

**NATIONAL CREDIT UNION ADMINISTRATION
OFFICE OF INSPECTOR GENERAL**

**Semiannual Report
to the Congress**

April 1, 2005 – September 30, 2005

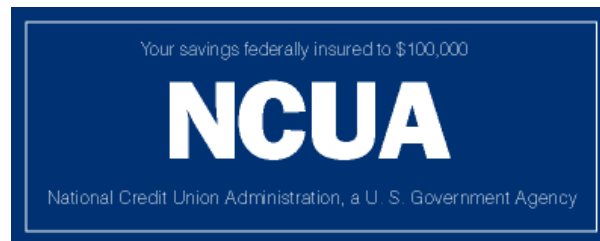


TABLE OF CONTENTS

INSPECTOR GENERAL’S MESSAGE.....	i
NCUA AND OFFICE OF INSPECTOR GENERAL MISSION STATEMENTS.....	1
INTRODUCTION.....	2
NCUA ORGANIZATION CHART.....	4
NCUA HIGHLIGHTS.....	5
FEDERALLY INSURED CREDIT UNION HIGHLIGHTS.....	7
LEGISLATIVE HIGHLIGHTS.....	8
OFFICE OF THE INSPECTOR GENERAL.....	10
Audit Activity.....	11
Investigative Activity.....	15
Legislative and Regulatory Reviews.....	20
TABLE I – REPORTS WITH QUESTIONED COSTS.....	22
TABLE II – REPORTS WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE.....	23
TABLE III – SUMMARY OF OIG ACTIVITY.....	24
INDEX OF REPORTING REQUIREMENTS.....	25



INSPECTOR GENERAL'S MESSAGE TO THE NCUA BOARD AND THE CONGRESS

I am pleased to transmit to the NCUA Board and the Congress the Office of Inspector General's (OIG) Semiannual Report for the period April 1 through September 30, 2005. The submission of this report is in accordance with the Inspector General Act of 1978, as amended (IG Act). Section 5 of the IG Act requires that the Chairman transmit this report to the appropriate committees or subcommittees of the Congress within 30 days of its receipt.

This past reporting period witnessed one of the most devastating natural disasters our country has ever experienced. Hurricane Katrina and its aftermath closed 139 credit unions in Louisiana, Mississippi, and Alabama when it struck on August 29. NCUA quickly established an emergency response policy and has reported that by September 16, all credit unions in the affected area had returned to operation. The OIG is participating in monthly meetings with the other federal financial institution regulatory inspectors general to monitor the response of the financial regulators to this tragedy.

During this past reporting period, the OIG issued three audit reports and an audit memorandum on NCUA employees' compliance with state income tax obligations. Audit reports issued included a review of NCUA's process for reviewing federally insured state chartered credit unions; our annual independent evaluation of NCUA's information security program, as required by the Federal Information Security Management Act; and a report to the Office of Management and Budget (OMB) summarizing our evaluation of the agency's information security program presented in the OMB prescribed format.

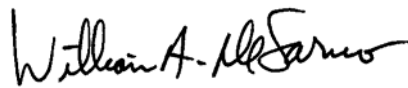
Also during this reporting period, the Office of Investigations experienced a marked increase in the number of matters referred or reported for investigative consideration. During this period we initiated eight new investigations and closed six. Investigation reports issued this period involved the use of non-public information for personal gain; false statements; and time and attendance fraud.

Recently, our office learned that the agency's Office of Human Resources (OHR) had been routinely disclosing the names of witnesses identified in OIG Reports of Investigation in proposed disciplinary action letters resulting from our investigations. In a recent case, we learned that the OHR was planning to send a letter of proposed removal to an employee who had

been the subject of an OIG investigation. The letter contained the name of a witness in the investigation. We notified the agency that we would not authorize the release of the witness's name, and the OHR disregarded this direction and released the name and large portions of the witness's testimony to the subject of the investigation. I have since met with the head of the agency and made our position clear that the release of such information contained in OIG reports is the decision of the OIG and that future proposal letters from the agency based on OIG Reports of Investigation may not include witness names without the authorization of the OIG.

Also during this investigation, the issue arose of OIG staff's access to requested documents. A document was requested and withheld, at the direction of the same individual on whom we reported a similar incident in our October 2000 Semiannual Report. I reported this incident to the head of the agency, and made clear the OIG authority to have access, upon request and without delay, to agency records and information.

There are many challenging issues facing NCUA in the near future and I look forward to working with Chairman Johnson and the new, soon to be confirmed, NCUA Board members in meeting these challenges.

A handwritten signature in black ink that reads "William A. DeSarno". The signature is written in a cursive style and is positioned to the left of a vertical red line.

William A. DeSarno
Inspector General

MISSION STATEMENTS

THE NCUA MISSION

NCUA's charge is to foster the safety and soundness of federally insured credit unions and to better enable the credit union community to extend the availability of financial services for provident and productive purposes to all who seek such service, while recognizing and encouraging credit unions' historical emphasis on extension of financial services to those of modest means.

The NCUA's mission is accomplished by managing the National Credit Union Share Insurance Fund in an efficient and prudent manner through an effective supervision program and a regulatory environment that encourages innovation, flexibility and continued focus on attracting new members and improving financial service to existing members.

THE OFFICE OF INSPECTOR GENERAL MISSION

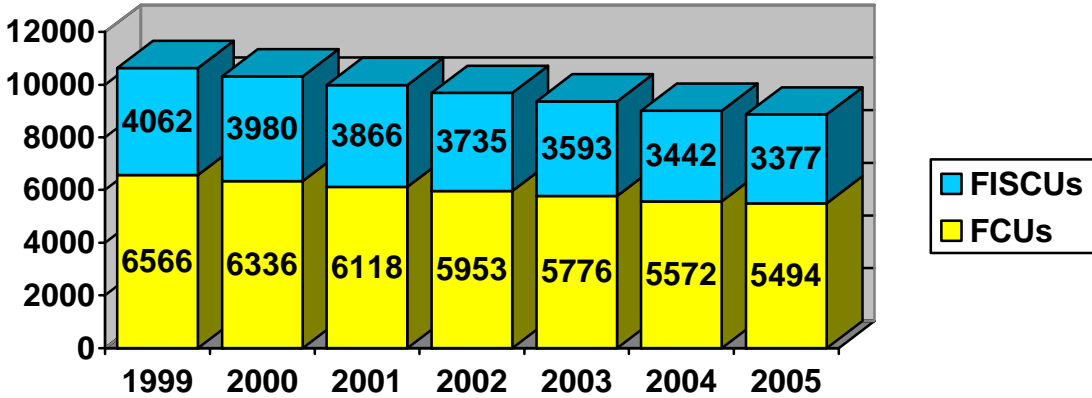
The OIG promotes the economy, efficiency, and effectiveness of NCUA programs and operations, and detects and deters fraud, waste, and abuse, thereby supporting the NCUA's mission of monitoring and promoting safe and sound federally insured credit unions.

We accomplish our mission by conducting independent audits, investigations, and other activities, and by keeping the NCUA Board and the Congress fully and currently informed of our work.

INTRODUCTION

The National Credit Union Administration (NCUA) was established as an independent, federal regulatory agency on March 10, 1970. The agency is responsible for chartering, examining, supervising, and insuring federal credit unions. It also insures state-chartered credit unions that have applied for insurance and have met National Credit Union Share Insurance requirements. The NCUA is funded by the credit unions it supervises and insures. As of June 30, 2005, the NCUA was supervising and insuring 5,494 federal credit unions and insuring 3,377 state-chartered credit unions, a total of 8,871 institutions. This represents a loss of 78 federal and 65 state-chartered institutions since December 31, 2004, for a total loss of 143 credit unions nationwide.

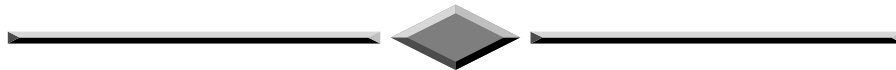
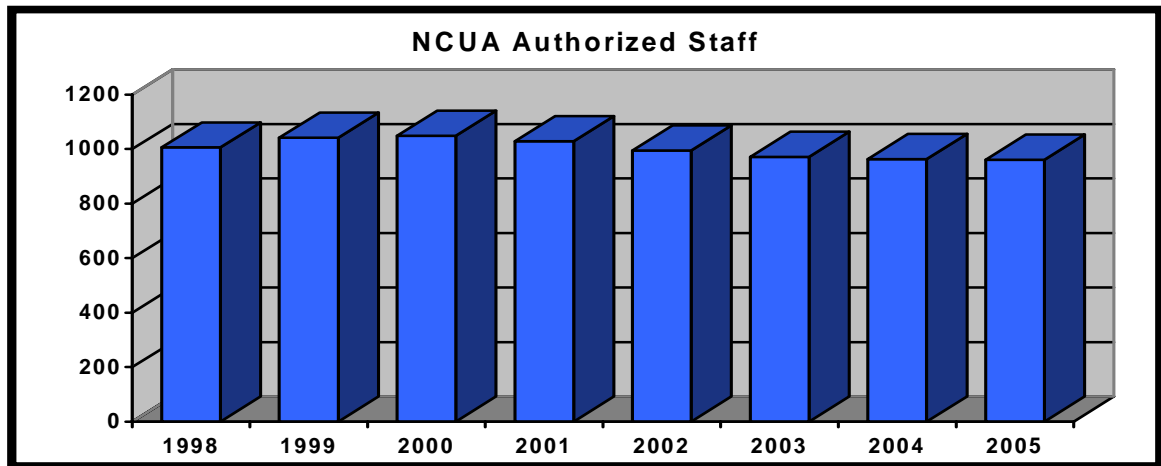
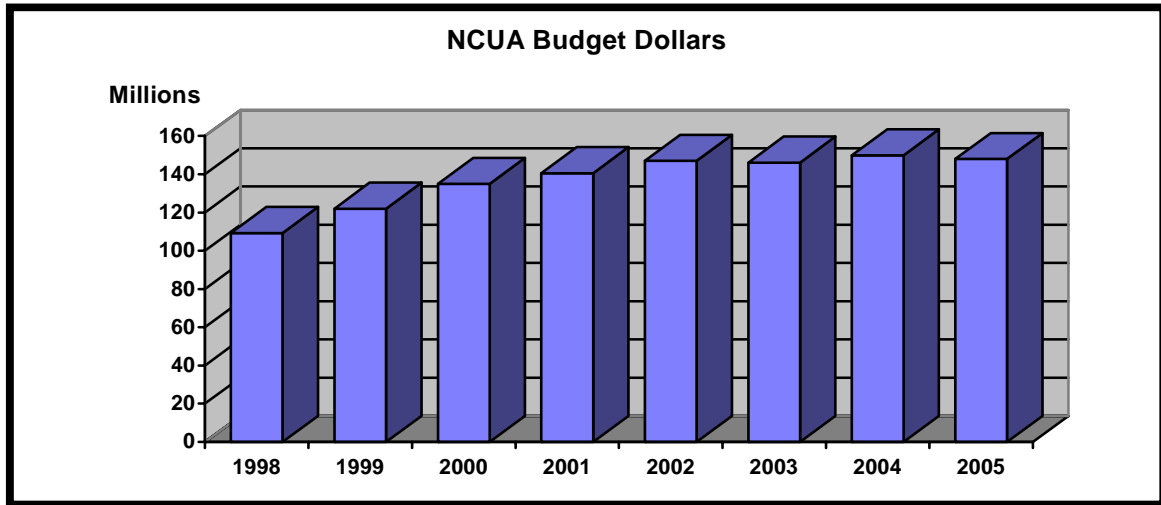
Federally Insured Credit Unions



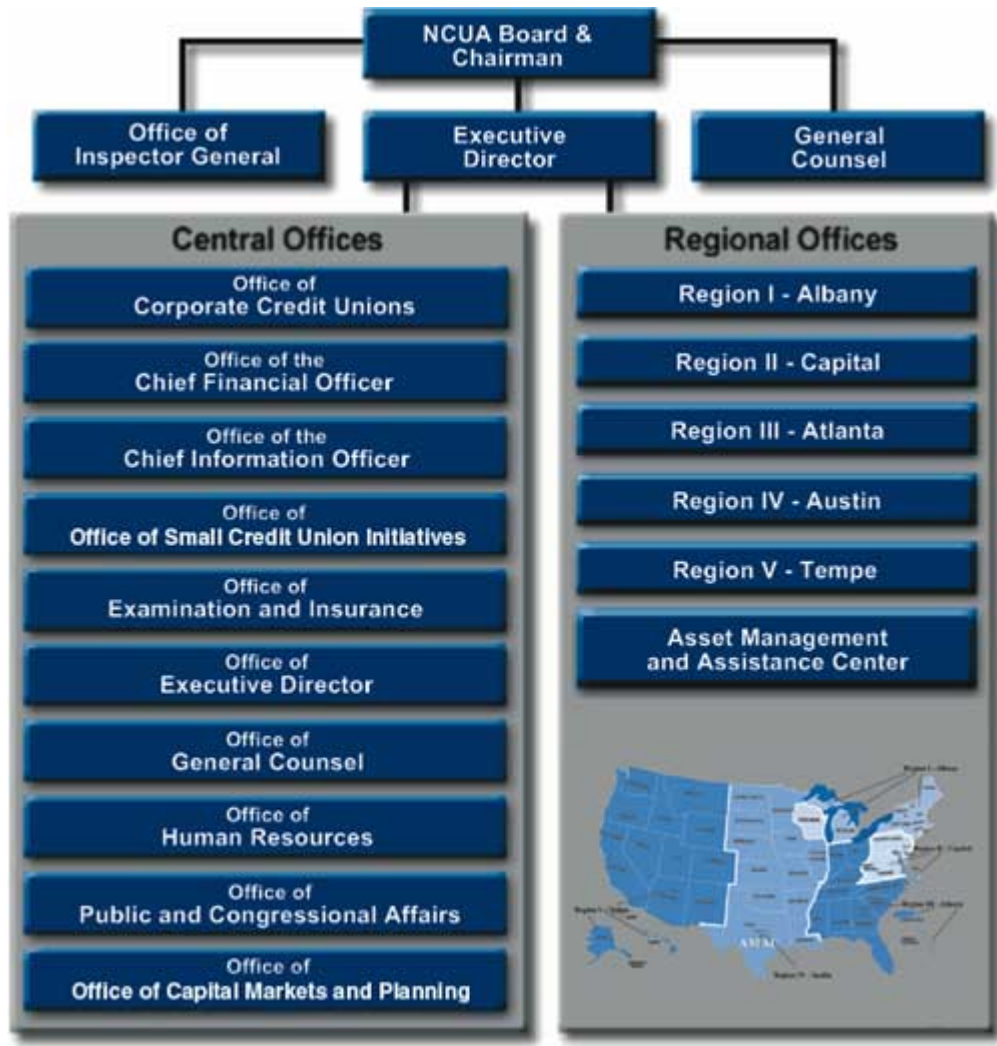
The NCUA operates under the direction of a Board composed of three members. Board members are appointed by the President and confirmed by the Senate. They serve six-year terms. Terms are staggered, so that one term expires every two years. The Board is responsible for the management of the National Credit Union Administration, including the NCUA Operating Fund, the Share Insurance Fund, the Central Liquidity Facility, and the Community Development Revolving Loan Fund.

The National Credit Union Administration executes its program through its central office in Alexandria, Virginia and regional offices in Albany, New York; Alexandria, Virginia; Atlanta, Georgia; Austin, Texas; and Tempe, Arizona. The NCUA also operates the Asset Management and Assistance Center (AMAC) in Austin, Texas. Please refer to the NCUA organizational chart on page 4.

The NCUA Board adopted its 2005 budget of \$147,996,144 on November 18, 2004. The Full-Time Equivalent (FTE) staffing authorization for 2005 is 961, a reduction of 2 positions from the 2004 total of 963.



NCUA ORGANIZATION CHART



NCUA HIGHLIGHTS**ALL HURRICANE KATRINA AND RITA - AFFECTED CREDIT UNIONS OPERATIONAL**

Hurricane Katrina and its aftermath closed 139 federally insured credit unions in Louisiana, Mississippi, and Alabama when it struck on August 29, 2005. By September 16, 2005, all 139 credit unions representing \$3.4 billion in assets and 100 percent of area members had returned to operation. While some credit unions may still be operating from back-up sites, members have access to their funds. Likewise, the fifty federally insured credit unions with assets totaling \$1.9 billion that were temporarily closed due to Hurricane Rita are all now operational in Louisiana and Texas. One of NCUA's initial steps after the hurricanes struck was to activate an emergency response policy encouraging credit unions to assist affected institutions and consider all reasonable and prudent actions that could help meet the critical financial needs of members and communities.

BOARD MEMBER MATZ RESIGNS FROM NCUA'S BOARD

With her term having expired on August 2, 2005, NCUA Board Member Deborah Matz submitted her resignation and left the agency on September 30, 2005. President George W. Bush named Matz a recess appointee to the NCUA Board on January 22, 2002, and the Senate confirmed her nomination on March 20, 2002. Before her appointment, Matz was the Executive Officer at the Liaison Office for North America of the Food and Agriculture Organization of the United Nations in Washington, D.C. In her resignation letter Matz expressed her gratitude to the President for the "extraordinary opportunity" to serve the credit union services sector.

PRESIDENT BUSH NOMINATES RODNEY E. HOOD TO THE NCUA BOARD

On April 29, 2005, President Bush announced his intention to nominate Rodney E. Hood to the NCUA Board. His nomination was sent to the U.S. Senate on May 10, 2005. Mr. Hood currently serves as the Associate Administrator of the Rural Housing Service at the U.S. Department of Agriculture. Assuming confirmation, Hood would fill the second Republican seat on the three-person board. NCUA's current Board Chairman, JoAnn Johnson, currently fills the first Republican seat on the Board. Hood's term would expire in 2009.

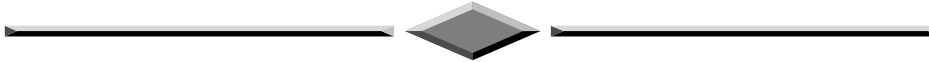
PRESIDENT BUSH NOMINATES GIGI HYLAND TO NCUA BOARD

One day after expressing his intention to nominate Gigi Hyland to serve as a Member of the NCUA Board, President Bush made it official on September 30, 2005, and asked the U.S. Senate to approve Hyland's nomination for a six-year term. Hyland is the senior vice president and general counsel for Empire Federal Credit Union in Albany, N.Y. If

confirmed, Hyland would fill the Democratic seat on the three-person board vacated by Deborah Matz. Hyland's term would expire in 2011. Hyland's nomination has been referred to the Committee on Banking, Housing and Urban Affairs and awaits further action.

TEXAS CONVERSION CASES SETTLED

On August 31, 2005, Chairman Johnson announced that the NCUA had settled the lawsuit filed against the agency by Community Credit Union of Plano, Texas. Another Texas credit union, OmniAmerican Credit Union, had also joined the lawsuit prior to the settlement. NCUA had originally rejected the credit union's membership vote to convert to a mutual savings bank. The settlement allowed the \$1.4 billion charter switch to proceed.



FEDERALLY INSURED CREDIT UNION HIGHLIGHTS

Credit unions submit quarterly call reports (financial and operational data) to the NCUA. An NCUA staff assessment of the June 30, 2005, quarterly call reports submitted by all federally insured credit unions found that virtually all key financial indicators were stable.

KEY FINANCIAL INDICATORS STABLE

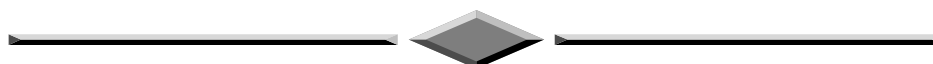
Looking at the June 30, 2005 quarterly statistics for major balance sheet items and key ratios shows the following for the nation's 8,871 federally insured credit unions: assets grew 3.51 percent, or \$22.7 billion; net worth to assets ratio increased from 10.96 to 11.04 percent; the loan to share ratio increased from 74.49 percent to 75.93 percent; the delinquency ratio decreased from .72 to .65 percent; and credit union return on average assets increased from .91 percent to .93 percent.

SAVINGS INCREASED

Total share accounts increased 2.9 percent, or \$16.1 billion. Regular shares comprise 35 percent of total share accounts; share certificates comprise 24 percent; money market shares comprise 18 percent; share draft accounts comprise 13 percent; and 10 percent is in other share accounts.

LOANS AND INVESTMENTS ALSO INCREASED

Loan growth of 4.89 percent resulted in an increase in total loans by \$20.2 billion. First mortgage real estate loans increased 5.4 percent; used auto loans increased 2.6 percent; other real estate loans increased 8.7 percent; unsecured credit card loans decreased 1.8 percent; all other unsecured loans decreased .8 percent; new auto loans increased 7.4 percent; and all other loans increased 4.6 percent. First mortgage real estate loans are the largest single asset category with \$137.1 billion accounting for 31.5 percent of all loans. Total investments increased \$2.4 billion or 1.5 percent. Investments with maturities less than one year account for 49.3 percent of all credit union investments.



LEGISLATIVE HIGHLIGHTS

CHAIRMAN JOHNSON OFFERS RECOMMENDATIONS FOR PROPOSED REGULATORY RELIEF BILL

Although the House passed regulatory relief legislation last Congress, the Senate did not then take the matter up. Consequently the 109th Congress is considering the issue again. On June 9, 2005, Chairman Johnson testified before the House Subcommittee on Financial Institutions and Consumer Credit, recommending specific credit union provisions in any regulatory relief bill. Subsequently, at the Senate Committee on Banking, Housing and Urban Affairs hearing held on June 21, 2005, Chairman Johnson provided that Committee with NCUA's recommendations for a regulatory relief bill Senator Crapo (R-ID) is assembling. At that hearing, Chairman Johnson also presented the case for risk-based Prompt Corrective Action (PCA) for federally insured credit unions and urged the Committee to include it in any forthcoming regulatory relief legislation.

NCUA ISSUES REGULATION IMPLEMENTING NEW POST-EMPLOYMENT RESTRICTIONS

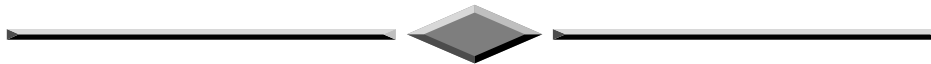
On December 17, 2004, Congress enacted Public Law 108-458 creating new post-employment restrictions for certain federal employees who examine banks and credit unions. On July 21, 2005, NCUA presented a proposed rule to implement the new, post-employment restrictions that will apply to certain senior NCUA examiners starting December 17, 2005. The proposed rule prohibits senior NCUA examiners, for a year after leaving NCUA employment, from accepting employment with a credit union if they had continuing, broad responsibility for examination of that credit union for two or more months during their last 12 months of NCUA employment.

HOUSE INTRODUCES "CREDIT UNION REGULATORY IMPROVEMENTS ACT OF 2005"

On May 12, 2005, House Financial Services Committee members Edward Royce (R-CA) and Paul Kanjorski (D-PA) introduced H.R. 2317, the "Credit Union Regulatory Improvements Act" (CURIA). The proposed legislation would, among other things, allow the NCUA to develop a modern risk-based PCA system; raise from 12.25% to 20% of assets the cap placed on credit union members business lending; exclude from the new cap, loans under \$100,000 and those made to nonprofit religious organizations; improve credit union leasing arrangements of Federal land in underserved communities; and allow federal credit unions to provide check cashing money transfer services to individuals within the credit union's field of membership.

ADVERSE LEGISLATION WITH REGARD TO CONVERSIONS OF INSURED CREDIT UNIONS INTRODUCED

Representative Patrick McHenry (R-NC) and others introduced adverse legislation, “The Credit Union Charter Choice Bill,” H.R. 3206, on July 12, 2005, to reduce NCUA authority with regard to conversions of insured credit unions to mutual savings bank charters. Specifically, the legislation would: amend the Federal Credit Union Act to repeal requirements governing oversight by the NCUA of the member vote concerning charter conversions of credit unions to mutual savings banks or savings associations; revamp requirements governing credit union notification to the NCUA Board of the intent to convert; set forth an NCUA Board approval process regarding materials submitted by converting credit unions; require the member vote on a proposed conversion to be conducted by secret ballot, with an independent inspector of elections appointed by the converting credit union to receive and tally the votes; require the Board of Directors of the converting credit union to certify vote results; and deny the NCUA Board any further review or approval authority over the conversion process, absent fraud or reckless disregard for fairness during the voting process that affects the vote outcome.

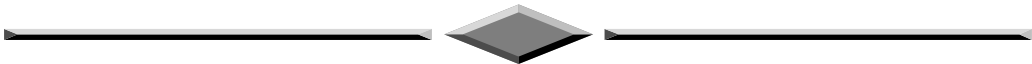
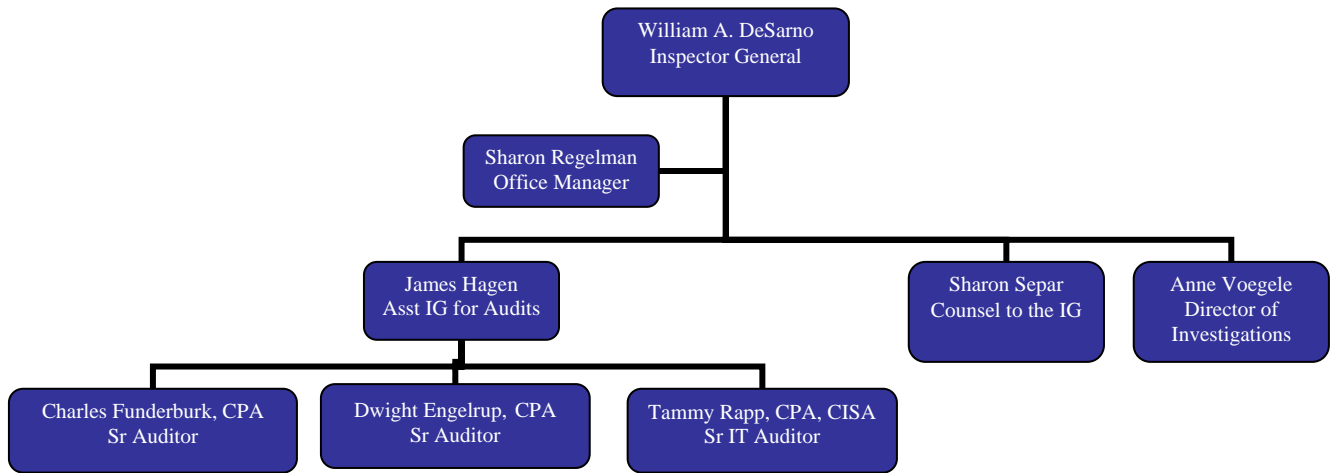


OFFICE OF THE INSPECTOR GENERAL

The Office of the Inspector General was established at the NCUA in 1989 under the authority of the Inspector General Act of 1978, as amended in 1988. The staff consists of the Inspector General, Counsel to the Inspector General, Assistant Inspector General for Audits, Director of Investigations, two Senior Auditors, Senior Information Technology Auditor, and Office Manager.

The Inspector General reports to, and is under the general supervision of, the NCUA Board. The Inspector General is responsible for:

- 1. Conducting, supervising, and coordinating audits and investigations of all NCUA programs and operations;
- 2. Reviewing policies and procedures to ensure efficient and economic operations as well as preventing and detecting fraud, waste, and abuse;
- 3. Reviewing existing and proposed legislation and regulations to evaluate their impact on the economic and efficient administration of agency programs; and
- 4. Keeping the NCUA Board and the Congress apprised of significant findings and recommendations.



AUDIT ACTIVITY**AUDIT REPORTS ISSUED****NCUA's Process for Reviewing Federally Insured State Chartered Credit Unions**
OIG-05-06 June 8, 2005

We completed our review of NCUA's process for reviewing federally insured state chartered credit unions. Our three review objectives were to: (1) determine whether the NCUA process for determining and managing the risk that federally insured state chartered credit unions pose to the share insurance fund is adequate; (2) determine whether NCUA varies its approach depending on the level of risk presented by the credit unions in the various state supervisory authority (SSA) programs; and (3) determine whether NCUA performs formal reviews of all SSA examination reports and how the agency handles identified problems.

Our review found the NCUA process for managing risk to be adequate. The results of our review also indicated that NCUA varies its approach based on the level of risk presented by the credit unions in the various state programs. In addition, we found that NCUA was adequately reviewing state examination reports. Our data review and analysis showed that 99.7 percent of all state chartered credit unions had a formal NCUA exam review or joint examination by NCUA between January 1, 2001 and December 31, 2003. Further, NCUA and SSAs agreed on composite CAMEL ratings 94 percent of the time.

Our report includes one matter for consideration by NCUA – to better leverage the resources NCUA devotes to reviews of state chartered credit unions.

Independent Evaluation of the National Credit Union Administration Information Security Program 2005
OIG-05-07 September 30, 2005

The Federal Information Security Management Act (FISMA) permanently reauthorized the framework laid out in the Government Information Security Reform Act of 2000 (GISRA) which expired in November 2002. FISMA continues annual review and reporting requirements introduced in GISRA.

During 2005, the OIG engaged Cotton & Company LLP to conduct an independent evaluation of NCUA's information systems (IS) and security program and controls for compliance with FISMA, Title III of the E-Government Act of 2002. This report discusses the effectiveness of IS controls to protect and secure NCUA's information technology (IT) infrastructure and assets.

Our work identified two issues that can be classified as significant deficiencies in NCUA's security structure. While the Chief Information Officer (CIO) has initiated

projects to address these issues, both of the significant deficiencies concerning NCUA's security program remain open and are being reported for the third consecutive year.

The first issue involves several weaknesses related to NCUA's General Support System (GSS) Certification and Accreditation (C&A) and its technical components. This is significant, because every major application relies on the security of the operating system and network infrastructure on which it resides. Prevention of unauthorized access is necessary to ensure infrastructure security. NCUA's general support system continues to operate under an interim accreditation based on several weaknesses identified during the formal certification process in 2004.

The second issue involves sensitive information stored on examiners' laptop computers that had not been addressed as part of NCUA's information security program. The OCIO recently upgraded the examination application which included requiring all examination data stored on laptops to be encrypted. When completed, this project will represent an improvement in the protection of sensitive data. Training and implementation for this project will not be completed until November 1, 2005. Therefore, we were not able to test the effectiveness of the program as part of the 2005 review.

While we noted other weaknesses in IT controls, we concluded the two conditions described above are the most significant to NCUA.

OIG Report to OMB on NCUA's Compliance with the Federal Information Security Management Act 2005
OIG-05-08 September 30, 2005

This report contains a summary of our evaluation of the NCUA's information security program presented in the OMB prescribed format.

The OIG issued two reports during the past year that reported on the testing of the effectiveness of information security and internal controls:

- On September 30, 2005, the OIG issued a report containing an Independent Evaluation of the NCUA's Information Security Program - 2005. The content of the independent evaluation report supports the conclusions presented in this report.
- On March 15, 2005, the OIG issued the Financial Statement Audit Report for the year ended December 31, 2004. The purpose of this audit was to express an opinion on whether the financial statements were fairly presented. In addition, the internal control structure was reviewed and an evaluation of compliance with laws and regulations was performed as part of the audit. The result of this audit was an unqualified opinion, stating that the financial statements were presented fairly. Although there were no material weaknesses identified during the review of the internal control structures pertinent to financial reporting, fourteen

recommendations were made relating to weaknesses in the financial and information security areas.

Audit Memorandum: Employee State Tax Withholdings
OIG-05-09 September 30, 2005

The NCUA OIG performed a proactive review of NCUA employees' compliance with personal state income tax obligations. We initiated this project as a joint audit and investigative engagement. The overall objective was to identify any NCUA employees who may be delinquent in paying state income taxes.

The scope of this engagement was to review and analyze employee state tax withholdings in 2004, as reported on employee Internal Revenue Service (IRS) W-2 forms. The OIG may conduct a separate analysis regarding employees' Federal tax withholdings pending information requested from the Department of the Treasury's Internal Revenue Service.

There were a total of 1,011 employee W-2 records for 2004. Ten states do not have a personal income tax on employee wages. We identified five employees who had \$0 state income tax withheld and resided in a personal income taxable state. In addition, we identified two employees who had an effective state tax withholding rate of 0%. These two employees resided in personal income taxable states. Finally, we identified four employees who had post office boxes – one potential fraud indicator - listed for their addresses. These post office box addresses were in non-taxable states but were located approximately 50 miles or less from a taxable state border.

Overall, our review revealed relatively few employees with no state withholding taxes or questionable post office box addresses. The few instances of questionable withholdings were referred to the OIG Director of Investigations for investigative consideration.

Risk Based Scheduling

In addition to the above audits, we also conducted a survey of the NCUA's Risk Based Scheduling program. Our objective was to determine if NCUA Regional Offices are effectively and consistently scheduling federally insured credit unions for examination in accordance with national guidance. Specifically, the survey was aimed at answering the following questions: is scheduling consistently applied among regions; did deferred credit unions meet criteria to be deferred; and, were there credit unions that met the criteria that did not get deferred?

In conducting our survey we found that NCUA's Office of Examination and Insurance (E&I) had recently conducted similar work to obtain answers to the objectives we had proposed. We conducted interviews with key personnel and reviewed the reports developed by E&I on the subject. We determined that the work conducted was substantially similar in nature to our objectives and that this area did not warrant an audit of the subject matter.

AUDITS IN PROGRESS

Risk Focused Exams

The National Credit Union Administration (NCUA) expends significant resources to ensure the safe and sound operation of Federal credit unions. The major NCUA effort in this area is the performance of risk focused examinations (RFE) and supervision. The current RFE program was initiated in 2002.

The Office of Inspector General (OIG) will be gathering information for a national review of certain aspects of the RFE program. The survey phase objective is to evaluate NCUA's process for identifying and addressing risk factors through the examination process for CAMEL 3 rated Federal credit unions.

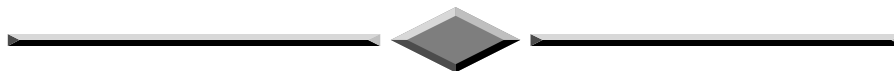
Share Insurance Fund

The National Credit Union Share Insurance Fund reports insurance losses due to failed federally insured credit unions. Several NCUA offices are involved in recording and reporting of such losses. The NCUA OIG performed an audit survey to assess the accuracy and reliability of reported insurance losses for credit unions that failed in 2004.

We assessed inherent risks, reviewed insurance loss recording and reporting procedures, and compared credit union failures and insurance losses among various reports. We also conducted an analysis of the data provided and conducted interviews with management to address any discrepancies we identified. We issued a draft report to management for comment in September 2005.

SIGNIFICANT AUDIT RECOMMENDATIONS ON WHICH CORRECTIVE ACTION HAS NOT BEEN COMPLETED

As of September 30, 2005, there were no significant audit recommendations on reports issued over six months ago that have not been either fully implemented or are in the process of implementation.



INVESTIGATIVE ACTIVITY

In accordance with professional standards and guidelines established by the Department of Justice, the OIG performs investigations of criminal, civil, and administrative wrongdoing involving agency programs and personnel. Our investigative program focuses on activities designed to promote economy, effectiveness, and efficiency, as well as fighting fraud, waste, and abuse in agency programs. In addition to our efforts to deter misconduct and promote integrity awareness among agency employees, we investigate referrals and direct reports of employee misconduct. Investigations may involve possible violations of regulations regarding employee responsibilities and conduct, Federal criminal law, and other statutes and regulations pertaining to the activities of NCUA employees.

Moreover, we receive complaints from credit union members and officials that involve NCUA employee program responsibilities. We examine these complaints to determine whether there is any indication of NCUA employee misconduct. If not, we refer the complaint to the appropriate regional office for response, or close the matter if contact with the regional office indicates that the complaint has already been appropriately handled.

OIG HOTLINE CONTACTS

The OIG maintains a toll free hotline to enable employees and citizens to call with information about waste, fraud, abuse or mismanagement involving agency programs or operations. We also receive complaints through an off-site post office box, electronic mail, regular U.S. mail, and facsimile messages. All information received from any of these sources is referred to as a hotline contact. The OIG hotline program is handled by our Office Manager, under the direction of our Director of Investigations. The majority of hotline contacts are from consumers seeking help with a problem with a credit union. These contacts are referred to the appropriate NCUA regional office for assistance. During this reporting period, we referred 89 consumer complaints to regional offices.

PHISHING ACTIVITY

During this reporting period, our hotline program experienced a significant increase in complaint activity. Much of this was due to a rash of Phishing attempts made by individuals using the NCUA name and logo in an effort to obtain personal and financial information from credit union members. Our office alone received over 600 complaints from citizens reporting suspected Phishing attempts. We responded directly to many of the individuals and referred their complaints to the NCUA Chief Information Officer (CIO).

The CIO, working in conjunction with the FBI; Secret Service; Department of Homeland Security; United States Attorney's Office (USAO); private consultants; credit unions;

banks; and card services network providers, have been working on this issue for several months and continue to do so. In addition, the agency moved quickly to educate and publicize the Phishing scams to as wide an audience as possible. This was achieved through press releases, letters to credit unions, and a notice prominently displayed on the homepage of NCUA's website. NCUA collects Phishing attack information through the agency's fraud hotline, the IG's hotline and email links provided on the NCUA website. NCUA computer systems, websites and networks have not sustained any damage, destruction or infiltration as a result of these Phishing attempts.

INVESTIGATIONS

During the last reporting period the Office of Investigations experienced a marked increase in the number of matters referred or reported for investigative consideration. During this period we initiated eight new investigations and closed six.

Use of Non-Public Information

One investigation involved allegations that an NCUA Examiner used information gained by reason of her employment to benefit personally from a potential dividend being paid as a result of a merger of two credit unions. The case was initially accepted for criminal prosecution and worked at the direction of the USAO. The investigation determined that the employee had opened a credit union account after learning through her job as an Examiner that the credit union was considering a merger. The higher than average level of retained earnings of the merging credit union made it more likely that a generous merging dividend would be paid to members with higher account balances. The OIG obtained considerable evidence, much of it through Grand Jury Subpoena, suggesting that the employee had intentionally diverted considerable funds from accounts she held with other financial institutions into her and her husband's credit union accounts, which would have resulted in a significant merging dividend once the institution completed the merger. During her interview with the OIG, the employee confessed to augmenting her and her husband's credit union accounts in order to increase the merging dividend. Ultimately, the USAO declined prosecution in favor of administrative action and the agency proposed the removal of the employee. The employee resigned. Additional issues developed during this investigation were referred to the Department of Justice for further investigative consideration.

During this same investigation, the OIG learned that another NCUA Examiner had also allegedly opened an account at the same credit union in order to benefit from the potential merging dividend. The OIG conducted an investigation of this employee and determined that while he had opened an account, there was insufficient evidence to conclude it had been done with the intention of benefiting from a potential merging dividend. On the basis of his actions creating an appearance of misuse of public information, the NCUA proposed a three day suspension of the employee which was later mitigated to no suspension.

Post Employment Ethics Issues

The OIG closed one matter through the issuance of a Management Implication Report (MIR) regarding the agency's process of providing ethics advice, specifically related to post-employment restrictions, to senior agency officials. The MIR was issued as a result of an allegation involving a former NCUA Board Member. The OIG received a complaint alleging that the Board Member's contacts with a trade association regarding prospective employment constituted a possible violation of criminal conflict of interest statutes and the *Standards of Ethical Conduct for Employees of the Executive Branch*.

Our investigation into this matter ultimately concluded that the subject's contacts with the prospective employer did not amount to "negotiations" and therefore, did not trigger a conflict of interest or ethics violation. The subject had, however, unknowingly interacted with members of the trade association in a way that technically violated conflict of interest statutes related to "seeking employment." The intricacies and peculiarities of the rules governing current Federal employees seeking employment underscore the need for periodic refreshers and updates for employees planning to retire or leave Federal service. During the investigation, we learned that the employee had on only one occasion—at the outset of his employment with NCUA a number of years previously -- received ethics information pertaining to rules for seeking employment or post employment activities. The information provided at that time was in the form of written handouts on numerous ethics issues, including conflicts of interest and seeking employment. More recently, however, even while agency ethics officials knew that the employee's departure from the agency was imminent, he was not provided additional or current guidance regarding his employment search.

In the course of reviewing this matter, the OIG referred to a similar matter that was the subject of an OIG investigation in 1997. That investigation concerned whether a senior agency official participated in particular matters at the same time he was negotiating for employment with a credit union trade association. In that case, the OIG made the recommendation that the Designated Agency Ethics Official (DAEO) should take a proactive approach in providing ethics advice to Board members, Board staff, and other high level employees with respect to outside and prospective employment. Responding to our recommendations in 1997, the NCUA then-Executive Director (ED) agreed to the recommendation and issued a reprimand to the DAEO on the issue.

Despite the OIG's recommendations and the agency's response to those recommendations, we were unable to find that the NCUA DAEO thereafter provided particularized ethics advice to senior officials planning to leave Federal service and return to private employment, in writing or otherwise. The DAEO at the time of this investigation (now retired) confirmed to the OIG that the NCUA did not have in place an established process by which outgoing senior staff and board members are made aware of potential conflicts of interest in seeking post-NCUA employment. The United States Office of Government Ethics emphasizes that employees planning to leave government service and return to the private sector should seek complete and specific advice from

their agency's ethics official, as early as possible. The culmination of the 1997 OIG investigation was our recommendation that it is likewise the responsibility of NCUA's DAEO to assume a proactive role in providing such advice.

Consequently, we reiterated in this report our previous recommendation that the DAEO take a more active role in advising employees regarding rules for seeking employment and post employment activities.

False Statements

One investigation involved an allegation that a career NCUA Examiner had provided false information during a routine background investigation, and when questioned about the alleged false information, reiterated his original false statement. The matter was referred to the OIG for investigation. The OIG investigation developed numerous instances spanning twenty years of the employee providing false or misleading information on official documents. The employee was interviewed by the OIG under a Kalkines agreement during which he provided additional false and misleading information. The agency proposed the removal of the employee. As of the date of this report, there has been no final determination.

During this investigation, the OIG learned that the agency's Office of Human Resources (OHR) had been routinely providing the names of witnesses identified in OIG Reports of Investigation in proposed disciplinary action letters resulting from our investigations. Contrary to the prohibition we include as a footer on each page of every report, these disclosures were without our knowledge or authorization. In this case, the Inspector General became aware that the OHR was planning to send a letter of proposed removal to an employee who had been the subject of an OIG investigation. The letter contained the name of a witness in the investigation. The Inspector General notified the agency in writing that he did not authorize the release of the witnesses' name, and the OHR disregarded this direction and released the name and large portions of the witness' testimony to the subject of the investigation. The Inspector General made his position clear to agency management that the release of such information contained in OIG reports is the decision of the OIG and that future proposal letters from the agency based on OIG Reports of Investigation must not include witness names without the authorization of the OIG.

Also during this investigation, the issue arose of OIG staff's access to requested documents. A document was requested and withheld, at the direction of the same individual on whom we reported a similar incident in our October 2000 Semiannual Report. The Inspector General reported this incident to the head of the agency, and made clear the OIG authority to have access, upon request and without delay, to agency records and information.

Time and Attendance Fraud

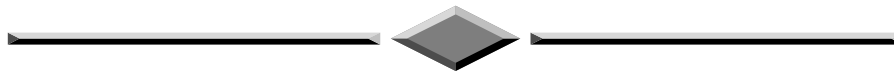
One investigation involved an allegation that an employee had been falsifying attendance records and had been using other employees to set up her work station in order to create the false impression that she was present at work. The subject employee and two other employees were interviewed and admitted to the allegations. The subject employee was given a proposed ten day suspension, which was later mitigated to a five day suspension. The two other employees were given letters of reprimand for their actions in assisting the subject employee.

Misuse of Government Property

One investigation involved allegations that an employee had used the agency computer to send sexually explicit material to another employee. The investigation found the allegation to be unsubstantiated.

Theft

The OIG closed to file another investigation into the theft of an agency computer at the NCUA Headquarters building in Alexandria, Virginia. Agency personnel initially believed the removal of the computer was done as a prank and the matter was not reported to the OIG until a few days after the theft had occurred. Once reported, the OIG reviewed video security footage and interviewed staff. No suspects were developed.



LEGISLATIVE AND REGULATORY REVIEWS

Section 4(a) of the Inspector General Act requires the Inspector General to review existing and proposed legislation and regulations relating to the programs and operations of the NCUA and to make recommendations concerning their impact. Moreover, we routinely review proposed agency instructions and other policy guidance, in order to make recommendations concerning economy and efficiency in the administration of NCUA programs and operations and the prevention and detection of fraud, waste and abuse.

During the reporting period, the OIG reviewed 20 items, including proposed and final changes to legislation and regulations and several NCUA issuances. The OIG submitted no comments on the items reviewed.

SUMMARY OF STATUTES AND REGULATIONS REVIEWED	
Legislation	Title
H.R. 3737 (Proposed)	“Special Inspector General for Hurricane Katrina Recovery Act”
H.R. 3805 (Proposed)	“Special Office of the Inspector General for Natural Disaster Response and Reconstruction within the DHS OIG”
H.R. 3810 (Proposed)	“Special Inspectors General Council for Hurricane Katrina”
S. ____ (Proposed)	“Special Inspector General for Relief and Reconstruction Act of 2005”
H.R. 3505	“Financial Services Regulatory Relief Act of 2005”
H.R. 2317	“Credit Union Regulatory Improvements Act of 2005”
H.R. 1042	“Net-Worth Amendment for Credit Unions Act”
Regulations/Rulings	Title
12 CFR 741.6	“Requirements for Insurance—Quarterly Financial and Statistical Report”
12 CFR Part 796	“Post-Employment Restrictions for Certain NCUA Examiners”
12 CFR Parts 701 and 741	“Uninsured Secondary Capital Accounts”
12 CFR Part 742	“Regulatory Flexibility Program”
12 CFR Part 717	“Fair Credit Reporting Medical Information Regulations”
12 CFR Parts 713 and 741	“Fidelity Bond and Insurance Coverage for Federal Credit Unions”
12 CFR Part 712	Final Rule: “Audit Requirement for Credit Union Service Organizations”

12 CFR Part 723	“Member Business Loans”
	Federal Credit Union Bylaws—Request for Comment
5 CFR Part 550	Pay Administration (General)
Agency Issuances	Title
IRPS 05-01	“Sales of Nondeposit Investments”
Instruction 5000.15 (Rev. 1)	Risk Based Examination Scheduling
Instruction 5000.18	Hurricane Katrina Examination and Supervision Program Flexibility
Instruction 13500.07	Security Backup of Files on NCUA Personal Computers

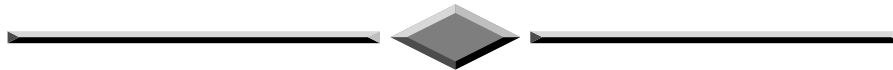


TABLE I

INSPECTOR GENERAL ISSUED REPORTS WITH QUESTIONED COSTS				
		Number of Reports	Questioned Costs	Unsupported Costs
A.	For which no management decision had been made by the start of the reporting period.	0	\$0	\$0
B.	Which were issued during the reporting period.	0	0	0
	Subtotals (A + B)	0	0	0
C.	For which management decision was made during the reporting period.	0	0	0
	(i) Dollar value of disallowed costs	0	0	0
	(ii) Dollar value of costs not disallowed	0	0	0
D.	For which no management decision has been made by the end of the reporting period.	0	0	0
E.	Reports for which no management decision was made within six months of issuance.	0	0	0

Questioned costs are those costs the OIG has questioned because of alleged violations of laws, regulations, contracts, or other agreements; findings which at the time of the audit are not supported by adequate documentation; or the expenditure for the intended purpose is unnecessary or unreasonable.

Unsupported costs (included in "Questioned Costs") are those costs the OIG has questioned because of the lack of adequate documentation at the time of the audit.

TABLE II

INSPECTOR GENERAL ISSUED REPORTS WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE			
		Number of Reports	Dollar Value
A.	For which no management decision had been made by the start of the reporting period.	0	\$0
B.	Which were issued during the reporting period.	0	0
	Subtotals (A + B)	0	0
C.	For which management decision was made during the reporting period.	0	0
	(i) Dollar value of recommendations agreed to by management.	N/A	N/A
	(ii) Dollar value of recommendations not agreed to by management.	N/A	N/A
D.	For which no management decision was made by the end of the reporting period.	0	0
E.	For which no management decision was made within six months of issuance.	0	0

Recommendations that "Funds to be Put to Better Use" are those OIG recommendations that funds could be used more efficiently if management took actions to reduce outlays, de-obligate funds from programs/operations, avoid unnecessary expenditures noted in pre-award reviews of contracts, or any other specifically identified savings.

TABLE III

<p align="center">SUMMARY OF OIG ACTIVITY APRIL 1, 2005 THROUGH SEPTEMBER 30, 2005</p>		
<p>PART I – AUDIT REPORTS ISSUED</p>		
Report Number	Title	Date Issued
OIG-05-06	NCUA’s Process for Reviewing Federally Insured State Chartered Credit Unions	6/08/2005
OIG-05-07	Independent Evaluation of the National Credit Union Administration Information Security Program 2005	9/30/2005
OIG-05-08	Report to OMB on NCUA’s Compliance with the Federal Information Security Management Act 2005	9/30/2005
OIG-05-09	Audit Memorandum: Employee State Tax Withholdings	9/30/2005
<p>PART II – AUDITS IN PROGRESS (as of September 30, 2005)</p>		
	Risk Focused Exams	
	Share Insurance Fund Losses	

INDEX OF REPORTING REQUIREMENTS

SECTION	DATA REQUIRED	PAGE REF
4(a)(2)	Review of Legislation and Regulations	20
5(a)(1)	Significant Problems, Abuses, or Deficiencies relating to the administration of programs and operations disclosed during the reporting period.	11
5(a)(3)	Recommendations with Respect to Significant Problems, Abuses, or Deficiencies.	11
5(a)(3)	Significant Recommendations Described in Previous Semiannual Reports on Which Corrective Action Has Not Been Completed.	14
5(a)(4)	Summary of Matters Referred to Prosecution Authorities and Prosecutions, Which Have Resulted.	None
5(a)(5)	Summary of Each Report to the Board Detailing Cases Where Access to All Records Was Not Provided or Where Information Was Refused.	ii
5(a)(6)	List of Audit Reports Issued During the Reporting Period.	24
5(a)(7)	Summary of Particularly Significant Reports.	11
5(a)(8)	Statistical Tables on Audit Reports With Questioned Costs.	22
5(a)(9)	Statistical Tables on Audit Reports With Recommendations That Funds Be Put To Better Use.	23
5(a)(10)	Summary of Each Audit Report Issued Before the Start of the Reporting Period for Which No Management Decision Has Been Made by the End of the Reporting Period.	None
5(a)(11)	Description and Explanation of Reasons for any Significant Revised Management Decision Made During the Reporting Period.	None
5(a)(12)	Information Concerning Significant Management Decisions With Which the Inspector General is in Disagreement.	None



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www.ncua.gov/oig