



NATIONAL CREDIT UNION ADMINISTRATION

WASHINGTON, D.C. 20456

October 30, 1991

Dominic S. Zappia
6290 Sweet Maple Lane
Boca Raton, FL 33433

Re: Conflict of Interest (Your August 22, 1991,
Letter)

Dear Mr. Zappia:

You have asked for our opinion regarding an alleged conflict of interest.

Background

You work part-time as a real estate agent and served as a member of the supervisory committee of the Eastern Federal Financial Federal Credit Union. You assisted the credit union's new executive vice president in buying a home in the area and received a commission on the sale from the seller. You state that a National Credit Union Administration (NCUA) examiner determined that your receipt of a commission while serving on the supervisory committee constituted a conflict of interest and demanded your removal. You ask whether your actions constituted a conflict of interest. Based on the facts you have presented, we do not think there was a conflict.

Analysis

The NCUA Rules and Regulations contain a number of conflict of interest provisions. Addressing the issue of prohibited fees on loans, Section 701.21(c)(8) of the NCUA Rules and Regulations, 12 C.F.R. §701.21(c)(8), states:

A Federal credit union (FCU) 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, or any immediate family members of such individuals, in connection with underwriting, insuring, servicing, or collecting the loan or line of credit

Addressing the issue of preferential loans, Section 701.21(d)(5), 12 C.F.R. §701.21(d)(5), provides:

The rates, terms and conditions on any loan or line of credit either made to, or endorsed or guaranteed by

- (i) an official
- (ii) an immediate family member of an official, or
- (iii) any individual having a common ownership, investment or other pecuniary interest in a business enterprise with an official or with an immediate family member of an official shall not be more favorable than the rates, term[s] and conditions for comparable loans or lines of credit to other credit union members. "Immediate family members" means a spouse or other family member living in the same household.

Section 701.27(d)(6) of the NCUA Rules and Regulations, 12 C.F.R. §701.27(d)(6), addresses the issue of compensation for an FCU board member employed by a credit union service organization (CUSO). It provides:

- (i) Individuals who serve as officials of, or senior management employees of an affiliated Federal credit unions as defined in (c)(1)), and immediate family members of such individuals, may not receive any salary, commission, investment income, or other income or compensation from a credit union service organization either directly or indirectly, or from any person being served through the credit union service organization. This provision does not prohibit an official or senior management employee of a Federal credit union from assisting in the operation of a credit

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union service organization, provided the individual is not compensated by the credit union service organization. Further, the credit union service organization may reimburse the Federal credit union for the services provided by the individual.

(ii) The prohibition contained in paragraph (d)(6)(i) also applies to any employee not otherwise covered if the employee is directly involved in dealing with the credit union service organization unless the board of directors determines that the employee's position does not present a conflict of interest.

(iii) All transactions with business associates or family members not specifically prohibited by this subsection (d)(6) must be conducted at arm's length and in the interest of the credit union.

Addressing federal credit union lease of officers' or directors' property, Section 701.36(e) of the NCUA Rules and Regulations, 12 C.F.R. §701.36(e), states:

(1) With the exception of a short term informal lease agreement (maturity less than 1 year) no Federal credit union may acquire or lease premises without the prior written approval of the Administration from any of the following:

(i) a director, member of the credit committee or supervisory committee, or senior management employee of the Federal credit union, or immediate family member of any such individual.

(ii) a corporation in which any director, member of the credit committee or supervisory committee, official, or senior management employee, or immediate family members of any such individual, is an officer or director, or has a stock interest of 10 percent or more.

(iii) a partnership in which any director, member of the credit committee or supervisory committee, or senior management employee, or immediate family members of any such individual, is a general partner, or a limited partner with an interest of 10 percent or more.

(2) The prohibition contained in paragraph (e)(1) also applies to any employee not otherwise covered

if the employee is directly involved in investments in fixed assets unless the board of directors determines that the employee's involvement does not present a conflict of interest.

(3) All transactions with business associates or family members not specifically prohibited by this subsection (e) must be conducted at arm's length and in the interest of the credit union.

Section 703 of the NCUA Rules and Regulations, 12 C.F.R. §703, addresses the issue of federal credit union investments, but Section 703.4(e)-(g) specifically provide:

(e) A Federal credit union's directors, officials, committee members and senior management employees, and immediate family members of such individuals, may not receive pecuniary consideration in connection with the making of an investment or deposit by the Federal credit union.

(f) The prohibition contained in subsection (e) also applies to any employee not otherwise covered if the employee is directly involved in investments or deposits unless the board of directors determines that the employee's involvement does not present a conflict of interest.

(g) All transaction with business associates or family members not specifically prohibited by subsection (e) must be conducted at arm's length and in the interest of the credit union.

Section 721.1 of the NCUA Rules and Regulations, 12 C.F.R. §721.1, allows group purchasing plans to be made available to members, but Section 721.2(c) specifically states:

No director, committee member, or senior management employee of a Federal credit union or any immediate family member of any such individual may receive any compensation or benefit, directly or indirectly, in conjunction with any [group purchasing plan].

In addition, Article XIX, Section 4, of the Standard Federal Credit Union Bylaws provides:

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No director, committee member, officer, agent, or employee of this credit union shall in any manner, directly or indirectly, participate in the deliberation upon or the determination of any question affecting his pecuniary interest or the pecuniary interest of any corporation, partnership, or association (other than this credit union) in which he is directly or indirectly interested. In the event of the disqualification of any director respecting any matter presented to the board for deliberation or determination, such director shall withdraw from such deliberation or determination; and in such event the remaining qualified directors present at the meeting, if constituting a quorum with the disqualified director or directors, may exercise with respect to this matter, by majority vote, all the powers of the board. In the event of the disqualification of any member of the credit committee or the supervisory committee, such committee member shall withdraw from such deliberation or determination.

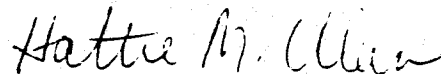
As you can see, there are a number of protections in place against "insider dealings" and conflicts of interest. While the number of known cases of such dealings is small, the aggregate cost to the National Credit Union Share Insurance Fund has been severe. Consequently, the subject is of very serious concern. NCUA examiners are charged with the difficult task of detecting such conflict situations and taking steps to correct them.

Unless there are additional facts we are unaware of, the regulation most likely to be implicated by your situation is Section 701.21(c)(8), which, as noted earlier, prohibits a credit union's committee members, among others, from receiving any fee or compensation in connection with underwriting, insuring, servicing, or collecting the credit union's loans. The purpose of the provision is to ensure that the decisions a federal credit union goes through at the various stages of making a loan will not be influenced by the receipt of things of value by those at the credit union involved in such decisions. Over the years, Section 701.21(c)(8) has been expanded so that more and more stages of making a loan are included in the prohibition. We have

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not yet stated, however, that receiving a fee for assisting a credit union member, employee, or official in selling or buying a home is prohibited, even if the home is financed by the credit union. Accordingly, your actions do not constitute a conflict of interest under Section 701.21(c)(8).

Sincerely,



Hattie M. Ulan
Associate General Counsel

GC/LH:sg
SSIC 3500
91-0836

cc: Regional Director, Region III