Deloitte & Touche LLP
1750 Tysons Boulevard
McLean, Virginia 22102-4219

Tel: (703) 251-1000
Fax: (703) 251-3400
www.us.deloitte.com

Deloitte & Touche

INDEPENDENT ACCOUNTANTS' REPORT ON APPLYING AGREED-UPON PROCEDURES

To the National Credit Union Administration:

We have performed the procedures, enumerated in the Attachment to this letter, which were agreed to by the National Credit Union Administration (NCUA), solely to assist the NCUA Office of the Chief Financial Officer (OCFO) and the Office of Examination and Insurance (OEI) in the assessment of the process used in FY 2000 to determine the FY 2001 annual expense allocation from the NCUA Operating Fund to the NCUA Share Insurance Fund.

This engagement to apply agreed-upon procedures was performed in accordance with standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of NCUA. Consequently, we make no representation regarding the sufficiency of the procedures described in the attachment either for the purpose for which this report has been requested or for any other purpose.

The procedures we performed and our findings are presented in the **Attachment** to this letter.

We were not engaged to, and did not, perform an audit, the objective of which would be the expression of an opinion on the specified elements, accounts, or items. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of NCUA and is not intended to be and should not be used by anyone other than NCUA.

Deloitte & Touche LLP

September 5, 2001

ATTACHMENT

AGREED-UPON PROCEDURES AND FINDINGS

CONDUCT AN ENTRANCE CONFERENCE

We conducted an entrance conference with the National Credit Union Administration (NCUA) Office of the Chief Financial Officer (OCFO) and the Office of Examination and Insurance (OEI) personnel to initiate the engagement and to confirm the understanding of the requested tasks. We determined a preliminary time frame for the engagement and all deliverables.

Findings:

The following information was provided to us during the entrance conference.

NCUA is responsible for regulating and insuring all federally chartered and insures the majority of state chartered credit unions under the provisions of The Federal Credit Union Act, as amended. The NCUA OCFO is responsible for the accounting and budgeting of the Agency's activities including those of the NCUA Operating Fund, and the National Credit Union Share Insurance Fund (NCUSIF). The NCUSIF was established in 1970. The NCUA OEI provides national guidance for NCUA's efforts to assure the safety and soundness of federally - insured credit unions.

From 1986 to 2000, one-half of all operating expenses were funded by operating fees assessed to federally chartered credit unions, and the other half by a monthly transfer of expenses from the NCUA Operating Fund to the NCUSIF called the overhead transfer. During Fiscal Year (FY) 2000, the OEI completed a time survey that resulted in a calculated overhead transfer rate of 66.72% to be applied to the transfer of operating expenses to the NCUSIF effective for FY 2001. Operating expenses include agency payroll and benefits, employee travel expenses, rent/communications/utilities expenses, administrative expenses, and contracted expenses.

The overhead transfer rate was developed from time surveys, which identified the time spent on insurance - related functions versus regulatory - related functions. A selected number of NCUA field examiners, Regional employees, and Central Office employees completed these surveys. For field examiners, this entailed compiling time spent on insurance and regulatory - related matters during the course of a credit union examination. Examiner time was distributed across seven major examination categories. An insurance factor was then allocated to each category to determine the insurance - related portion of average examination time. A similar approach to distributing Regional and Central Office employees' time spent on insurance - related versus regulatory - related functions was applied.

Much of the agency's resources are expended on tasks that serve both insurance - related and non - insurance - related roles.

NCUA believes that the overhead transfer rate methodology is equitable and consistent with insurance – related activities. Additionally, NCUA believes the overhead transfer rate methodology does not benefit federal over state credit unions or vice versa. NCUA also noted that in addition to its primary responsibility to conduct insurance reviews, it also provides a service to state chartered credit unions such that the states do not have to pay for items such as new examiner training, new regulation training, writing regulations, computers for state examiners, etc.

ATTACHMENT

AGREED-UPON PROCEDURES AND FINDINGS

MEETINGS WITH REPRESENTATIVES FROM THREE INDUSTRY GROUPS

The engagement team met with representatives from NCUA and each of three industry groups, the Credit Union National Association (CUNA), the National Association of Federal Credit Unions (NAFCU), and the National Association of State Credit Union Supervisors (NASCUS), at NCUA's offices. The groups provided expressions of their respective views on the annual expense allocation methodology and execution, both verbally and in written form.

CONDUCT ON-SITE INTERVIEWS WITH OCFO PERSONNEL, OEI PERSONNEL, AND FIVE PARTICIPANTS IN THE SURVEY PROCESS

We conducted interviews with OCFO personnel, OEI personnel, and participants in the survey process. Specifically, we met with two individuals from OEI, one from OCFO, one Regional Office Director and four Principal Examiners who participated in the FY 2000 time survey. The purpose of the interviews was to further understand and document the methodology used for the allocation of expenses to NCUSIF for FY 2001, including the time survey process.

We initially met with a Risk Management Analyst from OEI in order to understand the survey process and how the overhead allocation rate was determined. To learn how the overhead allocation rate was applied to agency monthly expenses, we spoke with a representative of the OCFO. We also interviewed five survey participants, selected from examiners and headquarters personnel.

OBTAIN AND READ NCUA'S STATUTORY INFORMATION AND BOARD AUTHORIZATION MEMORANDA AUTHORIZING THE ANNUAL EXPENSE ALLOCATION PROCESS

We obtained and read applicable sections of the Federal Credit Union Act authorizing the payment of NCUA expenses incurred in the conduct of examinations and for the protection of the NCUSIF from the fees and assessments levied on insured credit unions. We also read the Board Authorization Memoranda authorizing and describing the annual expense allocation process and the Board Action Memorandum of October 19, 2000 relating to the FY 2001 overhead transfer rate as well as similar documentation from the two previous surveys

OBTAIN AND READ THE OEI DOCUMENTATION OF THE FY 2001 TIME SURVEY PROCESS

We obtained and read the OEI documentation of the FY 2000 time survey process, including instructions to participants, used in the conduct of the most recent annual expense allocation determination.

IDENTIFY AND LIST THE ASSUMPTIONS AND DATA SOURCES USED IN THE PREPARATION OF THE ANNUAL OVERHEAD EXPENSE ALLOCATION

We identified and listed the data sources and assumptions used in the preparation of the documentation of the annual expense allocation determination for FY 2001 by the steps in the allocation process.

ATTACHMENT

AGREED-UPON PROCEDURES AND FINDINGS

Step	Data Source	Assumption
Determined survey methodology (defined categories, sampling methodology, approach)	Enabling legislation, staff expertise	Definition of insurance and regulatory functions are clear.
E-mail sent out to introduce the survey to participants (note: survey occurs during the same time of year each time--during the summer months).	Enabling legislation, staff expertise	Since survey has been done in the past, it was felt that there was not a need for extensive training or explanation.
Hard copy Survey forms distributed to three categories of employees: Principal Examiners (PEs), Regional Staff, and Central Office (CO) Staff. Surveys mailed to PEs and Regional Staff.	Board Memorandum	For PEs, respondents were selected randomly from a pool of examiners with at least five years of experience. Experienced examiners more fully understand the distinction between regulatory and insurance - related issues. These individuals have better time management abilities as well. In past surveys, only PEs were surveyed; this time, the CO Staff and Regional Staff were surveyed as well.
Respondents provided estimates of total hours spent among general examination categories (PEs only). All participants surveyed estimated the time spent on insurance and regulatory related activities.	For PEs, they used most recent examinations. CO and Regional staff totals were estimated.	E&I had each PE complete two surveys to ensure data included federal credit unions (FCUs) representing different levels of risk to the NCUSIF (one for an institution with a CAMEL rating of 1 or 2 and the other of 3,4, or 5). Regional Staff gave estimates of the time they spent on regulatory and insurance - related tasks while carrying out their specific duties. CO Staff followed the same process as Regional Staff except that the managers were also asked to fill out the survey estimating the time their staff devoted toward regulatory and insurance - related issues during the year.
E&I collects hardcopy forms from PEs, Regional Staff, and CO Staff	Survey Forms	

ATTACHMENT

AGREED-UPON PROCEDURES AND FINDINGS

Step	Data Source	Assumption
Clerical staff inputs survey responses into a database.	Survey Forms	
E&I personnel do a reasonableness check on responses from PEs, Regional Staff, and CO Staff. No corrections were made.	Information in the database	Individuals experienced with the definitions and the roles and responsibilities of the various offices can determine range of reasonableness of responses.
Survey responses broken down by CAMEL rating and asset size to ensure population meets the proper survey sampling. E&I requested an even distribution of FCUs with high and low CAMEL ratings to ensure distribution was close to statistics for all FCUs.	Survey Forms	Average CAMEL composite rating is close to the national average for all credit unions and asset size is close to industry average.
Examination hours broken down by category and further broken down by insurance or regulatory related activities within each category. Total percentage of insurance related activities was calculated.	Survey Forms	
Weighted average transfer rate for PEs determined by utilizing the projected 2001 resource budget hours (percentage of time in each area of four key areas - FCU examination, FCU supervision, FISCU supervision, and the 5300 Program) and applying this percentage to the insurance related percentages as calculated from the time survey.	Survey Forms & FY 2001 Budget	Projected budget resources determined by estimated hours requested from each region necessary to conduct its program. The estimated hours are equated to FTEs. FCU examination and supervision insurance percentages were obtained through the survey. 100% was attributed to insurance - related for FISCU-related supervision and the 5300 Program.
Surveys of CO Staff information were summarized and insurance - related activities percentage was calculated.	Survey Forms	Used the estimates of time allocated for "other activities" and put this proportionally into insurance and regulatory categories.

RECALCULATE THE INFORMATION RESULTING FROM THE TIME SURVEY PROCESS

We compared the information resulting from the time survey process to the completed time surveys, and recalculated mathematical calculations. We noted six differences between the accumulated information resulting from the time survey process and the completed survey forms. The differences were due to keying errors and are described in the table below. The errors identified did not result in differences in the calculation of the expense allocation percentage.

Findings

Survey Area		***Error Identified***
Chatel Federal Credit Union		Asset Size entered as $78 million rather than $7.8 million
First Source Federal Credit Union		"T" entered rather than CAMEL Rating
Bolling Federal Credit Union		Date Completed entered incorrectly
RHR Federal Credit Union		Date Completed entered incorrectly
Examination Report/Joint Conference		Insurance Issues entered as 2 rather than 8
Examination Report/Joint Conference		Regulatory Issues entered as 8 rather than 2

COMPARE THE DEFINITIONS OF REGULATORY VERSUS SAFETY AND SOUNDNESS USED IN THE TIME SURVEY PROCESS TO INTERNAL AND EXTERNAL DOCUMENTATION

We compared the definitions of regulatory versus safety and soundness activities used in the time survey process to internal and external documentation as available, or to other supporting documentation obtained from the OCFO and OEI, including information provided during the meetings with the three industry groups.

Findings

The time survey definitions of regulatory versus safety and soundness (or insurance - related) activities used in the 2000 survey are adapted to the NCUA environment, which relies heavily on examiners being knowledgeable of the institutions they examine as well as the standards against which credit unions are being reviewed. Comparing the definitions between the 1994, 1997 and 2000 surveys indicates an increasingly greater level of detail for the two categories as well as more examples of the categories to assist the respondents in the 2000 survey. In addition, the "Administrative" category in the 1997 survey was removed in the 2000 survey.

The comparison indicates that NCUA's focus on risks to the NCUSIF from such dynamics as diversification, concentration and increasing asset size has been recognized in the survey process. Other areas of risk are being identified as well, as credit unions are authorized by the Board to provide new products and services. For example, "e-commerce" is one of the new means of conducting business now available to credit unions and is cited as an example in the "Operational Analysis" category.

AGREED-UPON PROCEDURES AND FINDINGS

COMPARE NCUA ASSUMPTIONS WITH AVAILABLE INDUSTRY PRACTICES

NCUA was created by Congress in 1970 as an independent agency responsible for supervising and regulating Federal credit unions and, separately in 1970, was assigned the responsibility for managing the NCUSIF. NCUA carries out both responsibilities with the same examiner workforce and with one examination process.

NCUA's situation is not directly comparable with the other federal financial institution regulatory agencies, because their responsibilities are generally more fragmented. Specifically, the Federal Depository Insurance Corporation (FDIC) manages a comparable federal deposit insurance program for banks, but does not have comparable federal supervisory and regulatory responsibilities to those of NCUA. The Office of Thrift Supervision (OTS), the Office of the Comptroller of the Currency (OCC), and the Federal Reserve System have supervisory and regulatory responsibilities, but do not manage insurance funds.

NCUA more closely resembles a multi-product company that uses the same manufacturing operation to produce multiple product lines. Such companies must allocate their operating costs among multiple products using cost allocation methods. NCUA's overhead transfer process is very comparable to the methods used by private industry to accomplish such cost allocation.

We did obtain some information regarding the FDIC, as follows. We compared NCUA assumptions with FDIC's practices and found little for useful comparison. We found that the FDIC distributes its costs across its four Funds: the Bank Insurance Fund (BIF), the Savings Association Insurance Fund (SAIF), the FSLIC Resolution Fund (FRF) – FSLIC and FRF - RTC) based on the charter of institution (thrift or bank) for which it has any responsibility. All expenses associated with FDIC activities, whether insurance or regulatory related, are attributed directly to the Funds. Deposits of BIF - member institutions are primarily insured by the BIF; BIF members are predominantly commercial and savings banks regulated by the FDIC, the OCC, or the Federal Reserve System. Examinations are performed by the various regulatory agencies that charter the institutions, not just FDIC. Deposits of SAIF - member institutions are primarily insured by the SAIF; SAIF members are predominantly thrifts supervised by the OTS. Outstanding work on failed savings and loans closed by the former FSLIC (prior to 1989) and RTC (up until 1996) are charged against the FSLIC - FRF and FSLIC - RTC funds, respectively. Given the unique, legally defined roles of the Funds, there are few transfers among the Funds.

A point of possible interest is the approach that FDIC is developing to gather, estimate and allocate its costs. We understand that FDIC does not use a survey of staff time devoted to various functions to determine its allocation of costs across the functions. Program Division management has determined in which twenty business processes its staff performs work and then distributes its total work effort against these processes. Each program code has a lead Division.

The business processes have unique relationships to the Funds and defined "drivers" per Division that determine in percentage terms how total costs associated with providing the services are to be charged against the appropriate Fund. For example, 80% of the Division of Insurance's (DOI) costs associated with supporting Risk Management under the Insurance

AGREED-UPON PROCEDURES AND FINDINGS

Program are attributed to BIF and 20% to SAIF. Moreover, each of these areas is tied to a goal in FDIC's strategic plan and specific general ledger (GL) codes to move FDIC toward an integrated budgeting, planning and accounting process.

As an example, FDIC has designated program codes for "Risk Management" in both its Insurance and Supervisory Programs. In its Insurance Program, both the DOI and the Division of Supervision (DOS) participate. Activities include identifying, analyzing, and reporting on current and emerging risks to the *respective* deposit insurance Fund (e.g., electronic banking) and evaluation of risks, financial conditions and economic factors affecting insured depository institutions. In this case, the "driver" for DOI is based on total domestic deposits for FDIC insured institutions, *excluding* deposits residing in foreign offices, as a percentage of total insured deposits. For DOS, the "driver" is defined as the total domestic deposits at FDIC insured institutions.

Under FDIC's Supervision Program, there are two other program codes for "Risk Management," one for safety and soundness and one for compliance and enforcement. The latter specifically identifies compliance with consumer protection laws and regulations, fair lending and the Community Reinvestment Act (which does not apply to NCUA) and is managed by the Division of Consumer Affairs. The former includes examinations, site visitations, and EDP and trust examinations for a given institution undertaken by DOS.

Various other Divisions and Offices support these programs to a lesser degree than the main Division and spread their costs more directly. For example, overhead costs associated with personnel or other resources (e.g., Legislative Affairs, Human Resources) devoted to general activities are distributed across the Funds based on how much effort these areas support the line functions (i.e., whether for banks or thrifts). This is true for the Office of the Chairman as well.

OBSERVATIONS FROM INTERVIEWS CONDUCTED WITH SURVEY PARTICIPANTS

During our interviews, we found that most individuals felt that they were estimating the percent of time they spent on regulatory and insurance - related activities. In particular, the Principal Examiners found that it was difficult to allocate time spent after the fact and felt that having an opportunity to review the survey's content prior to performing examinations would be beneficial. In addition, we also learned that the definitions of insurance versus regulatory - related activities were not always clear. We have developed some observations that NCUA may wish to consider for future surveys.

Observations

Communication of Survey Process and Results

- Develop strategy for conveying growing focus of NCUA on insurance - related matters to trade associations.
- Have NCUA senior management convey the importance of the survey to NCUA personnel to facilitate accountability and cooperation.
- Consider tools such as Web conferencing in communicating with industry and NCUA personnel.

ATTACHMENT

AGREED-UPON PROCEDURES AND FINDINGS

Frequency/Timing of Survey

- Vary time of year that the survey is taken (either over the course of the year or earlier in year).
- Incorporate surveys (or time accumulation forms) into NCUA's automated examination system.
  - PE or examiners can complete the survey while on-site and their experience is more recent.
  - This will preclude a late in fiscal year survey that may conflict with other examiners and headquarters personnel responsibilities.

Methods of Survey Distribution

- Conduct on-line training, perhaps as part of examiners' training.
- Consider automating time accumulation sheets to break down each examination by regulatory and insurance hours per exam (could reduce cost of gathering data).

Update of Survey Definitions and Purpose

- Update the definitions of insurance - related and regulatory - related activities; reduce the "Other" category, where possible.
- Provide examples.
- Provide a help - line for questions.
- Provide a list of frequently asked questions (FAQs) on intranet (if available).

*****