

October 2, 1997

Paula Walpole-Moehrig, President
Texas Associations of Professionals
Federal Credit Union
9110 I.H. 10 West
San Antonio, Texas 78230-3112

Re: Conflict of Interest
Your letter dated July 28, 1997

Dear Ms. Walpole-Moehrig:

You have asked whether an arrangement that Texas Associations of Professionals Federal Credit Union (TAP FCU) has with Megamerica Mortgage for real estate loan services presents a conflict of interest in violation of NCUA regulations or the Federal Credit Union Bylaws. The issue arises because Megamerica is owned by TAP FCU's Chairman. You note that a recent examination cited the arrangement as potentially in violation of §701.21(8)(i) of the NCUA regulations, which addresses prohibited fees in connection with loans, and Article XIX, Section IV of the FCU bylaws, which deals with disqualification of officials from determining matters in which they have a pecuniary interest.

Based upon the information provided, it is our opinion that the arrangement does not violate either of the above provisions but it does run afoul of NCUA's group purchasing regulation, which also includes a conflict of interest provision. 12 C.F.R. Part 721

BACKGROUND

TAP FCU does not make real estate loans but has entered into an arrangement with Megamerica Mortgage to provide its membership with access to real estate loan services. Under this arrangement, TAP FCU is responsible for taking loan applications, gathering documentation, counseling members, and ordering credit reports and appraisals. The real estate loans are closed at a title company and funded by a lender, other than TAP FCU, arranged through Megamerica Mortgage. TAP FCU receives a fee from Megamerica Mortgage for performing the above administrative functions as well as any profits received by Megamerica Mortgage on the real estate loans for TAP FCU members, less \$300 for Megamerica Mortgage's direct expenses. TAP FCU's chairman of the board owns Megamerica Mortgage.

In a recent NCUA examination, the examiner cited a possible conflict of interest problem as a result of the arrangement with Megamerica Mortgage. The examiner noted that the arrangement may violate Section 701.21(c)(8)(i), prohibited fees on loans, and Article XIX, Section 4 of the bylaws.

ANALYSIS

Section 701.21(c)(8)(i) of NCUA regulations provides:

[N]o official or employee of a Federal credit union, or immediate family member of an official or employee of a Federal credit union, may receive, directly or indirectly, any commission, fee, or other compensation in connection with any loan made by the credit union. (Emphasis added).

Assuming the facts are as provided, the arrangement between TAP FCU and Megamerica Mortgage would not create a conflict of interest in violation of §701.21(c)(8) because TAP FCU is not making the loans. The loans are funded by a lender arranged through Megamerica Mortgage. Any compensation received by an official of the credit union would not be considered in connection with a loan made by TAP FCU.

Article XIX, Section 4 of NCUA FCU Bylaws provides:

No director . . . 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.

As long as the chairman of the board does not participate in any "deliberation" or "determination" related to the arrangement with Megamerica Mortgage, TAP FCU should be in compliance with this bylaw.

TAP FCU's arrangement with Megamerica Mortgage is subject to Part 721 of NCUA Rules and Regulations concerning group purchasing activities and appears to violate the restriction on the amount of reimbursement for an FCU and the conflict of interest provision in this regulation. Part 721 permits an FCU to make the services of a third-party vendor, such as Megamerica Mortgage, available to its members, perform administrative functions on behalf of the vendor, and have the vendor reimburse or compensate the FCU for performing such services.

An FCU, however, cannot make a profit for providing group purchasing activities to its membership. Any reimbursement or compensation received by the credit union from a vendor cannot exceed the "cost amount" of providing such services. 12 C.F.R.

§721.2(b)(3). The "cost amount" is defined as the "total of the direct and indirect costs to the Federal credit union of any administrative functions performed on behalf of the vendor," 12 C.F.R. §721.2(a)(2), and must be justified using standard accounting procedures. 12 C.F.R. §721.2(b)(3). TAP FCU would be in violation of Part 721 for receiving profits on the real estate loans made to its members through Megamerica Mortgage.

In addition, §721.2(c) provides that "[n]o director . . . of a Federal credit union . . . may receive any compensation or benefit, directly or indirectly, in conjunction with any activity under this Part." 12 C.F.R. §721.2(c). As owner of Megamerica Mortgage, TAP FCU's chairman would be considered the recipient of any compensation or benefit received by Megamerica Mortgage from the real estate loans made to TAP FCU members.

Since Megamerica Mortgage profits from the real estate loans made to TAP FCU members and these profits cannot be passed to the credit union, they would be a direct benefit to Megamerica Mortgage. As a benefit to Megamerica Mortgage, the profits would be considered a benefit to TAP FCU's chairman of the board, as owner of the company. Accordingly, the chairman of the board would be receiving compensation or a benefit in conjunction with a group purchasing activity provided by the credit union which is a violation of §721.2(c). Accordingly, TAP FCU's chairman of the board either will have to resign from the board or the credit union will have to cease doing business with Megamerica Mortgage.

From your conversation with Staff Attorney, Nicole Williams, it is clear that TAP FCU's chairman of the board is a valued volunteer and that he and his family have contributed much to the credit union since its inception. Unfortunately, the §721.2(c) prohibition is clear and does not provide for an exception.

Sincerely,

Sheila A. Albin
Associate General Counsel

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SSIC 3500
97-0811

cc: Tracy Bombarger, Region V