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# Highlights

Highlights of GAO-04-977, a report to the Ranking Minority Member, Committee on Banking, Housing, and Urban Affairs, U.S. Senate

September 2004

# CORPORATE CREDIT UNIONS

## Competitive Environment May Stress Financial Condition, Posing Challenges for NCUA Oversight

### Why GAO Did This Study

Thousands of credit unions have placed about $55 billion of their excess funds in corporate credit unions (corporates). In a three-tiered system, corporates provide lending, investment, and processing services for their member credit unions. Problems with investments in the past prompted regulatory changes that required higher capitalization and stricter risk management, but allowed for expanded investment authorities. GAO assessed (1) the changes in financial condition of the corporate network and (2) the oversight of corporates by the National Credit Union Administration (NCUA), the federal regulator of credit unions.

### What GAO Recommends

To improve oversight of corporates, GAO recommends that the Chairman of NCUA (1) establish a process and structure to systematically involve specialists in identifying and addressing problems, (2) track and analyze examination deficiencies to address complex and emerging issues, (3) pay increased attention to oversight of corporates' risk management functions, (4) provide improved guidance to corporates and examiners for preparing and reviewing merger packages, and (5) require internal control reporting consistent with other financial institutions. NCUA agreed to implement all of these recommendations, except for providing improved guidance to examiners reviewing mergers.

www.gao.gov/cgi-bin/getrpt?GAO-04-977.

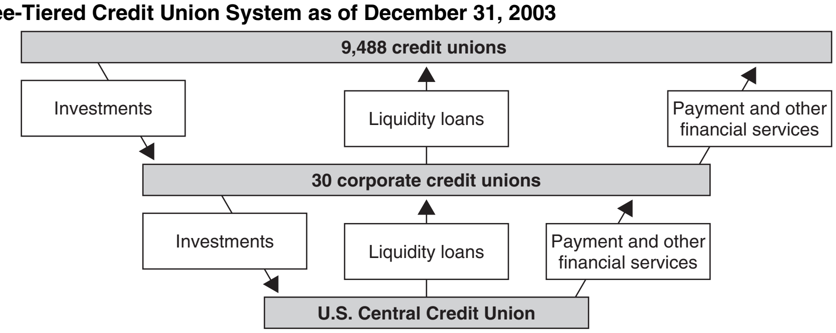
To view the full product, including the scope and methodology, click on the link above. For more information, contact Richard J. Hillman at (202) 512-9073 or hilmanr@gao.gov.

### What GAO Found

Corporates face an increasingly challenging business environment that potentially could stress their overall financial condition. In response to the competitive environment, corporates are offering new and more sophisticated products and services, expanding their use of technology, and seeking opportunities to merge or collaborate with other corporates. The corporates' financial condition as measured by profitability and capital ratios remained close to a range that has prevailed since the mid-1990s. However, since 2000, a large influx of deposits, coupled with low returns on traditional corporate investments, has constrained earnings and caused a downward trend in corporates' overall profitability. To generate earnings, corporates increasingly have targeted more sophisticated and potentially riskier investments, but appear to be managing risk by shifting toward more variable-rate and shorter-term investments, providing a potentially better match for the relatively short-term nature of their members' deposits. However, the corporates' changing business environment and utilization of more sophisticated and riskier investments increases the importance of NCUA regularly assessing its oversight processes to ensure that corporates are properly managing these risks.

NCUA has strengthened its oversight of corporates by creating a centralized office for oversight, revising regulations, implementing risk-focused supervision, and hiring specialists. However, NCUA faces challenges in identifying networkwide problems on a consistent basis, using specialists effectively, providing relevant guidance on mergers, and assuring the quality of corporates' internal controls. Although NCUA identified deficiencies during its examinations, it has not systematically tracked their resolution or evaluated trends in examination data, which could help anticipate emerging issues facing corporates. NCUA also did not fully consider all risks when allocating resources or assigning specialists to examinations, leading to NCUA overlooking some information system deficiencies. Although corporates continue to consider mergers to remain competitive, NCUA had not developed adequate guidance for submitting and reviewing merger proposals. Finally, NCUA has not ensured that corporates' internal controls have remained consistent with those of similarly sized financial institutions.

**Three-Tiered Credit Union System as of December 31, 2003**




Sources: Call report data and U.S. Central.