



# National Credit Union Administration

Office of Examination and Insurance

August 5, 2022

SENT BY FEDERAL EXPRESS AND EMAIL

XXXX, Chairperson  
XXXX Credit Union  
XXXX  
XXXX

Dear XXXX:

On July 7, 2022, on behalf of the Board of XXXX Credit Union, your attorney filed a request for review of your credit union's required divestiture of impermissible investments and removal of board member XXXX from any current and future investment transactions. You filed this request pursuant to 12 C.F.R. Part 746.106, which allows a credit union to seek my review of a written material supervisory determination by a program office.

The review of material supervisory determinations you are requesting involve two matters:

- First is a review of the June 7, 2022, reconsideration of the April 13, 2022, written determination made by Regional Director XXXX, which requires your credit union divest of two impermissible investments. Specifically, the credit union is ordered to divest of the preferred stock with XXXX and the preferred stock with XXXX. You requested reconsideration of this decision in your letter dated May 13, 2022. Regional Director XXXX, in XXXX letter dated June 7, 2022, denied your request for reconsideration of divestiture. In this appeal request you are seeking my permission to continue to hold these two investments.
- Second is a review of the determination to ensure board member XXXX is removed from any current and future investment activities of the credit union where he is an interested party. Regional Director XXXX made this material determination in the letter addressed to you on April 13, 2022. You requested reconsideration of this decision in your letter dated May 13, 2022. As no written decision, stating the reasons for the decision, was rendered within 30 days, per § 746.105 of the NCUA Rules and Regulations, the request for reconsideration will be deemed to have been denied.

As discussed more fully below, I conclude your credit union must immediately, and not later than September 6, 2022, divest of the impermissible investments. Further, I must emphasize the credit union board must ensure all future investment transactions are conducted in compliance with Part 703, including mitigating any appearance of or potential conflicts of interest.

### Background

Over the course of several transactions from September 2, 2020, to November 4, 2021, XXXX CU purchased \$ XXXX in preferred stock with XXXX and \$ XXXX in preferred stock with XXXX.

The permissibility of these investments was originally questioned by Region XXXX during the credit union's December 31, 2021, examination. Upon identification of the impermissible investments, it was determined appropriate to issue a Regional Director Letter to the credit union dated April 13, 2022, while the examination was ongoing. The Regional Director Letter instructed the credit union to divest of these investments. Further, the Regional Director Letter identified a potential conflict as board member XXXX acted as the investment representative for these transactions. As such, the Regional Director required board member XXXX be removed from any current or future investment activities of the credit union where he is an interested party. In your letter dated May 13, 2022, you requested Regional Director XXXX reconsider these actions.

On June 7, 2022, Regional Director XXXX affirmed XXXX earlier determination the XXXX and XXXX investments were impermissible and again concluded the credit union must divest of the investments. Regional Director XXXX further stated additional information was necessary to assess the Region's concern with board member XXXX's involvement in the investment transactions, thus deferring determination on the matter.

On July 5, 2022, you filed your request for Director of Examination & Insurance (E&I) review of Regional Director XXXX's material supervisory determinations with respect to the investments and the potential conflict of board member XXXX.

### Discussion

E&I has jurisdiction to review the Regional Director's decision, as your request for review was timely and it is a material supervisory determination as defined by 12 C.F.R. Part 746.103. Specifically, the material supervisory determination you are appealing meets the requirements of Part 746.103 as the requirement to divest of the investments in question have a material impact on the credit union's earnings.

Following the receipt of your request, my staff performed a full and careful review of relevant law. Upon completion of that review, I have confirmed the credit union's XXXX and XXXX investments are impermissible.

Under Section 107 of the Federal Credit Union Act (Act), 12 U.S.C. §1757(7)(B), a credit union may invest its funds in specified permissible investments. Part 703 of NCUA Rules and Regulations identifies certain investments and deposit activities permissible under the Act and prescribes regulations governing those investments and deposit activities. Additionally, Part 703 identifies and prohibits certain investments and deposit activities.

XXXX

August 5, 2022

Page 3

Your investments in XXXX and XXXX are categorized as preferred stock. While preferred stock is like a debt security, it is not listed as a permissible investment under Section 703.14, which defines permissible investments. Any security investment must be included in Section 703.14 to be permissible for federal credit unions. Section 703.16 of NCUA Rules and Regulations provides a limited listing of prohibited investments. While preferred stock is not specifically listed, it is not appropriate to assess whether an investment is permissible based solely on the limited listing of specifically prohibited investments contained in section 703.16.

You have submitted a settlement proposal with your appeal. Under the settlement proposal, rather than immediately divesting of the impermissible investments as directed by Regional Director XXXX, the credit union would continue to hold the investments for now and divest of them at a later time. The credit union would exercise the redemption option of the XXXX investment at the first available time. Similarly, the credit union would hold the XXXX investment until September 6, 2022, to lessen the estimated redemption penalty.

I recognize the financial impact of the early redemption penalties on your earnings and your desire to hold onto the investment to a later date. While I agree with Regional Director XXXX's determination to divest of the investments immediately, the timeframe established for the XXXX investment in your settlement proposal is reasonable. However, as no tangible date was specified for the XXXX investment, I will require it also be divested immediately but not later than September 6, 2022.

In addition to appealing Regional Director XXXX's determination on the permissibility of these investments, the credit union has asked for the Director of E&I's review of the violation of Section 703.17 of NCUA Rules and Regulations due to board member XXXX's involvement as the investment representative for these transactions. Under the rule, a federal credit union's officials and senior management employees, and their immediate family members, may not receive anything of value in connection with its investment transactions. Regional Director XXXX in XXXX reconsideration letter noted a determination on this matter could not be made at the time of XXXX review because additional information was needed and was being collected during the examination in process. However, because a definitive determination was not rendered in a written decision, stating the reasons for the decision, within 30 days, for the purpose of this review your request for reconsideration is deemed to have been denied.

Your appeal to the Director of E&I includes an affidavit from board member XXXX stating he did not receive any compensation associated with these investment transactions. We note that this affidavit was not available for consideration by Regional Director XXXX at the time of XXXX review. Thus, while Regional Director XXXX was reasonable in deferring XXXX determination based on the incomplete information he had at the time of XXXX review, in light of this affidavit from board member XXXX we accept that no direct compensation was received in connection to the purchase of these investments. Based on the facts presented, board member XXXX does not appear to be sufficiently linked to the investment transactions to raise a prohibited conflict of interest in violation of §703.17(a). However, it is difficult to determine if a board member is receiving anything of value in the form of indirect compensation, and I emphasize the need to ensure all federal credit union officials conduct all transactions at arm's length and in the credit union's best interest per §703.17(b). Further, I encourage the credit

union board to ensure all future investment transactions are conducted in compliance with Part 703, including mitigating any appearance of or potential conflicts of interest.

Decision

**My decision is that your credit union may not continue to hold the impermissible investments in XXXX and XXXX. You have until September 6, 2022, to sell the investments. XXXX CU must provide confirmation of divestiture to Regional Director XXXX upon completion of the sale.**

**Based on the affidavit provided with your appeal, we agree direct compensation was not received by XXXX.** I encourage the credit union board to ensure all future investment transactions are conducted in compliance with Part 703, including mitigating any appearance of or potential conflicts of interest.

Pursuant to NCUA's Regulations, 12 C.F.R. Part 746.107, you may appeal this decision to the Supervisory Review Committee within 30 calendar days of receipt of this letter. Such an appeal must follow the requirements of the regulation and must be filed in writing with the Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314-3428. Please refer to Part 746.107 for additional information regarding the required contents of an appeal.

Sincerely,

Kelly Lay  
Director

cc: Board Chairperson XXXX  
Regional Director XXXX  
Board Secretary Conyers-Ausbrooks  
XXXX  
XXXX  
XXXX