U.S. CENTRAL™

SUITE 100
9701 RENNER BLVD.
LENEXA, KANSAS 66219
TEL: (913)227-6000
TOLL FREE: (888)872-0440
FAX: (913)438-1564
WWW.USCENTRAL.COOP

Via e-mail: regcomments@ncua.gov

July 25, 2005

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

Re: Proposed Interpretive Ruling and Policy Statement No. 05-1

Dear Ms. Rupp:

U.S. Central Credit Union (U.S. Central) is pleased to comment on NCUA's proposed Interpretive Ruling and Policy Statement on Sales of Nondeposit Investments (the "Proposed IRPS"). The Proposed IRPS is intended to provide requirements, direction, and guidance to federally-insured credit unions on the establishment and operation of third-party brokerage arrangements, and to update and replace NCUA's Letter to Credit Unions No. 150 ("Letter No. 150") on the sales of nondeposit investments. In many cases, the Proposed IRPS strikes a reasonable regulatory balance that would permit the safe and sound growth of credit unions through third-party brokerage arrangements for sales of nondeposit investments. However, while recognizing NCUA's valid regulatory concerns, we do have several comments and suggestions that we believe would be beneficial to corporate credit unions and their broker/dealer credit union service organization (CUSO) subsidiaries that serve institutional customers, not consumers.

Proposed Guidance as to Best Practices

The stated purpose of the Proposed IRPS is "to help credit unions conduct third part brokerage activities in a manner that is legal, protects members from potential securities fraud and abuse, and minimizes safety and soundness concerns for the credit union." (Proposed IRPS, Section II) The Proposed IRPS contains both (a) legal requirements for credit unions, and (b) guidance as to suggested best practices for credit unions to follow. U.S. Central supports the spirit and intent of the Proposed IRPS, in general, including all of the legal requirements summarized therein. The suggested guidance as to best practices contained in the Proposed IRPS, however, should in some circumstances distinguish between

third-party brokerage arrangements for the sale of nondeposit investments to consumer members of federally-insured natural person credit unions ("NPCUs"), and those third-party brokerage arrangements for the sale of nondeposit investments to financial institution members of federally-insured corporate credit unions ("Corporates"). In the latter case, sales of securities solely to institutional customers, not consumers, warrants more flexibility in the recommended guidance. Other suggested best practices should be revised to clarify and underscore that the broker, not a credit union, should remain responsible for ensuring compliance with securities laws and applicable rules and regulations issued by the Securities and Exchange Commission ("SEC") and the National Association of Securities Dealers ("NASD").

Sale of Nondeposit Investments to Financial Institution Members of Corporates

In the Supplementary Information in support of the Pending IRPS, NCUA appropriately notes that credit union management must be aware how the credit union's members will perceive the relationship between the credit union and a broker, including how the two might be connected in a member's mind; "the greater the possible connection, the more management must be involved in oversight of nondeposit investment sales practices." (Proposed IRPS, Supplementary Information, page 6) The cases cited in support of this proposition involve unsophisticated consumer members of financial institutions.

When the member is itself a financial institution, not an unsophisticated consumer, there is less likelihood of creating confusion between the respective roles of the Corporate and the broker. When the member in question is not a consumer, but instead a NPCU or other financial institution member of a Corporate, U.S. Central submits that the level of management involvement in oversight of nondeposit investment sales practices would not need to be as significant as the level of oversight appropriate for nondeposit investment sales to consumers.

ISI's Corporate Agent Program

U.S. Central's wholly-owned CUSO subsidiary, CU Investment Solutions, Inc. ("ISI"), is a registered broker/dealer offering third-party brokerage services to the member Corporates of U.S. Central. One program ISI offers is its Corporate Agent Program, whereby third-party brokerage services are provided to NPCU and other financial institution members of Corporates. Under the Corporate Agent Program, ISI enters into a written tri-party contractual arrangement with a Corporate and a Corporate employee who serves a dual function as an independent contractor registered representative of ISI. As such, the Corporate Agent Program is structured similar to a "dual employee" sales representative program, in that the independent contractor registered representative of ISI also serves as an employee of Corporate for non-securities business purposes. The tri-party contract between ISI, a Corporate and each independent contractor registered representative, expressly states that the parties are required to observe all applicable laws and applicable regulations of the SEC, SEC guidance applicable to credit unions as contained in a series of "no action" letters (e.g., SEC Letter Re: Chubb Securities Corporation (Nov. 24, 1993), and applicable NCUA

regulations and guidance, including Letter No. 150. Indeed, each of the SEC requirements summarized in Section IV of the Proposed IRPS is expressly addressed in the tri-party agreement.

Physical Separation of Deposit-Taking from Sales of Nondeposit Investments

Section IV of the Proposed IRPS, however, also includes a suggested best practice that deposit-taking activities be physically separated from nondeposit sales functions. While this suggested best practice may be appropriate for sales of nondeposit investments to consumer members of NPCUs, it is not as germane to the sale of nondeposit investments and securities to financial institution members of Corporates. A vast majority of sales of nondeposit investments and securities by ISI to financial institution members of Corporates, including those conducted by its independent contractor registered representatives in the Corporate Agent Program, involve telephonic and electronic communications, not face-to-face transactions that predominate between NPCUs and their consumer members. Deposit-taking activities at Corporates, moreover, including sales of non-securities by a Corporate to its member NPCU or financial institution, often are conducted remotely, by telephone or electronic means. Accordingly, U.S. Central suggests that the recommended best practice be revised to state that deposit-taking, *to the extent practicable*, be physically separated from nondeposit sales functions, *particularly if those nondeposit sales are to consumer members of a credit union*. Because the sale nondeposit investments to institutional customers does not entail physical contact with the general public, less physical separation of deposit-taking functions from nondeposit sales functions should be permitted.

Responsibility for Compliance

Section V of the Proposed IRPS contains suggested guidance that relates to the safety and soundness of credit unions involved in third-party brokerage arrangements. That proposed guidance includes the recommendation that a credit union's policies and contract with a broker "make clear that the brokerage firm is *primarily* responsible for ensuring that the nondeposit sales function is conducted in compliance with all applicable laws, regulations, and policies. The contract, should, however, recognize that the credit union has the right to check for compliance and may *access member accounts* for verification and oversight." (Proposed IRPS, Section V, pages 18, 20-21; emphasis added)

U.S. Central is concerned that this guidance places too great a compliance burden on credit unions. Some credit unions may not have the requisite securities expertise to effectively check for the broker's compliance with securities laws and the rules and regulations of the SEC and NASD. That burden should fall solely on the broker. U.S. Central thus respectfully suggests that NCUA clarify that the responsibility for ensuring compliance with applicable securities laws and SEC and NASD rules and regulations concerning the sale of nondeposit investments, must reside solely with the broker, not the credit union. The credit union, in turn, should only be responsible for ensuring compliance with applicable NCUA regulations, including any requirements and guidance included in the Proposed IRPS.

U.S. Central also is concerned that the proposed guidance regarding a credit union's access to member accounts for verification and oversight may run afoul of privacy and confidentiality obligations owed by the broker to its customers. Accordingly, NCUA should clarify the suggested guidance to provide that credit unions, in performing verification or oversight of the sales of nondeposit investments by the broker to the credit union's members, should access and review their own account information they maintain for their members, including any information pertaining to transactions with the broker, but need not seek access to or review of the broker's separate customer account information.

Because the Corporate Agent Program involves the sale of nondeposit investments only to financial institution members of Corporates and not any consumers, ISI does not access or receive any information regarding consumers or their nonpublic personal information. U.S. Central notes, however, that brokers contracting with NPCUs for sale of nondeposit investments to consumer members of a NPCU would have obligations regarding Privacy of Consumer Financial Information under Part 248 (Regulation S-P) of the SEC's Rules and Regulations, and of Part 313 of the Federal Trade Commission's (FTC) Rules and Regulations that would prevent the credit union from accessing the broker's accounts for a member of the credit union, absent applicable notices to the consumers.

Indemnification

NCUA recommends that "credit union policies should require a specific and unambiguous contractual agreement from the brokerage firm to indemnify the credit union for any monetary damages arising from nondeposit sales activities, including but not limited to any improper sales practices by the broker." (Proposed IRPS, Section V, pages 18 and 22) Any such indemnification clause, however, should include a limitation to the effect that the broker should not be required to indemnify the credit union for the credit union's performance of its obligations under the Proposed IRPS.

Separation of Duties of "Dual Employees"

In the Proposed IRPS, NCUA recommends that credit unions establishing a third-party brokerage arrangement through the use of "dual employees" should have separate written job descriptions for the respective duties to be performed for the credit union and the nondeposit investment sales duties to be performed as a registered representative of the brokerage firm. (Proposed IRPS, Section V, page 21) NCUA also recommends that the duties to be performed for the credit union should be unrelated to the sale of nondeposit investments. U.S. Central and ISI support both recommendations, as long as the dual employee, when acting in his or her capacity as an employee of a Corporate, may engage in the sale of the Corporate's depository instruments to the Corporate's members.

NCUA also recommends, however, that the duties to be performed for the credit union "should not bring the employee into contact with members that might also purchase nondeposit investments." U.S. Central respectfully submits that this proposed guidance is too restrictive, at least for Corporate employees involved in the sale or delivery of products or

services to non-consumer financial institution members of the Corporate. As long as a dual employee (or as in the case of ISI's Corporate Agent Program, a Corporate employee also serving a dual function in the capacity as an independent contractor registered representative of a broker) gives the non-consumer financial institution customer of the broker the clear, complete and accurate disclosures required by law, as summarized in Section IV of the Proposed IRPS, that employee should be permitted to sell both (a) any product or service of the Corporate, including but not limited to shares, share certificates and other authorized non-securities depository instruments, and (b) nondeposit investments, in his or her capacity as a registered representative of the broker. The key should be avoidance of creating any undue confusion at the financial institution customer between sale of nondeposit investments through the broker and the sale of authorized depository instruments, including shares and share certificates, through the Corporate. Any such potential undue confusion should be adequately mitigated if the employee, when selling nondeposit investments in his or her capacity as an authorized, registered representative of the broker, clearly identifies to the non-consumer member that he or she is acting solely in his or her capacity as a registered representative of the broker, not the credit union, and that the securities being offered (a) are not shares or other obligations of the credit union, (b) are not guaranteed by the credit union, (c) are not insured by the NCUA or any other federal agency, (f) involve investment risks, including the possible loss of principal, and (g) are being offered by a dual employee (or in the case of ISI's Corporate Agent Program, an independent contractor registered representative of the broker who also is employed by the Corporate for services other than the sale of securities) who serves both functions of accepting a deposits from members of the Corporate and the selling of nondeposit investment products. U.S. Central and ISI therefore respectfully request that the guidance be revised accordingly.

Conclusion

U.S. Central appreciates the opportunity to comment on the Proposed IRPS.

Sincerely,

Dan Kampen
President/CEO

cc: Jerel Wright, Kansas Administrator
Warren Meyer, KDCU Examiner
Russell Moore, NCUA Capital Markets Specialist
Joann Lang, Compliance Manager