

45



July 21, 2005

PMB 3419 Via Lido  
Suite 135  
Newport Beach,  
California 92663

Mary Rupp, Secretary of the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, VA 22314-3428

Phone:  
(888)462-2870

Local Phone:  
(949)645-5296

Fax:  
(949)645-5297

Email:  
info@nacuso.org

Web  
www.nacuso.org

Re: Draft of Comment Letter to Proposed Interpretative Ruling and Policy Statement No. 05-1 Sales of Nondeposit Investment Products

Dear Ms. Rupp,

I am writing this comment letter on behalf of NACUSO. Our General Counsel, Guy Messick, has filed a comment letter. NACUSO endorses his comments. This letter supplements Mr. Messick's comments.

NACUSO members have been offering nondeposit investment products through affiliated broker/dealers in networking arrangements with CUSOs and credit unions since the 1980's. Many of these programs have been with dual employees.

NCUA has indicated that it is concerned that the dual employee status of some registered representatives may create liability for the credit union. In the two cases cited in the proposed IRPS, the customer/member was involved in a loan with the financial institution which became an integral part of the plaintiff's claim. In the case of Dime Bank, a Bank employee encouraged the customer to borrow more so he could make investments which were recommended by the dual employee investment representative. In the case of US Alliance Federal Credit Union, the securities secured the loans and the dual employee investment representative gave advice to the member regarding how to handle the sale of shares as loan collateral. This mixing of the lending function with the broker/dealer function is the reason why the respective courts thought that the financial institution did not preserve a clean line of non-involvement in the nondeposit investment process.

The facts in the two cited cases are very rare. Typically, a dual employee acts on behalf of the broker/dealer and sells nondeposit investment products with no contact with the credit union or any of its products. There is no line blurred in the mind of the member who receives the disclosure that the credit union is not involved with or guarantees the nondeposit investments products. With the possible exception of the US Alliance Federal Credit Union case, NACUSO could not find any cases where a credit union has been held liable or potentially liable for the acts of a dual employee.

We note that NCUA has expressed a concern that some credit union investment programs have broker/dealers who are not located near the credit union. The fact that a broker/dealer is located some distance from the credit union is not a *per se* compliance issue. The broker/dealer

has responsibility to supervise and monitor the transactions. A great deal of the supervision and monitoring these days is performed electronically by monitoring the registered representatives' notes, correspondence and trades. The program's registered principal also has to monitor the program on-site. While we acknowledge that the more the registered principal is available on-site, the more desirable the situation, it is not financially feasible for most credit union programs to have its registered principal on-site all the time. It has been proven over and over again that compliance is not compromised in programs where the registered principal monitors the program full time through the written material coupled with periodic on-site visits. If this method of supervision were a problem, you would see wide spread concern by broker/dealers and their regulators but this is not the case. If it appears to be a problem in a particular case, the credit union can address the issue with the broker/dealer or its regulator.

NACUSO is concerned with the economic, legal, and reputation risk to the credit union offering nondeposit investment products. NACUSO provides education to its members on the best practices in offering nondeposit investment products. This helps credit unions be successful and reduce the economic risk to credit unions.

For the reasons stated in Mr. Messick's comment letter, NACUSO is concerned that putting credit unions in a regulatory oversight role over the broker/dealers is putting credit unions and the share insurance fund in greater legal jeopardy. NACUSO would offer the following alternative practice to deal with the reputation and legal risks.

The credit union shall select a broker/dealer that has demonstrated the ability to effectively supervise the activity of its registered representatives and monitor compliance with state and federal laws applicable to the sales of nondeposit investment products. The credit union shall designate a credit union employee who is not associated with the operation of the nondeposit investment services to be the service and compliance liaison with the broker/dealer. Members shall be advised if they have a service or compliance issue that is not being resolved to their satisfaction, to contact the credit union's liaison. The credit union's liaison shall report any service or compliance issues to the broker/dealer and shall follow up with the broker/dealer and member to insure that the service and/or compliance issues are resolved as promptly as possible. The credit union liaison shall make periodic reports of any service or compliance issues to the credit union. If the credit union determines that there are service or compliance issues that are not being adequately addressed, the credit union shall take further action which, depending on the circumstances, could be termination of the relationship with the broker/dealer and/or reference of the matter to the broker/dealer's regulators.

If credit unions assume the role of liaison or ombudsman, they can monitor problems and oversee the resolution of the problems by the broker/dealer as soon as possible. This role will enable credit unions to protect their reputation risk without injecting themselves into actual

47

compliance functions which will create significant legal risk. This role for the credit union can be set forth in the IRPS.

NACUSO encourages NCUA to resolve the non-member service issue per the comments of Mr. Messick.

Very truly yours,

*Victor Pantea*

Victor Pantea, President