

## Chapter 102

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# CORPORATE CREDIT UNION SUPERVISION AND EXAMINATION PROCESS

### Introduction

The Office of Corporate Credit Unions (OCCU) fulfills its mission by promoting and ensuring the safety and soundness of the Corporate Credit Union System (System) principally through a program of continual supervision. Supervision includes, but is not limited to, the on-site examination of corporate credit unions (corporates) resulting in an examination report. Supervision entails vigilance encompassing all regulatory efforts to formulate, implement, and maintain an ongoing process to ensure that:

1. Corporates report their condition in a timely and comprehensive manner;
2. OCCU evaluates and reports the condition of corporates;
3. Corporates correct deficiencies in a timely manner; and
4. The System remains safe and sound.

### OCCU's Supervision Goal

OCCU's overall supervision goal is to ensure the safety and soundness of the System by (1) continuously evaluating and supervising the financial condition and performance of individual corporates and their service organizations, and (2) reporting those conditions to the NCUA Board in a timely manner. OCCU provides high-quality "targeted" supervision. The key element in accomplishing OCCU's goal is the timely identification and resolution of any problem or condition that may have a material impact on a corporate, the System, or the National Credit Union Share Insurance Fund (NCUSIF).

OCCU's efforts are focused on (1) identifying existing and/or emerging material problems in individual corporates and/or the System, and (2) ensuring such problems are corrected in a timely and appropriate manner. Since accepting risk is inherent to the business of the System, OCCU's philosophy is centered on evaluating risk.

OCCU applies this philosophy in all its supervisory activities. OCCU combines the structure of consistent supervision with reasoned flexibility to ensure its procedures are appropriate for both the corporate and the dynamic, evolving marketplace in which it operates. Flexibility allows examiners to adjust the supervisory effort to meet the risks posed by a particular corporate while ensuring risks are addressed throughout the System.

### **Elements of the Supervision Process**

Regardless of the approach taken, effective supervision includes, at a minimum, the following elements:

1. Performing high quality annual examinations of all corporates that accept deposits from any federally insured credit union, whether federal or state chartered;
2. Conducting periodic or continuous on-site reviews of corporate activities based on the degree of existing or perceived risk they undertake;
3. Conducting monthly off-site reviews of corporate activities through review of financial and management reports including operating budgets and strategic plans; and
4. Conducting monthly reviews of corporate financial data (NCUA 5310 reports) to determine trends in individual corporates and the System.

In conjunction with its efforts to implement these four elements, OCCU communicates with State Supervisory Authorities (SSA) to coordinate an overall supervision plan. Agreements with SSAs are contained in Chapter 104 and may be supplemented by special agreements with individual SSAs. Examiners should familiarize themselves with any agreements prior to initiating a contact with the SSA to discuss supervision and examinations plans.

### **Targeted Risk Approach**

OCCU employs targeted risk procedures to ensure the examination scope appropriately focuses resources toward areas of material risk. While all areas of risk are addressed, an appropriate examination plan may utilize one or more of the following techniques:

1. Allocate examination hours based on perceived risk the examination areas pose and the extent and results of prior years' review of the area;
2. Prioritize areas for a comprehensive review once every two or three years (depending on risk) unless there is a demonstrable need for more frequent or thorough review; and
3. Use examination procedures that test the quality of managerial supervision of the area, reliability of the area's internal controls, and the quality of oversight provided by the board of directors and its auditors.

Targeting risk requires examiners to determine how existing or emerging situations confronting a corporate, or the credit union industry, affect the nature and extent of risks in that institution. The examiner then structures supervisory plans and actions based on the corporate's risk profile. The Targeted Risk approach provides flexibility for the examiner to prioritize the use of resources toward the areas of greatest risk. It officially sanctions the ability and elevates the responsibility of the examiner-in-charge (EIC) to prioritize procedures for resource maximization.

OCCU recognizes corporates must take risks to earn a return. Risk levels, however, must be appropriately identified, measured, monitored, reported, and controlled. The significance of risks must be continually evaluated.

Corporate management is responsible for controlling risk. OCCU assesses how well a corporate manages risk over time, rather than at a single point in time. Targeted risk procedures focus on the oversight rather than an audit role. Targeted risk allows OCCU to concentrate on systemic risks and institutions that pose the greatest risk to the System and the NCUSIF.

OCCU's targeted risk approach identifies areas that, in the aggregate, pose the potential for presenting an unacceptable level of risk to the System and the NCUSIF. To address high-risk activities that can be influenced by market conditions, OCCU's goal is to communicate with, and influence, the System through direct supervision, policy, and NCUA regulation. In situations where corporates are not properly managing risks, OCCU uses appropriate means to influence management to adjust its practices to conform with sound business practices.

### Inherent Risks

Some risks are inherent to the System. A wide body of knowledge exists within the System on how to identify, measure, monitor, report, and control these inherent risks. Targeted risk acknowledges these inherent risks and evaluates whether they are properly managed. Other risks in the System are more diverse and complex. These more sophisticated risks require enhanced controls and monitoring by both the corporate and OCCU. OCCU is committed to focusing its resources on these complex and evolving risks, especially when they present material actual or potential risks to the System.

### Supervisory Response to Degree of Risk Exposure

Risks that large corporates assume are generally diverse and complex and warrant a targeted risk approach. Under this approach, examiners do not attempt to eliminate appropriate risk-taking, but rather ensure corporates understand and control the levels and types of risk they assume. In situations where risk is not properly managed, OCCU will direct management to take corrective action so the corporate is managed in a safe and sound manner. In all cases, OCCU's supervisory focus is to determine that management identifies, measures, monitors, reports, and controls risks to ensure sufficient capital is present in relation to the corporate's risk activities.

"Pass-through" corporates (those which primarily rely on another corporate for investment placement and product offerings) are generally less diverse and complex than those which deal directly in the financial marketplace. Regardless of each corporate's complexity,

the targeted risk approach still emphasizes that all risks be adequately managed.

### Targeted Risk Approach

The Corporate Examiner's Guide stratifies targeted risk within base, standard, and expanded examination procedures as discussed in Chapter 101.

A crucial element of the targeted risk approach is the EIC's pre-examination risk assessment of the corporate. (The framework for this process is described in Appendix 102A entitled "Application of the Targeted Risk Approach in the Identification, Measurement, and Assessment of Risk.") During this assessment, the EIC determines and documents the level of supervisory concern for each risk category. Having prioritized the corporate's risk exposure, the EIC selects and documents a detailed examination scope. A determination not to use the standard examination scope will be documented. Advance Corporate Field Supervisor (CFS) approval is required for using anything other than the standard examination scope. While implementing the examination scope as part of the on-site field work, the EIC may determine expanded or base review procedures are more appropriate. These situations should be discussed with the CFS before the examination scope is adjusted.

### Targeted Risk Summary

The Targeted Risk approach allocates greater resources to those areas with higher risks. OCCU accomplishes this by:

1. Identifying risks using common definitions. This set of risks forms the basis for supervisory assessments and actions;
2. Measuring risk based on common evaluation factors. Risk measurement is not always quantified in dollar terms; it is sometimes a relative assessment of exposure. For example, numerous internal control deficiencies may indicate a corporate has an excessive amount of transaction risk;

3. Evaluating risk management to determine if the corporate's systems adequately manage and control risk levels. System sophistication will vary based on the level of risk present and the size and/or complexity of the institution;
4. Assigning greater resources to areas of higher or increasing risk, both within an individual institution and among corporates in general; and
5. Performing examinations based on risks, reaching conclusions on risk profile and condition, and following up on areas of concern.

To accomplish these tasks, examiners will discuss preliminary conclusions with corporate management and adjust conclusions and strategies based on these discussions, as appropriate. OCCU can then target supervisory efforts on significant risks.

The targeted risk approach provides OCCU and the System with:

1. A high level of consistency in supervision by using minimum core procedures;
2. An allocation of resources based on risk;
3. Sufficient flexibility to allow examiners to tailor the supervisory effort to the risks present;
4. Less supervisory review of low risk areas; and
5. Help in determining the sufficiency of each corporate's capital level and risk management system.

### **Planning**

Examination/supervision planning is the process of identifying and establishing supervisory goals and objectives for incorporation into OCCU's supervisory strategy for each corporate. On-site examinations, supplemented by on- and off-site supervision activities, are the means by which OCCU's supervisory strategies are implemented and its supervisory goals and objectives are achieved.

The targeted risk approach ensures that OCCU's resources are efficiently used by establishing appropriate examination procedures, and developing appropriate guidelines for OCCU personnel to follow when completing assignments.

Examination/Supervision Planning

OCCU's supervision policies require a specific supervisory strategy for each corporate. The strategy includes detailed, planned supervisory activities. Planning normally begins at the conclusion of a full-scope, on-site examination with the completion of the three-year plan (TYP). Reference should be made to Appendix 102C for OCCU's format and content requirements for TYPs and additional discussion in the section below (Developing and Examination/Supervision Plan).

On-going Modification of Examination/Supervision Plans

Examiners perform ongoing supervision and periodic follow-up activities throughout a supervision cycle to identify and assess risks and changing conditions. As supervisory strategy is dynamic, EICs and CFSs should review examination/supervision strategies and revise or update them to reflect the corporate's changing risk profiles, developments in the System, and regulatory changes. Examiners should discuss any approved changes to examination/supervision plans with corporate management.

Developing an Examination/Supervision Plan

Examination/supervision of individual corporates is tailored to conditions and needs according to OCCU policy. This approach balances consistency with flexibility. Annual examination/supervision plans for each corporate are developed as follows:

1. Budget - In conjunction with preparing OCCU's budget, each CFS will recommend to the OCCU Director (Director), the category Type of supervision (discussed below) planned for each corporate during the next examination cycle. The CFS consults with examiner staff before making a recommendation. The Director approves the type of supervision recommended (i.e., assuming agreement with the recommendation), subject to NCUA Board budget approval;
2. TYP - After each annual examination, the CFS and the EIC will develop the corporate's supervision and examination scope for the forthcoming year, and contingent plans for the subsequent two years (three years total). The TYP addresses what needs to be

- accomplished and outlines the most efficient and effective method for achieving the goals established in the TYP. This includes use of base, standard, and expanded examination procedures (Chapter 101). The plan should also include any on-site visits to monitor operational changes (e.g., software, key staff, and conversions.) The TYP will be submitted to the Director for approval; and
3. The CFS and the EIC will monitor implementation of the plan on an ongoing basis, notifying the Director of any needed changes/revisions.

### Supervision Types

Based on the criteria listed below, each corporate is assigned a supervision type category. The supervision type of each corporate is a key component of the target risk supervision approach and provides standard on- and off-site supervision strategies, based on each corporate's established supervision type. OCCU staff may vary the from the supervision strategies for each type if approved by their CFS and the Director.

A corporate's assigned supervision type is not a rigid function of asset size, expanded authority level, or Corporate Risk Information System (CRIS) rating. Rather, it represents a combination of factors that may include these elements in addition to perceived risk levels, quality of or changes in management, financial condition, trends, etc.

#### Type I

Type I corporates do not have expanded authorities above the Base Plus level.

Supervision of Type I corporates includes:

1. Monthly off-site monitoring by the EIC.
2. Ongoing monitoring of NCUA 5310 report data and trends, as well as monthly verification of data by the EIC.
3. Examination and on-site supervision:
  - a. Risk Management and Financial Risk rated either 1 or 2:

- 1) Annual Examination
  
- b. Risk Management and/or Financial Risk rated no worse than a 3:
  - 1) Annual Examination
  - 2) Semiannual on-site follow-up contact
  
- c. Risk Management or Financial Risk rated 4:
  - 1) Annual Examination
  - 2) Semiannual Examination
  - 3) Quarterly on-site follow-up contact
  
- d. Risk Management and Financial Risk rated 4:
  - 1) Annual Examination
  - 2) Semiannual Examination
  - 3) Monthly on-site follow-up contact

Type II

To qualify for Type II supervision, corporates must generally exceed \$1 billion in assets, and/or have expanded authorities above the Base Plus level and exercise its approved powers in a significant and assertive manner. Additionally, Type II corporate have complex and innovative operations, and/or have significant impact in the marketplace, and/or present unusual or unique examination and supervision problems that cannot be adequately addressed by Type I supervision.

Supervision of Type II corporates includes:

- 1. Monthly off-site monitoring by the EIC.
- 2. Ongoing monitoring of NCUA 5310 reports, as well as monthly verification of data by the EIC.
- 3. Examination and on-site supervision:
  - a. Risk Management and Financial Risk rated either 1 or 2:

- 1) Annual Examination
  - 2) Monthly one or two week on-site contact by EIC
- b. Risk Management and/or Financial Condition rated no worse than 3:
- 1) Annual Examination
  - 2) Semiannual follow-up Examination
  - 3) Monthly one or two week on-site contact by EIC
- c. Risk Management rated 4 and Financial Risk rated 3:
- 1) Annual Examination
  - 2) Semiannual Examination
  - 3) Monthly two week on-site contact by EIC
- d. Risk Management rated 3 and Financial Risk rated 4:
- 1) Annual Examination
  - 2) Semiannual Examination
  - 3) Monthly two week on-site contact by EIC
  - 4) Weekly review of financial deficiencies
- e. Management and Financial Condition rated 4:
- 1) Annual Examination
  - 2) Semiannual Examination
  - 3) Full time, on-site presence

### Type III

Corporates which qualify for Type III supervision, generally, have billions of dollars in assets, and/or have expanded powers in excess of Part I and exercise their approved powers in a significant and assertive manner. Additionally, Type III corporates have complex and innovative operations, and/or have a significant impact in the marketplace and on the corporate and/or credit union system, and/or present unusual or unique examination and supervision problems, which cannot be adequately addressed by Type I or Type II supervision.

Supervision of Type III corporates includes:

1. Monthly off-site monitoring by the EIC.
2. Ongoing monitoring of NCUA 5310 report data and trends, as well as monthly verification of data by the EIC.
3. Examination and on-site supervision - regardless of Risk Management and Financial Risk ratings:
  - a. Incremental annual examination, scoped with two separate contacts (i.e., typically investment and ALM phase and an operational risk phase)
  - b. Full time presence by on-site examiner, not necessarily the EIC
  - c. Monthly on-site EIC contact

For incremental examinations, the CRIS ratings are normally assigned after the operational examination phase. However, OCCU staff has the flexibility to adjust CRIS ratings after any examination phase. These situations should be discussed with the CFS, and if appropriate, the OCCU Director.

## **Examinations**

### **Scheduling Examinations**

Annual examinations are required and performed for all corporates. On-site follow-up examinations and supervisory contacts are performed consistent with the corporate's supervision category. Appendix 102B provides a timeline for completion of examination related activities.

### **Examination Teams**

Examinations are performed by examination teams, composed of an EIC and one or more team members. The EIC and team members are assigned by the CFS based on a variety of factors such as corporate complexity, examiner experience, examiner proximity to the corporate, and scheduling considerations. Appendix 102F, Reduced On-Site Examinations (ROSE) also impacts examination team planning.

### **Examination Steps**

An examination entails a number of steps in planning and execution. These steps generally include:

1. Off-site pre-examination planning;
2. On-site pre-examination preparation;
3. Examination field work;
4. Exit briefing;
5. Report writing;
6. Joint conference; and
7. Wrap-up.

### **Pre-Examination Planning**

Prior to each examination, the EIC has responsibility to plan the on-site (field) examination work. This planning effort is accomplished during a period referred to as pre-examination. The pre-examination effort may be accomplished both on- and off-site, by the EIC.

By necessity, pre-examination planning is conducted approximately 45 - 60 days in advance of the examination, and generally requires from three days to one week to complete. Pre-examination planning is an opportunity for the EIC to:

1. Make team participant lodging arrangements;
2. Arrange for corporate management to complete and return to the EIC, the Pre-Examination Questionnaire (OCCU 102Q);
3. Develop the preliminary examination scope and time budget;
4. Prepare a memorandum to team participants regarding their participation on the examination; and
5. Prepare a letter to the corporate being examined to communicate the dates of the on-site examination, the exit and joint conference dates and times, to provide them with the information request list, and to request arrangement for review of the annual audit work papers.

Factors to consider in the pre-examination planning process:

1. Attain goals and objectives - The examination effort should be directed toward attaining the supervisory goals and objectives that were previously identified and established during the examination/supervision planning process. (e.g., TYP, pre-examination questionnaire, monthly management reports.)
2. Develop scope - Examination procedures contained in the individual programs are designed to be comprehensive and target risk areas. Therefore, it is important appropriate procedures are selected within each program.
3. Plan for optimum productivity - The EIC should plan opportunities for meetings with examination staff and corporate personnel, arrange adequate workspace for the examination team, and prioritize and schedule workflow.
4. Make assignments and monitor job - The EIC must determine the expertise necessary to perform certain aspects of the examination and make assignments accordingly. When assigning more than one individual to an area, it is recommended that a team leader be assigned who will be responsible for its completion. Training and development needs should also be considered when making examination assignments.
5. Budget and monitor overall time - The EIC must consider the time budget when assigning tasks. A useful tool for improved personnel planning is a time and planning summary organized according to sections of the examination. Such a summary specifies areas for which procedures are planned and provides a comparison of actual and budgeted hours. As the examination progresses, the time budget should be modified as deemed appropriate.
6. Assign priorities - The EIC assigns priorities to each area. Ordinarily this can be accomplished by assigning related areas to one team leader who subsequently coordinates the work of others.
7. Schedule examination - To minimize costs and disruption to the corporate, it is important that the examination be conducted as quickly as practical. It is the responsibility of the EIC to discuss any planning problems with the CFS. If corporate management is concerned about scheduling, this matter should also be discussed.

Pre-Examination Questionnaire (OCCU 102Q)

This questionnaire contains questions detailing the nature and complexity of the corporate's operations and internal controls. It is designed to assist the EIC in planning examination procedures and resources. It should be completed as one of the first steps of the Pre-Examination planning effort. Ideally, it should be prepared by corporate management or by the EIC during an interview with corporate management.

### **On-Site Pre-Examination Preparation**

Examiners utilize on-site examination preparation time to accomplish several purposes:

1. Review the Pre-Examination Questionnaire which management has completed at the EIC's request and make any necessary changes in the preliminary scope;
2. Ensure management fills the items listed in the information request list so they will be available when the examination team arrives;
3. Ensure adequate work space is available for the team; and
4. Review the work papers supporting the annual audit.

On-site examination preparation efforts are generally performed during the first few days of the week preceding the on-site arrival of the examination team (first day of examination field work). This timing allows the EIC to review information provided by management pursuant to the pre-examination request, make any necessary changes in the preliminary scope, and follow-up on any requested information management has yet to make available.

### **Examination Field Work**

Depending on the size and complexity of the corporate, an examination usually entails two to three weeks of on-site field work. The duration of a Type III incremental examination may vary.

During this period, the examination team gathers information and performs procedures as outlined in the examination scope.

### **Managing An Examination**

Managing an examination is as important as planning it. The level and sophistication of management methods and procedures varies depending on the activities to be performed and the size and nature of the corporate. The EIC carries the responsibility for managing the examination.

Inherent in the EIC's responsibilities is ensuring supervisory objectives are met and activities are completed timely. To accomplish these goals, the EIC must continually monitor the progress of the examination and supervise, coordinate, and evaluate the work flow.

Key elements the EIC should consider during the course of the examination are:

1. Communicate examination objectives – The EIC must ensure that examiners understand the objectives of the examination and their assigned programs. Examiners should notify the EIC as questions occur regarding scope or depth of review. Examiners should not vary from standard examination procedures unless the EIC determines that such procedures are necessary to address potential risks. Ongoing communication between the EIC and team participants is critical to effective examination management;
2. Monitor staff performance - Examiners' performance must be monitored throughout the examination to ensure objectives are being met according to schedule and to prevent problems from developing. It is also important to avoid material deviations from the examination scope into unplanned activities. Early identification of work-related problems also allows examiners the opportunity to correct mistakes and to immediately improve skills;
3. Monitor the examination - Monitoring the examination's progress allows early adjustments to the scope, staffing, and completion date, as necessary. The EIC must notify the CFS if examination scope adjustments are necessary;
4. Training and evaluating examiners - Examiners may frequently need guidance, depending on their experience and ability. Questions should be encouraged and the EIC is responsible to ensure someone is available to provide guidance;
5. Communicate effectively - The EIC must maintain effective communications with the CFS, corporate management, the SSA, and examiners regarding the examination's progress;

6. Complete work papers - Prepare, file, index, and review work papers to facilitate efficient preparation of the examination report; and
7. Out-brief examiners - The out-briefing process is critical to the conclusion of the on-site examination effort. As the field work draws to a close, the EIC must have a complete understanding of the work performed and issues identified by each team member. Ideally, the EIC will monitor all team members' activities during the examination so the out-briefing is minimal. The out-briefing should provide an orderly transfer of examination materials, such as work papers, reference material, time sheets, etc., from the participant to the EIC or the EIC's designee. The EIC should also be informed of any additional items requested during the examination that should be added to the request list for the next examination.

#### Work Paper Documentation

Integral to the targeted risk approach is its system of work papers designed to assist the EIC in examination planning, coordinating, observing, understanding, critiquing, reporting, and follow-up. Overall, examination work papers provide efficient vehicles for the examiner to report both the understanding obtained and concerns identified.

Required work papers for each examination include:

1. A Corp110 form identifying the ratios, CRIS ratings, time spent, and problem areas;
2. National Credit Union Administration Examination Report, OCCU 102B and OCCU 102C - These forms are the standard report letter page for the distribution of an examination report. OCCU 102B is utilized for a report to a federally chartered corporate credit union and OCCU 102C is used for a state chartered corporate credit union. These forms list the procedures used during and objectives of the examination, cite the responsibility of the board of directors and management, and provide instructions on how to address the report's findings;
3. Executive Summary, OCCU 102D - The Executive Summary summarizes the examiner's review, analysis, and findings in major

areas of the corporate's operation, financial condition, management, and CRIS ratings;

4. Supplementary Facts, OCCU 102E - The Supplementary Facts is used to discuss material facts or situations not contained in other narrative sections of the examination report or to expand on Executive Summary discussions. This form is optional;
5. Document of Resolution (DOR), OCCU 102F - This form is designed to record and report the findings, issues, and actions needed to correct findings for issues of major importance. Matters presented on this form must represent violations of law, regulation, policy, and/or must constitute a material safety and soundness issue. As OCCU 102F issues are identified, examiners should:
  - a) Confirm their understanding of the facts and circumstances surrounding the issue and the corresponding basis for the exception;
  - b) Prepare the OCCU 102F; and
  - c) Report the finding and provide a copy of the OCCU 102F to the team leader (if any) and the EIC.

The EIC should seek management's agreement for action plans, responsible parties, and the time frame for resolving DOR issues. However, sometimes management's time frame may be inadequate to bring out regulatory compliance or adequate management of risks. Nevertheless, due dates should be reasonable and attainable and due dates not met will require additional correspondence between the OCCU/SSA and the corporate. OCCU/SSA must officially approve all due date changes after the final report is presented;

6. Other Examiner's Findings (OEF), OCCU 102G - The examiner has broad latitude regarding the documentation of issues, which do not merit inclusion on the OCCU 102F. The OCCU 102G has been devised to serve as a vehicle to report issues about which the examiner has a concern, but which are not material and are not appropriate for inclusion on the OCCU 102F.

OCCU 102G issues should be discussed with departmental management as they are identified during the examination. This form will be provided to the corporate's directors no later than the conclusion of the joint conference. Normally, it will not be

included in the official examination report. However, with the concurrence of the CFS, the examiner may include the form with the report if the number of non-material items, when considered as a whole, will have a material impact on the overall evaluation of any component of either the financial risk or risk management rating. When it is included as a part of the report, the examiner will explain the reasons to the corporate's board. The Executive Summary will detail to the officials whether this form is included in the examination report or handed out separately;

7. Trends on the Consolidated Balance Sheet Report (CBS, a product of the 5310 System) – The CBS is generated and analyzed during each examination and it, or a similar financial trend work paper is included in the examination report. The CBS provides monthly balance sheet, income, and ratio trends;
8. Procedures and Questionnaires - These forms are developed as part of the examiner's review responsibilities. The examiner should ensure that adequate comments are made as appropriate. The comment should be descriptive enough for a reviewer to draw a conclusion. Repetitive comments in the examination procedures, questionnaires, or Corporate Examiner Memorandums (CEM) should be avoided or at least minimized;
9. CEM, OCCU 102H - This form is developed as part of the examiner's Observation/Reviewing responsibilities. The examiner develops a thorough understanding of assigned processes as they are uniquely implemented in the corporate being examined.

OCCU 102H should be a professionally written document that outlines the review area. The document should not contain non-verified information or hearsay. The document is presented to the corporate for accuracy and verification of the examiner's understanding of the policies, procedures, and practices. OCCU 102H is designed to be carried forward from year to year and updated/revised only as necessary to reflect any changes to the operation that have been made since the prior examination. Concluding each OCCU 102H is a brief narrative overview summarizing the examiner's conclusions regarding the operational status of the area reviewed. This should be a conclusions reached memorandum - not a listing of the review steps the examiner accomplished;

10. CRIS, OCCU 102I - This form is used to support the CRIS ratings (See Chapter 401) assigned by examiners during the examination. From this form, the EIC will derive the composite and component CRIS ratings which will be included in the Executive Summary, OCCU 102D. The SSA may have a separate rating or may use the CAMEL rating system for state chartered corporates;
11. Confidential Section, OCCU 102J - The Confidential Section is for NCUA's internal use only. However, situations exist when all or part of a report's Confidential Section may be released by court order or in compliance with a Freedom of Information Act request. The possibility of release should not dissuade examiners from presenting necessary information; however, examiners should maintain their professionalism and objectivity when writing the Confidential Section.

Examiners are to report corrective and constructive work accomplished during the examination in the Confidential Section if not included in the open sections of the report. Examiners should comment briefly but completely enough to clearly reflect actions taken. Of particular importance is an explanation of what the examiner accomplished during discussions with officials and management. If not discussed elsewhere in the report, the Confidential Section should state what formal actions the board took and how the officials will handle major problems. At a minimum, this form should report:

- a. Advanced meetings with management;
- b. Joint conference;
- c. Deviations from scope and budget;
- d. Date of problem code assignment and elimination;
- e. Report distribution;
- f. Transmittal letter dissemination; and
- g. Recommended follow up.

Examiners should include in the Confidential Section pertinent matters of a private or restricted nature, including professional opinions based on the examiner's observations. However, the examiner should not make statements based on gossip or hearsay;

12. Other examiner-designed work papers - Examiners are authorized and encouraged to use their professional judgment in devising

unique work papers to supplement core work papers for the assigned area of review. However, excessive documentation should be avoided and such work papers should only include information that is relevant and/or may require follow-up. Time spent recording extraneous information is better spent examining high-risk areas; and

13. Electronic database storage – The final examination report, CEMs, procedures, questionnaires, and custom work papers will be submitted to OCCU mail for electronic filing. All OCCU staff will ensure they abide by all policies and guidelines in maintaining and transmitting sensitive examination information (i.e., use NCUA computers, the VPN, etc.).

### **Exit Briefing**

The exit briefing with corporate officials and management will be held at the conclusion of the examination fieldwork. The EIC must verify that all officials have been invited to attend the exit briefing. It is up to the board members (not operating management) to decide which officials will be in attendance. It is up to the discretion of the EIC what will be discussed during the exit briefing (e.g., DORs, OEFs). The EIC must have sufficient understanding of the issues to proficiently discuss them during the exit briefing.

### **Report Writing**

Depending on the size and complexity of the corporate and/or deficiencies noted during the examination, the EIC is afforded one week to consolidate, review, and analyze the team's work papers and prepare and submit a draft report for supervisory review. It is expected that the draft report will be a professional product, void of grammatical, punctuation, and spelling errors. The draft report will be sent to the CFS and SSA (if applicable) for review and finalization.

While writing styles will vary, the EIC should ensure the examination report discusses facts, expresses OCCU's assessment of the various risks or issues, and provides closure for the issue at hand.

### **Joint Conference**

The joint conference is usually scheduled as part of the pre-examination planning process. The joint conference should be set to accommodate the corporate, OCCU, and the SSA. Regularly scheduled board meetings usually work; however, special meetings may need to be called. A visual aide must be used for each joint conference. This could include power point, flip charts, handouts, etc. The joint conference must be a professional meeting held to summarize the financial condition of the corporate and examination findings. The ratings of the corporate will not be disclosed until the end of the joint conference.

OCCU attendees at the joint conferences are normally provided advance notification via an information memorandum developed by the EIC. A sample of this memorandum is shown in Appendix 102D.

### **Wrap-Up**

After the joint conference the EIC will finalize the examination work papers and necessary forms. This includes:

1. Finalizing the confidential section;
2. Finalizing the transmittal letter to the corporate, region memorandum (see Appendix 102E), and SSA memorandum;
3. Preparing a TYP per this chapter, including establishing the scope for the next 12 months supervision;
4. Sending a zip copy of the database to OCCU;
5. Uploading the Corp110;
6. Sending work papers to OCCU, CFS, and SSA (if requested); and
7. Updating all other forms/logs required by OCCU (e.g., CUSO Logs, Privacy Checklist), if applicable.

## **Supervision**

### **On-Site and Off-Site Supervision Process**

Corporates are an integral part of the System and the credit union industry. Additionally, they have the ability to take risks in the management of their assets as they provide services to their members. Due to the complexity and inherent importance of corporates, on-going supervision is needed to ensure the safety and soundness of

individual corporates and the System. Effective and continuous review of a corporate's operations is an essential part of the supervision process.

### Files

EICs maintain field files for each corporate in their district. These files should include not only documents, analysis, and reports related to previous examinations and supervision contacts, but also current policies and procedures for all critical areas of operation. The files should be well organized to ensure their efficient use and, when necessary, their orderly transfer to other OCCU staff. It is imperative that hard and electronic examination information be formally and safely maintained and transferred. The following minimum information should be maintained:

1. Permanent file (containing a history of examination reports, regulatory information, critical correspondence, etc.);
2. The last one or two complete examination work papers;
3. Supervision contacts during the examination period;
4. Board and ALCO packages for the examination period;
5. Current budget and strategic plan;
6. Examination period correspondence; and
7. Monthly management reports, 5310s, and Corp110s.

### Information Received

To supplement the files maintained, each EIC will receive monthly board and ALCO packages from corporates in their district. The packages, at a minimum, should include the following:

1. Monthly board and committee minutes with supplemental attachments (e.g., proposed policies, individual new product business plans, status of DOR and OEFs);
2. ALM reports (e.g., NEV, spread analyses, and book of business);
3. Financial statements, including a delinquent loan report;
4. Audit and internal control reviews completed;
5. Budget comparisons; and
6. Current lists of investments and new investments purchased during the month.

The examiner must verify DORs are completed within the agreed upon due dates. The examiner will initiate necessary correspondence, which includes correspondence from the Director and SSA (if state chartered), if due dates will not or have not been met.

### **Analyses Performed**

While conducting on-site and off-site supervision contacts, the EIC will perform, at a minimum, specific supervision functions. The following supervision tasks are key to determining whether an immediate on-site contact is required, the current on-site contact is expanded, and the scope of the next examination or supervision contact.

1. Analyze financial trends;
2. Ensure timely compliance with the previous examination report's DOR and OEF;
3. Assess management changes (e.g., board of directors, senior management, and other key employees);
4. Assess changes to MIS systems or major related systems (e.g., item processing);
5. Monitor and analyze changes in the investment portfolio and ALM strategies;
6. Review and verify for accuracy financial information submitted monthly by corporates, via the 5310 system; and
7. Review all material changes in policies, procedures, practices, and operations.

### **Other On-site Supervision Contacts**

Other situations could warrant an on-site contact. This could be completed by the district examiner or with a team of examiners. The following situations could warrant an on-site contact:

1. CRIS rating - to follow-up on the status of completing DORs and correcting OEFs;
2. Expanded Authority Request (EAR) - to evaluate the EAR and prepare for the OCCU Director and/or NCUA board action and SSA concurrence, if required;

3. Request for NCUA board action - to evaluate the corporate's request and prepare for the board action;
4. Senior management change - a change in senior management could warrant a contact to verify accuracy of reports and overall condition of the corporate; and
5. Addition or deletion of a service - a purchase or sale of a service or a fixed asset that could have a material impact on the membership.

In all situations the examiner should prepare appropriate documents supporting the contact. This could include a contact memorandum documenting work performed, status reports for DORs and OEFs, and appropriate documents for requested actions.

If appropriate, CRIS ratings can be reevaluated during a supervision contact. Ratings will be changed, as deemed appropriate, based on favorable/deteriorating financial, managerial, and/or operational factors. OCCU reserves the right to change CRIS ratings, as warranted, with the concurrence of the OCCU Director.

## **Examination Objectives**

### **Examination Planning and Control Objectives**

1. Prepare for supervisory activities, including the on-site examination, in an efficient manner;
2. Select and structure examination programs that target the goals and objectives of the supervisory strategy;
3. Ensure the examination is conducted in a professional manner;
4. Establish controls and record keeping systems to communicate examination findings effectively; and
5. Maintain review processes to ensure prescribed work is completed and workpapers support conclusions.

## **Supervision Contact Objectives**

### **Objectives of both on- and off-site supervision contacts**

1. Obtain reasonable assurances each corporate will continue to be financially sound;
2. Determine NCUSIF risk;
3. Determine compliance with applicable laws and regulations; and
4. Determine that the corporate's activities and financial condition does not adversely affect the System.

**Examination Procedures** See Corporate Examination Procedures - Examination Administration (OCCU 102P).

**Examination Questionnaire** See Pre-Examination Questionnaire (OCCU 102Q).

**Appendices**

- 102A – Application of the Targeted Risk Approach in the Identification, Measurement and Assessment of Risk
- 102B - Examiner’s Guideline for Completing an Examination
- 102C - Template for the Three-Year Supervision Plan
- 102D – Template of Joint Conference Information Memorandum
- 102E – Sample Transmittal Memo to the Region
- 102F – Reduced On-Site Examinations