



BOARD ACTION MEMORANDUM

TO: NCUA Board **DATE:** November 20, 2014

FROM: Office of the Chief Financial Officer **SUBJ:** FY 2015 Budget

ACTION REQUESTED: Board approval of the fiscal year 2015 operating and capital budgets

DATE ACTION REQUESTED: November 20, 2014

OTHER OFFICES CONSULTED: All regional and central office directors and Executive Director

VIEWS OF OTHER OFFICES CONSULTED: Concur

BUDGET IMPACT: \$279.5 million and 1,268.7 full-time equivalents (FTE)

SUBMITTED TO INSPECTOR GENERAL FOR REVIEW: Yes

RESPONSIBLE STAFF MEMBERS: Chief Financial Officer Mary Ann Woodson

AUTHORITY: Per the Federal Credit Union Act, the management of the Administration is vested in the National Credit Union Administration (NCUA) Board. It is the Board's responsibility to determine the expenses necessary to carry out its responsibilities under the Act. 12 U.S.C. § 1752a(a). The Board is authorized to expend such funds and perform such other functions or acts as it may deem necessary or appropriate in accordance with the rules and regulations or policies established by the Board. § 1766(i)(2)

Upon determination of the budgeted expenses, the Board determines a fee schedule with respect to federal credit unions, giving consideration to the expenses of the Administration in carrying out its responsibilities in connection with federal credit unions and the ability of federal credit unions to pay a fee. § 1755(a)-(b). That fee schedule is documented in the separate operating fee assessment Board Action Memorandum (BAM). Fees collected are required to be deposited with the Treasurer of the United States for the account of the Administration, and expended by the Board to defray the expenses incurred in carrying out the agency's operations, including the examination and supervision of federal credit unions. § 1755(d). Via the Overhead Transfer Rate, which is documented in the a separate BAM, the Board transfers additional National Credit Union Share Insurance Fund (NCUSIF) money to its operating fund to account for budgeted expenses related to both federal credit unions and federally insured, state-chartered credit unions, in accordance with its authority to use the Share Insurance Fund to carry out its responsibilities. § 1783(a)

At the end of the calendar year, NCUA's financial transactions are subject to audit in accordance with Generally Accepted Accounting Principles. §§ 1783(b) & 1789(b).

BACKGROUND: This memorandum recommends that the NCUA Board approve the proposed 2015 budget of \$279,477,779 and 1,268.7 full-time equivalents (FTE). NCUA's budget process uses the agency's strategic goals and objectives set forth in the [NCUA Strategic Plan 2014 through 2017](#) as a framework to ensure agency priorities and initiatives drive resulting resources needs and allocations. The annual budget provides the resources to execute against the strategic plan and undertake tasks in NCUA's major programs: examination and supervision, insurance, small credit union initiatives, consumer protection, and asset management. The Strategic Plan also identifies the NCUA's goals and objectives including the following priorities: manage operational vulnerabilities by implementing a robust supervision framework for financial reform regulations, including interest rate risk and stress testing; prepare for and promote awareness of critical risk issues and related threats such as cybersecurity risks; develop and promote financial literacy education and consumer protection programs; develop and communicate guidance to credit unions to explain regulatory changes and best practices; and, strengthen security programs and communications.

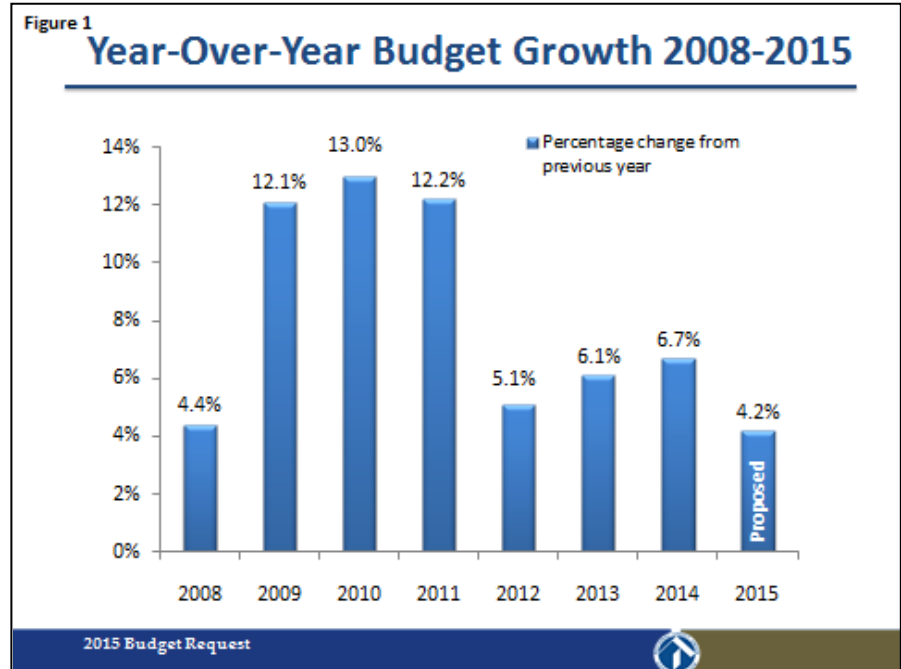
Each regional and central office director developed a budget request identifying resources required to support NCUA's mission and strategic goals and objectives. These budgets were developed using zero-based budgeting techniques to ensure each office's requirements were individually justified and consistent with the agency's overall strategic plan. One of the primary inputs in the development process is a comprehensive workload analysis that captures the amount of time necessary to conduct examinations and supervision of federally insured credit unions in order to carry out NCUA's dual mission as insurer and regulator. This process starts with a field level review of every credit union to determine the number of workload hours needed for the current year. The workload estimates are refined by each level of management in the field program until the final budget proposal is completed and forwarded to the central office for review and analysis. The final workload analysis establishes the foundation for the NCUA's five regional office budget requests and for the Office of National Examinations and Supervision (ONES), representing 72 percent of NCUA personnel. In addition to the workload analysis, which is used to develop personnel and travel costs, all offices developed cost estimates for fixed and recurring items such as rent or leased property, operations and maintenance, repair on owned facilities, supplies, telecommunications, and other administrative and contracted services costs.

All office budget submissions within NCUA underwent thorough reviews by the responsible regional and central office directors, the Chief Financial Officer, and executive leadership. NCUA's Information Technology Prioritization Council (ITPC) met with every regional and central office to review and prioritize software initiatives and align those information technology (IT) investments with NCUA's mission. These multi-level reviews result in a mutually agreed-upon budget to support NCUA's top priorities: implementing a robust supervision framework, promoting awareness of critical risks and related threats, developing financial literacy and consumer protection programs, providing guidance to credit unions, and strengthening security programs.

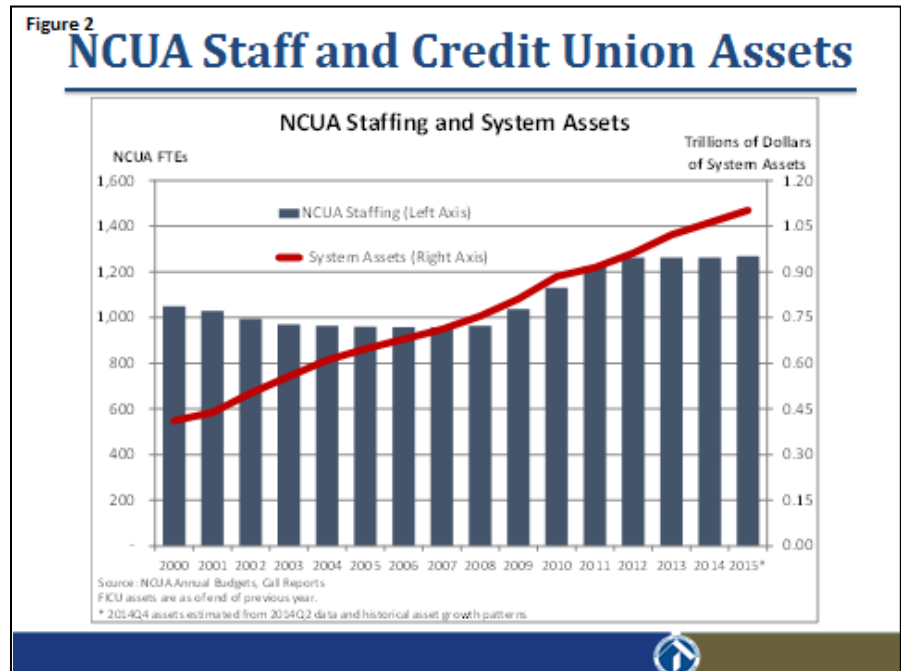
For reporting purposes and comparability with the practices of other Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) agencies, comparisons to last year's approved budget are included in this document. A summary description of the major spending

items in each budget category is included to provide improved transparency and understanding of how the budget resources will be used. Further, NCUA will provide supporting documentation for this request on the NCUA website to assist the public in understanding its budget development process.

SUMMARY: The proposed 2015 budget of **\$279,477,779** represents an increase of **4.2 percent** or **\$11,187,483 over** the 2014 budget of \$268,290,296. This is the smallest percentage increase since 2008. The budget increase reflects necessary expenditures to ensure successful execution of the agency’s mission and strategic plan.



The 2015 budget proposes a modest net increase to authorized staffing levels. The 2015 Full Time Equivalent (FTE) level is increased to a new authorized level of **1,268.7**. This includes a net increase of 4.2 FTEs from the 2014 mid-session budget. As seen in Figure 2, NCUA staffing growth continues to remain well below credit union asset growth¹.



¹ Source data: NCUA Annual Budget, Call Reports. FICU assets for 2015 are estimated.

Attachment 1 shows the breakout of the proposed 2015 budget by office.

The components of the 2015 budget as compared to the 2014 budget are:

<u>Category</u>	2014 Budget	2015 Budget	\$ Change	Percent Change	Percent of Total Budget
Employee Pay and Benefits	\$ 194,632,214	\$ 201,895,097	\$ 7,262,883	3.7%	72%
Travel	28,514,578	29,288,793	774,215	2.7%	11%
Rent, Communications & Utilities	5,615,191	5,772,087	156,896	2.8%	2%
Administrative	15,393,236	16,334,758	941,522	6.1%	6%
Contracted Services	<u>24,135,077</u>	<u>26,187,044</u>	<u>2,051,967</u>	8.5%	9%
Total	<u>\$ 268,290,296</u>	<u>\$ 279,477,779</u>	<u>\$ 11,187,483</u>	4.2%	100%

SIGNIFICANT BUDGETARY CHANGES:

Staffing Changes:

NCUA's top two priorities, consistent with an evolving credit union industry, are to: 1) maintain a robust supervision framework and 2) promote awareness of critical risks and related threats. This includes identifying and resolving traditional risk concerns such as interest rate risk, credit risk and concentration risk, as well as new and evolving operational risks including cybersecurity threats. To address these priorities and risk concerns, the budget proposes to reallocate 18 existing regional staff from generalist positions to the priority areas of capital markets, lending, and information systems. Employing specialists rather than generalists adds expertise commensurate with the increasing sophistication of credit union operations, so that NCUA will be better equipped to address these risk areas going forward.

In addition to realigning regional resources to priority needs, NCUA's budget proposes to add mission support staff to further support the stated priorities of a robust supervision framework, developing financial literacy and consumer protection programs, providing guidance to credit unions, enhancing cybersecurity and strengthening security programs. Additional staff proposed includes nine new positions as outlined below. This increase is offset by the reduction of five general examiner positions to be eliminated from the regional offices for a net increase of 4.2 FTEs. The new positions, linked to the strategic priorities, include:

1. Supervision – To support NCUA's priority of implementing a robust supervision framework, it is recommended that three new staff positions be added to:
 - a. The Office of National Examinations and Supervision (ONES) for a Senior Capital Markets Analyst to support capital planning and stress testing regulations

for natural person credit unions with assets over \$10 billion. This will focus on large institution risk in relation to the NCUSIF.

- b. ONES for an additional Lending Specialist Examiner to serve as an expert to staff during examinations or reviews of credit unions and credit union service organizations with complex lending programs. This position is needed to support the existing cadre of lending personnel.
 - c. The Office of Chief Economist for an economist position to support the increasing demands for in-depth analytical resources including simulation and modeling to support the examination workforce.
2. Cybersecurity – It is recommended that a cybersecurity manager be added to the Office of Examination and Insurance so the agency can be better prepared for and promote the awareness of critical risks and related threats. This position will help to establish the policy, risk management and communication objectives to support the cybersecurity priorities of NCUA and the interagency initiatives jointly managed with the Federal Financial Institutions Examination Council (FFIEC) to protect the financial services industry.
3. Consumer Protection - It is recommended that the Office of Consumer Protection add two personnel to support NCUA’s financial literacy and consumer protection programs.
 - a. A new consumer affairs program officer is required to support the accurate and timely processing of consumer inquiries and complaints about credit unions, as well as proactively identify consumer protection concerns. NCUA’s Consumer Assistance Center volume has doubled in 2014 over 2013.
 - b. A consumer compliance policy and outreach officer is necessary to provide expanded outreach to support NCUA staff and credit union officials on federal financial consumer protection matters.
4. Provide Guidance to Credit Unions – It is recommended the Office of Small Credit Union Initiatives add a staff member responsible for field consultation, automated tools and reports, and the OSCUI web microsite. This will further improve the efficiency and effectiveness of OSCUI so it can deliver timely and more user-friendly products and services to its portfolio of credit unions.
5. Security Programs – It is recommended that to strengthen NCUA’s security programs, supporting multiple agency objectives related to security and financial sector threats, the Office of Continuity and Security Management be expanded by two personnel:
 - a. A classified information security specialist is required to manage the NCUA sensitive compartmented information facility, ensure compliance with national security requirements for the safeguarding of classified information as mandated

by the Director of National Intelligence (DNI), and to oversee the operations and conduct of the secure communications operations and testing in compliance with DNI and National Communications System Directives. This work has become increasingly complex and must adhere to requirements in the National Communications System Directive 3-10 and guidance from DNI.

- b. An intelligence specialist with knowledge of both financial sector threats and cyber threats will provide support to NCUA network security and business operations by sharing information on critical infrastructure protection for the credit union sector. The cyber intelligence analysis requires specialized skills that include mastery knowledge of national security threats, cybersecurity, the Intelligence Community, analytical techniques, and applicable regulations, principles, Director of National Intelligence regulations and standards.

Employee Pay and Benefits:

The employee pay and benefits expense category net increase of \$7.3 million brings the total 2015 cost of pay and benefits to \$201.9 million, a 3.7 percent change, as compared to 2014.

Pay and benefits represent 72 percent of the total budget request. A major driver of the increase is merit and locality pay increases, primarily due to NCUA's current collective bargaining agreement. NCUA's compensation continues to "maintain comparability with other federal bank regulatory agencies" as stipulated in the Federal Credit Union Act². NCUA staff will be eligible to receive an average merit-based increase of four percent and a locality adjustment of up to three percent for most staff. In addition, the cost for the net increase of four new positions proposed is estimated to be \$443,000 and assumes these personnel will be on board for only one-half of the year.

In addition, the Office of Personnel Management (OPM) revised the economic assumptions used for actuarial valuation of the Federal Employees Retirement System (FERS). Under the new methodology, for 2015 all federal agencies must contribute 13.2 percent of FERS employees' salary to the retirement system. This is up from 11.9 percent, and is estimated to cost NCUA an additional \$1.8 million for a total of \$17.9 million in 2015. OPM also announced the government's portion of the Federal Employees Health Benefits program will increase an average of three percent in 2015. The estimated cost of NCUA's health benefits in 2015 are expected to total \$12.6 million.

The employee pay and benefits category also includes increased costs associated with promotions, position changes, and other mandatory employer contributions such as social security, retirement, transportation subsidies and worker's compensation.

² The Federal Credit Union Act states that, "In setting and adjusting the total amount of compensation and benefits for employees of the Board, the Board shall seek to maintain comparability with other federal bank regulatory agencies." 12 U.S.C. Section 1766(j)(2).

The NCUA also achieved savings in the employee pay and benefits line item. For example, benefit costs were adjusted downward by \$650,000 associated with lower-than-anticipated employee participation in health insurance benefit programs. Also, the agency made assumptions related to staff turnover, which lowered overall pay and benefits because more experienced personnel that separate from NCUA are assumed to be replaced by a combination of entry-level and midcareer staff employees.

Travel:

Travel comprises 11 percent of the overall 2015 budget proposal and reflects less than a three percent increase, or \$774,215 over 2014. The total travel budget of \$29.3 million includes expenses to cover per diem and lodging, air fare, reimbursements for privately owned vehicle usage, auto rentals, and other travel costs. These are necessary expenses for examiners' on-site work in credit unions. A total of 64 percent of NCUA's workforce is comprised of virtual field staff who spend over 30 percent of their time traveling to conduct the annual examination and supervision program and to a lesser degree to attend training.

The standard government-wide 2015 U.S. General Services Administration lodging and per diem rates are unchanged from 2014; however, there are many non-standard areas with higher per diem rates. This includes large metropolitan cities such as Miami, San Francisco and Boston that reflect an average four percent increase over 2014 lodging and meal expenses. These cost increases, combined with the planned 2015 examination schedule, result in an increase to regional travel. Central office travel expenses will also increase to support field exams. As examples, technical experts such as payment system, capital market, and lending specialists will assist field examiners with program examinations and training, while consumer access analysts will support field consumer compliance issues and follow-up field assessments of business marketing plans for field of membership expansions.

Rent, Communication, and Utilities:

Rent, communication, and utilities proposed at \$5.8 million is the smallest component of NCUA's budget and covers mainly the agency's telecommunications and network expenses. Lease and rental expenses as well as utilities and postage are also part of this budget category. Total expenses in this budget category are expected to increase just under three percent, or a net amount of \$156,896. Most of this budget line item increase, approximately \$200,000, is attributed to telecommunications costs that include the addition of broadband and network connections to improve data capacity and reliability. Additional dedicated communication lines for the central offices and Region I also account for part of this cost increase. Subscription services with financial and portfolio risk analytics critical to support program examinations account for an increase of \$47,000.

The agency identified cost savings in this budget category. The leases in Regions II and III were recently renegotiated resulting in savings of approximately \$119,000. NCUA continues to support its green initiative by increasing delivering of materials in electronic format and reducing

its postal expenditures by \$46,000 in 2015. Additionally, an effort to consolidate meeting and training requirements for field staff will result in savings of \$64,000.

Administrative Expenses:

Administrative expenses primarily include depreciation and amortization expenses of capital acquisition and software licenses that support operational requirements, FFIEC fees, relocation expenses, and employee supplies. These costs are expected to increase by a net of \$941,522 or six percent, for a total budget of \$16.3 million for 2015.

Software licensing fees will increase by \$137,000 for both new licenses and for inflationary increases on existing licenses. These licenses provide critical analytical tools for examiners to strengthen off-site monitoring, perform asset valuation and risk metrics, enhance statistical surveillance of credit union risks and program efficiencies, and further improve program consistency.

The proposed budget also includes \$752,000, an increase of \$279,000, to fund NCUA's enterprise agreement for a suite of Microsoft software products. This funding supports server and end-user licensing costs for Microsoft products, including email, word processing, spreadsheet and database management applications. These tools support NCUA's mission achievement across all of the agency's strategic goals. Total software licenses and maintenance fees will cost NCUA \$3.1 million in 2015.

In 2015, NCUA's laptops will be at the end of their useful life, in a business setting, which is the prevalent industry standard of three years. Although the annual costs for the computer leases are expected to remain unchanged from 2014, there will be a one-time cost of \$365,000 to replace computer peripherals such as docking stations, hard drives, and other accessories.

The agency expects to achieve savings of \$90,000 by utilizing webinars and internet resources for small credit union engagements.

Contracted Services:

Contracted services is budgeted at \$26.2 million for 2015. The request represents an increase of \$2.1 million, or nine percent, over the 2014 budget and is in support of NCUA's top priorities of implementing a robust supervision framework, promoting awareness of critical risks and related threats, developing financial literacy and consumer protection programs, providing guidance to credit unions, and strengthening security programs. The contracted services line items of the budget reflect costs incurred when products and services are acquired in the commercial marketplace through a competitive process for all contracts over \$7,500. These services include critical mission support such as information technology hardware and software development support, accounting and auditing services, and specialized subject matter expertise that enable NCUA to meet its mission. Contracting specific expertise is often a cost-effective approach to support career FTEs.

The majority of contract services funding is related to NCUA's priority goal to implement a robust supervision framework, to include identifying and resolving traditional risk concerns such as interest rate risk, credit risk and concentration risk, as well as new and evolving operational risks including cyber-security risks.

A portion of the funding requested for this category is for recurring infrastructure costs to the agency. For example, the agency incurs recurring contracted services funding to maintain a number of NCUA systems including critical legacy systems such as Automated Integrated Regulatory Examination System (AIRES) and CU Online. Other examples include:

- Funding to meet training requirements of the examiner workforce. NCUA's most important resource is a highly qualified, skilled workforce. It is important that staff have the proper knowledge, skills, and abilities to perform assigned duties and meet emerging needs. Examiners are required to attend five levels of examiner training, followed by training in core areas such as capital markets, consumer compliance, and specialized lending. NCUA training program costs, primarily conducted at the agency's training facility in the central office, are expected to remain at the same level as 2014. This includes conducting over 100 training sessions annually with more than 2,100 attendees for both NCUA staff and state supervisory authorities. The central office training facility is in use over 300 calendar days per year. Contract resources will be used to modify and strengthen NCUA examiner training in member business lending. In addition to supporting the agency's programmatic priorities, employee development supports the strategic goal to cultivate an environment that fosters a diverse, well-trained and motivated staff.
- Information technology system costs. These funds for NCUA's information security program are required to strengthen cybersecurity, a high priority to ensure the agency is in compliance with the Federal Information System Management Act .
- Funds for agency financial management services, human resources technology support, and payroll services. NCUA contracts for these services with the U. S. Department of Transportation's Enterprise Service Center and the U.S. General Services Administration.
- Funds to conduct the annual audit for NCUA's five funds.

Funds are also requested to evaluate the staffing structure and analytical software needs to support internally developed stress testing results for natural person credit unions greater than \$10 billion in assets. This analysis is expected to cost \$100,000. A loan portfolio analysis tool estimated to cost \$150,000 will be used to assist with supervision responsibilities for natural person credit unions over \$10 billion in assets.

There are several federally mandated security costs such as the secure electronic surveillance system. These costs will increase over the prior year budget by \$235,000. Other required security costs are associated with the personally identifiable verification program and background

investigation checks and are estimated to increase \$110,000. This includes cost increases charged by the Office of Personnel Management for five-year reinvestigations.

Dedicated contractor support was approved during the 2014 mid-session budget review to meet growing audiovisual demands, evolving communication platforms, and enhance staff effectiveness and efficiency through the use of technology. This contractor support will continue to assist NCUA with video teleconferencing, web conferencing, and provide IT support for more efficient training at a cost of \$176,000.

There are several minor maintenance projects needed for the King Street Station property to provide general upkeep and replacement items for the 20-year old property in the amount of \$140,000. In addition, realtor commission costs to replace an existing tenant expected to move next year is estimated at \$85,000.

The U.S. Equal Employment Opportunity Commission has several mandatory compliance requirements. NCUA will hire a contractor to conduct a barrier analysis to assess NCUA's personnel recruitment policies and procedures to ensure there are no employment barriers to full participation in the workplace by individuals of all races and ethnicities. The cost of this contract is estimated to be \$185,000. In addition, an expanded workforce recruitment program costing \$60,000 will increase hiring opportunities from underrepresented groups. These initiatives support the diversity inclusion requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act, as well as NCUA's objective of recruiting and retaining a well-diversified and highly qualified workforce.

Capital Acquisitions:

An itemized listing for \$8.9 million of capital acquisitions is provided in Attachment 2.

A total of \$5.9 million is requested for information technology software development projects approved by NCUA's Information Technology Prioritization Council. Several of these systems were part of mid-session budget approved projects to plan and assess the specifications to implement these projects.

- \$1.5 million: Business Intelligence tools to provide robust enhanced reporting
- \$1.3 million: Redesign of the examination management system; Consumer Assistance Center complaint management system replacement
- \$1.1 million: CU Online Version 3 for natural person credit unions
- \$325,000: Background investigation management system
- \$250,000: Enterprise portal for staff to securely share and distribute large files
- \$216,000: Replacement of system that supports administrative functions including budget formulation, travel voucher audits, and human resource data.

A total of \$200,000 is requested for a new Office of Minority and Women Inclusion data management and complaint tracking system to comply with a recent Office of Inspector General

recommendation. A more robust automated system is needed to ensure that the increased level of information required by various government entities is readily available.

A total of \$263,000 is requested for information technology hardware including replacement of five-year old regional servers, upgrade of the audiovisual system in the central office, and expansion of production storage infrastructure to meet growing data capacity needs.

A total of \$2.5 million is requested for central office building renovation projects. The retail space in the King Street building will be retrofitted to be used as the agency's training facility. Renovation of the vacated space in the central office from the former training rooms will repurpose it for office space. This repurposing project is designed to ensure the central office space will be used more efficiently and will avoid the expense of purchasing or leasing additional space outside of the central office in 2015.

There are also several necessary heating, ventilation, and air conditioning replacement projects as well as electrical upgrades necessary for the ongoing maintenance of the building.

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

1. The fiscal year 2015 budget of \$279,747,779 and 1,268.7 FTEs, as presented in Attachment 1.
2. The 2015 capital acquisitions of \$8,872,500 as presented in Attachment 2.

ATTACHMENTS: 2015 proposed budget by office, and 2015 capital acquisition schedule.