



NATIONAL CREDIT UNION ADMINISTRATION

OFFICE OF INSPECTOR GENERAL

***YEAR 2000 WAIVER PROCESS REVIEW
REPORT NUMBER 992***

March 31, 1999

A handwritten signature in black ink, which appears to read 'Frank Thomas', is positioned above a horizontal line.

***FRANK THOMAS
INSPECTOR GENERAL***

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Introduction

This is the first of the Office of Inspector General's (OIG) series of reports addressing the Year 2000 (Y2K) computer problem as it relates to the National Credit Union Administration (NCUA) and federally insured credit unions (FICUs). Because of the time critical nature of the Y2K problem, and in order to provide the NCUA Board with timely information, we are not making formal recommendations or asking for a written response. Rather, we are offering certain suggested actions as matters for consideration by the NCUA Board and agency management.

Other Y2K reviews in process include an independent assessment of NCUA's internal systems and project management; and a review of FICUs progress in meeting the renovation phase milestone established by NCUA. Additional planned Y2K work includes reviews of the credit union quarterly reporting requirement; vendor status; and high risk credit unions.

Background

The NCUA, in addressing potential Y2K problems in federally insured credit union information systems, adopted milestone dates for credit unions to accomplish specific Y2K tasks. The purpose of the milestone dates was to ensure credit union information systems were ready to function in a timely manner. Benchmark milestone dates were developed to address awareness, assessment, renovation, validation/testing, and implementation phases. In early 1998, NCUA established a policy of providing waivers or extensions to the milestone dates. In specific instances such as converting from one information system to another, or vendor and credit union lack of ability to meet the milestone dates because of system renovation. Waivers and extensions have been granted for individual credit unions and blanket waivers for some credit unions with common information system vendors. If credit union remediation efforts were not performed in a timely manner in accordance with the milestone dates and waivers, the NCUA could take administrative action against the credit union because of unsafe and unsound practices.

The overall objective of our review was to evaluate NCUA's efforts in monitoring and assisting federally insured credit unions to address Y2K date compliance through the waiver process. Our review emphasized the justification for the waiver and agency follow-up during and after the waiver period ended.

Objectives

The specific objectives of our review were to determine if NCUA had adequate justification for granting credit union Y2K compliance waivers, and whether NCUA is exercising timely and appropriate waiver follow-up.

Scope and Methodology

Our review scope included agency Y2K waiver activities for federally insured credit unions. The review was performed at the NCUA Office of Examination and Insurance; and Region II (Alexandria, Virginia), Region III (Atlanta, GA), and Region V (Austin, Texas). Our review was performed during December 1998 through March 1999. Because of the limited review scope and our desire to provide NCUA management with timely information, we followed the President's Council on Integrity and Efficiency Quality Standards for Inspections with the exception of the standards for fraud and other illegal acts and follow-up.

We performed the following procedures to meet our review objectives:

- Interviewed certain central and regional office staff.
- Reviewed Central Office and regional waiver process guidance and procedures.
- Reviewed a sample of thirty-five (29 percent) waivers from universe of one hundred twenty-two waivers granted at the time of our review for Regions II, III, and V. Our review focused primarily on the completion of the renovation phase with an NCUA benchmark milestone date of January 31, 1999.

REVIEW OBSERVATIONS

As a result of our review we observed that waiver actions were justified; there was a lack of documented follow-up actions; the waiver process was lengthy; and additional attention may be needed for federally insured state chartered credit unions.

Waiver Actions Justified

Our review of thirty five waiver actions in Regions II, III, and V, indicated that the reasons given for the waiver/extension request were valid and the action approved was justified. The waiver request documentation submitted by the credit union and/or examiner was sufficient to warrant the approval of the waiver or extension of the milestone date. The primary reasons for waiver requests were institutions converting from one information system to another or upgrading their current system. Most identified issues were beyond the control of the credit union. In most instances the examiner indicated that credit union management had the ability to complete the conversion/upgrade and could meet succeeding milestone dates.

We evaluated NCUA guidance and practices regarding the waiver process focusing on the adequacy of guidance in preparation of the waiver; and the reasonableness of justification for the waiver request and approval. In addition, we evaluated the timeliness of agency approval; monitoring of credit union status; and follow-up of the waiver/extension approval.

The December 1998 agency Readiness Report indicated the agency had received 287 waivers/extensions from the approximate 11,000 federally insured credit unions. Waiver/extension request volume increased significantly in the months of January and February 1999, when NCUA received an additional 150 requests for a total of 437 indicated in the February 1999 Readiness Report.

Lack of Documented Follow-up

In the majority of cases in our review (more than 70 percent) we found limited evidence of documented follow-up and monitoring of existing waiver actions by examiner and regional office staff. However, when we performed follow-up with staff we found that some follow-up was being performed.

In a limited number of instances (17 percent) in our review sample we found inconsistent recommendations for removal of outstanding waiver or extension actions. In some cases if the action was substantially complete the examiner recommended removal of the action, while in others the action was completed prior to removal. In one instance two examiners were responsible for the same credit union (district responsibility was in transition) with one examiner recommending removal of an action because the work was substantially completed, while the other examiner did not recommend removal of the action.

In most instances, responsibility to determine Y2K readiness in individual credit unions and any necessary follow-up is the responsibility of the district examiner to whom the credit union has been assigned. Prior to the 4th quarter 1998, examiners performed Y2K review procedures contained in Y2K program fiscal year 1998 exam requirements during the financial examination and during other contacts at credit unions.

Examiners began using the Federal Financial Institution Exam Council (FFIEC) Year 2000 Workprogram Phase II (workprogram) in the fourth quarter 1998 examinations. The FFIEC workprogram provides examination procedures that help the examiner to determine if the credit union has addressed the Y2K problems inherent in many computer software, hardware, and environmental systems as well as indirect risks associated with external sources, customers, or fiduciary activities. The examination procedures are designed to focus on the adequacy of the credit union's plans and processes for achieving Y2K readiness, with particular emphasis placed on the final phases of the Y2K project. The program includes specific benchmark dates that the credit union must meet.

NCUA staff do not perform testing of information systems to ensure Y2K readiness in credit unions. Each calendar quarter the examiner receives a hardcopy status report from assigned credit unions indicating the status of Awareness, Assessment, Renovation, Testing, and Implementation phases for critical and non-critical information systems. The examiner would review, input and upload the information to the agency database. The quarterly information is reviewed by the Y2K specialist for apparent completeness and then the information is forwarded to E&I.

The examiner uses information developed during contacts, examinations, and information supplied by the requesting credit union to develop the waiver/extension documentation package. E&I developed a checklist for examiner and regional office use in developing the waiver package. In addition, regions developed clarification guidance. The E&I checklist were not required in the documentation for the waiver as long as all identified issues were addressed.

Lengthy Waiver Process

Waiver turnaround time starts from when the request leaves the examiner or credit union, is processed through the regional office, processed in E&I, returned to the regional office, and the regional director letter is finalized and sent to the credit union. This process often takes up to and in excess of sixty days. In some cases, the extension period had already expired by the time the waiver approval was communicated to the credit union.

For quality control purposes the waiver process features a review by the district examiner, the regional office and the central office. The process ensures a good review, however it also slows down the process. E&I instituted a streamlined waiver approval process in January 1999. However, as the volume and complexity of the cases have increased, the backlog and total process time has increased. Processing time in E&I alone for the first fifty extensions and waiver actions were completed in seven days on average. However, the last fifty extensions and waiver actions were completed in 24 days on average. As the numbers and complexities of waiver actions increase so does the backlog. The December 1998 backlog in E&I was thirty five actions, while the February 1999 backlog was fifty actions.

Turnaround time is particularly significant to ensure that the action is received at the credit union in a timely manner to ensure corrective action. Also, milestone dates in 1999 are progressively closer together with testing to be completed by June 30th and implementation to be completed by July 31st.

A waiver/extension request can originate from the credit union or district examiner assigned the credit union following guidance provided to the credit union. The waiver/extension documentation package is forwarded to the regional office for review and concurrence. Reasons for waivers include not meeting benchmark dates or not meeting Letters of Understanding and Agreement prepared during examinations. The regional office Y2K specialist reviews the request, prepares a draft Regional Director Letter that will accompany the waiver package, and sends the package to Office of Examination and Insurance Risk Management Division (E&I) for concurrence. E&I concurs or requests inclusion of additional requirements to approve the waiver and returns the approved package to the regional office. Most waiver/extension requests are ultimately approved by the region and E&I. After the approved request is returned to the region, the Y2K specialist prepares the final Regional Director Letter and sends the letter including the approved waiver to the credit union for signature acceptance by the credit union. Outstanding waivers are to be monitored for compliance by the regional office.

NCUA granted 83 waivers through 9/3/98. Seventy-two waivers were granted for extensions of assessment dates, and 11 waivers were granted for extensions of renovation and testing dates (due to computer system conversions). Requests for waivers and extensions increased the latter part of 1998 and 1999. As of December 1998, 287 waivers/extensions were received by E&I; and as of February 1999 a total of 437 waivers/extensions have been received.

FISCUs Need Increased Attention

At the time of our review, in two of the three regions there were fewer waiver/extension requests as a percentage of federally insured state chartered credit unions (FISCUs) compared to Federal credit unions (FCUs). At the same time there was a larger percentage of FISCUs that were not one hundred percent renovated, as compared to FCUs. One large information system vendor with clients not fully renovated as of January 31, 1999, indicated that 43 of the 70 clients served by the vendor were FISCUs. The identified clients are potential candidates for an approved blanket waiver, but had not been previously identified as needing a waiver. While our review sample focused primarily on FCUs, the information mentioned above is troubling and indicates that increased attention may need to be devoted to FISCUs.

National and regional guidance regarding the waiver process were provided to the State Supervisory Authorities (SSAs) responsible for the regulation of FISCUs. In addition some SSAs have received training by NCUA staff. Regional staff maintain a close relationship with the SSA regarding safety and soundness and Y2K issues. The respective SSA is responsible to ensure Y2K readiness in state chartered credit unions. In some instances joint SSA and NCUA examinations and Y2K reviews are performed. During our review we saw no direct evidence of a lack of regulatory Y2K effort by SSAs in FISCUs.

MATTERS FOR CONSIDERATION

As a result of our limited review of the Y2K waiver process, the OIG is suggesting the following actions as matters for consideration by the NCUA Board and agency management:

- Waiver/extension actions should not be removed prior to the completion of the requested and approved action to ensure that action is completed.
- Develop stronger monitoring and follow-up documentation of waiver/extension actions.
- To decrease waiver/extension turnaround time and reduce backlog of actions, consideration should be given to decentralizing the individual credit union waiver process. Specific guidelines to ensure consistency in regional application and monitoring by the Office of Examination and Insurance should be utilized for quality control purposes.
- The Office of Examination and Insurance should continue to process and approve blanket waivers for information system vendors to ensure consistency of application. E&I should continue to delegate the assignment of individual credit union blanket waiver/extension dates to the regional offices since the regions are more familiar with the requirements of assigned credit unions.
- NCUA should place increased attention on the progress of FISCUs in order to identify and resolve Y2K problems in a timely manner.