



NATIONAL CREDIT UNION ADMINISTRATION

WASHINGTON, D.C. 20456

July 12, 1990

Joseph L. Lents, CPA
Nearman & Lents
Certified Public Accountants
11961 S.W. 144th Street
Miami, FL 33186

Re: CPA Audits (Your July 9 Letter)

Dear Mr. Lents:

You asked when federally insured credit unions are required to obtain CPA audits. CPA audits are not required under Section 701.12 of the NCUA Rules and Regulations (12 C.F.R. 701.12). Pursuant to Section 701.12, the supervisory committee may perform the required annual audit itself, or it may engage the services of an outside auditor. An audit performed by a CPA is only required when one of the conditions set forth in Section 701.13 is present. Enclosed are copies of Sections 701.12 and 701.13, as well as the Federal Register publications of the proposed and final versions of Section 701.13 which include explanatory information.

In addition, CPA opinion audits are required for corporate federal credit unions pursuant to Section 704.5 of the NCUA Regulations, enclosed.

I hope that we have been of assistance.

Sincerely,

Hattie M. Ulan
Associate General Counsel

GC/HMU:sg
SSIC 3500
90-0706
Enclosures

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and the continuing Federal credit union as of June 30. For purposes of this requirement, a purchase and assumption transaction wherein the continuing Federal credit union purchases all or essentially all of the assets of another credit union shall be deemed a merger. Federal credit unions merging with other Federal or state credit unions will not receive a refund of the operating fee paid to the Administration in the year in which the merger takes place.

(4) *Liquidations.* A Federal credit union placed in liquidation will not pay any operating fee after the date of liquidation.

(c) *Notification.* Each Federal credit union shall be notified at least 30 days in advance of the schedule of fees to be paid. A Federal credit union may submit written comments to the Board for consideration regarding the existing fee schedule. Any subsequent revision to the schedule shall be provided to each Federal credit union at least 15 days before payment is due.

(d) *Assessment of Administrative Fee and Interest for Delinquent Payment.* Each Federal credit union shall pay to the Administration an administrative fee, the costs of collection, and interest on any delinquent payment of its operating fee. A payment will be considered delinquent if it is postmarked later than the date stated in the notice to the credit union provided under §701.6(c). The National Credit Union Administration may waive or abate charges or collection of interest if circumstances warrant.

(1) The administrative fee for a delinquent payment shall be an amount fixed from time to time by the National Credit Union Administration Board and based upon the administrative costs of such delinquent payments to the Administration in the preceding year.

(2) The costs of collection shall be the actual hours expended by Administration personnel multiplied by the average hourly salary and benefits costs of such personnel as determined by the National Credit Union Administration Board.

(3) The interest rate charged on any delinquent payment shall be the U.S. Department of the Treasury Tax and Loan Rate in effect on the date when the payment is due as provided in 31 U.S.C. §3717.

(4) If a credit union makes a combined payment of its operating fee and its share insurance deposit as provided in Section 741.9 and such payment is delinquent, only one administrative fee will be charged and interest will be charged on the total combined payment.

§701.7 Deleted June 1979.

§701.8 Deleted June 1979.

§701.9 Deleted May 1977.

§701.10 Deleted February 1988.

§701.11 Deleted August 1981.

§701.12 **Supervisory committee audits and verifications.**

(a) The supervisory committee is responsible to determine that the financial condition of the credit union is accurately and fairly presented in the credit union's statements and that management practices and procedures are sufficient to safeguard members' assets. To accomplish this responsibility, the supervisory committee shall determine that the credit union's accounting records and reports are prepared promptly and accurately reflect operations and results, that internal controls are established and effectively maintained to safeguard the credit union's assets, and that the plans, policies, and control procedures established by the board of directors are being properly administered. The supervisory committee is also responsible for reviewing policies and control procedures to safeguard against error, carelessness, fraud, and self-dealing (conflict of interest). The audit and verification of members' accounts, mandated in the Act, are the activities generally used to carry out these responsibilities; however, the committee is expected to exercise such other tests and reviews as may be necessary in the committee's judgment to meet its responsibilities.

(b) An audit of each Federal credit union shall occur at least once every calendar year and shall cover the period elapsed since the last audit. The audit shall be made using generally accepted auditing procedures and standards. However, each Federal credit union's annual audit shall, as a minimum, test the Federal credit union's assets, liabilities, equity, income, and expenses for existence, proper cut off, valuations, ownership, disclosures and classification, and internal controls. Upon completion, a report of the audit shall be made promptly to the board of directors of the Federal credit union and, upon request, of the National Credit Union Administration's regional director. It is the responsibility of the supervisory committee to ensure that the completion of the annual audit is timely, that generally accepted auditing procedures

are used, that adequate audit of the credit union records is made, and that the audit report is promptly prepared and reported to the board of directors.

(c) The supervisory committee and/or its independent auditors shall be responsible for the preparation and the maintenance of workpapers used to support each audit. Such workpapers shall be made available by the supervisory committee and its independent auditors for review by any authorized employee of the National Credit Union Administration.

(d) Federal credit union compensated auditors, performing audits for supervisory committees, must be independent of the credit union's employees, members of the board of directors, supervisory and credit committees and/or the credit union's loan officers, and members of their immediate families. "Members of their immediate families" means a spouse, or a child, parent, grandchild, grandparent, brother or sister, or the spouse of any such individual.

(e) The verification of members' accounts shall be made using any of the following methods:

(1) A controlled verification of 100 percent of members' share and loan accounts;

(2) A controlled random statistical sampling method that accurately tests sufficient accounts in both number and scope to provide assurance that the General Ledger accounts are fairly stated and that members' accounts are properly safeguarded. That sampling procedure must provide each member account an equal chance of being selected.

Records of those accounts verified will be maintained and will be retained until the next verification of members' accounts is completed.

§701.13 Requirements for an Outside Audit

(a) A Federal credit union shall obtain an outside, independent audit by a certified public accountant for any fiscal year during which any one of the following three conditions is present:

(1) the supervisory committee on the Federal credit union has not conducted an annual supervisory committee audit;

(2) the annual supervisory committee audit conducted did not meet the audit requirements of §701.12 including §701.12 (e);

(3) the Federal credit union has experienced serious and persistent recordkeeping deficiencies as defined in Subsection (c) below.

(b) In the case of an audit required pursuant to condition (1) or (2) in paragraph (a) above, the scope of the outside, independent audit conducted by a

certified public accountant must fully encompass the requirements set forth in §701.12. In the case of an audit required pursuant to condition (3) above, the outside, independent audit by a certified public accountant must be an opinion audit as that term is understood under generally accepted auditing standards.

(c) As used in condition (3) of paragraph (a) above, persistent recordkeeping deficiencies shall mean serious recordkeeping problems which continue to exist past a usual, expected, or normal period of time. Persistent recordkeeping deficiencies shall be considered serious if the Administration has a reasonable doubt that the financial condition of the credit union is accurately and fairly presented in the credit union's statements and that management practices and procedures are sufficient to safeguard members' assets.

§701.14 Deleted May 1982.

§701.15 Deleted June 1979.

§701.16 Deleted December 1981.

§701.17 Deleted December 1981.

§701.18 Deleted December 1981.

§701.19 Retirement Benefits for Employees of Federal Credit Unions.

(a) A Federal credit union may make provision for reasonable retirement benefits for its employees and for officers who are compensated in conformance with the Act and the bylaws, either individually or collectively with other credit unions. In those cases where a Federal credit union is to be a plan trustee or custodian, the plan must be an individual retirement account maintained in accordance with the provisions of Part 724. Where the trustee or custodian is a party other than the Federal credit union, the employee benefit plan must be maintained in accordance with the applicable laws governing employee benefit plans and such rules and regulations as may be promulgated by the Secretary of Labor, the Secretary of the Treasury, or any other Federal or state authority exercising jurisdiction over such plans.

(b) No Federal credit union shall occupy the position of a fiduciary, as defined in the Employee Retirement Income Security Act of 1974 and rules and regulations promulgated thereunder by the Secretary of Labor, unless provision has been made

NCUA intends to propose procedural rules to advise persons of the process to be utilized when a nuclear safety violation has been alleged. The initiation of that rulemaking will be noticed in the Federal Register in the near future.

Issued in Washington, DC, September 15, 1989.

Eric J. Fygi,

Acting General Counsel.

[FR Doc. 89-22332 Filed 9-20-89; 9:45 am]

CALLING CODE 8718-01-M

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 701 and 741

Requirements For An Outside Audit; Requirements for Insurance

AGENCY: National Credit Union Administration (NCUA).

ACTION: Proposed rule.

SUMMARY: This proposed rule adds § 701.13 and amends § 741.2. The proposed rule prescribes the regulatory requirement for an outside, independent audit of any federally insured credit union by a certified public accountant under certain specified conditions. The proposed rule is being added to reflect applicable provisions of Public Law 101-73, the Federal Financial Institutions Reform, Recovery, and Enforcement Act of 1989.

DATE: Comments must be received on or before October 23, 1989.

ADDRESS: Send comments to Becky Baker, Secretary of the Board, National Credit Union Administration, 1776 G Street, NW., Washington, DC 20456.

FOR FURTHER INFORMATION CONTACT: D. Michael Riley or Karen K. Kefly, Office of Examination and Insurance, Telephone Number: (202) 682-0840.

SUPPLEMENTARY INFORMATION.

Paperwork Reduction Act

The Office of Management and Budget has approved the collection requirements contained in § 701.12 of NCUA's Regulations (OMB No. 3133-0075) relating to supervisory committee audits and verification of accounts. The proposed rule is within this collection requirement.

Background

This proposed rule is necessitated by section 919 of the Federal Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FFIRREA) which amends section 202(a) of the Federal Credit Union Act (12 U.S.C.

1791(a)). FFIRREA requires that within 120 days of its enactment, the NCUA Board prescribe, by regulation, audit requirements for the outside, independent audit of any federally insured credit union by a certified public accountant under certain conditions.

Current Audit Requirements

Section 115 of the Federal Credit Union Act (12 U.S.C. 1761(d)) requires that the supervisory committee of a federal credit union make or cause to be made an annual audit. Section 701.12(a) of the NCUA Rules and Regulations (12 CFR 701.12(a)) discusses the supervisory committee's responsibilities and the audit and verification activities generally used to carry out these responsibilities. Section 701.12(b) references generally accepted auditing standards and discusses the minimum audit tests needed and the audit reporting requirements. Section 701.12(c) discusses the preparation, maintenance and availability requirements for workpapers in support of the annual audit. Section 701.12(d) requires that credit union compensated auditors be independent as defined therein. And § 701.12(e) provides instructions for the verification of members' accounts, which must be accomplished at least once every 2 years.

It is NCUA's understanding that most, if not all, states have comparable annual audit requirements for federally insured state chartered credit unions. In any event, FFIRREA clearly imposes a requirement that every federally insured credit union annually obtain either a complete and satisfactory supervisory committee audit or an independent audit by a certified public accountant. Additionally, § 741.2 of the NCUA Rules and Regulations requires any federally insured credit union to make or cause to be made a verification of member's accounts not less frequently than once every 2 years consistent with § 701.12(e).

Proposed Additional requirement

This proposed rule would add § 701.13 for federal credit unions which provides that, under certain specified conditions (discussed below), the Administration will require an outside, independent audit or verification, as applicable, to be conducted by a certified public accountant. Additionally, the proposed rule would amend § 741.2 to require federally insured credit unions to meet the audit requirements of § 701.12 and § 701.13.

As required by section 919 of FFIRREA, § 701.13 defines the three conditions under which an outside, independent audit by a certified accountant shall be required:

- (1) The supervisory committee of the credit union has not conducted an annual supervisory committee audit; or
- (2) The annual supervisory committee audit conducted was not complete and satisfactory; or
- (3) The credit union has experienced serious and persistent recordkeeping deficiencies.

The proposed regulation is discussed in greater detail below in light of each of these three conditions.

No Audit Conducted

If a credit union fails to obtain an annual audit or does not verify members' accounts at least once every 2 years, the proposed rule would require an outside, independent audit by a certified public accountant, such audit or verification to fully comply with the existing rules in § 701.12.

Audit Incomplete or Unsatisfactory

Any supervisory committee audit which does not satisfactorily and completely address the § 701.12(a) general guidelines, does not encompass the § 701.12(b) minimum testing requirements, is not properly supported by adequate and complete workpaper evidence in accordance with § 701.12(c), or was conducted by a compensated auditor who was not independent as defined in § 701.12(d), will be considered to fall within the scope of this proposed rule, i.e., the credit union will be required to obtain an outside, independent audit by a certified public accountant, such audit to fully comply with § 701.12.

Additionally, verifications which do not fully meet the requirements of § 701.12(e) and amended 741.2(b) will fall within the scope of this proposed rule and the credit union will be required to obtain an outside, independent verification by a certified public accountant.

Serious and Persistent Recordkeeping Deficiencies

The proposed rule will require a more comprehensive audit (greater audit scope than § 701.12 minimum tests) for credit unions having serious and persistent recordkeeping deficiencies as defined herein. Credit unions with serious and persistent recordkeeping problems will be required by the Administration to obtain an outside, independent audit by a certified public accountant in accordance with generally accepted auditing standards which results in an opinion, i.e., the audit must provide a reasonable basis for expressing an opinion regarding the financial statements taken as a whole.

The Administration believes this higher level of review is necessary for safety and soundness reasons when a credit union has serious recordkeeping problems which continue to exist past a usual, expected, or normal period of time. Persistent recordkeeping deficiencies will be considered serious if the Administration has a reasonable doubt that the financial condition of the credit union is accurately and fairly presented in the credit union's statements and that management practices and procedures are sufficient to safeguard members' assets.

Audit work performed by other than a certified public accounting firm will be accepted provided that a certified public accountant certifies the financial statements and attests to the opinion, therefore bearing full responsibility and accountability to the Administration for the opinion expressed thereon.

Executive Order 12612

Congress has mandated in section 919 of FFIRREA that NCUA prescribe regulations requiring that all federally insured state chartered credit unions obtain an outside, independent audit by a certified public accountant if the credit union has not obtained an annual supervisory committee audit, the supervisory committee audit is not complete and satisfactory or the credit union has experienced serious and persistent recordkeeping deficiencies as defined by the NCUA Board.

To implement the FFIRREA provisions, it is incumbent upon NCUA to define what constitutes a "complete and satisfactory supervisory committee audit" and "serious and persistent recordkeeping deficiencies". To accomplish this, NCUA has proposed to apply to federally insured state credit unions the same standards that exist in § 701.12 and proposed § 701.13 for federal credit unions.

It is the NCUA Board's belief that this is the most fair and administratively feasible method of accomplishing the requirements of FFIRREA, and that, inasmuch as state-chartered credit unions are already subject to comparable audit requirements under state law, significant new burdens will not be imposed beyond those legislatively mandated by FFIRREA. Comments are requested on this approach.

Regulatory Procedures

Regulatory Flexibility Act

The NCUA Board certifies that the proposed rule, if made final, should not have a significant impact on a substantial number of small credit

unions. The proposed rule will only affect small credit unions to the extent they do not adhere to existing regulations. Accordingly, the NCUA Board has determined that a Regulatory Flexibility Analysis is not required.

List of Subjects

12 CFR 701

Credit unions, Reporting and recordkeeping requirements, Supervisory committee audits.

12 CFR 741

Credit unions; Reporting and recordkeeping requirements.

By the National Credit Union Administration Board on September 14, 1989.

Becky Baker,

Secretary of the Board.

Accordingly, NCUA proposes to amend its regulations as follows:

PART 701—(AMENDED)

1. The authority citation for part 701 is revised to read as follows:

Authority: 12 U.S.C. 1755, 1756, 1757, 1759, 1761(a), 1761(b), 1766, 1767, 1782, 1784, 1787, 1789, and 1796; and P.L. 101-73. Section 701.37 is also authorized by 15 U.S.C. 1601 et. seq., 42 U.S.C. 1861 and 42 U.S.C. 3601-3610.

2. Section 701.13 be added to read as follows:

§ 701.13 Requirements for an outside audit.

(a) A federal credit union shall obtain an outside, independent audit by a certified public accountant for any fiscal year during which any one of the following three conditions is present:

(1) The supervisory committee of the federal credit union has not conducted an annual supervisory committee audit;

(2) The annual supervisory committee audit conducted did not meet the audit requirements of § 701.12 including § 701.12(e);

(3) The Federal credit union has experienced serious and persistent recordkeeping deficiencies as defined in paragraph (c) of this section.

(b) For the purposes of this section and in relation to conditions (a) (1) and (2) of this section, the scope of the outside, independent audit conducted by a certified public accountant must fully encompass the requirements set forth in § 701.12. For the purposes of this section and in relation to condition (a)(3) of this section, the outside, independent audit by a certified public accountant must be an opinion audit as that term is understood under generally accepted auditing standards.

(c) For the purposes of this section and in relation to condition (a)(3) of this section, persistent recordkeeping deficiencies shall mean serious recordkeeping problems which continue to exist past a usual, expected, or normal period of time. Persistent recordkeeping deficiencies shall be considered serious if the Administration has a reasonable doubt that the financial condition of the credit union is accurately and fairly presented in the credit union's statements and that management practices and procedures are sufficient to safeguard members' assets.

PART 741—(AMENDED)

1. The authority citation for part 741 is revised to read as follows:

Authority: 12 U.S.C. 1757, 1786(a), and 1781 through 1790; P.L. 101-73.

2. Section 741.2 be revised to read as follows:

§ 741.2 Audit and verification requirements.

(a) The supervisory committee of each credit union insured pursuant to title II of the Act shall make or cause to be made an audit of the credit union at least once every calendar year covering the period elapsed since the last audit. The audit must fully meet the requirements set forth in §§ 701.12 and 701.13.

(b) Each credit union which is insured pursuant to title II of the Act shall verify or cause to be verified, under controlled conditions, all passbooks and accounts with the records of the treasurer not less frequently than once every 2 years. The verification must fully meet the requirements set forth in §§ 701.12(e) and 701.13.

[FR Doc. 89-22318 Filed 9-20-89; 8:45 am]
BILLING CODE 7030-01-8

DEPARTMENT OF TRANSPORTATION

Office of the Secretary

14 CFR Part 255

[Docket No. 46494; Notice No. 89-18]

RIN 2105-AB47

Computer Reservation System

AGENCY: Office of the Secretary, DOT
ACTION: Advance notice of proposed rulemaking.

SUMMARY: The Department is initiating this rulemaking to determine the need to continue or modify its existing rules governing computer reservations

acquisition, in whole or in part, of a BIF member during such semiannual period.

(4) "Deposits acquired by the bank." As used in paragraph (a)(3)(i) of this section, the term "deposits acquired by the bank" means all deposits that are held in the institution acquired by such bank on the date of such transaction; *Provided*, That if the Corporation or the Resolution Trust Corporation has been appointed as conservator or receiver for the acquired institution, such term—

(i) Does not include any deposit held in the acquired institution on the date of such transaction which the acquired institution has obtained, directly or indirectly, by or through any deposit broker; and

(ii) Does not include that part of any remaining deposit held in the acquired institution on the date of such transaction that is in excess of \$80,000;

(iii) Is limited to 80 per centum of the remaining portion of the aggregate of the deposits specified in paragraph (a)(4)(ii) of this section.

(5) "Deposit broker." As used in paragraph (a)(4) of this section, the term "deposit broker" has the meaning specified in section 29 of the Federal Deposit Insurance Act (12 U.S.C. 1831f).

(b) *Procedures for computation and payment.* A bank subject to subpart D of this part shall follow the payment procedure that is set forth in subpart B of this part.

§ 327.33 Form of certified statement.

The certified statement to be filed by a bank subject to subpart D of this part shall be in the form prescribed by the Corporation.

By order of the Board of Directors.

Dated at Washington, DC, this 5th day of December 1989.

Federal Deposit Insurance Corporation.

Hoyle L. Robinson,

Executive Secretary.

[FR Doc. 89-29188 Filed 12-14-89; 8:45 am]

BILLING CODE 6174-01-M

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 701 and 741

Requirements For An Outside Audit; Requirements for Insurance

AGENCY: National Credit Union
Administration (NCUA).

ACTION: Final rule.

SUMMARY: This final rule adds § 701.13 and amends § 741.2. The rule prescribes the regulatory requirement for an outside, independent audit of any federally insured credit union by a

certified public accountant (CPA) under certain specified conditions. The rule is being added to reflect applicable provisions of Public Law 101-73, the Federal Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). The rule is substantially unchanged from a proposed rule issued in September 1989.

EFFECTIVE DATE: December 7, 1989.

ADDRESS: National Credit Union Administration, 1776 G Street, NW., Washington, DC 20456.

FOR FURTHER INFORMATION CONTACT: D. Michael Riley or Karen K. Kelbly, Office of Examination and Insurance, at the above address or telephone (202) 682-9640.

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The proposed rule stated that this rule imposed no additional paperwork requirements. During the comment period, NCUA staff reconsidered this position and determined that the proposed rule did impose additional requirements. They are as follows:

a. Some additional paperwork burden may be added in the case of a credit union which performed an audit under § 701.12 which was deemed unsatisfactory; and

b. Additional audit workpapers required by a CPA to complete an opinion audit will be required in the case of a credit union which has been determined to have serious and persistent recordkeeping problems.

These additional requirements were submitted to the Office of Management and Budget (OMB) on October 31, 1989. NCUA will publish a notice in the Federal Register once OMB action is taken on the submitted requirements.

Background

This rule is necessitated by section 919 of the Federal Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) which amends section 202(a) of the Federal Credit Union Act [12 U.S.C. 1782(a)]. FIRREA requires that within 120 days of its enactment, the NCUA Board prescribe, by regulation, audit requirements for the outside, independent audit of any federally insured credit union by a certified public accountant under certain conditions. Accordingly, this rule is effective December 7, 1989, rather than allowing for a 30-day delayed effective date.

In September 1989, consistent with FIRREA, the NCUA Board issued a proposed revision to § 701.13 and § 741.2 of the NCUA Rules and Regulations. The Board sought comments and recommendations concerning the

proposal, with the comment period ending on October 23, 1989. (See 54 FR 32870, September 21, 1989).

The proposed rule, in § 701.13, sets forth the three statutory conditions under which an outside, independent audit by a certified public accountant is to be required:

- (1) The supervisory committee of the credit union has not conducted an annual supervisory committee audit; or
- (2) The annual supervisory committee audit conducted was not complete and satisfactory; or
- (3) The credit union has experienced serious and persistent recordkeeping deficiencies.

It was proposed that under either of the first two conditions, the scope of the audit would be that required by existing § 701.12; under the third condition, an opinion audit would be necessary. The proposal also defined what constitutes a "complete and satisfactory supervisory committee audit" and "serious and persistent recordkeeping deficiencies".

The proposal also recommended amending § 741.2 to require annual audits of federally-insured, state-chartered credit unions using the same standards as for federal credit unions.

Comments

A total of twenty-three comment letters were received in response to the proposed revisions to §§ 701.13 and 741.2. Seventeen letters were from Federal credit unions, two were from federally-insured state credit unions, three were from trade associations, and one from a Federal government department.

Nine commenters supported the proposed rule unchanged. One of these nine, as well as five additional commenters, voiced their support to regularly require an outside, CPA audit of all federally-insured credit unions. Because the financial hardship a routine CPA audit requirement would place on many smaller credit unions, the Board has no immediate plans to change the existing § 701.12 audit and verification requirements.

At the opposite end of the spectrum, four commenters objected to any requirements for a CPA audit arguing that audit quality is not assured by a CPA and that a CPA audit places an undue hardship on smaller credit unions. The FIRREA, which mandated that the Board institute this regulation, also mandated that the audit be "an outside, independent audit . . . by a certified public accountant." As a result, the Board is unable to consider these comments.

Several commenters did not understand that the proposed rule would take effect only if a particular credit union was not meeting existing regulatory audit and verification requirements (§§ 701.13 and 741.2), and thus, argued that the supervisory committee's and the credit union board's autonomy were being infringed. Based on this misunderstanding of the facts, one commenter criticized the lack of a regulatory flexibility analysis. The Board wishes to stress that credit unions can control their own destiny in this regard; if a credit union's supervisory committee is functioning in a manner that protects the members and the credit union as a whole consistent with the existing regulations, the new rule will have no effect on the credit union. Accordingly, the Board continues to feel that a Regulatory Flexibility Analysis is not required.

Because of differing state requirements and the fact that some state credit unions have audit committees rather than supervisory committees, one commenter suggested the Board drop the § 741.2 reference to the supervisory committee for federally-insured credit unions. While the Board recognizes that the intent of Congress was not to mandate the formation of supervisory committees by state-chartered credit unions, the Board has opted to retain the supervisory committee reference consistent with the FIRREA. The Board does not intend to take exception merely on the use of the term "supervisory committee" as opposed to other state-required language.

One commenter requested clarification of the Board's intent with regard to league auditing services and the permissibility of league audits to fulfill the § 701.13 and § 741.2 audit and verification requirements. In cases where the supervisory committee audit has not been conducted or was incomplete or unsatisfactory, league auditors may perform the audit through satisfying the requirements of § 701.12, provided the auditor is a certified public accountant. The condition triggered by serious and persistent problems may not be met through use of league auditing services but rather, requires an opinion audit performed by a certified public accountant accepting responsibility under those credentials. Auditors lacking certified public accountant standing will continue to be permitted to conduct § 701.12 audits and verifications.

One commenter expressed concern that credit unions with cited deficiencies be given a reasonable time for

compliance and the implementation of corrective action before requirements of the new rule take effect. Two commenters believe the regulation should state precisely what the consequences would be if a credit union does not comply. One commenter felt the regulation permitted the Administration too much subjectivity in determining what constitutes "a complete and satisfactory audit" and "serious and persistent recordkeeping deficiencies." The Board believes the regulation as written provides as specific guidance as is advisable while affording the Administration the flexibility needed to carry out its supervisory responsibilities.

One letter of comment supported amending § 741.2(b) to read the credit union shall verify "all passbooks and accounts with the records of the treasurer not less frequently than on a yearly basis" rather than the existing "not less than once every 2 years." The commenter argued that in the case of "serious and persistent recordkeeping deficiencies," 2-years time is too prolonged a period between account verifications and would be detrimental to member's assets. Section 115 of the Federal Credit Union Act (12 U.S.C. 1761(d)) requires the supervisory committee to verify accounts every 2 years. The Board believes the proposed rule is consistent with statutory requirements and ensures the protection of member's accounts. Credit unions having serious and persistent recordkeeping problems are required by the new rule to obtain an outside, independent CPA audit which results in an opinion. Under generally accepted auditing standards, the CPA would have to perform tests (verifications) and gather evidential material to gain a level of assurance that all accounts, including member's deposits, were not materially misstated. The CPA's opinion would reflect the results of such tests and disclose his opinion/assurance with regard to member's deposits.

One commenter criticized the Board for allowing an insufficient period for comment. The Board did not have the option of permitting a longer period for comment; the FIRREA required implementation of the new rule within 120 days of enactment (December 1989). The final rule is substantially similar to the proposed regulation.

Regulatory Procedures

Regulatory Flexibility Act

The NCUA Board certifies that the proposed rule, if made final, will not have a significant impact on a substantial number of small credit

unions. The rule will only affect small credit unions to the extent they do not adhere to existing regulations. Accordingly, the NCUA Board has determined that a Regulatory Flexibility Analysis is not required.

Executive Order 12612

Congress has mandated in section 919 of FIRREA that NCUA prescribe regulations requiring that all federally-insured, state-chartered credit unions obtain an outside, independent audit by a certified public accountant if the credit union has not obtained an annual supervisory committee audit, the supervisory committee audit is not complete and satisfactory or the credit union has experienced serious and persistent recordkeeping deficiencies as defined by the NCUA Board.

To implement the FIRREA provisions, it is incumbent upon NCUA to define what constitutes a "complete and satisfactory supervisory committee audit" and "serious and persistent recordkeeping deficiencies". To accomplish this, NCUA has applied to federally-insured, state-chartered credit unions the same standards that exist in §§ 701.12 and proposed 701.13 for federal credit unions.

It is the NCUA Board's belief that this is the most fair and administratively feasible method of accomplishing the requirements of FIRREA, and that, inasmuch as state-chartered credit unions are already subject to comparable audit requirements under state law, significant new burdens will not be imposed beyond those legislatively mandated by FIRREA.

List of Subjects

12 CFR Part 701

Credit unions; Reporting and recordkeeping requirements; Supervisory committee audits.

12 CFR Part 741

Credit unions; Reporting and recordkeeping requirements.

By the National Credit Union Administration Board on December 7, 1989.
Becky Baker,

Secretary of the Board.

Accordingly, NCUA proposes to amend its regulations (12 CFR parts 701 and 741) as follows:

PART 701—ORGANIZATION AND OPERATIONS OF FEDERAL CREDIT UNIONS

1. The authority citation for part 701 is revised to read as follows:

Authority: 12 U.S.C. 1755, 1756, 1757, 1759, 1761(a), 1761(b), 1766, 1767, 1768, 1769, 1787, 1789, and 1790, and Pub. L. 101-73. Section 701.31 is also authorized by 15 U.S.C. 1601 et seq., 42 U.S.C. 1801 and 42 U.S.C. 3601-3610. Section 701.6 is also authorized by 31 U.S.C. 3717.

2. Section 701.13 is added to read as follows:

§ 701.13 Requirements for an outside audit.

(a) A federal credit union shall obtain an outside, independent audit by a certified public accountant for any fiscal year during which any one of the following three conditions is present:

(1) The supervisory committee of the federal credit union has not conducted an annual supervisory committee audit;

(2) The annual supervisory committee audit conducted did not meet the audit requirements of § 701.12 including § 701.12(e);

(3) The federal credit union has experienced serious and persistent recordkeeping deficiencies as defined in paragraph (c) of this section.

(b) In the case of an audit required pursuant to paragraph (a)(1) or (2) of this section, the scope of the outside, independent audit conducted by a certified public accountant must fully encompass the requirements set forth in § 701.12. In the case of an audit required pursuant to paragraph (a)(3) of this section, the outside, independent audit by a certified public accountant must be an opinion audit as that term is understood under generally accepted auditing standards.

(c) As used in paragraph (a)(3) of this section, persistent recordkeeping deficiencies shall mean serious recordkeeping problems which continue to exist past a usual, expected, or normal period of time. Persistent recordkeeping deficiencies shall be considered serious if the Administration has a reasonable doubt that the financial condition of the credit union is accurately and fairly presented in the credit union's statements and that management practices and procedures are sufficient to safeguard members' assets.

PART 741—REQUIREMENTS FOR INSURANCE

1. The authority citation for part 741 is revised to read as follows:

Authority: 12 U.S.C. 1757, 1788(s), and 1761 through 1790; Pub. L. 101-73.

2. Section 741.2 is revised to read as follows:

§ 741.2 Audit and verification requirements.

(a) The supervisory committee of each credit union insured pursuant to title II of the Act shall make or cause to be made an audit of the credit union at least once every calendar year covering the period elapsed since the last audit. The audit must fully meet the requirements set forth in §§ 701.12 and 701.13.

(b) Each credit union which is insured pursuant to title II of the Act shall verify or cause to be verified, under controlled conditions, all passbooks and accounts with the records of the treasurer not less frequently than once every 2 years. The verification must fully meet the requirements set forth in §§ 701.12(e) and 701.13.

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12 CFR Parts 705 and 701

Community Development Revolving Loan Program for Credit Unions; Nonmember and Public Unit Accounts

AGENCY: National Credit Union Administration.

ACTION: Final Rule.

SUMMARY: This rule makes several clarifying changes to Part 705 of NCUA's Rules and Regulations ("Community Development Revolving Loan Program for Credit Unions") and one corresponding change to § 701.32 of NCUA's Rules and Regulations ("Nonmember and Public Unit Accounts"). These amendments result from a review of Part 705 following a recent amendment to the Federal Credit Union ("FCU") Act clarifying that the Community Development Credit Union Revolving Loan Fund ("Fund") is subject only to the rules and regulations prescribed by the NCUA Board. NCUA has been unable to approve any loans because the Office of Management and Budget did not make an allotment to NCUA for use of the funds. The monies in the Fund are now available for loans.

The Board has made this rule effective immediately since it simply updates and clarifies the existing regulations, and does not impose any new requirements.

EFFECTIVE DATE: December 15, 1989.

ADDRESS: National Credit Union Administration, 1776 G St., NW., Washington, DC 20456.

FOR FURTHER INFORMATION CONTACT: Robert J. LaPorte, Central Liquidity Facility, or Julie Tamuleviz, Staff Attorney, at the above address or telephone: (202) 682-9780 (Mr. LaPorte) or (202) 682-9630 (Ms. Tamuleviz).

SUPPLEMENTARY INFORMATION:

Background

The Community Development Revolving Loan Fund Program for Credit Unions

Congress established the Community Development Revolving Loan Fund Program ("Program") to make loans to participating credit unions to enable them to provide basic financial and related services to residents in needy communities and to stimulate economic activities in the communities they serve resulting in increasing income, ownership and employment opportunities for low-income residents and other community-growth efforts. In 1988, Congress transferred the Fund and the authority to administer the Fund from the Secretary of Health and Human Services ("HHS") to the NCUA. Part 701 of NCUA's Regulations established the program under which loans from the Fund are made.

No state or local funds are required. Federal or state-chartered credit union applies to NCUA for a loan from the Fund. 12 CFR 705.5(a). A state-chartered credit union seeking a loan must obtain "written concurrence from [its] state regulatory authority." 12 CFR 705.8. A state-chartered credit union receiving a loan under the Program remains subject to supervision and examination by the state regulator.

Funding for the Program comes from Congressional appropriation. The Fund received a \$8,000,000 appropriation in 1979 and currently has a balance of \$6,679,000. Since the Fund was transferred to NCUA in 1986, NCUA has solicited, received, and reviewed loan fund applications from eligible credit unions. However, NCUA has been unable to approve any loans because the Office of Management and Budget had not authorized use of the appropriation.

Public Law 101-144

Public Law 101-144, enacted on November 9, 1989, amended Section 120 of the FCU Act (12 U.S.C. 1766) by adding the following new subsection (k):

(k) Notwithstanding any other provision of law, the Board may exercise the authority granted to it by the Community Development Credit Union Revolving Loan Fund Transfer Act (Public Law 99-609, sec. 1, November 6, 1986, 100 Stat. 3475) subject only to the rules and regulations prescribed by the NCUA Board.

The amendment provides NCUA with

behalf of the member. No individual may serve as the representative of more than one organizational member in the same corporate Federal credit union.

§704.5 Annual Audit.

(a) The supervisory committee of a corporate Federal credit union shall cause an annual opinion audit to be made by an independent, duly licensed CPA and shall submit the audit report to the board of directors. A summary of the audit report shall be submitted to the membership at the next annual meeting.

(b) A copy of the audit report shall be submitted to the appropriate Regional Office of the National Credit Union Administration within 30 days after receipt by the board of directors.

§704.6 Programs and Services.

Pursuant to Section 120(a) of the Federal Credit Union Act (12 U.S.C. 1766(a)), and subject to other applicable provisions of law, regulation, bylaws, and any orders of the NCUA Board, a corporate Federal credit union may provide, to its members, services involving investments, liquidity management, payment systems, and correspondent services.

§704.7 Prepayment Penalties.

If provided for in the loan contract, a corporate Federal credit union is authorized to assess prepayment penalties on loans made at fixed rates and for specified maturities to member credit unions or other organizations.