulating its budget, three-year budgetary projections are unlikely to be particularly

precise or informative, and would require additional resources throughout the agency that are better used for other purposes.

Financing the NCUA Programs

The NCUA's expenses are funded primarily through fees paid by federal credit unions and transfers from the Share Insurance Fund using the Overhead Transfer Rate (OTR). As the annual budget is developed for Board review and approval, the approved methodologies for calculating the OTR and Operating Fees are applied to determine the amount of the budget that will be financed by each. The Board delegated authority to the Chief Financial Officer to administer the approved methodology for calculating the Operating Fees, and to set the fee schedule. There is no change to the underlying methodology for the OTR or the Operating Fee calculations for 2019, rather, the change in assessments results from a re-estimated OTR and from indexing the fee schedule to projected asset growth.

To promote transparency about how the NCUA finances its programs, pages 45 through 49 of the Budget Justification include a new section that discusses the methodology for calculating the OTR and the Operating Fee. Worksheets that show the specific steps used to determine the Operating Fee and the scale for rates charged to different sized credit unions are included on pages 49 and 50.

The OTR and Operating Fee estimates presented in the draft Budget Justification have been revised based on refined workload modeling. The final 2019 Overhead Transfer Rate increases by 10 basis points to 60.5 percent when compared to the draft budget. This remains a decrease from the 61.5 percent rate used for the 2018 budget. Since the residual 39.5 percent of the 2019 budget will be collected through the Operating Fee, the rate charged to federal credit unions will increase by an average of 2.0 percent, a 20 basis point reduction from the draft budget. The Operating Fee will be assessed on federal credit unions based on a projection of their year-end assets. Based on the June 30, 2018 Call Report data, annual asset growth is projected to be 6.2 percent at year-end.

As shown on page 48 of the Budget Justification, federal credit unions cover just over 70 percent of the costs of the NCUA's operations, while federally insured state-chartered credit unions pay just under 30 percent. Federal credit unions with assets less than \$1 million are not assessed an Operating Fee. For federal credit unions with assets greater than \$1 million, the NCUA establishes a three-tiered scale to compute the fee charged, also known as the assessment scale. The dividing points on the assessment scale are adjusted upward on an annual basis by the projected asset growth rate. The dividing points are indexed annually to preserve the same relative relationship of the scale to the applicable asset base.

To illustrate the average rate impact for smaller federal credit unions, the final fee rate applied to assets under \$1.5 billion increases from \$264 per one million dollars of assets, to \$269 per one million dollars of assets, a reduction of \$1 when compared to the draft budget, but an increase of \$5 per million, or 2.0 percent when compared to the 2018 budget. Federal credit union assets between \$1.5 billion and \$4.5 billion would be assessed at a rate of \$78.52 per million, a

reduction of \$0.17 compared to the draft budget, and assets above \$4.5 billion would be assessed at \$26.22 per million, a reduction of \$0.06 compared to the draft budget. These rates are also 2.0 percent higher than the comparable 2018 levels.

RECOMMENDED ACTIONS: It is recommended that the NCUA Board approve:

1. The 2019 Operating Fund Budget of \$304.4 million and 1,173 FTEs, the 2020 Operating Budget of \$316.2 million and 1,173 FTEs, reorganization expenses to be paid from past budgets' unused balances of \$9.5 million, and an extension through 2020 of the Executive Director's authority to reallocate reorganization funds.
2. The 2019 Capital Budget of \$22 million and the 2020 Capital Budget of \$18.6 million.
3. The 2019 Share Insurance Fund Administrative Budget of \$8.4 million and five FTEs and the 2020 Share Insurance Fund Administrative Budget of \$9.1 million and five FTEs.

ATTACHMENTS:

2019 – 2020 Budget Justification