

BOARD ACTION MEMORANDUM

TO: NCUA Board **DATE:** November 20, 2013
FROM: Office of Examination & Insurance **SUBJ:** Overhead Transfer Rate 2014

ACTION REQUESTED: Approve the recommended overhead transfer rate for 2014

DATE ACTION REQUESTED: November 21, 2013.

OTHER OFFICES CONSULTED: Office of the Chief Financial Officer.

VIEWS OF OTHER OFFICES CONSULTED: Concur.

BUDGET IMPACT, IF ANY: None. The overhead transfer rate is one of the funding sources for the budget, but does not affect the amount of the budget. The NCUA Board approves the budget separately and without regard to the overhead transfer rate. The overhead transfer rate is applied to actual expenses incurred each month.

SUBMITTED TO INSPECTOR GENERAL FOR REVIEW: N/A

RESPONSIBLE STAFF MEMBERS: Larry Fazio, Director Office of Examination & Insurance, JeanMarie Komyathy, Director of Risk Management and Loss/Risk Analysis Officer Brian McDonough.

SUMMARY: The *Federal Credit Union Act* authorizes NCUA to expend funds from the National Credit Union Share Insurance Fund (NCUSIF) for administrative and other expenses related to federal share insurance (12 U.S.C. §1783). An overhead transfer from the NCUSIF covers the expenses associated with insurance-related functions of NCUA's operations. The NCUA Board approved the current overhead transfer rate of 59.1 percent for fiscal year 2013 in November 2012.

At the November 20, 2003 board meeting, the NCUA Board approved a refined method for calculating the recommended overhead transfer rate. The overhead transfer methodology incorporates the following key factors:

- The value to the NCUSIF of the insurance-related work performed by state supervisory authorities (SSAs).
- The cost of NCUA resources and programs with different allocation factors from the examination and supervision program. Allocation factors are reviewed annually.
- The distribution of insured shares between federal credit unions and federally insured state-chartered credit unions.
- Operational costs charged directly to the NCUSIF.

- The results of the annual Examination Time Survey (ETS). The ETS captures the time NCUA spends in federal credit unions carrying out its dual missions as an insurer and a federal credit union regulator. NCUA primarily achieves its missions through the examination and supervision process, and examinations and supervision are the primary catalysts for other agency functions.

Clarification Adopted for ETS

In 2012, the Office of Examination and Insurance (E&I) clarified the application of the insurance-related and non-insurance related definitions in the ETS in response to industry and examiner comments. This clarification involved how examiners record on the ETS time they spend examining for compliance with various regulations. Specifically, the NCUA rules and regulations were individually mapped to the proper ETS category based on the extent to which a regulation was designed to protect the NCUSIF (a new sub-category of insurance related labeled “insurance-regulatory”) or to govern commerce and/or provide consumer protection (labeled “non-insurance or consumer regulatory”).

This breakdown and mapping of regulations is consistent with the existing overall definitions of insurance-related and non-insurance related. The primary definitions have not changed; the regulations have merely been explicitly mapped based on the overarching definitions. While examiners continue to use their judgment as to what exam procedures to perform during an examination or supervision contact based on the risks and product-service mix of the credit union, this clarification creates more consistency as to where examiners record the time on the ETS.

In 2013, E&I contracted with PricewaterhouseCoopers, LLP to review the mapping of NCUA regulations to the categories on the ETS. The PricewaterhouseCoopers, LLP review concludes: *“The NCUA rules and regulations matrix aligns consistently with the insurance and regulatory activities and provides a documented basis supporting the allocation of examiner time between insurance and regulatory activities.”* A copy of the full report is attached to this memorandum.

OTR Results for 2014

For the 2012-2013 ETS results, examiners report an average of 88 percent of their exam and supervision time spent on insurance related activities,¹ with the remaining 12 percent allocated to non-insurance related activities.

Based on the OTR methodology, the overhead transfer rate for 2014 calculates as 69.2 percent. The OTR for 2013 was 59.1 percent. The primary driver of the increase in the 2014 OTR is the higher time examiners record on the ETS for insurance related activities.

Distribution of Operating Budget Costs

The overhead transfer rate represents insurance-related costs in the NCUA operating budget to be paid for out of the NCUSIF; thus, 69.2 percent of the total operating budget will be paid out

¹ Compared to 67 percent in the previous ETS cycle.

of the NCUSIF. The remaining 30.8 percent of the operating budget is paid for through the federal credit union (FCU) operating fee.

Thus, the explicit and implicit distribution of total operating budget costs for federal credit unions and federally insured state chartered credit unions (FISCUs) is as follows:

Portion of Operating Budget covered by:	FCUs	FISCUs
FCU Operating Fee	30.8%	0.0%
OTR x Percent of Insured Shares	37.2% (69.2% x 54%)	32.0% (69.2% x 46%)
Total	68.0%	32.0%

RECOMMENDED ACTION: Establish an overhead transfer rate of 69.2 percent for 2014.

ATTACHMENTS:

- (1) Calculation of 2014 overhead transfer rate
- (2) PricewaterhouseCoopers, LLP ETS 2013 review

Attachment 1

Calculation of the 2014 Overhead Transfer Rate

STEP 1 – Workload Program (2014)

Core Programs	2014 Workload Hours	Non-Insurance Percent	Non-Insurance Hours	Allocation Basis
Federal Examination	440,480	12.8%	56,381	Examiner time survey.
Federal Supervision	73,629	7.6%	5,618	Examiner time survey.
State Exam & Supv	206,693	0%	0	FISCU work is insurance-related.
State Exam Review	5,418	0%	0	FISCU work is insurance-related.
5300 Program - FCU	27,746	12.8%	3,551	FCU time uses examiner time survey.
5300 Program – FISCU	16,296	0%	0	FISCU portion considered insurance-related.
Total Core Program	770,262	n/a	65,551	
Special Programs				
Fair Lending Exams		100.0%		Regulatory program now completed by OCP.
RLS	4,326	12.8%	554	Based on insurance but includes a portion of regulatory.
FOM & Chartering	430	100.0%	430	Regulatory program.
RCMS	5,044	0%	0	NCUSIF risk management program.
RISOs	2,436	12.8%	312	Allocation based on % from time surveys.
Small Credit Unions	16,802	4.0%	672	Allocation based on types of assistance provided by Time Reporting categories.
CUSO Exams	6,617	0%	0	NCUSIF risk management program.
Total Special Program	35,655	n/a	1,968	
Total Core & Special Programs	805,917	n/a	67,518	
Percent of Workload Programs devoted to NCUA's Non-Insurance Role			8.4%	

NOTE: The totals may not reconcile exactly due to rounding.

STEP 2 – Financial Budget (2014)

Cost Area 2014 Financial Budget	Dollar Budget (\$M)	Non- Insurance Percent	Non- Insurance Cost (\$M)
All Regional Costs: Based on regulatory related portion of core and special programs.	\$147.34	8.4%	\$12.35
Office of Consumer Protection: Primarily non-insurance (regulatory) function i.e. chartering/FOM - net of work related to share insurance coverage for members and FISCUs.	\$9.37	82.0%	\$7.71
Asset Management Assistance Center and Assistance Program: Manages liquidation payouts, assets acquired from liquidations and assistance programs, and recoveries for the NCUSIF.	\$6.21	0%	\$0
Office of Small Credit Unions: Primarily regulatory related function to facilitate the expansion of credit union services. However, 10% FISCU participation rate.	\$5.88	4.0%	\$0.24
Office of National Examinations and Supervision: NCUSIF risk management function other than chartering, FOM, and mergers.	\$8.93	0%	\$0
Office of Minority and Women Inclusion	\$2.50	100.0%	\$2.50
Other Internal Offices: Based on non-insurance percent. (OHR, OCIO, OCFO)	\$88.06	8.4%	\$7.38
Total 2013 NCUA Budget	\$268.29		\$30.16

STEP 3 – Calculate NCUSIF Costs (2014)

Imputed NCUSIF Costs

	Millions
2014 Financial Budget	\$268.29
Non-Insurance Costs (see Step 2)	(\$30.16)
SSA imputed Value	\$46.12
Direct Operational Charges to NCUSIF	\$1.44
Total NCUSIF Imputed Costs	\$285.68

STEP 4 – Allocation of NCUSIF Costs (2014)

Insured Shares Allocation

	FCU	FISCU
Total Cost of Providing NCUSIF Insurance	\$285.68	\$285.68
Times Proportional Allocation Basis	53.9%	46.1%
Equals Allocated Insurance Costs	\$153.98	\$131.70

Net of Imputed SSA Value

	Millions
Total Allocated Insurance Costs - FISCUs	\$131.70
Minus SSA Insurance Work Imputed Value	(\$46.12)
Equals Net Cost of NCUSIF Insurance – FISCUs	\$85.58

Dollar Amount of OTR

	FISCUs	FCUs	Dollar Amt.
FISCU Portion of NCUA Insurance Cost	\$85.58	\$100.06	\$185.65
Divided by Percentage of Insured Shares	46.1%	53.9%	

OTR as a Percent of Budget

Dollar Amount of OTR	\$185.65
Divided by NCUA Budget	\$268.29
Equals OTR	69.20%

Imputed SSA Value Step 1 – 2014

Gross Workload

Table 1

Average Exam Time (Hours) FCU (Dec. 2012)	Assets < \$10M	\$10M - \$100M	\$100M - \$250M	\$250M - \$500M	> \$500M
CAMEL 1	37	72	145	239	395
CAMEL 2	40	95	182	305	350
CAMEL 3	69	148	319	470	690
CAMEL 4	169	247	448	305	722
CAMEL 5	493	332	209	750	

Table 2

FISCUs (#) in Each Category (as of Dec 2012)	Assets < \$10M	\$10M - \$100M	\$100M - \$250M	\$250M - \$500M	> \$500M
CAMEL 1	73	138	44	38	74
CAMEL 2	430	694	185	100	110
CAMEL 3	205	251	52	16	19
CAMEL 4	42	51	12	2	7
CAMEL 5	2	2	0	0	0

Table 3

Total Hours (Table 1 cells x Table 2 cells)	Assets < \$10M	\$10M - \$100M	\$100M - \$250M	\$250M - \$500M	> \$500M
CAMEL 1	2,687	9,945	6,368	9,094	29,324
CAMEL 2	17,354	65,953	33,627	30,349	38,457
CAMEL 3	14,238	37,263	16,602	7,513	13,118
CAMEL 4	7,077	12,594	5,373	610	5,055
CAMEL 5	985	665	0	0	0
Total					
Total Gross Exam Hours					364,270

Imputed SSA Value Step 2 - 2014

Net Workload

Net of Insurance-Related Time

FISCUs	Hours
Gross FISCU Exam Hours	364,270
x Insurance Factor Based on Exam Time Survey	87.2%
= Total Insurance Hours w/out Risk-Based Scheduling	317,644

Net of NCUA Time in FISCUs

	Hours
Total FISCU Hours	317,644
+ 2014 Budgeted Supervision Hours	62,360
- 2014 Budgeted Insurance Review Hours	144,333
Total Additional FISCU Insurance Hours Needed	235,671

*Uses the larger of two calculations – current budgeted state exam insurance hours or projected FISCU exam insurance hours based on ETS.

Imputed SSA Value Step 3 - 2014

Additional Staff Needed

Examiner Productive Time

2013 Core and Special Workload Program Hours	805,917
/ Total 2014 Workload Program Hours	1,510,551
= Productivity Ratio	53.4%
Total Work Hours in a Year Per Full Time Equivalent (FTE)	2,080
x Productivity Ratio	53.4%
= Productive Hours per FTE Examiner	1,110

Number of Examiners Needed

Net Additional FISCO Hours Needed	230,253
/ Productive Hours per FTE Examiner	1,110
= Number of Additional FTE Examiners Needed	207.5

Total Additional Staff Needed

Additional Staff Needed	Ratio Examiners to Position	FTEs Per Position
Examiners	1/1	207.5
Supervisory Examiners	1/9	23
Analysts	1/15	13.8
Directors	1/25	8.3
Other Regional Staff	1/20	10.4
= Number of Additional FTEs Needed		263.00

**Imputed SSA Value Step 4 - 2014
Imputed Cost**

Gross Cost

Total Cost of Regions (2014 Budget)	\$147.36M
/ FTEs in Regions (2014 Budget)	869.6
= Per Regional FTE Cost	\$169.45M
x Number of Additional FTEs Needed	263.0
= Cost of Additional Regional Positions	\$44.57M

Net Cost

	Millions
Cost of Additional Regional Positions	\$44.57M
+ Additional OHR Costs (21.0% budget)	\$3.00M
- SSA Training and Equipment Cost	(\$1.44M)
= Imputed SSA Value	\$46.12M

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