NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

August 25, 1989

Office of General Counsel

GC/JT:sg
SSIC #3550
89-0803

Mr. John J. Smolinsky
President
Saugus Federal Credit Union
448 Lincoln Avenue
Saugus, Massachusetts 01906

Re: Section 701.21(c)(8) of NCUA Rules and Regulations (Your July 31, 1989, Letter to Chairman Jepsen)

Dear Mr. Smolinsky:

Chairman Jepsen asked that this office respond to your letter to him regarding Section 701.21(c)(8) of NCUA's Rules and Regulations (12 C.F.R. 701.21(c)(8)). This section of the regulations is intended to prevent insider abuse related to Federal credit union ("FCU") lending. You suggested that the regulation may be overly broad, and asked that NCUA consider loosening the restrictions contained in the regulation. While we agree that the regulation may restrict certain business transactions by FCU officials that do not involve insider abuse, this Office continues to believe that the regulation is necessary to protect FCU's from insider abuse, and to protect the NCUSIF from losses occasioned by such abuse.

BACKGROUND

A director of your FCU recently resigned from the FCU board when it was determined that he was in violation of Section 701.21(c)(8). The former director owns an insurance agency that writes homeowners' policies for some mortgagors of the Credit Union. No insider abuse was involved. You have

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suggested that Section 701.21(c)(8) be amended to exclude from its prohibition the receipt by FCU officials of income from the sale of homeowners' insurance to FCU members with mortgage loans from the FCU.

ANALYSIS

Section 701.21(c)(8) provides in part:

> A Federal credit union shall not make any loan or extend any line of credit if, either directly or indirectly, any commission, fee or other compensation is to be received by the credit union's directors, committee members, senior management employees, loan officers, or any immediate family members of such individuals, in connection with underwriting, insuring, servicing, or collecting the loan or line of credit. However, salary for employees is not prohibited by this Section. . . .

This section is intended to ensure that decisions that an FCU makes at the various stages of making a loan will not be influenced by the receipt of things of value by those at the FCU involved in such decisions. Insider abuse of this type has resulted in losses to the NCUSIF.

The language of the regulation is somewhat broad, and may result in the restriction of activities, such as in the case of your FCU, where no insider abuse is involved. We believe that the language of the regulation continues to be necessary to protect against insider abuse. Although the amendment you suggested may be appropriate in an FCU where insider abuse is not involved, it may open the door for insider abuse in other credit unions.

Sincerely,

Hattie M. Ulan

HATTIE M. ULAN
Assistant General Counsel