National Credit Union Administration

OFFICE OF INSPECTOR GENERAL

AUDIT OF THE NCUA'S CENTRAL LIQUIDITY FACILITY

Report #OIG-25-06
March 4, 2025

National Credit Union Administration

Office of Inspector General

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TO: Distribution List

FROM: Inspector General James W. Hagen

SUBJ: Audit of the Central Liquidity Facility

DATE: March 4, 2025

The National Credit Union Administration (NCUA) Office of Inspector General (OIG) conducted this self-initiated audit to assess the Central Liquidity Facility (CLF). The objectives of our audit were to determine: (1) whether the NCUA operates the CLF in accordance with relevant laws, regulations, policies, and procedures; and (2) the utilization of the CLF by credit unions covered by the temporary authority granted by the CARES Act.

Results of our audit determined the NCUA operated the CLF in accordance with applicable laws and substantially complied with regulations and its own policies and procedures. We determined the annual stock adjustment done by the CLF was not entirely done in accordance with regulations as the CLF did not receive payments for adjustments to member capital stock subscriptions no later than March 31. However, we determined the financial impact of these payments not being received by March 31 was de minimis. We also determined the CLF was being utilized as evidenced by its growth in members. While we are making no recommendations in our report to management, we are suggesting management determine whether they want to pursue any action to extend the due date beyond March 31st for the annual stock adjustment payments to the CLF.

We appreciate the cooperation and courtesies NCUA management and staff provided to us during the audit. If you have any questions on the report and its recommendation, please contact me at 703-518-6350.

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EXECUTIVE SUMMARY

The NCUA OIG conducted this self-initiated audit to assess the Central Liquidity Facility (CLF or Facility). The objectives of our audit were to determine: (1) whether the NCUA operated the CLF in accordance with relevant laws, regulations, policies, and procedures, and (2) the utilization of the CLF by credit unions covered by the temporary authority granted by the Coronavirus Aid, Relief, and Economic Security Act of 2020 (CARES Act).[1] The scope of our audit covered the NCUA's operation of the CLF from January 2020 to March 31, 2024.

Our audit determined the NCUA operated the CLF in accordance with applicable laws and substantially complied with regulations and its own policies and procedures. We determined the annual stock adjustment done by the CLF was not entirely done in accordance with regulations as the CLF did not receive payments for adjustments to member capital stock subscriptions no later than March 31. However, we determined the financial impact of these payments not being received by March 31 was de minimis. We also determined the CLF was being utilized as evidenced by its growth in members. While we are making no recommendations in our report to management, we are suggesting management determine whether they want to pursue any action to extend the due date beyond March 31st for the annual stock adjustment payments to the CLF.

We appreciate the cooperation and courtesies NCUA management and staff provided to us during this audit.

[1] Pub. L. No. 116-136, § 4016, 134 Stat. 281, 481-482 (2020).

BACKGROUND

The NCUA is an independent federal agency created by the U.S. Congress that insures deposits of federally insured credit unions, protects members who own credit unions, and charters and regulates federal credit unions. The NCUA's organizational structure consists of a Headquarters, Asset Management and Assistance Center, and three regional offices.[2] The NCUA CLF was created by the National Credit Union Central Liquidity Facility Act.[3] The Facility is a mixed ownership government corporation within the NCUA. It is an instrument of the federal government owned by its member credit unions and managed by the NCUA Board. The purpose of the Facility is to improve the general financial stability by providing member credit unions with a source of loans to meet their liquidity[4] needs and thereby encourage savings, support consumer and mortgage lending, and provide basic financial resources to all segments of the economy. The NCUA Board, in its capacity as the CLF Board, approved the 2024 CLF budget of $2.2 million in December 2023 and approved the 2025-2026 budget of $2.3 million and $2.4 million, respectively, in November 2024.

The CLF was created by Congress in 1979 because credit unions needed their own source of funds to meet their liquidity needs in the same way the Federal Reserve System discount window provided access to loans for banks. Over time, credit unions have gained access to federal contingent liquidity sources (for example, credit unions who qualify may now borrow from the Federal Reserve discount window), but the CLF continues to be a back-up source of liquidity for both federal and state-chartered credit unions. Regular membership is voluntary and open to all federal credit unions, federally insured state-chartered credit unions and privately insured credit unions.

<u>CLF Membership and Annual Adjustment to Capital Stock Subscription</u>

A credit union primarily serving natural persons may be a regular member of the Facility by subscribing to the capital stock of the Facility in an amount not less than one-half of 1 percent of the credit union's paid-in and unimpaired capital and surplus. A credit union or group of credit unions, primarily serving other credit unions, may be an agent member of the Facility by: (1) obtaining the approval of the Board;[5] (2) subscribing to the capital stock of the Facility in an amount not less than one-half of 1 percent of the paid-in and unimpaired capital and surplus of all those credit unions which primarily serve natural persons, which are members of such credit union or of any credit union comprising such credit union group, and which are not regular members; (3) agreeing to comply with rules and regulations the Board shall prescribe with respect to, but not limited to, management quality, asset and liability safety and soundness, internal operating and control practices and procedures, and participation of natural persons in the affairs of such credit union or credit union group, and (4) agreeing to submit to the

[2] The three regional offices are the Eastern, Southern, and Western regions.
[3] 12 U.S.C. § 1795-1795k.
[4] Liquidity is a credit union's capacity to meet it cash and collateral obligations at a reasonable cost.
[5] In April 2020, the Board delegated its authority to approve corporate credit unions becoming agent members of the CLF to the CLF President, with that delegation expiring on December 31, 2020.

supervision of the Board which shall include, but not be limited to, reporting requirements and periodic unrestricted examinations.

Stock subscriptions shall be: (1) based on an arithmetic average of paid-in capital and surplus over the 6 months preceding application and membership, and (2) adjusted at the close of each calendar year in accordance with an arithmetic average of paid-in capital and surplus over a period determined by the Board. To become a CLF regular or agent member, the credit union is to forward funds equal to one-half of the initial stock subscription to the Facility.

Capital stock subscriptions are to be adjusted at the close of each calendar year in accordance with an arithmetic average of paid-in and unimpaired capital and surplus over the 12 months in such calendar year. Payments for adjustments to the capital stock subscription must be received by the Facility no later than March 31 of the following year. The purpose of the adjustment is to maintain the original intent of the capital subscription, which is to have it be in line with the member's paid-in and unimpaired capital and surplus. If a member's paid-in and unimpaired capital and surplus goes up or down, the member's capital stock subscription should reflect that.

<u>Extensions of credit</u>

A regular or agent member may apply for a Facility advance. Applications are to be filed with a Facility lending officer. Each application that is completed and properly filed is to be approved or denied within 5 working days after the day of receipt. Prior to Facility approval of each application, the CLF is required to consider the creditworthiness of such member. A regular member may apply for an extension of credit from the Facility only for liquidity-need purposes and any application must include or adequately reference some demonstrable evidence the institution meets the statutory meaning of liquidity needs.[6]

<u>Dividends</u>

The NCUA Board delegated the authority to the CLF President to set the dividend rate on a monthly or quarterly basis to distribute CLF net income to the CLF members. The CLF President determines an expected dividend rate based on projected portfolio earnings at the beginning of each period so that the CLF Accountant can reasonably accrue for the liability. Dividends are calculated at the end of the period based on the amount of capital stock held during the period. Dividends are posted to individual capital stockholders accounts on the last day of the period, then moved to their individual liquidity reserve and clearing (LRC) accounts[7] on the first day of the following period.

[6] Liquidity needs mean the needs of credit unions primarily serving natural persons for:
(A) short-term adjustment credit available to assist in meeting temporary requirements for funds or to cushion more persistent outflows of funds pending an orderly adjustment of credit union assets and liabilities;
(B) seasonal credit available for longer periods to assist in meeting seasonal needs for funds arising from a combination of expected patterns of movement in share and deposit accounts and loans; and
(C) protracted adjustment credit available in the event of unusual or emergency circumstances of a longer term nature resulting from national, regional or local difficulties.

[7] LRC accounts are member deposits, which represent amounts remitted by members over and above the amount required for membership or deposited there on their behalf.

Investments

The Board on behalf of the Facility can invest in obligations of the United States or any agency thereof, make deposits in federally insured financial institutions, and make investments in shares or deposits of credit unions. The Board delegated responsibility for CLF investment activities to the CLF President. The objectives of the investment activity are first to meet credit union liquidity needs by holding sufficient funds in overnight accounts to meet unexpected loan demand, liquidity and clearing account withdrawals, and any member cancellations. The balance of the funds is placed in authorized investments. The funds that are invested are from members' capital stock and LRC accounts plus CLF retained earnings. Except for $100,000 in cash to cover any unexpected operational expenses, the total amount of funds in those accounts are invested. The requirement to hold sufficient funds to meet loan demand, liquidity and clearing account withdrawals, and any member cancellations is addressed through utilization of overnight and short-term investments. What is earned on those investments is used to pay quarterly dividends on members' capital stock, interest on LRC accounts, and to help cover expenses. The CLF had almost $824 million invested in Treasury securities as of September 30, 2024.

CARES Act

The CARES Act was signed into law on March 27, 2020, and included key changes to the CLF that were to sunset on December 31, 2020. Among the changes, the CARES Act considerably increased the CLF's borrowing capacity.[8] Before the CARES Act was enacted into law, the CLF had the authority to borrow, provided its obligations did not exceed 12 times the subscribed capital stock and surplus of the CLF (that is, the sum of its retained earnings and capital stock). The CARES Act temporarily increased the multiplier from 12 to 16. The CARES Act also temporarily relaxed the requirements on agent membership, making such membership more affordable for corporate credit unions. An agent member was no longer required to buy capital stock for all its member credit unions but could buy CLF capital stock for a subset of the credit unions it served. In addition, the CARES Act changed the definition of liquidity needs to include the needs of any credit union, not only natural-person credit unions. This new definition broadened access by allowing the CLF to meet the liquidity needs of corporate credit unions.

The Consolidated Appropriations Act of 2021,[9] extended the CARES Act's CLF provisions to December 31. 2021. After enactment of this law, the NCUA Board issued an interim final rule on March 24, 2021, to update the NCUA regulations consistent with the statutory changes. The 2021 interim rule also extended the temporary relaxing of the requirements on agent membership. Upon the sunset of the amendment made in the CARES Act, as extended by the Consolidate Appropriations Act, 2021, within 1 year from the sunset date (December 31. 2021) any corporate credit union or corporate credit union group that became an agent member under this provision was to either purchase Facility stock for all its member credit unions or terminate its membership in the Facility. This extended the agent member provision of the CARES Act to December 31, 2022.

[8] The CLF borrows from the U.S. Treasury's Federal Financing Bank to make loans to member credit unions and the Share Insurance Fund.
[9] Pub. L. No. 116-260, Title V, Subtitle C, § 540(b), 134 Stat. 1182, 2090 (2020).

Since 2022, the NCUA Board has advocated for permanent statutory authority to allow corporate credit unions and other agent members of the CLF to purchase capital stock for a subset of credit unions served. These statutory CLF enhancements would make the Facility a more affordable option for corporate credit unions to subscribe to on behalf of their smaller credit union members. In testimony to Congress, the NCUA's Chairman noted the temporary statutory enhancements that assisted the agent membership of corporate credit unions expired on January 1, 2023. As a result, 3,322 credit unions with less than $250 million in assets lost access to the CLF, and the Facility's capacity contracted by almost $10 billion.

RESULTS IN DETAIL

The objectives of our audit were to determine: (1) whether the NCUA operates the CLF in accordance with relevant laws, regulations, policies, and procedures, and (2) the utilization of the CLF by credit unions covered by the temporary authority granted by the CARES Act. Based on our audit work, we determined the NCUA operated the CLF in accordance with applicable laws and substantially complied with regulations and its own policies and procedures. We determined the annual stock adjustment done by the CLF was not entirely done in accordance with regulations as the CLF did not receive payments for adjustments to member capital stock subscriptions no later than March 31. However, we determined the financial impact of these payments not being received by March 31 was de minimis. We also determined the CLF was being utilized as evidenced by its growth in members.

The detailed results of our audit follow.

CLF Processes Substantially Complied with Requirements

We determined the NCUA operated the CLF in accordance with applicable laws and substantially complied with regulations and its own policies, and procedures. We reviewed the CLF's processes for new membership, payment of dividends, annual member stock adjustment, advances, large dollar transactions, and termination of membership and compared the implementation of those processes to relevant requirements. We determined the processes for new membership, payment of dividends, advances, and termination of membership operated in accordance with requirements. The Government Accountability Offices (GAO) Standards for Internal Control in the Federal Government (Green Book) set internal control standards for federal entities.[10] Our audit determined the CLF adhered to the GAO's Green Book, in particular, Principle #10 – Design Control Activities and Principle #12 – Implement Control Activities. Principle #10 requires management to design control activities to achieve objectives and respond to risks. Principle #12 requires management to implement control activities through policies. While we determined the CLF did not fully comply with its policy for reporting large dollar deposits and disbursements to the U.S. Treasury as it did not communicate some required information in 2020, once the CLF started using FS Form 187[11] in June of 2022, the large dollar notifications sent to the Treasury later that year did contain all required information.

Regarding the required annual member stock adjustment, the CLF did not receive payments from members for the annual adjustments to their capital stock subscriptions by the March 31st deadline. This was not due to a lack of implementing internal controls or not having a process for stock adjustments but because the annual stock adjustment calculation performed by the CLF relies on credit union call report data and that data is not available to the CLF in a timeframe which would allow the March 31 deadline to be met. Our testing of a sample of CLF members

[10] GAO-14-704G (September 2014)
[11] Agency Report for Treasury Cash Forecasting Advance Notice of Large Deposits or Payments of $50 Million or More

identified that in all 12 instances where a member was required to make a payment to the CLF, the payment was late by 4 to 32 days, with 12 days being the average delay. 12 C.F.R. § 725.5 requires payments for adjustments to capital stock subscriptions be received by the Facility no later than March 31 of the following year. By not receiving payments by March 31, the CLF was delayed in investing these paid-in funds, which impacted the amount of interest the CLF could earn. However, we determined the financial impact to the CLF of these payments not being received by March 31 was de minimis.

Details

The activities we performed and the results that support this conclusion are detailed below.

New Membership

Based on our sample of 15 credit unions that became regular members and 4 corporate credit unions that became agent members of the CLF during the scope period of our audit, we determined the process for credit unions or corporate credit unions to become CLF members operated in accordance with relevant laws, regulations, policies, and procedures. Title 12 C.F.R. § 725.3 requires a credit union to subscribe to capital stock of the Facility in an amount equal to one-half of 1 percent of the credit union's paid-in and unimpaired capital and surplus to become a CLF member. We determined, without exception, the amount of the new member's capital stock subscription was equal to one-half of one percent of the credit union's paid-in and unimpaired capital and surplus based on an arithmetic average of paid-in capital and surplus over the 6 months preceding the application as required. New members are required to transfer funds equal to one-half of their capital stock subscription to the CLF. We determined, without exception, the funds transferred to the CLF by the new member credit unions equaled one half of their capital stock subscription as required. CLF's operating procedures for new membership, among other things, includes steps for the review and approval of the CLF share calculation, the review and approval of the new membership application by the CLF President, and a CLF analyst to request the funds from the applicant and then confirm the transfer of funds for the capital stock. Without exception, we determined those steps were performed.

Advances

The execution of the application process for the one advance made by CLF during the audit scope was done in accordance with applicable laws, regulations, policies, and procedures. Title 12 C.F.R. § 725.17 requires each completed and properly filed application for credit be approved or denied by the CLF within 5 working days after the day of receipt. We determined the application for the advance was approved or denied within 5 working days after receipt as required. The application for advance was signed by the CLF member and received by the CLF on November 30, 2023, and the CLF President approved the advance request on December 7, 2023, which was within 5 working days after day of receipt. Also, the Facility is required to consider the credit worthiness of the applicant. We determined the Facility considered the credit worthiness of the applicant. The CLF Vice President reviewed the credit union's borrowing arrangements, repayment strategy, collateral, recent examination findings, liquidity, credit worthiness, and financial performance report and call report. The CLF Vice-President recommended the CLF President approve the advance and the CLF President reviewed the Vice President's underwriting and approved the advance request.

Title 12 C.F.R. § 725.19 requires the collateral for each facility advance and each agent loan to be secured by a first priority security interest in collateral of the credit union with a net book value at least equal to an amount as required by the Facility's collateral table, published at www.NCUA.gov, or by guarantee of the National Credit Union Share Insurance Fund. We determined the advance was secured by a first priority security interest in collateral of the credit union with a net book value at least equal to an amount as required by CLF's collateral table. The member borrowed $1,000,000 and pledged $1,480,000 of bonds to perfect and secure the advance by transferring the securities to their CLF corporate credit union correspondent. The corporate credit union and the CLF accepted the securities of $1,480,000, which had a CLF collateral margin value[12] of $1,239,172 so the margin value of the collateral was at least equal to the amount advanced.

The CLF's operating procedures for advances[13] require the terms of the Facility advance, such as the date of the advance, amount of the advance, the interest rate, the principal repayment date(s), the principal amount due on each repayment date (excluding interest), the interest payment dates, and the maturity date to be specified in a confirmation to the member at the time the advance was made. We determined the confirmation sent by the CLF to the member included those required terms of the advance. Also, in accordance with these operating procedures, we determined, per its note purchase agreement with the Federal Financing Bank (FFB),[14] the CLF borrowed from the FFB to fund the advance to its member. In addition, the operating procedures require the review process for the advance application include conferring with the NCUA Regional Director of the region where the credit union is located, and in the case of federally insured state-chartered credit unions, the State Supervisory Authority. We determined the CLF consulted with the appropriate NCUA Regional Director before the approval decision on the advance was made.

Dividends

The calculation and payment of dividends to CLF members was done in accordance with regulation, policy, and procedures. Title 12 C.F.R. § 725.5(e) requires that dividends be paid on capital stock and the NCUA Board declare such dividends no less frequently than annually, all issued (paid for) capital stock is to share in dividend distributions without preference, and payment of dividends be made by the issuance of capital stock to the member in the amount of the dividend. As noted in the Background section, the NCUA Board delegated the authority to the CLF President to set the dividend rate on a monthly or quarterly basis in order to distribute CLF net income to the CLF members. Based on our sample of CLF members, we determined

[12] Collateral margin serves as a protective buffer for lenders in the event of a default. It is an amount or percentage of value required to be pledged by the borrower.
[13] NCUA Central Liquidity Facility Operating Circular 20-02: Regular Member Facility Advances
[14] The FFB provides financing to help federal agencies manage their borrowing and lending programs, and to ensure all federal government borrowing from the public is conducted through the Treasury and not through program agencies.

dividends had been declared no less frequently than annually, all issued capital stock shared in the dividend distribution without preference, and CLF members were paid with the issuance of capital stock in the amount of the dividend. We reviewed documentation provided by the CLF that showed the Facility calculated and paid dividends quarterly and the quarterly dividend calculations were performed for all CLF members.

The CLF Dividend Payment Policy, among other things, requires dividends to be calculated at the end of the period based on the amount of capital stock held during the period. Those dividends are to be posted to individual capital stockholders account on the last day of the period, then moved to individual LRC accounts on the first day of the following period. We reviewed CLF documentation that showed each members' capital stock at the end of the period/quarter, the dividend rate, and the dividend for each of the 3 months in the quarter to determine if dividends were calculated at the end of the period based on the amount of capital stock held during the period. We reviewed the quarterly dividend statements for the CLF members in our sample to determine if quarterly dividend payments went into their CLF capital stock accounts on the last day of the period, then were moved to individual LRC accounts on the first day of the following period. Based on our review, we determined dividends were calculated at the end of the period based on the amount of capital stock held during the period and dividends were posted to individual capital stockholders accounts on the last day of the period, then moved to individual LRC accounts on the first day of the following period.

Termination of Membership

The termination of credit unions' membership in the CLF was done in accordance with relevant regulations, policies, and procedures. We reviewed the termination documentation associated with the six credit unions that became members and then terminated their membership during our audit scope. We determined the withdrawal of the 6 credit unions from CLF membership was done within the required/allowed timeframes established by regulation. We also determined the CLF redeemed all six member's stock when the credit unions terminated their CLF membership in accordance with regulation.

Title 12 C.F.R § 725.6 states a member of the Facility whose stock subscription constitutes less than 5 percent of total subscribed Facility stock may withdraw from membership 6 months after notifying the NCUA Board in writing of its intention to do so. One of the six credit unions provided notice to the CLF on February 23, 2023, that it would withdraw its subscription and membership in the CLF 6 months from the date of the notice. Because it owned less than 5 percent of capital stock invested in the CLF, it was required to wait 6 months under the regulation. On August 25, 2023, 6 months later, the CLF notified this credit union it would process the return of its account balance. CLF's disbursement to this credit union was posted on September 9, 2023. The credit union's withdrawal from CLF membership was done within the required timeframe.

Title 12 C.F.R § 725.6 allowed any credit union that became a member of the Facility between April 29, 2020, and December 31, 2020, to immediately terminate its membership until December 31, 2022. Three of the six credit unions notified the CLF in 2022 (April 26, August

26, and October 18) that they would immediately withdraw their membership in the CLF. These three credit unions all became members of the CLF between April 29, 2020, and December 31, 2020. The Facility posted disbursements to the three credit unions on May 31, 2022, September 7, 2022, and November 4, 2022, respectively. These terminations of CLF membership were done within the allowed timeframe, in this case, immediately.

The remaining two credit unions, that became members and terminated their membership during our audit scope, were both regular members and agent members. The CLF notified both credit unions on December 23, 2022, that their membership was expiring, and their subscribed capital would be returned by an expected date of December 30, 2022. The CLF posted disbursements to these two credit unions for their regular and agent member stock subscription on December 29, 2022. These two members withdrawal from CLF membership was done within the required timeframe and avoided remitting additional subscribed capital for all their members. We note the CLF also emailed all the other corporate credit unions that their agent membership in the facility would be closed on December 31, 2022, unless they notified the CLF by December 29, 2022, that they wished to remain agent members, and they remit additional subscribed capital for all of their natural person credit union members. The CLF also posted disbursements to the other corporate credit unions on December 29, 2022, terminating their agent memberships.

In accordance with operating procedures, we also determined the CLF: (1) prepared and sent a letter confirming receipt of the member's request to withdraw their membership from the CLF that included the member's account balances, and (2) sent requests to the Office of the Chief Financial Officer (OCFO) for all six terminations requesting payment be made due to the closure of the credit unions CLF accounts and each request was reviewed and approved by OCFO personnel.

Large Dollar Transactions

With one exception, the CLF complied with its policy for reporting large dollar deposits and disbursements to the U.S. Treasury. CLF's Large Dollar Notification Policy requires deposits and disbursements of $50 million or more be reported by the CLF to the U.S. Treasury in advance of the transaction settlement date. We determined there were four large dollar notifications done during the scope of the audit. Two instances involved a credit union paying in funds to become a member of the CLF and when CLF returned the funds to the same credit union because it terminated its membership in the CLF. The other two instances were when the corporate credit unions became agent members of the CLF in 2020 and when the CLF returned their funds in 2022 because those corporate credit unions terminated their membership.

We determined the four large dollar transactions were reported to the U.S. Treasury in advance of the transaction settlement date, as required by policy. Transactions totaling $50 million to $500 million require a minimum of 2 business days advance notice and, without exception, we determined the requirement was met. The CLF's policy also requires certain information be reported to U.S. Treasury when making a large dollar notification. We determined the two notifications sent to Treasury in 2020 were done by email and did not contain all the required information. In one case, the notification was missing information on the deposit mechanism that would be used and the name of the credit union depositing the funds into the CLF. In the other case, the notification did not include the names of the corporate credit unions depositing the funds into the CLF. According to CLF personnel, the CLF began using FS Form 187 in June of 2022 for large dollar notifications to Treasury. We determined both large dollar notifications sent to the Treasury later that year did contain all required information. We note FS Form 187 has blocks to be filled out for all the required information. Because the issue of the large dollar notifications not containing all required information has been remedied by using FS Form 187, we are not making a recommendation to address the issue.

<u>Annual Adjustment</u>

The annual stock adjustment done by the CLF was not entirely done in accordance with regulations. Title 12 C.F.R. § 725.5 requires members' capital stock subscriptions to be adjusted at the close of each calendar year in accordance with an arithmetic average of paid-in and unimpaired capital and surplus over the twelve months in such calendar year. Also, payments for adjustments to the capital stock subscription must be received by the Facility no later than March 31 of the following year. We note the payment deadline of March 31 is not mentioned in the National Credit Union Central Liquidity Facility Act, 12 U.S.C. § 1795, which established the CLF.

We determined capital stock subscriptions had been adjusted at the close of each calendar year in accordance with an arithmetic average of paid-in and unimpaired capital and surplus over the 12 months. We reviewed the annual stock subscription statements for the sampled members to make this determination. Fourteen of the nineteen sampled members had an annual stock subscription statement in 2023 and/or 2024. The four agent members in our sample did not have any annual stock adjustments. CLF officials told us the CARES Act granted the NCUA Board the authority for a corporate credit union to become an agent member of the CLF for a subset of their members. This was a temporary provision. In early 2021, the NCUA and the agent members decided the agent membership would remain the same for 2021 and no stock adjustment would be done. Due to the uncertainty of the temporary provision, there also was no stock adjustments for the agent members in 2022. One CLF regular member in our sample did not have an annual adjustment in 2023 or 2024 as that credit union did not become a CLF member until March 15, 2024. The other 14 CLF regular members in our sample had 1 or 2 annual stock subscription statements during 2023 - 2024, depending on when they became a member of the CLF. Based on our review of these statements, we determined, without exception, the capital stock of these 14 CLF members was adjusted at the close of each calendar year and the arithmetic average of paid-in and unimpaired capital and surplus over 12 months was used to calculate any needed adjustment to each member's capital stock subscription.

We determined the CLF did not receive payments for adjustments to member capital stock subscriptions no later than March 31. Based on the adjustment of capital stock subscriptions in 2023 and 2024 for our sample of CLF regular members, we determined 12 of the 22 annual stock subscription statements showed that, after funds were transferred from the member's LRC account to its capital stock account, those members still owed the CLF $1.3 million ($953,595.63 in 2023 and $346,294.02 in 2024). The other 10 adjustment calculations did not result in the member having to pay in additional funds to the CLF.[15] Based on our sample, in every instance (12 of 12) a payment from a CLF member was required, the payments were not received by the CLF by the required deadline of March 31. Payment dates ranged from April 4 to May 2, or 4 to 32 days late, with the average payment delay being 12 days. We determined the annual stock subscription statements issued by the CLF to its members in 2023 and 2024 had a payment due date of May 1. By not receiving payments by March 31, the CLF was delayed in investing these paid-in funds, which impacted the amount of interest the CLF could earn.

CLF officials told us the validated year-end (December) call report data the CLF uses to adjust the members' capital stock is not available from the NCUA until March 1. Not until the NCUA validates the information and makes it available, does the CLF review and verify the information pertinent to the computation of the new subscribed capital amount and complete the annual adjustment processes including the billing statements, which are emailed/mailed to CLF members by April 1st. The CLF then requests payment from its members within 30 days (May 1 due date). CLF officials told us to ensure consistency across all uses of prospective or current CLF credit union member financial and statistical data, the CLF only uses the financial and statistical report data reported and included on NCUA 5300 form (call report) to compute items such as the initial CLF stock subscription or required annual adjustment amount. The added integrity of the information obtained from the online reporting-system for the NCUA 5300 provides enhanced accuracy of the credit union data. CLF officials told us they believe the process they use for the annual stock adjustment is as efficient as possible. The process they have is necessary to meet the intent of the annual adjustment and to ensure accuracy.

We contacted Office of Examination and Insurance (E&I) personnel who provided the December 2023 call report schedule. The call report schedule was as follows, which confirms call report data is not available for use until March.

- Data collection closed on January 30, 2024.
- Data scrub process ran from January 31 to Feb 16, 2024.
- Databases and tables were updated from Feb 19 to March 1, 2024.
- The data was put into the production environment March 1, 2024, for use by everyone.

E&I personnel stated they have had discussions in the past on reducing the time this process takes but have not found a way to do it. The timeline is discussed/negotiated with stakeholders every quarter. They believe the processes and activities performed on the call reports ensure the accuracy of the data.

To determine the potential impact of the CLF not receiving member payments by the March 31 due date, we asked CLF officials to provide us with the total amount of funds (annual adjustments) CLF members paid in for 2022, 2023 and 2024 along with the average rate of return that CLF received in those years. A CLF official told us the receipt of annual adjustment

[15] Six annual stock subscription statements showed the member had to increase its capital stock account, but the increase was entirely covered by a transfer from the member's LRC account. The other four statements showed the member's capital account needed to decrease so funds were transferred out to the member's LRC account.

capital deposit funds is not solely an income generator, but also includes accompanying expenses which must be considered. The official explained that the annual adjustment cash receipts generate both investment income (from invested funds) and dividend expense (from dividends paid on those same capital deposits), both of which must be taken into account when determining the overall financial impact on the CLF due to the cash receipts being received after March 31.

In Table 1 below, CLF officials provided us with the total annual adjustment cash receipts for 2022-2024, the average investment yield in April (the month when this cash is received and invested) for each of those years, and, using those figures, an estimated potential income from investing those funds for a full month. CLF officials also provided the second quarter dividend rate for 2022-2024 and, using the cash receipts figure (representing capital stock increase), the estimated potential net impact to the CLF in dollars (estimated potential income minus estimated potential dividend expense).

Table 1

Annual Adjustment (AA) – Cash Collections for Capital Stock

	2022	**2023**	**2024**
AA Cash Receipts Due (To Invest)	$104,757,973	$50,051,788	$16,294,897
April Average Investment Yield	0.95%	4.44%	4.93%
Estimated Potential April Income	$82,523	$185,025	$66,999
AA Paid-in Capital Stock Increase	$104,757,973	$50,051,788	$16,294,897
Quarter 2 Dividend Rate	0.82%	4.59%	4.56%
Estimated Potential April Dividend Expense	$71,585	$191,448	$61,921
Net CLF Impact (estimated potential income – estimated potential expense)	$10,938	($6,423)	$5,079

We believe the methodology above used to estimate the impact to the CLF of member payments from the annual adjustment not being received by March 31 is reasonable. The calculations show the estimated net financial impact of these payments not being received by March 31 over those

3 years was de minimis. Therefore, we are not making a recommendation to management to address the annual adjustment payments not being received by the CLF by March 31. However, we suggest NCUA management determine whether they want to pursue any action to extend the due date beyond March 31st for member payments to the CLF.

The CLF is Being Utilized

We determined the CLF is being utilized as evidenced by its growth in membership. Additionally, the NCUA continues to advocate for permanent statutory authority to allow corporate credit unions and other agent members of the CLF to purchase capital stock for a subset of credit unions served. This would allow more credit unions to have access to the CLF. We also determined the CLF's membership application process was not viewed as an obstacle to becoming a member and that there were multiple ways credit unions became aware of what the CLF is and does. The activities we performed and the results that support this conclusion are detailed below.

Details

We reviewed the utilization of the CLF regarding the number of CLF members and advances made by the CLF. We also looked at credit unions' awareness of the CLF, the membership application process, and the CLF as a liquidity source as things that might impact the utilization of the CLF. In terms of CLF membership, we determined the number of members has grown. The number of regular members increased from 276 in January 2020 to 430 as of September 30, 2024, a 56 percent increase. Correspondingly, the following also have increased in size during the same period:

- capital stock of regular members - from $289 million to $882 million,
- CLF's statutory borrowing authority - from $7.4 billion to $21.7 billion, and
- CLF's total assets - from $322 million to $966 million.

We note the CARES Act, and its expiration, impacted the number of credit unions covered by the CLF. As mentioned in the Background section of this report, the CARES Act temporarily relaxed the requirements on agent membership, making such membership more affordable for corporate credit unions. An agent member was no longer required to buy capital stock for all its member credit unions but could buy CLF capital stock for a subset of the credit unions it serves. In testimony to Congress, the NCUA's Chairman noted the temporary statutory enhancements that assisted the agent membership of corporate credit unions expired on January 1, 2023. As a result, 3,322 credit unions with less than $250 million in assets lost access to the CLF, and the Facility's capacity contracted by almost $10 billion. Since 2022, the NCUA Board has advocated for permanent statutory authority to allow corporate credit unions and other agent members of the CLF to purchase capital stock for a subset of credit unions served. These statutory CLF enhancements would make the Facility a more affordable option for corporate credit unions to subscribe to on behalf of their smaller credit union members.

We determined one CLF member utilized the CLF for an advance of $1 million during the scope period of our audit. The CLF approved the loan and borrowed the money for the loan in December 2023. We inquired with the CLF members we selected in our sample about the use of the CLF as a liquidity source and several members mentioned how they viewed the CLF as a lender of last resort. We note the NCUA's view is the CLF is not to be used as a conventional funding facility or standard market alternative for borrowing by credit unions as the CLF does not extend credit to fund an expansion of credit union portfolios and does not seek to compete with conventional market sources. The NCUA's position is the CLF was established to be a federal contingent liquidity source for credit unions to effectively deal with liquidity risk in all environments, particularly during times of reduced liquidity or system stress. This protection safeguards creditworthy credit unions in times when liquidity needs threaten to disrupt credit unions' ability to provide basic financial resources to their members. Accordingly, NCUA's long-held policy is that the CLF is a backup liquidity provider.

As growth of the CLF may be impacted by credit unions' awareness of the CLF, we asked a sample of 15 credit unions that became regular members of the CLF how they became aware of the CLF and what it is and does. Respondents (12 of 15) cited a number of sources for their awareness of the CLF. These included their NCUA examiner, being a provisional CLF member through their corporate credit union, NCUA issued guidance on ensuring sufficient access to liquidity, conducting their own research and getting advice from their corporate credit union, a consultant working on their merger with another credit union, different articles and publications, and from their asset and liability management third party provider. We also asked a sample of 15 credit unions that were not members of the CLF if they were aware of the CLF and what it is and does. Four of the eight credit unions that responded indicated they were not aware of the CLF while the other four credit unions stated they were aware of the CLF. The CLF President told us one of his primary roles is to conduct outreach and make people aware of the CLF. The CLF President and Vice-President have conducted briefings with various state credit union leagues, credit union service organizations, and presidents of corporate credit unions. They also have briefed personnel in all three NCUA regions in the past year. They believe this outreach has resulted in the growth in the number of CLF members.

Because the growth of the CLF may be impacted by the membership application process, we also asked a sample of CLF regular members about their experience when they applied to become a member. We asked each of these members about the following:

- Ease of the process,
- Reasonableness of the amount of information asked to be provided,
- Responsiveness of CLF personnel to any questions or concerns raised during the process, and
- Their satisfaction with the timeliness of CLF's decision to approve the membership application.

None of the 12 credit unions that responded had a negative response to these four areas of the application process. They described the application process as easy, reasonable, or seamless. In addition, they expressed the amount of information asked to be provided with their application was not overly cumbersome, seemed reasonable, and was needed. Respondents described CLF personnel as responsive and helpful during the application process and also expressed satisfaction with the timeliness of the CLF's application review and decision on membership.

Based on the information presented above, we determined the CLF is being utilized as evidenced by its growth in membership. Therefore, we are not making a recommendation to NCUA management.

Appendix A

OBJECTIVES, SCOPE, AND METHODOLOGY

We developed our objectives for this engagement based on the OIG's 2024 Annual Work Plan. Specifically, the objectives of our audit were to determine: (1) whether the NCUA operates the CLF in accordance with relevant laws, regulations, policies, and procedures, and (2) the utilization of the CLF by credit unions covered by the temporary authority granted by the CARES Act.

To accomplish our audit, we performed fieldwork with information obtained from various NCUA sources relevant to the operation of the CLF. The scope of our audit covered the NCUA's operation of the CLF from January 2020 to March 31, 2024. To achieve our objectives, we:

- Reviewed laws and regulations relevant to the CLF.
- Reviewed CLF policies and procedures for applying for membership, advances, large dollar notifications, dividend payments, investments, capital stock annual adjustments, and membership withdrawal.
- Interviewed CLF and E&I personnel.
- Sampled the 160 credit unions that became CLF members during the scope of the audit and tested for compliance with laws, regulations, policies, and procedures. We used a non-statistical random sample of these members and reviewed processes and related documentation for applying for membership, dividend payments, and the capital stock annual adjustment. We used a random number generator to select 15 credit unions that became regular CLF members. We also randomly selected four corporate credit unions who became agent members of the CLF, bringing our total sample of members tested to 19.
- Reviewed the one advance the CLF made during the scope of the audit and related documentation to determine compliance with laws, regulations, and procedures.
- Reviewed the four large dollar transaction notifications by the CLF and related documentation to determine compliance with policy.
- Reviewed the termination of membership of six members and related documentation to determine compliance with regulations and procedures.
- Sampled the 4,152 credit unions that were not CLF members as of March 31, 2024, to determine their awareness of the CLF. We used a non-statistical random sample and a random number generator to select 15 credit unions.
- Evaluated internal control over the CLF's processes.

We did not rely on computer-processed data from NCUA systems to answer the audit objectives. While we determined that computer processed data from Delphi[16] was significant to the audit objectives, Delphi's provider is the Department of Transportation and as such we did not evaluate the information system controls. The CLF uses Delphi in the calculation of dividend payments, the production of annual adjustment statements, and capital and dividend statements. It is also utilized for collections from new members and annual stock adjustments and the return of capital or dividends to members using the Delphi payment module. We compared data on various documents and CLF statements and relied on interviews and correspondence with NCUA officials to assess the validity of the data and confirm its reliability.

We conducted this audit from June 2024 through December 2024 in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We assessed the effectiveness of internal controls we determined were significant to the audit objectives. Specifically, we assessed 4 of the 5 internal control Components and 7 of the 17 associated underlying Principles defined in the Government Accountability Office's Standards for Internal Control in the Federal Government.[17] We summarize in Table 2 below the Components and Principles we assessed.

Table 2: Internal Control Components and underlying Principles Assessed

Component: Control Environment
Principle #3 – Establish Structure, Responsibility and Authority
Principle #4 – Demonstrate Commitment to Competence
Component: Risk Assessment
Principle #6 – Define Objectives and Risk Tolerances
Principle #7 – Identify, Analyze and Respond to Risk
Component: Control Activities
Principle #10 – Design Control Activities
Principle #12 – Implement Control Activities
Component: Information and Communication
Principle #13 – Use Quality Information

[16] Standard transaction and reporting services on the Department of Transportation's Enterprise Service Center system (Delphi) includes management of payables, revenue, reimbursables, and receivables and collections.
[17] The Standards for Internal Control in the Federal Government organizes internal control through a hierarchical structure of 5 components and 17 principles. The five components, which represent the highest level of the hierarchy, consist of the Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring. The 17 principles support the effective design, implementation, and operation of the components, and represent the requirements for establishing an effective internal control system.

We determined the internal controls that are significant to the audit objectives have been appropriately addressed by the NCUA. However, because our audit was focused on these significant internal control Components and underlying Principles, it may not have disclosed all internal control deficiencies that may have existed at the time of this audit.

Appendix B

NCUA MANAGEMENT RESPONSE

National Credit Union Administration
Central Liquidity Facility

SENT VIA EMAIL

TO: Inspector General, James Hagen

FROM: CLF President, Anthony Cappetta ANTHONY CAPPETTA Digitally signed by ANTHONY CAPPETTA Date: 2025.03.03 15:13:42 -05'00'

SUBJ: Management Response- *Audit of the Central Liquidity Facility*

DATE: March 3, 2025

We reviewed the Office of Inspector General's audit report titled *Audit of the Central Liquidity Facility*.

We concur with the report's conclusions and will determine whether to pursue any action to extend the due date for the annual stock adjustment payments to the Central Liquidity Facility.

Thank you for the opportunity to comment.

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Appendix C

ACRONYMS AND ABBREVIATIONS

Acronym	Term
CARES Act	Coronavirus Aid, Relief, and Economic Security Act
CLF or Facility	Central Liquidity Facility
E&I	Office of Examination and Insurance
FFB	Federal Financing Bank
GAO	Government Accountability Office
LRC	Liquidity reserve and clearing
NCUA	National Credit Union Administration
OCFO	Office of the Chief Financial Officer
OIG	Office of Inspector General