

CREDIT UNION COMMISSION MEETING

Credit Union Department Building 914 East Anderson Lane Austin, Texas

July 12, 2019 9:00 a.m.

AGENDA

The Committee may discuss and take action regarding any item on this agenda.

TAB PAGE A. Call to Order (9:00 a.m.) – Chair Missy Morrow 4 Public Comment - Public comment on any agenda item or issue under the jurisdiction of the Credit Union Commission is allowed. Unless authorized by a majority vote of the meeting quorum, the comments of any persons wishing to address the Commission will be limited to no more than ten (10) minutes. B. Minutes of the March 8, 2019 Credit Union Commission Meeting 7 C. Committee Reports a. Commissioner Evaluation Committee Report 1. Commissioner's FY 2020 Performance Objectives and Goals 19 2. Procedures for the Commissioner's FY 2019 Performance Review 31 D. Pending and Ongoing Matters Before the Commission a. Final Post-Payment Audit Report 33 b. Department's 2019 Budget and Financial Performance 54 c. Status of the State Credit Union System 56 E. New Matters Before the Commission a. Department's Operating Plan and Budget for Fiscal Year 2020 61 b. Proposed Amendments to 7 TAC Section 91.101 **Concerning Definitions and Interpretations** 98 c. Adoption of the Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter H (relating to Investments), Sections 91.801, 91.802, 91.803, 91.804, 91.805 and 91.808, and re-adoption of rules 106 d. Proposed Amendments to 7 TAC Section 91.801 Concerning Investments in Credit Union Service Organizations 122 e. Proposed Amendments to 7 TAC Section 91.803 Concerning **Investment Limits and Prohibitions** 129 f. Adoption of the Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter I (relating to Reserves and Dividends), Sections 91.901 and 91.902, and re-adoption of rules 136

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g.	Proposed Amendments to 7 TAC Section 91.901 Concerning	
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	that may impact the Department	153
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m.	Date for Next Commission Meeting (November 1, 2019)	

Adjournment

Note: The Credit Union Commission may go into executive session (close its meeting to the public) on any agenda item if appropriate and authorized by the Open Meetings Act, Texas Government Code, Chapter 551.

Meeting Recess: In the event the Commission does not finish deliberation of an item on the first day for which it was posted, the Commission may recess the meeting until the following day at the time and place announced at the time of recess.

Meeting Accessibility: Under the Americans with Disabilities Act, the Credit Union Commission will accommodate special needs. Those requesting auxiliary aids or services should notify Cheli Castro, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752--(512) 837-9236, as far in advance of the meeting as possible.

CALL TO ORDER

TEXAS CREDIT UNION COMMISSION MEMBERS

- Allyson "Missy" Morrow, Chair
- Elizabeth L. "Liz" Bayless
- Beckie Stockstill Cobb
- Yusuf E. Farran
- Steven "Steve" Gilman
- Sherri B. Merket
- Jim Minge
- Kay Stewart
- Rick Ybarra

Legal Counsel

• Melissa Juarez

Staff

- John J. Kolhoff
- Robert W. Etheridge
- Joel R. Arevalo
- Isabel Velasquez

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FUTURE CREDIT UNION COMMISSION MEETING DATES

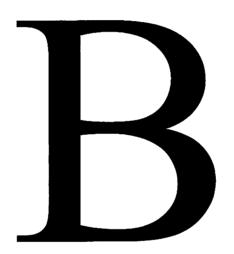
Friday, November 1, 2019

Friday, March 13, 2020

Friday, July 10, 2020

All regular scheduled meetings will begin at 9:00 a.m. unless notified differently.

If anyone has conflicts with the proposed dates, please contact Isabel Velasquez at (512) 837-9236.



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CREDIT UNION COMMISSION MEETING MINUTES

Draft copies of the minutes for the March 8, 2019 meeting, and the corresponding follow-up action report, are located under **Tab B**.

RECOMMENDED ACTION: The Department requests that the Commission approve the minutes as presented.

RECOMMENDED MOTION: I move that the minutes of the Commission's regular meeting of March 8, 2019 be approved as presented.

CREDIT UNION COMMISSION MEETING MINUTES Credit Union Department Building 914 East Anderson Lane, Austin, Texas March 8, 2019

A. CALL TO ORDER - ASCERTAIN A QUORUM – Chair Allyson "Missy" Morrow called the meeting to order at 9:00 a.m. in the conference room of the Credit Union Department Building, Austin, Texas, pursuant to Chapter 551 of the Government Code, and declared that a quorum was present. Other members present included, Beckie Stockstill Cobb, Yusuf Farran, Steven "Steve" Gilman, Sherri Merket, Jim Minge, Kay Stewart, and Rick Ybarra. Commission Member Liz Bayless was absent due to medical reasons. Assistant Attorney General Melissa Juarez was in attendance to serve as legal counsel. Representing the Department staff were John J. Kolhoff, Commissioner, Robert E. Etheridge, Deputy Commissioner and Joel Arevalo, Director of Information Technology. Chair Morrow appointed Isabel Velasquez as Recording Secretary. The Chair inquired and the Commissioner confirmed that the notice of the meeting was properly posted (February 25, 2019, TRD#2019001230).

CEREMONIAL SWEARING-IN OF COMMISSIONER KOLHOFF –

Chair Morrow welcomed everyone to the swearing-in ceremony of John Kolhoff as the Commissioner of the Credit Union Department. Mrs. Morrow expressed the importance of this event and being named the Texas Credit Union Commissioner is an extraordinary responsibility and the Commission is very pleased to have been fortunate enough to appoint someone with Mr. Kolhoff's knowledge and experience. Mr. Kolhoff was ceremoniously swornin. Mr. Kolhoff thanked the Commission, the Texas credit union industry, the trade associations for allowing him the opportunity to serve as Commissioner, and the warm reception since his arrival in Texas. The Chair recessed the meeting at 9:04 a.m., to enjoy coffee/juice and pastries. The Chair reconvened the meeting at 9:20 a.m.

- INVITATION FOR PUBLIC INPUT FOR FUTURE CONSIDERATION – Chair Morrow invited public input on matters that were not scheduled items on the agenda for possible future consideration by the Commission.
 - Melodie Durst Executive Director Credit Union Coalition welcomed Commissioner Kolhoff. Ms. Durst stated that they have had an opportunity to spend some time together around the state and at the Capitol and it has been a pleasure to get to know him. The Coalition looks forward to continuing to work with Mr. Kolhoff, staff and the commission.
- RECEIVE REQUESTS AND MOTIONS FOR EXCUSED ABSENCES – Chair Morrow inquired if there were any requests or motions to excuse an absence. Ms. Merket moved to excuse Commission Member Liz Bayless from the Commission meeting on March 8, 2019. Mr. Farran seconded the motion, and the motion was unanimously adopted.

B. RECEIVE MINUTES OF PREVIOUS MEETING (October 15, 2018). The Chair referred the members to the draft minutes of the previous meeting included in the agenda packet. Mr. Gilman moved for approval of the minutes of October 15, 2018 as presented. Ms. Cobb seconded the motion, and the motion was unanimously adopted.

C. PENDING AND ONGOING MATTERS

(a) Discussion, Consideration, and Possible Vote to Recommend that the Credit Union Commission Take Action on the Completed Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter E Concerning Direction of Affairs. Commissioner Kolhoff reported that this is part of our normal review required by Section 2001.039, Government Code. At its July 8, 2016 meeting, the commission approved a plan which establishes a date for the required review for each of the affected rules. He indicated that the Department received no written comments during the public comment period.

After a short discussion, Mr. Minge moved that the Commission find that the reasons for adopting 7 TAC, Part 6, Chapter 91, Subchapter E continue to exist and that the commission readopt these rules. Ms. Stewart seconded the motion and the motion was unanimously adopted.

(b) Discussion, Consideration, and Possible Vote to Recommend that the Credit Union Commission Take Action on the Completed Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter F Concerning Accounts and Services. Commissioner Kolhoff reported that this is part of our normal review required by Section 2001.039, Government Code. At its July 8, 2016 meeting, the Commission approved a plan which establishes a date for the required review for each of the affected rules. He indicated that the Department received no written comments during the public comment period.

After a brief discussion, Mr. Gilman moved that the Commission find that the reasons for adopting 7 TAC, Part 6, Chapter 91, Subchapter F continue to exist and that the commission readopt these rules. Ms. Cobb seconded the motion and the motion was unanimously adopted.

(c) Discussion and Consideration of the Department's FY 2019 Financial Performance. Commissioner Kolhoff indicated that for the first five months of FY 2019, operating income totaled \$2,265,259 which is \$8,897 above the YTD budgeted amount. Mr. Kolhoff explained that during the same period of time, \$910,136 was spent operating the Department. He reiterated that most bills are not paid until 30 days after the due date so some of the operating cost being reflected are only for a four-month period. He further reported that the request for the second installment of the annual operating fee was mailed out to all credit unions on February 25th with a 19.74% discount to more closely match revenues with anticipated expenses.

After a brief discussion, no formal action was taken by the Commission.

(h) Discussion and Consideration of Current Status of the State Credit Union System. Deputy Commissioner Etheridge indicated that Texas credit unions are performing well and continue to realize positive loan growth, good asset quality trends, high earnings performance, and strengthening net worth positions.

After a short discussion of some of the key financial trends, no formal action was taken by the Commission.

D. NEW MATTERS

(a) Discussion, Consideration and Possible Vote to Approve and Authorize the Submission of the Department's Annual Risk Assessment Report for FY 2019 as Required by Section 2102.004, Government Code. Commissioner Kolhoff noted that Government Code Section 2102.013 requires certain state agencies to conduct a formal internal risk assessment each year and submit the assessment to the State Auditor's Office. He indicated that staff had completed the internal risk review for 2019 and had prepared a written assessment of the risks along with the controls the Department has in place to mitigate those risks.

After a brief discussion, Ms. Merket moved that the Commission approve the Department's Internal Risk Assessment Report for 2019 and authorize its submission to the State Auditor's Office. Mr. Ybarra seconded the motion and the motion was unanimously adopted.

(b) Discussion, Consideration, and Possible Vote to Take Action to Approve the Proposed Amendments to the Commission's Policies Manual, as Part of its Annual Policy Review. Commissioner Kolhoff indicated that in accordance with Policy, the Commission is required to review its policies manual at least once each year. He noted that at this time, staff has no recommendation for changes to any of the policies contained in the manual. Unless the commission members have suggested modifications to the policies, the record will reflect that the commission has reviewed the manual and no modifications are necessary at this time.

(c) Discussion, Consideration, and Possible Vote to Take Action on the General Budget Assumptions and Parameters to be used in Guiding the Development of the Department's FY 2020 Budget. Commissioner Kolhoff reported that Section 16.003 of the Finance Code gives the Commission exclusive responsibility for approving the Department's annual budget. He noted that the budget is scheduled to be considered at the next meeting and that staff had drafted suggested budget guidelines for the commission's consideration. He also explained that salaries and benefits have been updated. At this time, we are not calculating any increases based on cost of living. Mr. Kolhoff also reported that retiring insurance cost is changing due to our former commissioner retiring. He reminded the

commission on how involved he is at the national level with the National Association State Credit Union Supervisors (NASCUS) and expenses are expected to rise from previous years for travel and conference expenses. Another change to the budget is the purchase of laptops for our field staff including replacing the desktop computers to laptops for our office staff over the next three years.

• Yusuf Farran – Commission Member, recommended that the Commission receive reports of travel expenses and the benefits gained when the Commissioner participates in meetings and conferences.

After a brief discussion, Mr. Farran moved that Commission adopt the proposed budget assumptions and parameters for FY 2020 as recommended by staff. Ms. Cobb seconded the motion and the motion was unanimously adopted.

(d) Discussion, Consideration, and Possible Vote to Adopt Resolution Commemorating A New Direction Credit Union for their Contribution to the Citizens of Texas on the Respective Milestone Anniversary Date of their Origin. Commissioner Kolhoff noted that in accordance with provisions of the Commission's Policies Manual, the Commission may adopt resolutions honoring credit unions for reaching certain milestone dates. In accordance with the criteria detailed in the policy, staff presented one resolution for the Commission's consideration.

After a short discussion, Ms. Stewart moved that the Commission adopt the Resolution Commemorating **A New Direction Credit Union** for their contribution to the citizens of Texas on the respective milestone anniversary of their origin and that a copy of the appropriate resolution be mailed to the individual credit union. Ms. Merket seconded the motion and the motion was unanimously adopted.

(e) Discussion and Consideration of Legislative Issues and Activities Relating to the 86th Regular Session that may Impact the Department or Credit Unions under its Jurisdiction. Commissioner Kolhoff reported that March 8 is the deadline for filing bills. May 27 will be the last day of the regular session and June 16 will be the last day the Governor can sign, or veto bills passed during the regular session. Mr. Kolhoff reported that on February 21 he testified to the Pensions, Investments and Financial Services Committee. He indicated that there is not really a whole lot out there that can directly affect the department but there are some bills worth mentioning that could impact the credit union system or the Department:

- HB 226 this bill would form a commission to review certain penal laws of this state and to make certain recommendations regarding those laws, to criminal offenses previously compiled in statutes outside the Penal Code, to repealing certain of those offenses, and to conforming punishments for certain of those offenses to the penalty structure provided in the Penal Code; increasing the punishment for the criminal offenses of sedition, sabotage, and capital sabotage; imposing a civil penalty.
- HB 592 this bill would authorize a credit union to act as a school district depository.
- **HB** 904 this bill would require The University of Texas at San Antonio to conduct a study regarding cyber attacks against financial institutions in this state.
- **HB 3166** this bill would prohibit a person from opening a line of credit in a minor's name without parental approval.
 - Suzanne Yashewski Regulatory and Compliance Counsel Cornerstone Credit Union League – reported that she has been working on these legal issues with credit unions for 18 years and concurred with Commissioner Kolhoff indicated that he addressed the issue perfectly. She explained that state laws handle this issue

differently, but he was spot on how it is handled in Texas as well. There are a handful of credit unions over the years that she has talked to that do this with very small dollar loans. These credit unions realize enforcement of lines of credit opened for minors without parental signature may be difficult or impossible and understand they might just have to write off such loans, but the institutions use these small loans as an opportunity to give minor children under the age of 18 the opportunity to learn some financial literacy and get involved in the process.

After a brief discussion, no formal action was taken by the Commission.

(h) Discussion and Consideration of the Date for Next Commission Meeting (July 12, 2019). Chair Morrow reminded everyone that the next regular meeting of the Commission has been tentatively scheduled for July 12, 2019 at 9:00 a.m. in Austin. Furthermore, Ms. Morrow stated that she believes this may be her last commission meeting. She wanted to extend her heartfelt appreciation and thanks to everybody that she has worked with. "Those of you that are new, those of you that have been here with us over the last 12 years I really appreciate it," she said. She further expressed that it has been a life changing experience and would highly recommend if anyone knew of someone in the credit union industry to impress on them the importance of the responsibility to volunteer.

ADJOURNMENT – There being no further business for the Credit Union Commission, Chairwoman Morrow adjourned the meeting at 10:19 a.m.

Allyson "Missy" Morrow Chairman

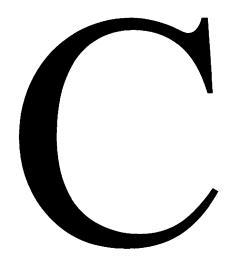
Distribution:

Legislative Reference Library

Isabel Velasquez Recording Secretary

FOLLOW-UP ACTION REPORT CREDIT UNION COMMISSION MEETINGS

MINUTES DATE AND REFERENCE/TOPIC	FOLLOW-UP ACTION REQUIRED	STATUS (As of 06-27-19)		
<u>March 8, 2019</u>				
7 TAC Sections 91.501, 91.502, 91.503, 91.510, 91.515, and 91.516 (Direction of Affairs)	Published in <i>Texas Register</i> as adopted rules.	Published in <i>Texas Register</i> on 03/22/19		
7 TAC Sections 91.601, 91.602, 91.608, and 91.610 (Accounts and Services)	Published in <i>Texas Register</i> as adopted rules.	Published in <i>Texas Register</i> on 03/22/19		



COMMISSIONER EVALUATION COMMITTEE REPORT

The Commissioner Evaluation Committee is a standing committee of the Commission. The Committee will report on their activities and recommendations to the Commission.

- (1) Approve the Commissioner's FY 2020 Performance Objectives and Goals.
- (2) Discuss Procedures for the Commissioner's FY 2019 Performance Review.

RECOMMENDED ACTION: The Department requests that the Commission accept the Committee's report as presented.



CREDIT UNION COMMISSION Commissioner Evaluation Committee Meeting Credit Union Department Building 914 East Anderson Lane

Austin, Texas

Thursday, July 11, 2019 2:00 p.m.

* * * AGENDA * * *

The Committee may discuss and take action regarding any item on this agenda

I. Call to Order (2:00 p.m.) - Chair Beckie Stockstill Cobb

- a. Ascertain Quorum
- b. Appoint Recording Secretary
- c. Acknowledge Guests
- II. Receive and Approve Minutes of the Committee Meeting on October 1, 2018
- **III.** New Business
 - a. Adoption of the Commissioner's FY 2020 Performance Objectives and Goals
 - b. Review of the Commissioner Succession Plan
 - c. Discussion Tentative Date for Next Committee Meeting (October 31, 2019)

Adjournment

<u>Note:</u> This is a meeting of the Commissioner Evaluation Committee of the Credit Union Commission. Because a quorum of the Credit Union Commission may attend this meeting of the Commissioner Evaluation Committee, it is being posted, simultaneously, as a meeting of the entire Commission.

Executive Session: The Credit Union Commission may go into executive session (close its meeting to the public) on any agenda item if appropriate and authorized by the Open Meetings Act, Texas Government Code, Chapter 551.

<u>Meeting Recess</u>: In the event the Commission does not finish deliberation of an item on the first day for which it was posted, the Commission might recess the meeting until the following day at the time and place announced at the time of recess.

<u>Meeting Accessibility</u>: Under the Americans with Disabilities Act, the Credit Union Commission will accommodate special needs. Those requesting auxiliary aids or services should notify Cheli Castro, Texas Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752--(512) 837-9236, as far in advance of the meeting as possible.

Performance Review Texas Credit Union Commissioner Instructions

The Commissioner review is a management-by-objectives program. The overall objective of this program is to align organizational goals and objectives with performance review and compensation.

Part I - Board Assessment

The Commission's Assessment is designed primarily to provide feedback to the Commissioner from each Commission member about his/her perception of the Commissioner's effectiveness.

Part I is totally subjective. As such, the weight assigned to this part of the review **should not exceed** 25% of the total review.

Each Commission member is asked to complete the Assessment Form annually and return it to the Chairman of the evaluation committee approximately one month prior to the scheduled review with the Commissioner. Data from each Commission member is compiled onto one form and shared with the Commissioner during the review.

Part II - Performance Objectives

The performance objectives section is a critical part of the Commissioner's performance review. Performance objectives are developed from the Department's strategic business plan and the plan year budget. These objectives are measurable/observable indicators that bridge the philosophy of the Texas Credit Union Department with measurable results.

Goals set for the objectives should be achievable. The best way to set goals is to look at absolute and relative measures. An absolute measure would be one in which the goal is established based on the Department's actual results. For example, if the goal is to have all state chartered credit unions examined within 18 months of the effective date of the last exam, and the result of that goal is usually 95%, a relative goal would be to have 100% of all credit unions examined within an 18 month period.

Part II is objective, in that achievement of results is verifiable, preferably measurable. This section of the review should be assigned the most weight.

Part III – Special Projects

The Special Projects section incorporates key, non-measurable strategies from the Department's strategic plan and annual operating plan & budget. Major projects and plans would be indicative of special project goals.

Individual Commission members are to evaluate results for each of the key strategies and submit their evaluations to the Chairman of the evaluation committee. <u>The Commissioner will provide Commission</u> <u>members with periodic updates regarding progress on each of the strategies throughout the plan</u>

year, as well as written documentation on the final results shortly after the conclusion of the plan year. Each Commission member's evaluation is compiled onto one form and incorporated into the overall review.

The sum of the weights assigned to Parts I, II, and III should equal 1.00.

Monitoring Results

We encourage everyone to track and review results throughout the year. Often during the course of a year, changes in the environment that are outside the control of the Commissioner may make it necessary to modify a goal. By reviewing the goals and progress toward meeting them on a quarterly basis, you can identify these situations and take action to modify them before the end of the plan period.

Final Review

The Chairman of the evaluation committee or his/her designate is responsible for distributing, collecting and compiling Assessment Forms (Parts I & III) from each Commission member. Normally, this process will begin approximately two months prior to the scheduled review date.

The Commissioner is responsible for reporting results from the Performance Objectives section of the plan. Since many of the results will be dependent on final financial reports, results should be provided to the Board within 15 days after the end of the plan period. The completed review will be given to the Commissioner during a formal performance review process when all data is known and calculated. The Chairman of the evaluation committee (and/or one of his/her designates) will meet with the Commissioner to give the formal review.

Time Table

The performance review should cover a Fiscal Year (September 1 through August 31). Each Commission member will receive electronic copies of both the Evaluation Form and a memorandum from the Commissioner outlining the Department's plan period accomplishments by September 15th.

It is important to create performance objectives for the new plan period before the end of the current plan. It is recommended that the performance objectives and goals for the next plan period be established in the last quarter of the current plan period.

Commissioner Compensation

The Commission has undertaken a market-based compensation strategy for the position of commissioner with an end objective of hiring and retaining a highly qualified commissioner to effectively and professionally discharge the duties of the agency.

The position of commissioner is the only position at the agency that is exempt from the State's Position Classification Plan. As the executive officer of the agency, the guidelines for the position's salary range are detailed in the Schedule of Exempt Positions, Article IX, Section 3.04,

General Appropriations Act (85th Legislature). The exact salary group for the position and the compensation paid to the incumbent is determined by the Commission after review of performance and salary comparisons through reports such as the State Auditor's Office August 2014 Report on Executive Compensation at State Agencies (Report No. 14-705) and comparable salary information of selected positions at state and federal regulatory agencies with similar responsibilities.



CREDIT UNION DEPARTMENT COMMISSIONER EVALUATION FORM FY____

Name:	
Date Employed	Date of Last Evaluation

I. 20 Commission Assessment

Average results from the Commission Assessment Tally Sheet (Part I Attached) are:

 $\frac{25\%}{\text{Average Points (Part I Average)}} X \frac{25\%}{\text{Weight}} = \frac{1}{\text{Part I Score}}$

II. 20__ Performance Objectives

Average results from the Texas Credit Union Department Performance Grid (Part II Attached) are:

X75%=Average Points (Part II Average)WeightPart II Score

III. 20 Special Projects

Average results from the Texas Credit Union Department Performance Grid (Part III Attached) are:

 Average Points (Part III Average)
 X
 0%
 =
 Part III Score

IV. Final Evaluation Score:

Final Evaluation Score

* The total of the weights must equal 100%

BASE PAY ADJUSTMENT

A base pay adjustment earned for a performance level achieved is strictly at the discretion of the Commission.

Current Base Pay: Pay Adjustment: New Base Pay: Effective Date:	%	\$ \$ \$		÷.
Additional Comments:				
Commissioner Comments:				
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				·

Commissioner Signature & Date

Evaluation Chair Signature & Date

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Part I Credit Union Department Commission Member Assessment Form

Commission Memb	er:			
	tributed to the Cred		er. Please indicate your agreen	nent or disagreemen
	Strongly Disagree 1	Agree - 23	Strongly Agree 5j	÷
	t result in achieveme		erm needs of the Department le to execute independent actio	
Comments: 2. I am satisfied with t Commissioner. This in be aware.	the level, quality and cludes issues that m	d timeliness of inforn ay arise between Cor	nation and communications pr nmission meetings of which the	ovided to me by the Commission should
Rating:				
3. The level to which subordinates. Demonstr Ensures that the most e	rates an atmosphere	of teamwork and a	the operations, activities and pility to motivate others to acc including staff.	performance of al complish their goals
Rating:				
Comments:				

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4. The Commissioner provides adequate focus on maintaining effective relationships with the governor's office, legislators and Credit Union leaders to ensure the continued safety and soundness of the credit union industry. Works well with NCUA to coordinate efforts for compliance and NASCUS for continued accreditation.				
Rating:				
Comments:	2			
The Commissioner has the technical knowledge necessary to complete the job. Has the capability to hire the cessary personnel to move the department forward to save time and money, while still ensuring the safety of the formation that is necessary to examiners to complete their assignments.				
Rating:				
Comments:				
	·. ·			
6. The Commissioner maintains a professional image at all times while representing the Department. The leadership skills are present to command attention and respect, while displaying confidence in their ability.				
Rating:	·.			
Comments:				
Other Comments on the Commissioner's performance this past period:				
SUM OF RATINGS:	<u>.</u>			
AVERAGE POINTS:				
	÷.			

II. PERFORMANCE OBJECTIVES

For each performance category, assign a rating from 1 to 5 based on the performance rating definitions described at the bottom of the form. Next, multiply the rating assigned by the weight shown and enter the result in the "weight x rating" box (i.e. 25% x 5 = 1.25).

I T I T G I I G H N H N T G T G
25%
25%
15%
25%
10%

PERFORMANCE RATINGS: The annual review will be classified in one of the following areas.

1. UNSATISFACTORY: Employee is not performing the minimum requirements of the responsibility area in a satisfactory manner. Performance meets few or none of the key goals/standards. Improved performance is required for continuation in the position.

2. BELOW REQUIREMENTS: Employee is not consistently performing all the requirements of the responsibility area. Performance is below expectations showing consistent weakness. Improved performance is necessary. Requires more than expected supervision.

3. MEETS REQUIREMENTS: Employee is performing all requirements of the responsibility area. Performance is standard, although some requirements are performed above expectations and occasionally below. Performance meets most key goals/standards. Fully competent performer.

4. **EXCEEDS REQUIREMENTS:** Employee is performing most requirements of the responsibility area consistently above expectations and significantly exceeds some requirements. Requires less supervision than expected.

 SIGNIFICANTLY EXCEEDS REQUIREMENTS: Employee is consistently performing all requirements of the responsibility area significantly above expectations. There are no weaknesses on key goals/standards. Makes significant contributions well beyond job demands.

Part II. Performance Objectives

1. Production

- Intervals between the effective dates of CU examinations shall not exceed 18 months.
- E-Time ratio shall not be less than 65% of available work time.
- 98% of reports of examination should be mailed within 21 days of last date on site.
- 100% applications submitted will be approved/denied not later than the 60th day after the date notice is published in the *Texas Register*.
- 95% of complaints will be responded to within 30 days.
- 100% of rule changes will be provided to credit unions within 60 days of adoption.
- Meet or exceed 90% of the Operating Plan's production targets within +/- 5% of the projected target.

2. Administration

- Attain and maintain at least 95% staffing level with continued.
- Participate in no less than 2 job fair events within the plan period.
- Post job vacancies within 7 days of notice of upcoming vacancy.
- Non-retirement turnover not to exceed 15% for plan period.
- Continue in the implementation and assimilation technology changes to increase efficiency.
- Conduct an annual examiner conference to ensure examiners receive adequate training to perform their duties.

3. Budgetary

- Ensure agency expenditures are necessary, prudent, and within budgetary constraints.
- Present quarterly financial statements to Commission and post on agency website
- Ensure compliance with all regulatory requirements for a SDSI agency
- Ensure revenues collected are adequate to cover expenditures and provide a cash reserve that complies with Commission policies.

4. Legislative

- Submit SDSI biennial and annual report filings in a timely manner.
- Prepare materials for the Legislature as requested or required.
- Respond timely to new legislative issues or requests for information or testimony.
- Remain active and involved at the national level on supervisory issues affecting credit unions.
- Attend at least one conference or training meeting during the plan period.
- Monitor and modify Texas Administrative Code rules as necessary.

5. Industry

- Continue to develop effective communication with credit unions and interested department stakeholders.
- Maintain an ongoing awareness of credit union risk profiles and the condition of the economy.
- Maintain continued accreditation from the National Association of State Credit Union Supervisors
- Publish a monthly newsletter for the industry
- Issue Interpretations and opinions within 30 days of request
- Share monthly accomplishment report with Commission Members
- Share periodic report as needed with Commission Members

Part III Special Projects/ Other Non-Quantifiable Objectives

Objectives	Weight	(1) Low Achievement	(2)	(3) Medium Achievement	(4)	(5) High Achievement
·		()	()	()	()	()
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COMMISSIONER'S PERFORMANCE REVIEW

The Commission's Policies Manual calls for an annual performance review of the Commissioner by an evaluation committee. The review is to be completed during the last Commission meeting of the calendar year. (The FY 2019 evaluation form was approved by the Commission during its July 12, 2019 meeting.)

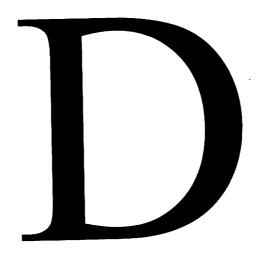
Each Commission member will be required to complete an evaluation form. After the completed forms have been submitted, the Commissioner Evaluation Committee will review the appraisals, gather any other necessary information, and prepare a proposed evaluation. The proposed evaluation will be reviewed in Executive Session and may be edited or revised by the Commission prior to presenting it to the Commissioner. The final evaluation will be presented to the Commissioner.

The performance evaluation of the Commissioner is intended to accomplish the following:

- Clarify the Commissioner's leadership and management role as viewed by the Commission.
- Maintain a harmonious working relationship between the Commission and the Commissioner.
- Assure the Commission that the Department is being effectively administered by the Commissioner.

PROPOSED PROCEDURES

- 1. Each Commission member will receive electronic copies of both the Evaluation Form and a memorandum from the Commissioner outlining the Department's FY 2019 accomplishments by **September 13, 2019.**
- 2. Each Commission member will be asked to provide the Chair of the Commissioner Evaluation Committee with a copy of their completed evaluation form by **October 11, 2019**.
- 3. The Commissioner Evaluation Committee will meet on **October 31, 2019** to gather any pertinent information and prepare a proposed evaluation.
- 4. During the Executive Session of the Commission meeting on **November 1, 2019**, the Commission will have the opportunity to review, comment on and/or revise the proposed evaluation.



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POST-PAYMENT AUDIT REPORT

D. (a) Final Post-Payment Audit Report.

BACKGROUND: On May 22, 2019 the Department received the final Post Payments Audit Report (PPAR) #469-18-01 from the Texas Comptroller of Public Accounts. The Audit covered the period from December 1, 2016 through November 30, 2017. The Department received a draft of the PPAR and its recommendations on April 15, 2019 and responded to the recommendations in May. The Commission was provided a copy of the audit on May 22, 2019 through email.

The PPAR found the Department in general compliance with the General Appropriations Act (GAA), relevant statutes and Comptroller requirements. Auditors found no issues with travel and property management records. However, the Department was asked to consider improving controls over verification of prior state service for new employees, compliance with procurement and contracting rules, system security access and expenditure processing. No recurring issues were noted from the prior post payment audit issued in August 2013.

As part of the response the Department initiated policy changes to ensure future compliance and acted to correct errors when necessary.

Results of the audit indicated internal control weaknesses that necessitated corrective action. However, part of management's recommended response includes the priority #4 strategic initiative to realign/add office staff to improve internal controls around the payment systems.

<u>RECOMMENDED ACTION:</u> See Strategic Initiative Priority #4.

Texas Comptroller of Public Accounts

May 22, 2019

Mr. John Kolhoff Commissioner Credit Union Department 914 E. Anderson Ln. Austin, Texas 78752

Dear Mr. Kolhoff:

We have completed a post-payment audit of certain payroll, purchase and travel transactions of the Credit Union Department (Department). We would like to thank you and your staff for your responsiveness and cooperation in assisting us with this audit. A draft of this audit report was sent to Deputy Commissioner Robert Etheridge on April 15, 2019. The Department's response to the draft is included in this report.

Our purpose was to determine whether the Department's expenditures complied with certain state laws and rules concerning expenditures and with the processing requirements of the Uniform Statewide Accounting System (USAS) and the Uniform Statewide Payroll/Personnel System (USPS). The Department is responsible for ensuring that its staff is knowledgeable in these areas.

We intend for this report to be used by the Department's management and certain state officials and agencies as listed in Texas Government Code, Section 403.071. However, this report is a public record and its distribution is not limited.

We noted other matters involving the processing of expenditures by the Department that we communicated to Robert Etheridge in an email dated April 15, 2019.

The Department may inquire about and register for training related to expenditures through the Fiscal Management <u>Training Center</u>.

We would like input from you or your designee on the quality of the audit process and the service the audit staff provided while conducting this audit. Please take our <u>Post-Payment Audit Survey</u> to rate and comment on the post-payment audit process. Your feedback is greatly appreciated.



Comptroller.Texas.Gov P.O. Box 13528 Austin, Texas 78711-3528 512-463-4444 Toll Free: 1-800-531-5441 ext: 3-4444 Fax: 512-463-4902 Mr. John Kolhoff May 22, 2019 Page Two

Thank you for your cooperation. If we can be of any further assistance, please contact jesse.ayala@cpa.texas.gov or 512-936-8456.

Sincerely,

Michael Apperley

Manager Statewide Fiscal Oversight Fiscal Management Division

Attachments

cc: Robert Etheridge, Deputy Commissioner, Credit Union Department Irma Rodriquez, Accountant, Credit Union Department Jesse Ayala, Auditor, Texas Comptroller of Public Accounts



An Audit of the Credit Union Department

Audit Report # 469-18-01 May 22, 2019

Glenn Hegar Texas Comptroller of Public Accounts



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Executive Summary

Purpose and Scope

The objectives of the Credit Union Department (Department) audit were to determine whether:

- Contracts were procured according to applicable state laws and Comptroller requirements.
- Payments were processed according to applicable state laws, Comptroller requirements and statewide automated system guidelines.
- Documentation to support those payments was appropriately maintained.
- Capital and high-risk assets were properly recorded.
- Appropriate security over payments was implemented.

This audit was conducted by the Texas Comptroller of Public Accounts (Comptroller's office), and covers the period from Dec. 1, 2016, through Nov. 30, 2017.

Background

The Credit Union Department is a Texas state agency with responsibility for supervising and regulating statechartered credit unions. The Department is governed by the nine-member Credit Union Commission, composed of four members from the credit union industry and five members from the general public with no direct involvement in the management of a financial institution.

Credit Union Department website

https://cud.texas.gov/

Audit Results

The Department generally complied with the General Appropriations Act (GAA), relevant statutes and Comptroller requirements. Auditors found no issues with travel and property management records. However, the Department should consider improving controls over verification of prior state service, compliance with procurement and contracting rules, system security access and expenditure processing.

The auditors noted no recurring issues from the prior post-payment audit issued in August 2013. An overview of audit results is presented in the following table.

Table Summary

Area	Audit Question	Results	Rating
Payroll Transactions	Did payroll transactions comply with all pertinent statutes and Comptroller requirements?	 Incorrect state service date entered, resulting in an overpayment of longevity for one employee. Prior state service not verified, resulting in underpayment of longevity for one employee. 	Compliant, Findings Issued
Purchase/ Procurement Transactions	Did purchase and procurement transactions comply with all pertinent statutes and Comptroller requirements?	 TIBH Industries not used to procure items available on the state contracts. DIR exemption not obtained for one transaction. 	Compliant, Findings Issued
Contract Transactions	Did contracting transactions comply with all pertinent statutes and Comptroller requirements?	 Missing CMBL for four contracts. Missing SAM search in two contracts. 	Compliant, Findings Issued
Travel Transactions	Did travel transactions comply with all pertinent statutes and Comptroller requirements?	No issues	Fully Compliant
Internal Control Structure	Are duties segregated to the extent possible to help prevent errors or detect them in a timely manner and help prevent fraud?	One employee can process and release payroll without oversight.	Compliant, Findings Issued
<u>Security</u>	Did all system access to process payments comply with all the Comptroller security guidelines?	 One CTIA form was signed after the individual had access to the Comptroller's statewide financial systems. The Department failed to timely submit a request to remove a terminated employee's security in USAS. 	Compliant, Findings Issued

Area	Audit Question	Results	Rating
Fixed Assets	Were tested assets in their intended location and properly reported in the State Property Accounting System?	No issues	Fully Compliant
argeted Analysis	Did the Department comply with the federal and Comptroller requirements for direct deposit?	Two missing Direct Deposit Authorization forms.	Compliant, Findings Issued

Key Recommendations

Auditors made several recommendations to help mitigate risk arising from control weaknesses. Key recommendations include:

- The Department must ensure all prior state service verifications are performed, documented, accurate and maintained in the personnel files.
- The Department must ensure WorkQuest (formerly TIBH Industries) is used to procure items that are on the state contract.
- The Department must obtain and maintain applicable procurement exemptions as required by the <u>State of Texas Procurement and Contract Management Guide</u> – Centralized Master Bidders List (CMBL) section.
- The Department must perform and document procurement searches required by the <u>State of Texas Procurement and Contract Management Guide</u> such as the CMBL and System for Award Management (SAM) searches.
- The Department must separate each task to the extent possible to ensure that no individual is able to process payments without another person's involvement.
- The Department must ensure that Direct Deposit Authorization forms are not processed if the International Payments Verification section is left blank or if the form is unsigned.
- The Department must ensure each employee signs a Confidential Treatment of Information Acknowledgement (CTIA) form before accessing the Comptroller's statewide financial systems.
- The Department must comply with the requirements for terminating employees' security revocation.



Detailed Findings

Payroll Transactions

Auditors developed a representative sample of the Department's 15 employees (41 payroll transactions) totaling \$127,215.77 to ensure the Department complied with the GAA, relevant statutes and Comptroller requirements. Audit tests revealed the following exceptions in payroll transactions.

Incorrect State Effective Service Date/Incorrect Longevity Payment

Auditors identified one employee from the payroll sample who had incorrect state service dates entered in Uniform Statewide Payroll/Personnel System (USPS) resulting in an overall overpayment in longevity pay.

The Department's procedures require verification of prior state service when an employee indicates previous state employment. The Department verified the prior state service when the employee was hired; however, the start date of a previous state employment was incorrectly entered in USPS, causing the system to miscalculate lifetime service credit for the employee. The incorrect service dates resulted in overpayments for longevity pay totaling \$280. The Department explained this was due to oversight.

When an agency hires an employee, the agency must research whether the employee has previous state employment. If prior state employment exists, the agency must confirm and properly record the amount of lifetime service credit. See <u>Texas Payroll/</u> <u>Personnel Resource – Non-Salary Payments – Longevity Pay</u>.

Auditors provided the Department with the schedule and calculation of the overpayment during fieldwork. This is not included with the report due to confidentiality issues.

Recommendation/Requirement

Auditors recommend the Department review its controls and personnel records to ensure accuracy and completeness, as well as guarantee that its internal operating procedures include quality control measures to detect and prevent incorrect compensation. See <u>34</u>. <u>Texas Administrative Code Section 5.40(c)</u>. The Department should consider recovering the overpayment in accordance with <u>Texas Government Code, Chapter 666</u>, unless it determines it is not cost effective to do so.





Department Response

Erroneous payments relative to the specific case have been recovered. A new staff services officer (SSO) has been named by the department and is in training. Eventual certification of the SSO has been established as a requirement.

Internal operating procedure 201 has been updated to ensure appropriate documentation is obtained from each employee on the start date and verified using the State of Texas Employment History Application. Additional training opportunities have also been provided to the SSO to ensure appropriate information is obtained.

Comptroller Response

Due to potentially inaccurate or incomplete information provided by the application, agencies and institutions must still verify employment history with the previous employing agency or institution, or its successor if abolished, to confirm prior state employment for purposes of state entitlements including longevity pay, hazardous duty pay and leave accruals.

Missing Prior State Service Verification/Incorrect Longevity Payment

In a report generated outside of the sample, auditors identified one employee missing prior state service verification. The employee listed prior state service on the job application and the Department's employment history form. The Department did not have documentation to show prior state service verification was conducted when the employee was hired, resulting in longevity underpayment of \$780.

During the audit, the Department conducted the prior state service verification for the employee in our sample, provided the auditor with the required documentation to validate the longevity pay amounts, updated USPS for the employee, and compensated the employee for the underpayment.

When an agency hires an employee, the agency must research and document whether the employee has prior state service. See <u>Texas Payroll/Personnel Resource – General</u> <u>Provisions – Required Documentation</u>. If there is prior state employment, the agency must confirm and properly record the amound of lifetime service credit.

If the agency fails to verify an employee's prior state service, the lifetime service credit for longevity will be based on the employment date at the new agency and the eligible employee might be underpaid longevity pay. See <u>Texas Payroll/Personnel Resource –</u> <u>Non-Salary Payments – Longevity Pay</u>.





Auditors recommend the Department continue to research and verify prior state service time for its employees. In addition, the Department must ensure all prior state service verifications are properly documented, accurate and maintained in the personnel files.

Department Response

The error was corrected with appropriate payments made by the department. A new SSO has been named by the department and is in training. Eventual certification of the SSO has been established as a requirement.

Internal operating procedure 201 has been updated to ensure appropriate documentation is obtained from each employee at the start date and verified using the State of Texas Employment History Application. Additional training opportunities have also been identified and will be provided to the newly appointed SSO to ensure appropriate information is obtained.

Comptroller Response

Due to potentially inaccurate or incomplete information provided by the application, agencies and institutions must still verify employment history with the previous employing agency or institution, or its successor if abolished, to confirm prior state employment for purposes of state entitlements including longevity pay, hazardous duty pay and leave accruals.

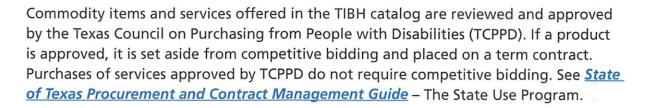
Purchase/Procurement Transactions

Auditors developed a representative sample of 20 purchase/procurement transactions totaling \$162,849.12 and also audited eight transactions in a report outside the sample to ensure the Department complied with the GAA, <u>eXpendit (FPP I.005)</u>, the <u>State of</u> <u>Texas Procurement and Contract Management Guide</u> and pertinent statutes. Audit tests revealed the following exceptions in purchase transactions.

TIBH Industries Contract Not Used

In a report generated outside the sample, auditors identified one transaction totaling \$313.76 where the Department failed to use the TIBH Industries (now WorkQuest) catalogs to procure items that were on the state contracts. Auditors could not identify any documentation to support using another vendor for this purchase. The Department stated that it did not purchase the items from TIBH because of an oversight.





Recommendation/Requirement

The Department must ensure that the set-aside contracts for goods and services offered by WorkQuest receive priority over open-market purchases, and that the proper reports are filed showing all delegated purchases made as exceptions to the set-aside contracts.

Department Response

Procedure 301 has been updated to highlight requirements to ensure current state contractor options are exhausted prior to reaching out to external vendors. Additional training is being provided to the newly appointed procurement officer to ensure thorough and complete understanding of Texas state purchasing requirements.

Missing Department of Information Resources (DIR) Exemption

Auditors identified one purchase transaction totaling \$4,495.61 for a unique IT good not available through a DIR term contract, for which the Department could not show it had obtained an exemption from DIR. See <u>State of Texas Procurement and</u> <u>Contract Management Guide</u> – Exemptions and Exclusions. The Department indicated documentation was either misplaced or lost.

Texas Government Code, Chapter 2157, requires state agencies to purchase hardware and/or software goods, as well as technical services, through DIR cooperative contracts. Both Texas Government Code, Section 2157.068, and <u>1 Texas Administrative Code</u>, Section 204.12, state that if a product or service is not available via an existing DIR purchasing program, a state agency can opt to use a different vendor as a secondary source. The agency must obtain a one-time exemption request from DIR that includes a maximum expense value that must be met. See <u>State of Texas Procurement and Contract</u> <u>Management Guide</u> – Exemptions and Exclusions.

Contracts must be retained for seven years after their expiration or termination. See <u>Texas Government Code, Section 441.1855</u> and the <u>State of Texas Procurement and</u> <u>Contract Management Guide</u> – Records Retention Section.





The Department must follow the procedures outlined in the state's procurement guide for IT goods or services. The Department must obtain an exemption-request authorization from DIR and include it in the procurement documentation file every time IT goods or services are purchased from a source other than DIR cooperative contracts.

Department Response

Procurement of the closed system intercom/video system for the entrances was erroneously determined to be outside of DIR procurement requirements. Additional staff training has been conducted and procurement procedures have been updated to require exhaustion of state contracted vendors and retention of documentation to support external vendor choices when state contractor service is not available. The department is establishing an additional position to ensure appropriate quality control reviews are conducted on adherence to procurement procedures and policies.

Contract Transactions

Two contracts totaling \$24,778.05 and \$10,000 respectively were selected for this audit. All phases of contract development, planning, solicitation, award, payments and monitoring were reviewed for compliance with the <u>State of Texas Procurement and</u> <u>Contract Management Guide</u>, pertinent statutes and best practices. Audit tests revealed the following exceptions in the procurement process.

Missing Central Master Bidders List Solicitation (CMBL)

The Department did not perform a CMBL search of all eligible suppliers for two contracts before awarding them for the amount of \$34,778.05. The Department stated it was an oversight that the CMBL search and profile printout of all eligible suppliers was not conducted before awarding the contracts.

The CMBL is a database of registered vendors who have provided contact information and a list of the goods and services they offer. Unless exempted by law, the CMBL must be used for all procurements subject to the authority of the Statewide Procurement Division. The CMBL must also be used to gather information for noncompetitive procurement processes and vendor performance data.

Agencies must print out the awarded vendor's CMBL profile showing the expiration date for file documentation. See <u>State of Texas Procurement and Contract Management</u> <u>Guide</u> – Centralized Master Bidders List section. Agencies must retain proof that they checked the CMBL system before awarding or renewing a contract. See <u>Texas</u> <u>Government Code, Sections 2155.263- 2155.264</u> and <u>34 Texas Administrative Code</u> <u>Section 20.107(g)</u>.



Recommendation/Requirement

The Department must use the CMBL for all purchases, including services for which competitive bidding or competitive sealed proposals are required. A copy of the CMBL search results from the specified website must be included in the contract file as evidence of the vendor search.

Department Response

Procurement procedure 300 has been updated to require retention of documentation to support all bid processes that are conducted in accordance with Texas procurement rules. Additional training has been made available to ensure staff's understanding of the required processes.

The department is establishing an additional position to ensure appropriate quality control reviews are conducted on adherence to procurement procedures and policies.

Missing System for Award Management (SAM) Check

Auditors identified two contracts where the Department was unable to provide required SAM printouts dated before the respective contract awards. The Department indicated documentation was either misplaced or lost.

The agency must check the SAM database to verify that the vendor is not excluded from grant or contract participation at the federal level. A contract cannot be awarded to a vendor named on the U.S. Treasury Department, Office of Foreign Assets Control's master list of Specially Designated Nationals and Blocked Persons (with limited exceptions set forth in the executive order). See <u>State of Texas Procurement and</u> <u>Contract Management Guide</u> – System for Award Management (SAM) and <u>State of Texas Procurement and Contract Management Guide</u>.

Recommendation/Requirement

The Department must conduct a vendor contract verification search before any purchase, contract award, extension or renewal. A final check of the Specially Designated Nationals and Blocked Persons list must be made before any contract award to ensure the Department does not award contracts to any person or vendor whose name appears on the list. A dated copy of the results from the SAM database must be retained as evidence and it must be included in the procurement file.

Department Response

Additional training is being provided to ensure staff's understanding of the bid process, including the importance of the SAM check.

The department is establishing an additional position to ensure appropriate quality control reviews are conducted on adherence to procurement procedures and policies.



Travel Transactions

Auditors developed a representative sample of 25 travel transactions totaling \$12,888.71 to ensure that the Department complied with the GAA, relevant statutes and Comptroller requirements. Audit tests revealed no exceptions in these transactions.

Internal Control Structure

Auditors reviewed the Department's employees' access to various Comptroller systems to determine if any individuals had multiple security abilities allowing the employees to process payments through the systems without oversight by another individual. Audit tests revealed the following exception.

Controls Weakness over Expenditure Processing

As part of the planning process for the post-payment audit, auditors reviewed certain limitations the Department placed on its accounting staff's ability to process expenditures. Auditors reviewed the Department's signature cards and security for USPS, the Uniform Statewide Accounting System (USAS) and the Texas Identification Number System (TINS). Auditors did not review or test any internal or compensating controls that the agency may have relating to security or internal transaction approvals in USAS, USPS or TINS.

Auditors identified one employee who could process and release payroll without oversight. As a result of the audit, the Department stated that the issue has been corrected and now the employee can only release payroll.

Recommendation/Requirement

The Department must work with Comptroller's office Statewide Fiscal Systems security staff to set up user profiles that separate the entry and approval of payroll transactions in USPS.

Department Response

The issues were corrected during the audit review under the old USPS system. The Department then converted to the CAPPS HR/Payroll system in July 2018. Now no individual departmental employee is able to both process and release payroll transactions.

The department is establishing an additional position to ensure appropriate quality control reviews are conducted on adherence to procurement procedures and policies.



Security

Auditors conducted a security review to identify any of the Department's employees with security in USAS, or on the voucher signature cards, who were no longer employed or whose security had been revoked. Upon termination or revocation, certain deadlines must be observed so that security can be revoked in a timely manner. Audit tests revealed the following exceptions.

Missing Confidential Treatment Information Acknowledgment Form (CTIA)

Auditors reviewed the Department's compliance with the requirement that all users of the Comptroller's statewide financial systems complete a CTIA form. When a new user needs access to the Comptroller's statewide financial systems, the agency's security coordinator has the new user read and sign the CTIA form and keeps the form on file for as long as the user has access to the systems, plus five years. Auditors identified one CTIA form signed 134 days after the individual had access to the Comptroller's statewide financial systems. The Department stated procedures were not followed and the CTIA form was not executed on the same day as the access date.

Recommendation/Requirement

The Department should improve its processes to ensure that employees sign the CTIA forms before obtaining access to the Comptroller's statewide financial systems.

Department Response

A new SSO has been appointed and is being trained. Additional training has been provided to ensure staff members with access to the Texas state systems provide all required documentation prior to account access.

Failure to Request Security Access Removal

During the audit period, the Department failed to submit a request to remove one employee's USAS security access on or before the effective date of the employee's termination. The request to remove the employee from the signature card was sent 111 days late. This could have permitted the employee to approve any vouchers that the Department submitted to the Comptroller through USAS after the employee's authority expired. Any payment approved by an employee whose security has been revoked would have constituted an unapproved expenditure. Auditors ran a report and determined that no unapproved documents were processed during the audit period.



The lack of timely notification meant this employee retained USAS security for 111 days after revocation. When an employee's authority to approve an agency's expenditures is revoked for any reason, the employee's security profile must be changed no later than the effective date of the revocation or termination to prevent the employee from executing electronic approvals for the agency. See <u>34 Texas Administrative Code Section</u> <u>5.61(k)(5)(A)-(B)</u>.

The Department has procedures to notify the security coordinator of personnel actions. In these instances, the request to remove the employees' security was delayed due to the Department's oversight.

Recommendation/Requirement

The Department must ensure compliance with the requirements for terminated employees. It must also ensure that the person responsible for sending revocation notifications to the Comptroller's office is aware of any terminations on or before the dates the revocations become effective, and will follow up with the Comptroller's office to ensure receipt of the notification, and that the revocation occurred.

Department Response

Department procedure 290 has been updated and includes a checklist to ensure all employee access to either department or statewide systems is terminated appropriately.

Fixed Assets

Auditors reviewed a limited number of fixed assets acquired by expenditures during the audit period to test for proper tracking in the Department's internal system. All assets tested were in their intended location, properly tagged and recorded in the State Property Accounting system.

Targeted Analysis

Auditors conducted a review of the Department's procedures to comply with the federal mandate to properly identify and handle payments involving the movement of funds internationally.

Missing Direct Deposit Authorization Form

Of the 10 employees selected and reviewed, two employees' Direct Deposit Authorization forms were missing. Without current and properly completed forms on file, the Department is unable to follow the direct deposit requirements.



The Office of Foreign Assets Control (OFAC) requires that all direct deposit payments transmitted outside the United States be identified and monitored. To avoid potential federal penalties, each state agency must:

- Show due diligence in the processing of all direct deposit payments.
- When possible, ensure direct deposit payments it issues to accounts at U.S. financial institutions are not ultimately being transferred to financial institutions outside of the United States.

International Automated Clearing House transactions (IATs) are payments destined for a financial institution outside of the United States. The Comptroller's office does not participate in IATs. If a payee informs an agency that a payment is destined for a financial institution outside of the United States, then the agency may not set up that payee for direct deposit.

According to the Department, failing to provide the Direct Deposit Authorization forms was an oversight. As a result of the audit, the Department had the two employees with missing forms complete the forms.

Recommendation/Requirement

The Department must ensure that all payees requesting payment by direct deposit submit a completed Direct Deposit Authorization form with the IAT question answered. A Direct Deposit Authorization form should not be processed if the IAT section is left blank or if the form is unsigned.

Department Response

Department procedure 201 has been updated to ensure the Direct Deposit Authorization forms are collected on the first day of employment and to verify the IAT section is completed and the form is signed. Additional training has been provided to responsible staff to ensure an understanding of the importance of the required documentation. Transition to the CAPPS HR/Payroll system utilizes employee-initiated updates of direct deposit authorization, eliminating some concerns in this area.



Appendices

Appendix 1 — Objectives, Scope, Methodology, Authority and Team

Audit Objectives

The objectives of this audit were to:

- Ensure payments are documented so a proper audit can be conducted.
- Ensure payment vouchers are processed according to the requirements of any of the following:
 - Uniform Statewide Accounting System (USAS),
 - The Uniform Statewide Payroll/Personnel System (USPS),
 - The Standardized Payroll/Personnel Report System (SPRS),
 - The Human Resource Information System (HRIS) or
 - The Centralized Accounting and Payroll/Personnel System (CAPPS).
- Verify payments are made in accordance with certain applicable state laws.
- Verify assets are in their intended locations.
- Verify assets are properly recorded for agencies and institutions of higher education that use the State Property Accounting (SPA) system.
- Verify voucher signature cards and systems security during the audit period are consistent with applicable laws, rules and other requirements.

Audit Scope

Auditors reviewed a sample of the Credit Union Department's (Department) payroll, purchase and travel transactions that processed through USAS and USPS during the period from Dec. 1, 2016, through Nov. 30, 2017, to determine compliance with applicable state laws.

Texas law requires the Texas Comptroller of Public Accounts (Comptroller's office) to audit claims submitted for payment through the Comptroller's office. All payment transactions are subject to audit regardless of amount or materiality.

The Department receives appendices with the full report, including a list of the identified errors. Copies

of the appendices may be requested through a **<u>Public Information Act</u>** inquiry.

The audit provides a reasonable basis for the findings set forth in this report. The Department should implement the recommendations listed in the Detailed Findings of this report. It is the Department's responsibility to seek refunds for all overpayments unless it determines it is not cost effective to do so. If necessary, the Comptroller's office may take the actions set forth in Texas Government Code, Section 403.071(h), to ensure that the Department's documents comply in the future. The Department must ensure that the findings discussed in this report are resolved.



Audit Methodology

The Expenditure Audit section uses limited sampling to conduct a post-payment audit.

Fieldwork

Each auditor in the Expenditure Audit section approaches each audit with an appropriate level of professional skepticism based upon the results of the initial planning procedures.

If an auditor suspects during an audit that fraud, defalcation or intentional misstatement of the facts has occurred, the auditor will meet with his or her supervisor, the Statewide Fiscal Oversight manager, or both, to decide what action or additional procedures would be appropriate.

Audit Authority

State law prohibits the Comptroller's office from paying a claim against a state agency unless the Comptroller's office audits the corresponding voucher.

• Texas Government Code, Sections 403.071(a), 403.078, 2103.004(a)(3).

State law allows the Comptroller's office to audit a payment voucher before or after the Comptroller's office makes a payment in response to that voucher.

• Texas Government Code, Section 403.071(g)-(h).

In addition, state law authorizes the Comptroller's office to conduct pre-payment or post-payment audits on a sample basis.

• Texas Government Code, Sections 403.011(a)(13), 403.079, 2155.324.

Audit Team

Jesse Ayala, Lead Auditor Melissa Hernandez, CTCM, CTPM Amanda Price, CFE, CTCD



Appendix 2 — Definition of Ratings

Compliance Areas

Definition	Rating
Agency complied with applicable state requirements and no significant control issues existed.	Fully Compliant
Agency generally complied with applicable state requirements; however, control issues existed that impact the agency's compliance, or minor compliance issues existed.	Compliant, Findings Issued
Agency failed to comply with applicable state requirements.	Noncompliant

Internal Control Structure/Security Areas

Definition	Rating
Agency maintained effective controls over payments.	Fully Compliant
Agency generally maintained effective controls over payments; however, some controls were ineffective or not implemented.	Control Weakness Issues Exist
These issues are unlikely to interfere with preventing, detecting, or correcting errors or mitigating fraudulent transactions.	Control Weakness issues Exist
Agency failed to effectively create or implement controls over payments.	Noncompliant

Repeat Finding Icon Definition

2

This issue was identified during the previous post-payment audit of the agency.

DEPARTMENT'S FY 2019 BUDGET AND FINANCIAL PERFORMANCE

D. (b) Discussion and Consideration of the Department's FY 2019 Budget and Financial Performance.

BACKGROUND: In March 2016, the Commission adopted a Strategic Plan for Fiscal Years 2017-2021. The \$4.2 million FY 2019 Budget, approved by the Commission in July 2018, includes the maintenance and operation budget and capital improvement budget in support of the second year of the Strategic Plan.

The following report highlights the Department's financial performance for the nine-month period ending May 31, 2019.

The financial report is unaudited and is prepared on a cash basis of accounting. As required, most expenditures are expensed 30 day after the invoice due date.

<u>RECOMMENDED ACTION:</u> No action is anticipated.

Credit Union Department BY 2019 Budget Analysis For the Period Ended 5/31/19

10 M C ().	5140040	DV 00 10 VTD			Percent of
	BY 2019	BY 2019 YTD	BY 2019 YTD	Over (Under)	YTD
	Budget	Budgeted	Actual	Budget	Budget
REVENUES:					1.1
Operating Income					
Operating Fees	\$4,201,909	\$4,201,909	\$4,046,425	(\$155,484)	96%
Out-of-State Branch Fees	\$9,000	\$9,000	\$9,500	\$500	106%
Examination Fees	\$0	\$0	\$0	\$0	
Application Fees	\$0	\$0	\$0	\$0	
Penalties	\$0	\$0	\$1,587	\$1,587	
Other	\$0	\$0	\$0	\$0	
Operating Income Subtotal	\$4,210,909	\$4,210,909	\$4,057,512	(\$153,397)	96%
Interest Income (Trust Acct #2972) Refunds			\$7,514	\$7,514	
TOTAL REVENUES	\$4,210,909	\$4,210,909	\$4,065,026	(\$145,883)	97%
Encumbrance from BY 18	\$50,000	\$50,000	\$50,000	\$0	100%
Excess from Reserve Account	\$00,000	\$00,000	\$139,209	\$139,209	1007
Excess from Reserve Account			\$139,209	\$139,209	5.
TOTAL FUNDS AVAILABLE TO					
COVER EXPENDITURES	\$4,260,909	\$4,260,909	\$4,254,235	(\$6,674)	100%

Personnel Expenses: Salaries and Wages	\$2,621,239	\$1,938,258	\$1,814,521	\$123,738	94%
Employee Benefits	\$821,630	\$617,084	\$543,576	\$73,507	88%
Total Personnel Expenses	\$3,442,869	\$2,555,342	\$2,358,097	\$197,245	92%
Travel Expenses:					
In State					100%
Examinations			\$302,251	~	
Training/Conferences	2		\$1,436		
Meetings			\$7,460		
Public Forums			\$0		
Other			\$5,111	1	
Total In-State	\$425,847	\$320,384	\$316,258	\$4,125	99%
Out-of-State	\$10,000	\$8,328	\$8,120	\$208	.97%
Commission	\$11,000	\$7,858	\$9,335	(\$1,477)	119%
Total Travel Expenses	\$446,847	\$336,570	\$333,713	\$2,856	99%
Other Operating Expenses:		100			
Communication/Utilities	\$51,028	\$34,021	\$31,486	\$2,535	93%
Professional Services/Fees	\$176,840	\$128,362	\$53,926	\$74,436	42%
Supplies/Materials	\$51,370	\$25,678	\$13,017	\$12,660	51%
Printing and Reproduction	\$2,855	\$2,142	\$1,663	\$479	78%
Repairs/Maintenance	\$2,800	\$2,101	\$2,811	(\$710)	134%
Rentals and Leases	\$7,250	\$5,873	\$5,594	\$279	95%
Other Operating	\$79,050	\$38,022	\$38,385	(\$363)	101%
Total Other Operating Expenses	\$371,193	\$236,199	\$146,883	\$89,317	62%
OTAL EXPENDITURES	\$4,260,909	\$3,128,111	\$2,838,693	\$289,418	91%
REMAINING FUNDS TO COVER					
XPENDITURES			\$1,422,216		

FINANCIAL CONDITION

D. (c) Discussion of the Financial Condition of the State Credit Union System.

BACKGROUND: The operating environment for Texas credit unions continues to be sound due to the strong economy in Texas. The Texas economy is in its ninth year of business cycle expansion, with crude oil prices trending upward, payroll employment growing steadily and unemployment at historically low levels. The record-low unemployment rate in Texas remains at 3.7 percent with three of the four major metropolitans in Texas below the state average. Austin has the lowest unemployment rate at 2.9 percent, followed by San Antonio at 3.2 percent. Despite pronounced labor shortages in the major metro areas, wages in Texas have declined over last year. Despite Austin paying the highest wages of the major Texas cities, it posted a 2.6 percent year over year inflation adjusted decline, the largest decline of the major metros.

Tariffs imposed and threatened by the President are estimated to cost credit unions 7.5 percent of the new auto loans they had expected to originate this year. The tariffs will increase the price of a new car an average of \$2,750 according to an Economic Update released by the Credit Union National Association in mid-June 2019. This could result in credit unions across the nation losing approximately 300,000 in new auto loan originations over the next two years.

Texas credit unions continue to perform well, and our industry is strong. Growth trends have been effectively managed and credit unions are experiencing moderate loan and deposit growth, sound earnings and Trends since year-end 2016 indicate increasing net worth positions. increases in the credit unions' net income levels have been driven primarily by higher investment yields and controlled operating expenses, as well as significant reductions in provision for loan and lease losses (PLLL) costs. The reduction in PLLL costs are attributable to reduced loan delinquencies and stable loan charge-off levels. Reportable loan delinquencies for Texas credit unions declined to 0.56 percent of total loans outstanding as of March 31, 2019 and are below year-end delinquency levels for the previous five The improvement in asset quality trends should indicate a vears. continuation of sound financial performance for our industry over the shortterm, and hopefully beyond. Regardless of the strong financial performance recognized by Texas credit unions for the last several years, increases in costs associated with new technologies, cybersecurity and maintaining regulatory compliance will continue to create challenges for credit unions.

Thus, improving operational efficiency and identifying new revenue streams will be crucial elements to the future financial performance of the Texas system.

AGGREGATE INDUSTRY STATUS: At March 31, 2019, there were 181 state-chartered credit unions in Texas. Assets in these credit unions totaled \$43.28 billion, which is an increase of \$2.06 billion since March 31, 2018, for an annualized growth rate of 5.0%. The average net worth ratio is 10.69%, up from 10.33% at March 31, 2018.

Loans at Texas chartered credit unions totaled \$31.73 billion as of March 31, 2019. This is an increase of \$1.67 billion since March 31, 2018 for an annualized growth rate of 5.56%.

Shares at Texas chartered credit unions totaled \$37.17 billion as of March 31, 2019. This is an increase of \$1.38 billion, or 3.86% since March 31, 2018.

Texas chartered credit unions average loan delinquency ratio was 0.56% as of March 31, 2019, compared to a ratio of 0.65% as of March 31, 2018.

At March 31, 2019, 28 state-chartered credit union reported year to date net operating losses of \$1.05 million; while the remaining 153 credit unions reported aggregate net income of \$94.11 million. A breakdown of credit unions with positive earnings performance, by asset category, is as follows:

Assets Size	# of CUs	# Profitable	%	% Profitable
			Profitable	(12 mos. ago)
\$1 Billion and Over	11	10	91%	100%
\$500 to \$999.9 Million	14	13	93%	100%
\$250 to \$499.9 Million	15	15	100%	100%
\$100 to \$249.9 Million	23	22	96%	95%
\$50 to \$99.9 Million	23	22	96%	85%
\$10 to \$49.9 Million	57	46	81%	76%
Under \$10 Million	38	25	66%	56%
Totals	181	153	85%	80%

PROBLEM INSTITUTIONS: As of May 31, 2019, there were 20 credit unions assigned a CAMEL rating of 3 or higher, compared to 26 credit unions at May 31, 2018. Credit unions in this category are monitored through a combination of off-site monitoring, regular on-site contacts, and ongoing reviews for compliance with outstanding Documents of Resolution and other supervisory agreements or orders.

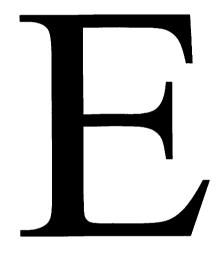
ENFORCEMENT ISSUES: As of May 31, 2019, the Department had the following administrative sanctions outstanding:

Dividend Restrictions	0
LUAs	0
Determination Letters	1
Conservatorships	0
Cease and Desist	1

Chartering Activity

New Charters 0

RECOMMENDED ACTION: No formal action is anticipated.



NEW MATTERS

Thirteen (13) new items are being presented to the Commission for its consideration and possible action. Specifically, the Commission will have:

- a. Department's Operating Plan and Budget for Fiscal Year 2020.
- b. Proposed Amendments to 7 TAC Section 91.101 Concerning Definitions and Interpretations.
- c. Adoption of the Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter H (relating to investments), Sections 91.801, 91.802, 91.803, 91.804, 91.805 and 91.808, and readoption of rules.
- d. Proposed Amendments to 7 TAC Section 91.801 Concerning Investments in Credit Union Service Organizations.
- e. Proposed Amendments to 7 TAC Section 91.803 Concerning Investment Limits and Prohibitions.
- f. Adoption of the Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter I (relating to Reserves and Dividends), Sections 91.901 and 91.902, and readoption of rules.
- g. Proposed Amendments to 7 TAC Section 91.901 Concerning Reserve Requirements.
- h. Proposed Amendments to 7 TAC Section 91.1003 Concerning Mergers/Consolidations.
- i. Legislative Issues and Activities Relating to the 86th Regular Session that may impact the Department.
- j. Resolution of Appreciation for Retiring Field Supervisor Cary L. Cabe.
- k. Status of the Department's Sunset Review.
- 1. Cybernance Request to Commission Study
- m. Confirm Date for Next Commission Meeting (November 1, 2019).

DEPARTMENT'S OPERATING PLAN AND BUDGET FOR FY 2020

E. (a) Approve the Department's Operating Plan and Budget for Fiscal Year 2020.

BACKGROUND: Consistent with the Budget Assumptions approved by the Commission, the following pages detail a proposed budget for FY 2020 of \$4,485,694 which represents a 5.3% increase from the FY 2019 budget. Removing the impact of the budgeted Sunset review expense the budget increase would fall to 2.9%. The proposed budget includes additional funding for the associated costs related to a performance-based merit increase program (\$102,339) funding for the NCUA Laptop rollover (\$22,000); increased examiner training and travel related costs. The Replacement/Capital improvement plan includes additional funding to maintain the Secure Data Portal and improve the functionality of the Departments management information systems.

RECOMMENDED ACTION: The Department recommends that the Commission approve the proposed FY 2020 Operating Plan and Budget.

RECOMMENDED MOTION: I move that the Commission approve the proposed FY 2020 Operating Plan and Budget, with a total budget of \$4,485,694 and 29.5 FTEs.

NEW MATTERS

Thirteen (13) new items are being presented to the Commission for its consideration and possible action. Specifically, the Commission will have:

- a. Department's Operating Plan and Budget for Fiscal Year 2020.
- b. Proposed Amendments to 7 TAC Section 91.101 Concerning Definitions and Interpretations.
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- i. Legislative Issues and Activities Relating to the 86th Regular Session that may impact the Department.
- j. Resolution of Appreciation for Retiring Field Supervisor Cary L. Cabe.
- k. Status of the Department's Sunset Review.
- 1. Cybernance Request to Commission Study
- m. Confirm Date for Next Commission Meeting (November 1, 2019).

BUDGET ASSUMPTIONS FOR BUDGET YEAR 2020

The following broad assumptions will establish the foundation for the development of the Department's Budget Year (BY) 2020 budget and provide a framework to staff and the Commission for setting priorities, determining service levels, and allocating limited financial resources.

- Balance Budget In accordance with Commission policy, the budget will be balanced using BY 2019 ending reserve balance funds in excess of the aggregate contingency reserves limit.
- 2. Contractual Obligations The Department intends to meet all contractual obligations. Purchase orders or contracts which were placed and committed prior to the end of Fiscal Year (FY) 2019 for which the requested services performed until after the start of FY 2020 are considered obligated funds. The budget authority for these obligated funds will automatically be carried over to BY 2020 and the BY 2020 budget will be increased by an amount exactly equal to the obligated amount.
- 3. **Compliance** The budget shall provide sufficient funding to continue compliance with all applicable statutes, governmental requirements, administrative rules, and Department policy in regulating and supervising the safety and soundness of credit unions.
- 4. **Strategic Plan Initiatives** Consistent with the FY 2019-2023 strategic plan, the budget will provide appropriate funding to implement the delineated initiatives for FY 2020.
- 5. Salary and Benefits The expenditures for FY 2020 will be based on authorized and existing positions as of August 31, 2019 and include any scheduled salary increases/promotions prescribed in the Salary Administration Plan for Examination Staff. Filled positions will be budgeted at the actual salary for the individual in that position and vacant positions will be budgeted at the mid-point of the salary range for the positions. Employee Benefits will be automatically calculated on all salaries with the appropriate benefit rates established for state agencies. The Department will also monitor legislative initiatives which could result in required legislative pay increases for State of Texas employees.
- 6. Merit Increases To foster, support, and reward outstanding performance and to retain key high performing staff, aggregate merit increase awards for staff are estimated at an amount equivalent to 3.5% of the total salaries for those positions and will be awarded based on the established merit pay tiers. The corresponding increase in Employee Benefits, resulting from the proposed merit awards, will also be properly reflected in the budget.

- 7. **Retiree Insurance Cost** Retiree Insurance Cost are a result of staff retiring from the Department. Changes in retiree insurance cost are anticipated to be allowable budget adjustments.
- 8. Inflation Factor No inflationary increases are anticipated, except for increases in the cost of utilities and in state staff travel.
- 9. Statewide Indirect Cost Statewide indirect cost allocations are a result of a statewide plan established by the Comptroller of Public Accounts. Changes in indirect cost allocations are anticipated to be allowable budget adjustments.
- 10.Out-of-State Travel Out of state travel related to examinations, conferences, training, or other authorized purposes will not exceed \$10,000. Travel for NASCUS and FBIIC related meetings for the Commissioner will not exceed \$20,000.
- 11. Database Platform The budget may include funding determined necessary for additional hardware, software and maintenance costs associated with the ongoing usage of the Department's new database platform which is replacing our prior Sage/Act! Database.
- 12. Electronic Document Management System (EDMS) The budget shall provide for the costs associated with the further development and maintenance of our EDMS.
- 13.**Information Technology** The budget shall provide sufficient funding for computer network upgrades and computer equipment replacement in accordance with the Information Resources Strategic Plan.
- 14.**Improvements** The budget shall provide sufficient funding for scheduled maintenance and repairs in accordance with the Replacement/Capital Improvement Plan.
- 15.NASCUS Dues The budget shall provide sufficient funding to accommodate the projected increase in the professional association's dues.
- 16.Accreditation Fees The budget shall provide sufficient funding to accommodate the fees associated with the Department's continued NASCUS accreditation.
- 17. Overnight Travel Stipend The budget shall provide sufficient funding to pay examiners an overnight travel stipend in accordance with the qualifying conditions included in the Department's policy. The stipend will not be considered a one-time merit award and may be paid to the eligible examiners regardless of their last merit pay or promotion action.
- 18. Examiners' Laptops and Support During FY 2018, NCUA leased laptops to the Department for a period of three years. In contrast to prior laptop leases where NCUA provided full hardware and software support, they are now providing only limited software support and no hardware support for the leased laptops. Furthermore, NCUA has indicated they will no longer provide laptops to state agencies after the expiration of the current three-year lease. The Department intends to replace all laptops for field staff with a phased-in approach during FY 2020 and FY 2021, prior

to the expiration of the lease period with the NCUA. The budget shall provide funding for the first phase of laptop replacements (nine to ten laptops) and any additional costs associated with procuring all software licensing, security and support for the new machines.

SUMMARY OF PROPOSED FY 2020 BUDGET

Budget Needed to Continue Existing Services	\$4,181,355
<u>Sunset:</u> Sunset Review (every 12 years)	\$100,000
Strategic Initiatives:Priority #1 – Laptop Refresh\$Priority #2 – Merit Increase Funding Pool\$Priority #4 – Realign/Add Office Staffing\$Priority #5 – Increase Examiner Training\$Priority #6 – Examiner Travel Costs\$Total Strategic Initiatives\$Replacement/Capital Improvement Plan:\$Priority #3 – Secure Data Portal Upgrade\$Priority #7 – SAGE/ACT Database Conv.\$	102,339 0 10,000 20,000 \$154,339
Total Replacement Capital Improvements	<u>\$ 50,000</u>
Grand Total Agency Requested Budget FY20 Grand Total Agency Budget FY19 \$ Increase over FY19 budget % Increase over FY19 budget % Increase over FY19 budget (w/o Sunset)	0 \$4,485,694 \$4,260,909 \$ 224,785 5.3% 2.9%
Full-Time-Equivalent Positions	29.5

SUNSET REVIEW FY2020-21

Sunset Review: estimated cost FY2020\$90,000estimated cost FY2021\$10,000

Sunset Review: total estimated cost FY2020-21 \$100,000*

Sunset is the regular assessment of the continuing need for a state agency or program to exist. The Sunset process works by establishing an automatic termination (Sunset) date on which an agency will be abolished unless a bill is passed to continue it. The Department's current Sunset date is August 31, 2021. The Sunset process creates a unique opportunity for the Legislature and stakeholders to look closely at each agency and make key improvements to how state government works. For the FY2021 legislative session, beginning in January 2021, there are twenty-one (21) state agencies going through the Sunset process. The Credit Union Department (Department) is one of those agencies. Currently, the Department is in the process of completing the first step of the Sunset Review process, which entails the completion of a Self-Evaluation Report (SER). The SER must be submitted to the Sunset Commission by September 1st, 2019, and upon submittal becomes a public document.

*The estimated cost is based upon a discussion with a representative from the Sunset Advisory Commission on June 3, 2019, and a subsequent email from that individual which provided a cost estimate for our Sunset Review of \$99,050. For budgetary purposes the estimated amount was rounded to \$100,000. The exact figures can change slightly depending on travel estimates or other changes to the Sunset Review Team's schedule; but should not change significantly. It is estimated that 90 percent of the total cost will be billed during FY2020, as most of the work will occur then, and the remaining 10 percent will be billed in FY2021. Since the billing percentages by year may be subject to slight changes, we are requesting the full estimated cost of \$100,000 be included in the FY2020 budget, and any remaining amount from this amount be carried forward to the FY2021 budget, upon approval of the FY2021 budget by the Commission. No excess budgeted funds for this line item will be available for other Department costs not related to the Sunset Review process.

BUDGET NEEDED TO CONTINUE EXISTING SERVICES

FY 2020 Base Budget Reconciliation

	FY 2019		Base
Object of Expenses	Budget	Adjustment	FY 2020
Salaries and Wages	\$2,621,239	<\$68,214>1	\$2,553,025
Payroll Related Costs	821,630	\$1,8392	823,469
Travel	446,847	\$26,125 ^{1a}	472,972
Professional			
Services/Fees	176,840	<\$46,800> ^{2a}	130,040
Supplies/Materials	36,370	\$14,900 ³	51,270
Communication/Utilities	51,028	<\$2,228>4	48,800
Repairs/Maintenance	2,800	\$1,3405	4,140
Rentals and Leases	7,250		7,250
Printing and			
Reproduction	2,855	<\$100>6	2,755
Other/State of Texas			
Services	94,050	<\$6,416>7	87,634
Grand Total	\$4,260,909	\$79,554	\$4,181,355

⁶Reduced by \$100 based on BY19 costs through 12/31/18 of \$1,308.

¹Reduced FY20 baseline salary and wages costs by \$63,214 based on one month (Dec. 2018) of double Commissioner salary - \$15,417; lump sum vacation for former Commissioner of \$39,633, \$37,805 reduction in staff baseline salaries, and \$1,440 reduction in longevity pay. Longevity pay of \$28k est. for announced retirement of Field Supervisor in FY20.

²Reduction in Payroll Related Costs of \$5,036 based on salaries as of 4/1/19. \$6,875 increase anticipated for retirees group insurance due to announced retirement of Field Supervisor.

^{1a}Travel increase based on \$20,000 baseline increase for conferences approved at March 2019 Commission meeting, baseline increase for all travel costs of 2.4% based on CPI index, and \$4,000 reduction due to backing out one-time budget amount for FY19 tied to the recruiting and hiring of the new Commissioner.
^{2a}Reduction due to removal of one-time costs of \$50k (FY19) tied to conversion of SAGE/ACT database to a new solution, and an increase of \$3,200 tied to the Employee Assistance Program (\$1,500) and reallocation of funds (\$1,700) from COBJ #7961 to #7285.

³Increased baseline by \$14,900 as follows: reallocation of \$15k for computer equipment, etc. to COBJ #7378 from Other Operating Expense category and reductions in Books and Reference of \$100 based on BY18 costs incurred.

⁴Reduced by \$2,228, based on CPI index add-on for Electric and Water utility bills of \$172 and \$2,400 reduction to COBJ #7961 based on actual monthly costs in BY19 of \$2.065.

⁵ Increased baseline by \$1,340 due to new lawn maintenance agreement executed during FY19. Funds reallocated from COBJ #7035 (\$419); COBJ #7961 (\$700) and COBJ #7382 (\$100); COBJ #7273 (\$100) and \$21 from Trust Service Fee.

⁷ Decreased baseline by \$6,416, as follows: Increase in NASCUS annual membership dues of \$6,700. Reallocation of \$15,000 from Other Operating Expense category (COBJ #7378) to Supplies/Materials category, \$1,905 increase for Statewide Cost Allocation Plan (#7953), and reallocation of \$21 from Trust Service Fees to COBJ #7271 under Repairs/Maintenance category.

OVERVIEW OF AGENCY REQUESTED FY2020 BUDGET

Proposed Budget with Strategic Initiatives

Object of Expenses	Base Budget	Strategic Initiatives	Budget Request	
Salaries and Wages	\$2,553,025	78,121	\$2,631,146	
Payroll Related Costs	823,469	24,218	847,687	
Travel	472,972	20,000	492,972	
Professional Services/Fees	130,040	160,000	290,040	
Supplies / Materials	51,270	22,000	73,270	
Communication/Utilities	48,800		48,800	
Repairs/Maintenance	4,140		4,140	
Rentals and Leases	7,250		7,250	
Printing and Reproduction	2,755		2,755	
Other/State of Texas	2			
Services	87,634		87,634	
Grand Total	\$4,181,355	\$304,339	\$4,485,694	

Percentage Increase over FY 2019 Budget

5.3%

Potential Revenues and Proposed Expenditures ³			
Potential Revenues	\$4,614,8044		
Proposed Expenditures	\$4,485,694		
Estimated Discount in FY2019 Operating			
Fees (Rule 97.113(d)	\$129,110		

Note: As required by Commission policy, staff has reviewed all fees established by Rule 97.113 and recommends that the Commission make no changes to the fee structure. The fees are currently at a level that ensures the recovery of the full cost of operating the Department.

⁴Actual fees will be based on assets as of June 30, 2019.

³ Using assets as of March 31, 2019.

REVENUE HISTORY

Fiscal Year 2017			
Total Fees Prescribed by Rule 97.113(b)	\$4,038,989		
Discount Permitted by Rule 97.113(d)	<\$ 356,052>		
Actual Assessment Collected	\$3,682,937		

Fiscal Year 2018	3
Total Fees Prescribed by Rule 97.113(b)	\$4,371,851
Discount Permitted by Rule 97.113(d)	<\$ 417,695 >
Actual Assessment Collected	\$3,954,156

Fiscal Year 20	19
Total Fees Prescribed by Rule 97.113(b)	\$4,494,724
Discount Permitted by Rule 97.113(d)	<\$ 448,299 >
Actual Assessment Collected	\$4,046,425

PERFORMANCE MEASURES					
Measure	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Number of Credit Unions	185	184	187	185	977D- 4/19 181
Credit Union Total Assets (billions)	\$33.8	\$35.9	\$39.6	\$41.5	\$43.3
Percent Increase in Credit Union Total Assets	7.0%	6.2%	10.3%	4.8%	4.3%
Average Regulated Assets per Examiner (billions)	1.88	1.80	2.08	\$2.30	\$2.78
Number of Examinations	156	166	170	151	99
Percent of Credit Unions Examined	84%	90%	91%	82%	54%
Percent of Credit Union Assets Examined	92%	94%	89%	90%	54%
Number of Remedial Contacts	38	37	28	34	21
Percent of Credit Unions Rated 1 or 2 (CAMELS)	82%	86%	89%	87%	88%
Percent of Assets in 1 or 2 Rated Credit Unions (CAMELS)	82%	93%	93%	97%	98%
Percent of Well-Capitalized Credit Unions	97%	98%	98%	97%	100%
Number of Credit Unions Rated 3, 4, or 5 (CAMELS)	33	25	21	24	20
Annual Examiner Turnover	22.2%	23.1%	5.3%	5.3%	5.7%
Average Tenure of Departing Examiners (Months)	50	37	14	33	51
Number of Examiners Hired	3	7	1	0	1
Annual Staff Turnover	18.2%	18.3%	10.5%	3.5%	7.3%
Number of Formal Training Days	169	311	386	314	97
Number of Applications Processed	57	57	62	62	53
Number of Request – Interpretation/Opinion	4	2	3	0	0
Number of Public Information Requests	18	25	12	19	13
Number of Written Credit Union Complaints Processed	253	265	280	338	242
Department Costs/\$100k Assets	\$9.67	\$10.26	\$10.33	\$9.33	TBD

STRATEGIC INITIATIVE FUNDING REQUEST #1

Initiative Name: **Examiner Laptop Refresh** Priority: **1**

Examiner Laptops			
Objects of Expense	Estimated Costs \$17,500		
Hardware (10 Laptops)			
Vintage Set-up Costs (est. @ \$300			
times 10 laptops)	\$3,000		
Miscellaneous (scanners, privacy			
screens, etc. at \$100 times 10			
laptops)	\$1,000		
Increased software and/or security			
costs, etc. (\$50 times 10 laptops)	\$500		
Total	\$22,000		

Description/Justification: The funding of this initiative is necessary to replace the field examiner's laptops, during FY20 and FY21. The NCUA currently provides leased laptops to our examiners but has indicated they will discontinue offering laptops in early 2021. To defray the cost over two fiscal years and to ensure a smooth transition to the new laptops, the Department is proposing we replace ten (10) laptops during fiscal year 2020 and nine (9) laptops during fiscal year 2021.

The Department will remain responsible for providing all laptop security and software support for the laptops, other than support for the NCUA Examination Program software. In addition, all Outlook services, including email addresses for state examiners will continue to be provided and managed by the Department. No significant additional ongoing cost is anticipated for security, software and email infrastructure for the new laptops, as those ongoing costs were budgeted for in fiscal year 2018. However, an additional \$500 has been conservatively budgeted should any unanticipated security and software costs arise.

As part of the described laptop transition, the Department is requesting funding for the items described in the above table. It is anticipated the hardware, set-up and miscellaneous costs associated with this initiative will

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recur every third year. Approval of this initiative will result in the inclusion of these anticipated recurring costs in the Department's future baseline budgets.

External/Internal Factors:

Internal: Having examiner laptops is imperative in providing examination staff the ability to complete examinations of state-chartered credit union. In addition, maintaining up to date security/encryption related software on the laptops is imperative to ensure examination and other Department data is securely maintained and transmitted. PDF 995 software which is compatible with the Aires examination software is necessary so that examiners may retain examination work papers and other examination related documents within the Aires program. Also, when examiners experience issues with non-Aires related software and security issues, it is imperative that support be available which results in minimal disruption and down time.

External: The NCUA has initiated a pilot program to change the examination software utilized by the federal and state examiners, from "Aires" to "Merit". They have provided states the tentative laptop compatibility requirements necessary for the "Merit" software to work appropriately. The Department will ensure compatibility requirements are met when purchasing the new examiner laptops.

The approval of funding for this initiative is imperative to minimize disruptions to our examination processes and ensure Department and member data is safely and securely maintained and transmitted. In addition, it will allow the Department to defray the cost over two fiscal years, to minimize the impact on our annual budgets.

STRATEGIC INITIATIVE FUNDING REQUEST #2

Initiative Name: Merit Increase Funding Pool Priority: 2

MERIT INCREASE FUNDING POOL			
Objects of Expense Estimated Costs			
Salary & Wages	\$78,121		
Payroll Related Costs	\$24,218		
Travel Expenses			
Other Operating Expenses			
Total	\$102,339		

Description/Justification: Merit pay has traditionally been one of the most effective tools to motivate and retain qualified staff. Recognizing and rewarding high performance is a key priority for driving excellence at the Department. A monetary reward is the strongest incentive for staff who exhibit greater enthusiasm, commitment and developmental skills than the other staff members around them. When budgeted, all classified staff members participate in the Department's merit pay program. The last merit increases for the staff was budgeted for September 1, 2018.

The Department is proposing to establish a pool to fund merit and promotion increases for staff. The aggregate amount of the pool will be equivalent to 3.5 percent of the total salaries for the applicable staff positions. All awards made from the pool will be based on performance.

Funding of this item is necessary for the Department to maintain examiner resources to ensure supervision to meet regulatory responsibilities, achieve performance measures, and preserve a safe and sound Texas credit union system. As credit unions continue to grow in sophistication and complexity, the ability to retain highly skilled and qualified examiners is an essential component in meeting these objectives. It is imperative that the Department keep examiner salaries at competitive levels to maximize retention of strong staff members.

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In absence of a merit-based pay program, there is the risk of discouragement for the highest performing staff. The most talented staff is aware of their strengths and like to accept the challenges of performance linked pay. If they find that all staff is awarded a uniform pay without regard to individual merit or contribution, there is a risk of the best performing staff leaving the Department.

External/Internal Factors:

Internal: Merit pay is an approach to compensation that rewards the higher performing employees with additional pay or incentive pay. Merit pay will help the Department differentiate between the performance of high performing and low performing employees and reward the higher performance. As a result, it is believed that merit pay is the best opportunity to ensure that your outstanding performers remain with the Department and continue to make their significant contributions.

External: The Commission approved a 3.5 percent merit increase to the existing FY19 salary pool at its March 2019 commission meeting.

STRATEGIC INITIATIVE FUNDING REQUEST #4

Initiative Name: **Realign/add Office Staffing** Priority: **4**

Increase Full-Time Equivalents			
Objects of Expense Estimated Costs			
Increase Full Time Equivalents	\$0.00		
(from 29.50 to 30)			
Total	\$0.00		

Description/Justification: The funding of this initiative is imperative for the Department to maintain an adequate level of administrative staff to ensure that Department operations are performed accurately and efficiently, and in accordance with applicable Texas state laws. Over time, credit unions have continued to change in size and complexity, and the administrative tasks/workload necessary to effectively maintain our examination supervision program has significantly increased.

A strong and experienced administrative staff is critical to ensure that the back-office functions of the agency are effectively operated, and appropriate internal controls are in place. It is also important for staffing levels to be appropriate to provide adequate back-up for administrative staff, in instances of short-term sickness, vacations, vacancies, etc.

At a minimum, the Department needs one additional full-time office staff member. This proposal assumes the Department would discontinue its usage of a student intern (part-time employee); thus, reducing the total cost of this initiative. Further, the realignment and reclassification of other office staff positions would significantly reduce the cost of this initiative. A breakdown of current salary and benefit costs and proposed costs for the existing positions to be impacted and the new positions, is as follows:

Proposed Changes					
Current Position	Current Salary Costs	New Position	Salary Costs with Changes (est.)		
Accountant VI (FT)	\$83,200	Same (FT)	\$69,000*		
Exec. Asst. I (FT)	\$53,136	Admin. Asst. III (FT)	\$35,000**		
Intern (PT)	\$13,200	Accounting Tech II/Admin. Asst. III (FT)	\$35,000		
Total	\$149,536		\$139,000		

*Filled June 1, 2019 **Filled May 7, 2019

As indicated above, there is no anticipated increase in total salary costs for the above proposed change. It is believed that any slight increase in benefit costs from this initiative will be absorbed by salary savings. The approval of this initiative will allow the Department to use current salary and benefit costs (\$149,536, plus benefits) for the impacted positions in the fiscal year 2020 budget.

External/Internal Factors:

Internal: Internal factors and impediments have included budgetary constraints and the lack of cross-training due to the normal workload associated with daily office operations. There has been no increase in office staff full-time equivalents in over ten (10) years. Unforeseen turnover can create extreme challenges given our small office environment and limited number of crosstrained employees. In addition, the long tenure of many existing staff members has made succession planning a critical factor for the Department during the next few years.

External: External factors are also driving the need to increase administrative staff. The Department's processing of credit union member complaints has approximately doubled since fiscal year 2012 through fiscal year 2018, increasing from 174 to 339. No additional staff has been utilized to assist with this process. Furthermore, during the Department's most recent audits from the State Auditor's Office (2016) and the Comptroller's Office (2018), there have been findings noted which are indicative of developing operational/internal control weaknesses. Department management feels the additional staffing proposed will greatly enhance its internal and quality control processes.

STRATEGIC INITIATIVE FUNDING REQUEST #5

Initiative Name: Increase Examiner Training Priority: 5

Increase Training			
Objects of Expense	Estimated Costs		
Provide for 1 to 3 days of additional training per examiner each year (est. using 19 examiners and 1 office staff @ \$500 each)	\$10,000.00		
Total	\$10,000.00		

Description/Justification: The funding of this initiative is imperative for the Department to maintain an adequately trained examination staff. As the complexity and size of credit unions continues to increase, it has become more important than ever before, to provide training opportunities to ensure examinations of Texas credit unions are effectively performed and provide protection to Texas citizens from fraud, unethical conduct and any other deviations from appropriate standards in connection with services provided by credit unions.

The Department needs to devote additional resources to mentoring and training field examiners to ensure they obtain/maintain the skills and expertise necessary to fulfill the Department's supervisory responsibilities. While on the job training and mentoring is provided by Field Supervisors to their respective field staff team members, external training opportunities could further enhance our examination staff's knowledge and skills. Approval of this initiative will result in the inclusion of these anticipated recurring costs in the Department's future baseline budgets.

External/Internal Factors:

Internal: The primary internal factors which have limited external training opportunities for our examination staff has been the costs of training and travel (time and money). The approval of this initiative would allow the Department to provide quality training to its staff while minimizing/reducing some of the normal travel costs and time associated with attending external training/conferences. By bringing the trainer(s) to us, the cost of training and

travel would be greatly reduced, <u>all</u> employees would receive the same training/message and it would promote a more consistent knowledge of key examination related topics among our entire team.

External: Professional organizations such as CUNA Mutual, the National Association of State Credit Union Supervisors (NASCUS), the Cornerstone League, etc. provide a variety of training opportunities geared specifically toward credit union employees, as well as credit union regulators. Training offerings are varied and include topics pertaining to compliance, information security, operational needs, etc. Often, these organizations will provide their training at a site of the regulator's preference using a turnkey pricing model. Such training opportunities greatly reduce the "normal costs" associated with an examiner traveling out of their local area to attend.

STRATEGIC INITIATIVE FUNDING REQUEST #6

Initiative Name: Increase Examiner Travel Budget Priority: 6

Increase Examiner Travel Budget			
Objects of Expense	Estimated Costs		
Increase annual budget for examiner travel costs.	\$20,000.00		
Total	\$20,000.00		

Description/Justification: The funding of this initiative is necessary to increase the baseline budget for the examination staff's annual travel costs. During the last two fiscal years, the state lodging and meal per diem rates have increased significantly and mileage reimbursement rates have increased as well. The increases in state reimbursement rates has resulted in a significant increase in the average annualized cost of travel per examiner, from \$23,419 at fiscal year-end 2017 to \$24,643 as of March 31, 2019. A breakdown of actual in-state travel costs since fiscal year 2017, including the average travel costs per examiner is as follows:

Fiscal Year	Avg.	No. of Exam	iners	Total In-State Travel	Avg. Travel Cost Per Examiner
	Dallas	Houston	Total		
17	10	8.83	18.83	\$440,989	\$23,419
18	9.83	8.75	18.58	\$427,502	\$23,009
19	8.14	9	17.14	\$422,383	\$24,643
				(annualized)	

Actual annualized travel costs (adjusted for a full examination staff of 19 examiners) has far exceeded budgeted amounts for each of the past three fiscal years. The table below reflects that trend.

Fiscal Year	Projected Cost \$ (Fully Staffed)	Budgeted In-State Travel	Variance \$ (Fully Staffed)
17	\$444,970	\$407,921	\$37,049
18	\$437,166	\$413,203	\$23,963
19	\$468,219	\$421,847	\$46,372

Further, an analysis of the Department's various travel expense categories indicates most of the annualized increase in examiner travel costs are tied directly to an increase in average meals/lodging expenses. The following table summarizes the average annualized meal/lodging costs per examiner for each of the last three years.

Average Meals/Lodging Per Examiner				
Fiscal Year	Avg. # Examiners	Mileage \$	Avg. Cost per Examiner	\$ Change
17	18.8	\$233,870	\$12,440	
18	18.6	\$228,492	\$12,285	(\$155)
19	17.1	\$233,662 (annualized)	\$13,664	\$1,380

When fully staffed, the \$ increase in average meals/lodging cost per examiner for fiscal year 2019 equates to a total increase in the annualized budget (from the prior year) of \$26,220 (\$1,380 times 19 examiners).

External/Internal Factors:

Internal: Budgeted baseline travel costs are adjusted each year based upon the annual consumer price index (CPI). However, the adjustments based upon the CPI have not maintained the baseline budget at a level which is sufficient to cover actual in-state travel costs. Further, while projected annualized travel costs (if fully staffed) for each of the last three years have exceeded the amount requested for this initiative, it is anticipated the Department will begin to realize some minor savings in examiner travel costs based upon performing more examination work remotely.

Approval of this initiative will result in the inclusion of the \$20,000 in the Department's future baseline budgets.

External: State meal and lodging per diem rates, as well as mileage rates have been increased significantly by the Texas Legislature during the last three fiscal years. Department increases in the baseline budget in-state travel costs have not kept pace with the increases in state per diem and mileage rates. The following table reflects the dollar and percentage change in state travel reimbursement rates for year-to-date 2019 and the prior two fiscal years.

State Rates - Lodging, Meals and Mileage				
ltem	Tot. Change (FY17 to FY19)	2019	2018	2017
Lodging - In-State		\$94	\$93	\$85
\$ Change	\$9	\$1	\$8	\$0
% Change	10.6%	1.1%	9.4%	0.0%

Meals		\$55	\$51	\$51
\$ Change	\$4	\$4	\$0	\$0
% Change	7.8%	7.8%	0.0%	0.0%
Mileage		\$0.58	\$0.545	\$0.535
\$ Change	\$0.045	\$0.035	\$0.010	\$0.005
% Change	8.4%	7.8%	1.9%	-0.9%

Higher in-state travel costs have also been a result of higher lodging costs in geographic areas where the economy has been impacted by the thriving oil and gas industry.

REPLACEMENT/CAPTIAL IMPROVEMENT PLAN FY 2020-2022

FY2020				
Proposed Maintenance Projects:	Estimated Cost			
None	\$ 0			
Proposed Capital Improvements:				
Priority #3: Secure Data Portal Upgrade ¹	\$10,000			
Priority #7: SAGE/ACT Database Conversion ²	\$40,000			

¹ The funding of this capital improvement is necessary to increase the number of user licenses within the Secure Data Transfer Portal. The portal enables the Department's examiners and credit unions to securely share examination-related documents, and to provide files transfers and file management over a reliable data stream. Our present capacity provides a maximum of 50 concurrent users in the portal at any given time. As more credit unions utilize the portal, it is anticipated an increase in the number of user licenses will be needed. The next level of upgrade provides usage to the portal for up to 250 concurrent users, at an increased cost of \$790 per month, or \$9,480 per year. The quoted annual cost has been rounded to \$10,000 to allow for any unanticipated, incidental costs. If approved, the amount requested would be a recurring monthly and annual cost.

²The funding of this initiative was originally approved with the FY18 budget in the amount of \$50,000. The purpose of this Capital Improvement Plan item was to build a hosted solution to manage and report the Department's internal organizational processes, while integrating with the agencies Office 365 solution. This project was not completed during FY18 as planned but a legally binding contract was executed prior to the fiscal year-end resulting in these funds becoming legally obligated for FY19. During FY19, this project was only partially completed with \$10,000 being funded for the work completed to date in 2019. In the spirit of being fully transparent and since the contract for this item has expired, the remaining amount of this initiative is being presented to the Commission for consideration and approval. It should be noted that our current version of SAGE/ACT is no longer supported or is it backed by the newer Windows 10 operating system.

Related Operating and Maintenance Costs (if any):

¹There are no related operating and maintenance costs associated with the Secure Data Portal Upgrade.

² On-going costs related to the SAGE/ACT Database Conversion initiative are estimated to be minimal and tied to periodic increases with Office 365/SharePoint storage costs, and the depreciation of any hardware and software.

FY2021

Proposed Maintenance Projects:

Estimated Cost

None

Proposed Capital Improvements:

Remodel Restrooms for ADA Compliance and Energy Efficiency¹ \$203,500

¹ The building's restroom partitions need to be replaced to be compliant with Title III of the American with Disabilities Act ("ADA") and due to corrosion. The current restroom partitions are not large enough for an individual with a disability to maneuver. Other ADA improvements to the building's restrooms include: insulating lavatory pipes under sinks to prevent burns, installing a raised lavatory seat, installing a full-length bathroom mirror, and repositioning paper towel dispensers and fixtures. Additionally, the sink fixtures should be replaced with modern, energy-efficient models, the lavatories should be replaced with low-flow toilets, and corroded water supply hoses should be replaced to prevent potential water leaks.

Related new operating and maintenance costs (if any):

The installation of the new ADA required restroom improvements will not result in any new material operating or maintenance costs, other than depreciation of the capital improvement. The installation of more energy-efficient fixtures will reduce operating and maintenance costs.

FY2022			
Proposed Maintenance Projects:	Estimated Cost		
None			
Proposed Capital Improvements:			
Replace the Roof ¹	\$251,500		

¹The Department's roofing is a low slope with built-up roof. It is deteriorated and should be scheduled for replacement. The Department's current roof is out of its workmanship warranty making continued maintenance expensive and inefficient. The Texas Facilities Commission provided us the following roof options.

System	Bldg. Ht.	Slope	Unit Cost	Sq. Ftg.	Construction Cost	Escalation to 2018	Soft Cost/ Contingency	Total
Mod. Bitumin (Hot Asphalt/Heat Welded)	1 – 2 Story	Low ' ¼"/Ft.	\$30	4,200	\$126,000	\$139,700	\$111,800	\$251,500
Single Ply TPO	1 – 2 Story	Low ¼"/Ft.	\$30	4,200	\$126,000	\$139,700	\$111,800	\$251,500
Single Ply PVC	1 – 2 Story	Low ¼"/Ft.	\$30	4,200	\$126,000	\$139,700	\$111,800	\$251,500
Arch. Metal *	1 – 2 Story	Pitched 4:12 Min.	\$25 - \$30	4,200	\$105,000 to \$126,000	\$139,700	\$111,800	\$251,500

* Not a recommended solution by TFC's roofing consultant.

Related new operating and maintenance costs (if any):

The installation of new roof will not result in any new material operating or maintenance costs other than depreciation of the capital improvement.



Credit Union Department State of Texas

FY 2020 Annual Operating Plan & Budget

Approved by the Credit Union Commission July _____, 2019

INTRODUCTION

In accordance with Chapter 16 of the Finance Code, the Department has crafted the following *FY 2020 Annual Operating Plan and Budget*. This document aligns the goals and measures developed for the Department's *Strategic Plan for Fiscal Years 2019-2023* with the Department's proposed budget. It aims to improve the links between the Department's resource needs, effectiveness, and outcomes.

THE DEPARTMENT TODAY

The Department is a self-directed and semi-independent agency that is responsible for ensuring a safe and sound credit union system for all Texans. This is accomplished through the effective chartering, regulation, and supervision of Texas-chartered credit unions. The operations of the Department are funded primarily by semiannual assessments levied on credit unions. The Department receives no state monies from the General Revenue Fund.

As of December 31, 2019, the Department was responsible for regulating and supervising 183 credit unions. Based on the year-end call reports, Texas-chartered credit unions held \$41.9 billion in assets or approximately 40 percent of total aggregate credit union assets in Texas.

GOALS AND OUTCOMES

The Credit Union Commission has established four strategic goals to guide the operations of the Department and to contribute to the achievement of its mission and performance goals. The Commission's goals are:

- 1. to ensure a safe and sound state credit union industry;
- 2. to provide a flexible regulatory framework that enables credit unions to provide a full competitive array of financial services;
- 3. to safeguard the interest of credit union members; and
- 4. to develop a professional and motivated staff that provides quality service to the citizens of Texas and supports achievement of the Department's statutory mission.

The Department works to meet these goals by, among other things, detecting violations and potential problems or issues in the Texas credit union system and ensuring that the violations are addressed; crafting rules that strengthen corporate governance and operations; ensuring credit union members are treated fairly; and making sure that the Department's human capital strategies, information technology initiatives, and resources are appropriately aligned to achieve the Department's mission, goals, and outcomes.

Like other regulatory agencies, the Department has found it challenging to develop measures that accurately depict the outcomes of the agency's activities. In many instances, the effects of the agency's efforts can only be indirectly assessed. The Department intends to continue refining its work in this area as it gains more experience in integrating its budget and performance functions. As part of this effort, the Department will continue to assess alternatives for measuring outcomes that help the public gauge the Department's progress in achieving its mission, as well as assisting staff in meeting their objectives.

Strategic Goal 1: To Ensure a Safe and Sound Credit Union Industry

Strategic Objective 1.1: The Department anticipates, understands, addresses, and communicates risk to credit unions. The Department seeks to fulfill this objective by:

- 1. establishing the appropriate regulatory framework;
- 2. being a prudent steward of Department resources;
- 3. ensuring risk-based supervision is properly implemented and focused on material risks to the industry and individual credit unions;
- 4. identifying emerging risk areas related to industry and individual credit unions;
- 5. complying with the examination requirements of 7 TAC Section 97.105;
- 6. resolving problem credit unions in a timely fashion, effectively, and when possible, without loss to the share insurance provider; and
- 7. taking prompt and effective enforcement actions when warranted.

Strategic Objective 1.2: The Department cooperates with other regulatory authorities on common interests. The Department seeks to fulfill this objective by:

- 1. working effectively with the NCUA, private share insurance providers, and other state regulators to identify and address risks and emerging issues; and
- 2. implementing and developing new coordination and collaboration agreements with NCUA, private share insurance providers, and other applicable state regulators regarding supervisory activities performed in credit unions and information exchange.

Strategic Objective 1.3: Supervisory methods and analytical tools keep pace with industry changes and appropriately support the broader mission of the Department. The Department seeks to fulfill this objective by:

- 1. utilizing analytical tools and reports to effectively use the data collected from credit unions to foster informed decision making for supervisory operations and policy;
- 2. deploying supervisory technology solutions to enhance data quality and provide user-friendly examiner access to key credit union and industry information; and
- 3. Providing transparency through the Department's reporting.

Key Performance Measures

- Percentage of credit unions receiving regular examination annually
 - Target for FY 2020: 75%
- Percentage of applications approved or denied within 60 days
 - Target for FY 2020: 100%
- Number of state-chartered credit unions
- ➢ Number of regular examinations performed
- Percentage of credit unions with composite CAMEL ratings of 1 or 2
 Target for FY 2020: 85%
- Percentage of assets held in credit unions with CAMEL ratings of 1 or 2
 - Target for FY 2020: 95%

Internal Measures

- Number of follow-up contacts made
- Number of enforcement actions issued
- Percentage of credit unions that are "Well Capitalized" as defined by federal statute
 - Target for FY 2020: **95%**
- Percentage of reports mailed to credit unions within 21 days
 - Target for FY 2020: 98%
- Percentage of total available work time utilized to conduct both regular and remedial examination work
 - Target for FY 2020: 65%
- Average Cost per Credit Union Examination
- Assets Examined per Examiner Day
 - Target for FY 2020: \$11.4 million*
- Average time to complete analysis of quarterly financial data
 - Target for FY 2020: within 30 days after the submittal deadline for the most recent 5300 Call Report

*Target same as FY19. Will be amended for FY20, based upon 95% of actual level realized for entire FY19.

Strategic Goal 2: To Provide a Flexible Legal and Regulatory Framework that Enables Credit Unions to Provide a Competitive Array of Financial Services

Strategic Objective 2.1: Each Commission rule is current, clearly written, and necessary for an effective supervisory process. The Department seeks to fulfill this objective by:

- 1. drafting, amending, and implementing rules to fulfill Legislative directives and to ensure relevance to current conditions;
- 2. conducting the mandatory rule review in accordance with Commission's approved plan; and

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3. implementing rulemaking through successful collaboration and consultation with interested parties.

Strategic Objective 2.2: The Department supports credit union efforts to remain competitive, consistent with safety and soundness. The Department seeks to fulfill this objective by:

- 1. supporting the continued recognition of the attributes of the state credit union charter through appropriate opinions and rules;
- 2. developing and modernizing attributes of the credit union charter and the role and status of the industry;
- 3. enhancing communication with NCUA and other state regulators to facilitate better coordination on issues affecting credit unions; and
- 4. communicating attributes of the state charter within and outside the Department.

Strategic Objective 2.3: Application procedures are efficient and consistent with safety and soundness. The Department seeks to fulfill this objective by:

- 1. providing a standardized application package;
- 2. establishing policies and procedures that provide clear and comprehensive guidance;
- 3. implementing and maintaining processes for prompt screening of applications; and
- 4. enhancing existing technology solutions that support effective application operations.

Key Performance Measures

- Percentage of rule changes provided to credit unions within 60 days after adoption
 - Target FY 2020: 100%

Internal Measures

- Number of new rules adopted
- > Number of rules amended
- Number of rules re-adopted without change
- Number of applications processed
- Number of requests for interpretations/opinions of Act and Rules
- Number of contested cases referred to SOAH
- Number of Public Information Act requests processed
- Number of public forums in which Department participates
- Total Assets in state-chartered credit unions
- Percentage increase in total aggregate credit union assets
- Percentage of interpretations/opinions issued within 30 days

• Target FY 2020: 100%

Strategic Goal 3: Safeguard the Interest of Credit Union Members

Strategic Objective 3.1: All credit union members have reasonable access to credit union services and are treated fairly and lawfully. The Department seeks to fulfill this objective by:

- 1. reinforcing the importance of fair and honest treatment of credit union members through appropriate supervisory and enforcement action;
- 2. expanding the agency's role in resolving and/or mediating member complaints handled by the Department;
- 3. strengthening role in addressing member privacy, information security, and identity theft; and
- 4. enhancing the Department's consumer compliance examination program.

Strategic Objective 3.2: Credit unions are involved in providing financial services in underserved communities within this State. The Department seeks to fulfill this objective by:

- 1. supporting the efforts of credit unions to expand their fields of membership to included underserved and low income communities;
- 2. facilitating the process for credit unions to obtain a low-income designation from NCUA; and
- 3. participating in financial literacy efforts by the industry and other agencies.

Key Performance Measure

Percentage of credit unions providing services to low income or underserved populations

Internal Measures

- Number of complaints processed
- Percentage of complaints responded to within 30 days
 - Target FY 2020: 95%

Strategic Goal 4: Develop a Professional and Motivated Staff that Provides Quality Service and Supports Achievement of the Department's Statutory Mission.

Strategic Objective 4.1: The Department maintains a competent, highly motivated, and diverse workforce in a fair and inclusive work environment. The Department seeks to fulfill this objective by:

- 1. maintaining a comprehensive Equal Employment and Workforce Diversity Plan;
- 2. executing an aggressive recruiting and comprehensive training strategy for new entry-level examiners;
- developing proactive initiatives focused on the retention of employees, including mentoring, employee feedback, incentives, and recognition programs;
- 4. creating a leadership development program to support and enhance management succession; and
- 5. implementing an external hiring strategy to augment specialized skills to enhance the Department's supervision of complex credit unions.

Strategic Objective 4.2: The Department is an efficient, effective, and ethical organization. The Department seeks to fulfill this objective by:

- 1. ensuring compliance with laws, rules, and stewardship of its resources through program evaluations and a quality management framework;
- 2. ensuring compliance with the rules, policies and procedures for ethical conduct by its employees;
- 3. ensuring reliable, secure, modern information technology systems are in place in support of an environment that meets the Department's mission, goals, and objectives; and
- 4. leveraging technology, with particular focus on information management initiatives, such as records and knowledge management.

Internal Measures

- Percentage of exam related travel cost reduced by remote work
 - Target FY 2020: 5%

Strategic Objective 4.3: The Department's resource decisions and operations reflect sound financial, security, and risk management principles. The Department seeks to fulfill this objective by:

- 1. implementing security controls to mitigate risk and to protect confidential information;
- 2. improving contingency planning for business continuity, including information technology recovery, compliance with Homeland Security requirements, and crisis management strategies; and
- 3. achieving reliable, accurate and timely financial resources management information.

Internal Measures

- Annual examiner turnover rate
 - Target FY 2020: 16%

- Average regulated assets per examiner (billions)
 - Target FY 2020: **\$2.2 billion**
- Number of days of formal training attended by staff
- Number of purchases made from HUB vendors
- > Percentage of purchases made from HUB vendors
 - Target FY 2020: Professional Services 23.7%; Other Services 26.0%; and Commodities 21.1%
- Percentage of credit unions indicating quality service annually
 - Target FY 2020: 90%
- Staffing level
 - Target FY 2020: 95%
- Number of jobs fairs attended
 - Target FY 2020: 2
- Turnover ratio (excluding retirements)
 - Target FY 2020: Less than 15%
- Accreditation by NASCUS Maintained in Good Standing
 - Target FY 2020: Yes
- > Total Department costs relative to every \$100,000 in assets regulated
 - Target FY 2020: \$10.04*

*Target same as FY19. Will be amended for FY20, based upon 105% of actual level realized for entire FY19.

	\$4,485,694
	\$4,485,694
\$2,631,146	
	\$3,478,833
	+0,000
\$451,972	
11,000	
	\$492,972
\$290,040	
73,270	
48,800	
4,140	
7,250	
2,755	
87,634	
	\$513,889
	\$4,485,694
	\$290,040 73,270 48,800 4,140 7,250 2,755

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¹ Budgeted operating fees will be set to cover the actual budget approved by the Commission. Any funds in excess of the prescribed Contingency Fund Reserve aggregate limit as of August 31, 2019, will also be used to reduce the operating fees for Texas credit unions during the fiscal year.

	CUMULATIVE RESOURCES					
Budget Year	2014	2015	2016	2017	2018	2019
Authorized FTE	25	27.5	28.5	29.5	29.5	29.5
Actual FTE	24.3	25.0	28	29	28.5	27.5
Budgeted Dollars	\$3,024,386	\$3,503,250	\$3,700,917	\$3,935,394	\$4,063,453	\$4,260,909
Actual Dollars Spent	\$2,984,998	\$3,066,134	\$3,466,068	\$3,850,838	\$3,874,028	TBD

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PROCEDURES FOR ADOPTING A PROPOSED RULE

- 1. A proposed rule is prepared by Credit Union Department staff and presented to legal counsel (Attorney General) for review.
- 2. The proposed rule is presented to the commission for consideration.
- 3. The commission reviews, amends, adopts, refers back to staff, or tables the proposed rule.
- 4. The proposed rule is adjusted by staff (if required), furnished to legal counsel and transmitted to the *Texas Register* for publication as a "proposed" rule.
- 5. A 30-day comment period follows initial publication which also is made in the Department's monthly newsletter or by a special mailing to credit unions.
- 6. The commission may reconsider the rule any time after the 30-day comment period. Any comments received are considered and the rule is available for adoption as "final" if no <u>substantive</u> changes are made. Any substantive change will result in the rule reverting to step four.
- 7. The rule is adopted as "final" and transmitted to the *Texas Register* for publication as a final rule. The rule becomes effective 20 days following filing for publication.
- 8. The rule is published or announced through the Department's newsletter.

EMERGENCY RULES

Rules, which are approved by the commission for emergency adoption, are transmitted to the *Texas Register* for filing. These rules become effective immediately upon filing unless another effective date is specified. They can be effective only for 120 days with a renewal provision for an additional 60 days -- a maximum of 180 days. "Day one" is the day of filing or the date specified as the effective date. While these emergency rules are in effect, regular rules should be initiated using the normal procedure described above. The Department rarely adopts emergency rules.

PROCEDURES FOR REQUIRED RULE REVIEW

Section 2001.39, Government Code, requires that a state agency review and consider for re-adoption each rule not later than the fourth anniversary of the date on which the rule took effect and every four years after that date. To comply with this requirement, the Commission follows the procedure below:

- 1. Every four years, the Commission adopts and publishes a Rule Review Plan, which establishes a date for the required review of each existing rule.
- 2. At least sixty days prior to a particular rule's scheduled review date, the Department publishes notice in the Newsletter reminding interested persons of the review and encouraging comments on the rules up for review.
- 3. Staff reviews each rule to determine whether it is obsolete, whether the rule reflects current legal and policy considerations, and whether the rule's structure as well as the specific language used is both clear and understandable.
- 4. If in reviewing existing rules, staff believes certain amendments may be appropriate, it provides an informal comment phase on any potential substantive amendments to all interested persons via its RuleRemarks blog on the Department's webpage.
- 5. After consideration of the informal comments, proposed amendments are prepared by staff and presented to the Rules Committee for review.
- 6. At a public meeting, the Rules Committee accepts public testimony on the each rule subject to review and considers staff recommended changes. The Committee reviews each rule and then amends the staff proposal and refers it to the Commission, refers the proposal back to staff, or refers the proposal, as recommended by staff, to the Commission.
- 7. The Committee's recommendation is presented to the Commission for consideration.
- 8. The Commission reviews, amends, approves the proposal for publications, refers it back to the Committee, or tables the proposed amendment.
- 9. If the Commission approves the proposal for publication, it is transmitted to the *Texas Register* for publication as a "proposed" rule amendment.
- 10. A 30-day comment period follows initial publication which also is announced in the Department's monthly newsletter.

- 11. The commission may reconsider the rule any time after the 30-day comment period. Any comments received are considered and the rule is available for adoption as "final" if no substantive changes are made. Any substantive change will result in re-publication of the proposal.
- 12. The rule as amended is adopted and transmitted to the *Texas Register* for publication as a final rule. The rule becomes effective 20 days following filing for publication.
- 13. The amended rule is announced through the Department's newsletter and copies are made available to credit unions.

DEFINITIONS AND INTERPRETATIONS

E. (b) Proposed Amendments to 7 TAC Section 91.101 Concerning Definitions and Interpretations.

BACKGROUND: The purpose of the proposed amendments would define the term "consolidated CUSO" utilized in Section 91.401 and fix minor grammar errors. The language is presented to clearly define the terms involved to both the industry and Department staff.

RECOMMENDED ACTION: The Department recommends that the Commission approve for publication and comment the proposed amendments to 7 TAC Section 91.101.

RECOMMENDED MOTION: I move that we approve for publication and comment in the *Texas Register* the proposed amendments to 7 TAC Section 91.101.

TITLE 7.	BANKING AND SECURITIES
Part 6.	Credit Union Department
Chapter 91.	Chartering, Operations, Mergers, Liquidations
Subchapter A.	General Rules
Rule §91.101	Definitions and Interpretations

The Credit Union Commission (the Commission) proposes amendments to Section 91.101, relating to Definitions and Interpretations. The proposed amendment would define the term "consolidated CUSO" utilized in Section 91.401 and fix minor grammar errors.

The Commission proposes the following amendment to Section 91.101. The language is presented to clearly define the terms involved to both the industry and Department staff.

FISCAL NOTE ON STATE AND LOCAL GOVERNMENTS. John J. Kolhoff, Commissioner, has determined that for the first five-year period the proposed amendments are in effect, there are no reasonably foreseeable implications relating to cost or revenues of state or local governments, under Government Code §2001.024(a)(4), as a result of enforcing or administering these amendments, as proposed.

PUBLIC BENEFIT/COST NOTE. Mr. Kolhoff has determined, under Government Code §2001.024(a)(5) that for the first five-year period the amended rules are in effect, the public benefit of rule clarity will provide improved guidance to the industry. He further has determined there will be no probable economic cost to the credit union system or to persons required to comply with the rule.

IMPACT ON LOCAL EMPLOYMENT OR ECONOMY. There is no reasonably forecasted effect on local economy for the first five years that the proposed amendments are in effect. Therefore, no economic impact statement, local employment impact statement, nor regulatory flexibility analysis is required under Texas Government Code §§ 2001.022 or 2001.024(a)(6).

COST TO REGULATED PERSONS (COST-IN/COST-OUT). This rule proposal is not subject to Texas Government Code § 2001.0045, concerning increasing costs to regulated persons, because this agency is a Self-Directed Semi-Independent (SDSI) agency under Finance Code Chapter 16 and is exempt from that cost provision.

ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS FOR SMALL BUSINESSES, MICROBUSINESSES, AND RURAL COMMUNITIES. Mr. Kolhoff has also determined that for each year of the first five years the proposed amendment is in effect, there will be no reasonably forecasted adverse economic effect on small businesses, microbusinesses, or rural communities as a result of implementing these amendments, and, therefore, no regulatory flexibility analysis, as specified in Texas Government Code § 2006.002 is required.

GOVERNMENT GROWTH IMPACT STATEMENT. In compliance with Texas Government Code §2001.0221, the Board has prepared a government growth impact statement. Unless indicated below, for each year of the first five years that the rule will be in effect, the rule will not:

• create or eliminate a government program;

- require the creation of new employee positions or the elimination of existing employee positions;
- require an increase or decrease in future legislative appropriations to the agency;
- lead to an increase or decrease in the fees paid to the department;
- create new regulations;
- expand, limit or repeal existing regulation
- increase or decrease the number of individuals subject to the rule's applicability;
- positively or adversely affect this state's economy.

TAKINGS IMPACT ASSESSMENT. No private real property interests are affected by this proposal, and the proposal does not restrict or limit an owner's right to his or her property that would otherwise exist in the absence of government action. Therefore, the rule does not constitute a taking under Texas Government Code § 2007.043.

REQUEST FOR PUBLIC COMMENT. Written comments on the proposed amendments may be submitted in writing to John J. Kolhoff, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register*.

STATUTORY AUTHORITY. The amendments are proposed pursuant to Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Texas Finance Code, Title 2, Chapter 15 and Title 3, Subtitle D.

STATUTORY SECTIONS AFFECTED. The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Chapter 15 and Title 3, Subtitle D.

LEGAL REVIEW. The Commission certifies that the proposed rule has been reviewed by legal counsel and has been found to be within the agency's authority to adopt.

CHAPTER 91

Subchapter A. General Rules

§91.101. Definitions and Interpretations.

(a) Words and terms used in this chapter that are defined in Finance Code §121.002, have the same meanings as defined in the Finance Code. The following words and terms, when used in this chapter, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Act--the Texas Credit Union Act (Texas Finance Code, Subtitle D).

(2) Allowance for loan and lease losses (ALLL)--a general valuation allowance that has been established through charges against earnings to absorb losses on loans and lease financing receivables. An ALLL excludes the regular reserve and special reserves.

(3) Applicant--an individual or credit union that has submitted an application to the commissioner.

(4) Application--a written request filed by an applicant with the department seeking approval to engage in various credit union activities, transactions, and operations or to obtain other relief for which the commission is authorized by the act to issue a final decision or order subject to judicial review.

(5) Appraisal--a written statement independently and impartially prepared by a qualified appraiser setting forth an opinion as to the market value of a specifically described asset as of a specific date, supported by the presentation and analysis of relevant market information.

(6) Automated teller machine (ATM)--an automated, unstaffed credit union facility owned by or operated exclusively for the credit union at which deposits are received, cash dispensed, or money lent.

(7) Community of interest--a unifying factor among persons that by virtue of its existence, facilitates the successful organization of a new credit union or promotes economic viability of an existing credit union. The types of community of interest currently recognized are:

(A) Occupational--based on an employment relationship that may be established by:

(i) employment (or a <u>long-term</u> [long term] contractual relationship equivalent to employment) by a single employer, affiliated employers or employers under common ownership with at least a 10% ownership interest;

(ii) employment or attendance at a school; or

(iii) employment in the same trade, industry or profession (TIP) with a close nexus and narrow commonality of interest, which is geographically limited.

(B) Associational--based on groups consisting primarily of natural persons whose members participate in activities developing common loyalties, mutual benefits, or mutual interests. In determining whether a group has an associational community of interest, the commissioner shall consider the totality of the circumstances, which include:

- (i) whether the members pay dues,
- association,
- (ii) whether the members participate in furtherance of the goals of the

(iii) whether the members have voting rights,

(iv) whether there is a membership list,

(v) whether the association sponsors activities,

(vi) what the association's membership eligibility requirements are, and

(vii) the frequency of meetings. Associations formed primarily to qualify for credit union membership and associations based on client or customer relationships, do not have a sufficient associational community of interest.

(C) Geographic-based on a clearly defined and specific geographic area where persons have common interests and/or interact. More than one credit union may share the same geographic community of interest. There are currently four types of affinity on which a geographic community of interest can be based: persons, who

(i) live in,

(ii) worship in,

(iii) attend school in, or

(iv) work in that community. The geographic community of interest requirements are met if the area to be served is in a recognized single political jurisdiction, e.g., a city or a county, or a portion thereof.

(D) Other--The commissioner may authorize other types of community of interest, if the commissioner determines that either a credit union or foreign credit union has sufficiently demonstrated that a proposed factor creates an identifiable affinity among the persons within the proposed group. Such a factor shall be well-defined, have a geographic definition, and may not circumvent any limitation or restriction imposed on one of the other enumerated types.

(8) A credit union service organization (CUSO) is an organization authorized by section 91.801. A consolidated CUSO is one where control or ownership by a credit union requires consolidation of the credit union and CUSO financial statements to comply with Generally Accepted Accounting Principles.

(9) [8] Day--whenever periods of time are specified in this title in days, calendar days are intended. When the day, or the last day fixed by statute or under this title for taking any action falls on Saturday, Sunday, or a state holiday, the action may be taken on the next succeeding day which is not a Saturday, Sunday, or a state holiday.

(10) [9] Department newsletter--the monthly publication that serves as an official notice of all applications, and by which procedures to protest applications are described.

(11) [10] Field of membership (FOM)--refers to the totality of persons a credit union may accept as members. The FOM may consist of one group, several groups with a related community of interest, or several unrelated groups with each having its own community of interest.

(12) [11] Finance Code or Texas Finance Code--the codification of the Texas statutes governing financial institutions, financial businesses, and related financial services, including the regulations and supervision of credit unions.

(13) [12] Imminent danger of insolvency--a circumstance or condition in which a credit union is unable or lacks the means to meet its current obligations as they come due in the regular and ordinary course of business, even if the value of its assets exceeds its liabilities; or the credit union has a positive net worth ratio equal to two percent or less of its assets.

(14) [13] Improved residential property--residential real estate containing on-site, offsite or other improvements sufficient to make the property ready for primarily residential

construction, and real estate in the process of being improved by a building or buildings to be constructed or in the process of construction for primarily residential use.

(15) [14] Interactive teller machine (ITM) -- a video-based interactive technology which allows members to conduct transactions and credit union services driven by a centrally based teller, in a real time video or audio interaction.

(16) [15] Indirect financing--a program in which a credit union makes the credit decision in a transaction where the credit is extended by the vendor and assigned to the credit union or a loan transaction that generally involves substantial participation in and origination of the transaction by a vendor.

(17) [16] Loan-to-value ratio--the aggregate amount of all sums borrowed and secured by the collateral, including outstanding balances plus any unfunded commitment or line of credit from another lender that is senior to the credit union's lien divided by the current value of the collateral.

(18) [17] Loan and extension of credit--a direct or indirect advance of funds to or on behalf of a member based on an obligation of the member to repay the funds or repayable from the application of the specific property pledged by or on behalf of the member. The terminology also includes the purchase of a member's loan or other obligation, a lease financing transaction, a credit sale, a line of credit or loan commitment under which the credit union is contractually obligated to advance funds to or on behalf of a member, an advance of funds to honor a check or share draft drawn on the credit union by a member, or any other indebtedness not classified as an investment security.

(19) [18] Manufactured home--a HUD-code manufactured home as defined by the Texas Manufactured Housing Standards Act. The terminology may also include a mobile home, house trailer, or similar recreational vehicle if the unit will be used as the member's residence and the loan is secured by a first lien on the unit, and the unit meets the requirements for the home mortgage interest deduction under the Internal Revenue Code (26 U.S.C. Section 163(a), (h)(2)(D)).

(20) [19] Market Value--the most probable price which an asset should bring in a competitive and open market under an arm's-length sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of ownership from seller to buyer where:

(A) Buyer and seller are typically motivated;

(B) Both parties are well informed or well advised, and acting in their own best interests;

(C) A reasonable time is allowed for exposure in the open market;

(D) Payment is made in cash in U.S. dollars or in terms of financial arrangements comparable thereto; and

(E) The price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.

(21) [20] Metropolitan Statistical Area (MSA)--a geographic area as defined by the director of the U. S. Office of Management and Budget.

(22) [21] Mobile office--a branch office that does not have a single, permanent site, including a vehicle that travels to various public locations to enable members to conduct their credit union business.

(23) [22] Office--includes any service facility or place of business established by a credit union at which deposits are received, checks or share drafts paid, or money lent. This definition includes a credit union owned branch, a mobile branch, an office operated on a regularly scheduled weekly basis, a credit union owned ATM, or a credit union owned ITM or other electronic facility that meets, at a minimum, these requirements; however, it does not include the credit union's Internet website. This definition also includes a shared branch or a shared branch network if either:

(A) the credit union has an ownership interest in the service facility either directly or through a CUSO or similar organization; or

(B) the service facility is local to the credit union and the credit union is an authorized participant in the service center.

(24) [23] Overlap--the situation which exists when a group of persons is eligible for membership in two or more state, foreign, or federal credit unions doing business in this state. Notwithstanding this provision, no overlap exists if eligibility for credit union membership results solely from a family relationship.

(25) [24] Pecuniary interest -- the opportunity, directly or indirectly, to make money on or share in any profit or benefit derived from a transaction.

(26) [25] Person--an individual, partnership, corporation, association, government, governmental subdivision or agency, business trust, estate, trust, or any other public or private entity.

(27) [26] Principal office--the home office of a credit union.

(28) [27] Protestant--a credit union that opposes or objects to the relief requested by an applicant.

(29) [28] Real estate or real property--an identified parcel or tract of land. The term includes improvements, easements, rights of way, undivided or future interest and similar rights in a tract of land, but does not include mineral rights, timber rights, growing crops, water rights and similar interests severable from the land when the transaction does not involve the associated parcel or tract of land.

(30) [29] Remote service facility--an automated, unstaffed credit union facility owned or operated by, or operated for, the credit union, such as an automated teller machine, cash dispensing machine, point-of-sale terminal, or other remote electronic facility, at which deposits are received, cash dispensed, or money lent.

(31) [30] Reserves--allocations of retained earnings including regular and special reserves, except for any allowances for loan, lease or investment losses.

(32) [31] Resident of this state--a person physically located in, living in or employed in the state of Texas.

(33) [32] Respondent--a credit union or other person against whom a disciplinary proceeding is directed by the department.

(34) [33] Shared service center--a facility which is connected electronically with two or more credit unions so as to permit the facility, through personnel at the facility and the electronic connection, to provide a credit union member at the facility the same credit union services that the credit union member could lawfully obtain at the principal office of the member's credit union.

(35) [34] Secured credit--a loan made or extension of credit given upon an assignment of an interest in collateral pursuant to applicable state laws so as to make the enforcement or promise more certain than the mere personal obligation of the debtor or promisor. Any assignment may include an interest in personal property or real property or a combination thereof.

(36) [35] TAC--an acronym for the Texas Administrative Code, a compilation of all state agency rules in Texas.

(37) [36] Title or 7 TAC--Title 7, Part VI of the Texas Administrative Code Banking and Securities, which contains all of the department's rules.

(38) [37] Underserved area--a geographic area, which could be described as one or more contiguous metropolitan statistical areas (MSA) or one or more contiguous political subdivisions, including counties, cities, and towns, that satisfy any one of the following criteria:

(A) A majority of the residents earn less than 80 percent of the average for all wage earners as established by the U. S. Bureau of Labor Statistics;

(B) The annual household income for a majority of the residents falls at or below 80 percent of the median household income for the State of Texas, or the nation, whichever is higher; or

(C) The commission makes a determination that the lack of available or adequate financial services has adversely <u>affected</u> [effected] economic development within the specified area.

(39) [38] Uninsured membership share--funds paid into a credit union by a member that constitute uninsured capital under conditions established by the credit union and agreed to by the member including possible reduction under §122.105 of the act, risk of loss through operations, or other forfeiture. Such funds shall be considered an interest in the capital of the credit union upon liquidation, merger, or conversion.

(40) [39] Unsecured credit-a loan or extension of credit based solely upon the general credit financial standing of the borrower. The term shall include loans or other extensions of credit supported by the signature of a co-maker, guarantor, or endorser.

(b) The same rules of construction that apply to interpretation of Texas statutes and codes, the definitions in the Act and in Government Code §2001.003, and the definitions in subsection (a) of this section govern the interpretation of this title. If any section of this title is found to conflict with an applicable and controlling provision of other state or federal law, the section involved shall be void to the extent of the conflict without affecting the validity of the rest of this title.

MANDATORY RULE REVIEW

E. (c) Adoption of the Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter H (Relating to Investments), Sections 91.801, 91.802, 91.803, 91.804, 91.805 and 91.808, and Readoption of Rules.

BACKGROUND: Section 2001.039, Government Code, requires that a state agency review and consider for readoption each rule not later than the fourth anniversary of the date on which the rule took effect and every four years after that date. As provided in the noted section, the reviews must include, at a minimum, an assessment by the agency as to whether the reason for adopting the rule continues to exist. At its July 2016 meeting, the Commission approved a plan which establishes a date for the required review for each of the affected rules. In accordance with that plan, staff has reviewed 7 TAC, Part 6, Chapter 91, Subchapter H (Investments) and believes certain revisions are appropriate and necessary. Amendments to the noted chapters are being separately presented for proposal.

Notice of the review and a request for comments on the rules in this chapter was published in the March 15, 2019 issue of the *Texas Register*. No comments were received regarding the review. The Department believes that the reasons for adopting the noted rules continue to exist.

RECOMMENDED ACTION: The Department recommends that the Commission adopt these rules.

RECOMMENDED MOTION: I move that we adopt Rules 91.801, 91.802, 91.803, 91.804, 91.805 and 91.808 without changes to the proposed text as published in the *Texas Register*.

The Credit Union Commission (Commission) has completed its review of Chapter 91, Subchapter H (relating to Investments), of the Texas Administrative Code, Title 7, Part 6, consisting of \S 91.801, 91.802, 91.803, 91.804, 91.805, and 91.808.

The rules were reviewed as a result of the Department's quadrennial rule review under Texas Government Code Section 2001.039.

Notice of the review of 7 TAC, Part 6, Chapter 91, Subchapter H, was published in the March 15, 2019, issue of the *Texas Register* (44 TexReg 1449). The Department received no comments on the notice of intention to review.

After reviewing these rules, the Commission finds that the reasons for initially adopting these rules continue to exist, and readopts Chapter 91, Subchapter H, §§91.801, 91.802, 91.803, 91.804, 91.805, and 91.808, in their entirety in accordance with the requirements of Texas Government Code, Section 2001.039. However, the Commission has determined certain sections should be amended and will propose changes in a separate section of the Texas Register. This concludes the review of 7 TAC, Part 6, Chapter 91, Subchapter H.

The Department hereby certifies that the proposal has been reviewed by legal counsel and found to be a valid exercise of the agency's legal authority.

§91.801. Investments in Credit Union Service Organizations.

(a) Definitions. As used in this section:

(1) A credit union service organization (CUSO) is an organization whose primary purpose is to strengthen or advance the credit union movement, serve or otherwise assist credit unions or their operations, and provide products or services authorized by this section to credit unions and their members.

(2) An investment in a CUSO includes the following:

(A) an investment in the stock, bonds, debentures, or other equity ownership interest of the CUSO; and

(B) loans granted by a third party to the CUSO which are guaranteed in writing by the credit union.

(3) A financing program is a plan, approved by the credit union's board of directors, that provides for multiple extensions of credit to a CUSO during the regular course of business.

(b) Authority. A credit union by itself, or with other parties, may organize, invest in or make loans to a CUSO only if it is structured and operated in a manner that demonstrates to the public that it maintains a legal existence separate from the credit union. A credit union and a CUSO must operate so that:

(1) their respective business transactions, accounts, and records are not intermingled;

(2) each observes the formalities of its separate corporate or other organizational procedures;

(3) each is adequately capitalized as a separate unit in light of normal obligations reasonably foreseeable in a business of its size and character;

(4) each is held out to the public as a separate and distinct enterprise;

(5) all transactions between them are at arm's length and consistent with sound business practices as to each of them;

(6) unless the credit union has guaranteed a loan to the CUSO, all borrowings by the CUSO indicate that the credit union is not liable; and

(7) their respective activities are in compliance with any licensing or registration requirements imposed by applicable federal or state law.

(c) Notice; Authorization; Supplemental Information; Written Objection.

(1) Required Notice. Before committing to any aggregate investment or loan to a CUSO in an amount greater than 15% of the credit union's net worth, a credit union shall provide at least thirty days' written notice to the commissioner of its intent to make or increase its investment in a CUSO, or make a loan to or enter into a financing program with a CUSO. Subject to the net worth threshold, a credit union shall also provide notice of its intent to engage in additional or substitute activities in an existing CUSO or its intent to materially alter an existing loan or financing program with a CUSO. The written notice shall include as applicable:

(A) a description of the organizational and legal structure of the CUSO and the proposed method of capitalizing the organization;

(B) a description of the loan, including the purpose, terms, guarantors, and collateral;

(C) a description of the products or services to be offered by the CUSO and the customer base it will serve;

(D) an explanation of how the CUSO will primarily serve credit unions or members of credit unions, or how the activities of the CUSO could be conducted directly by a credit union or are incidental to the conduct of the business of a credit union; and

(E) a representation that the activities will be conducted in accordance with applicable law, the requirements of this section, and in a manner that will limit exposure of the credit union to no more than the loss of funds invested in, or loaned to, the CUSO.

(2) Authorization to Proceed. If the commissioner issues a non-objection letter, the credit union may proceed with the proposed transaction when it receives the letter. Otherwise, a credit union may proceed with the proposed transaction or the CUSO may engage in the new activities 30 days after the department receives the required notice, unless the commissioner takes one of the following actions before the expiration of that time period:

(A) the commissioner notifies the credit union that it must file additional information supplementing the required notice. If a credit union is required to file additional information, it may proceed with the proposed transaction or the CUSO may engage in the new activities 30 days after the department receives the requested information, unless the commissioner issues a written objection before the expiration of that time period; or

(B) the commissioner notifies the credit union of an objection to the proposed transaction or new activity.

(3) Request for Supplemental Information. A credit union shall provide any additional information reasonably requested by the commissioner.

(4) Action on a Notice. The commissioner shall object to a proposed transaction or activity if the commissioner finds that:

(A) there is inadequate capital to support the proposed transaction or activity;

(B) the proposed transaction or activity does not comply with this section;

(C) the credit union's concentrated exposures to the CUSO give rise to safety and soundness issues; or

(D) the credit union has regulatory or operational deficiencies which would materially affect its ability to properly and effectively manage and monitor the risk associated with the CUSO.

(5) Written Objection. If the commissioner determines that an objection should be interposed, the commissioner will notify the credit union in writing of the determination and the actions the credit union must take to proceed with the proposed transaction or activity. A credit union receiving notification of an objection may appeal the commissioner's finding to the commission in the manner provided by Chapter 93, Subchapter C of this title (relating to Appeals of Preliminary Determinations on Applications).

(d) Limitations. The board of directors of a credit union that organizes, invests in, or lends to any CUSO shall adopt and maintain written policies, which establish appropriate limits and standards for this type of investment including the maximum amount relative to the credit union's net worth, that will be invested in or loaned to any one CUSO. The maximum amount invested in any one CUSO may not exceed the statutory limit established by Texas Finance Code §124.352(b). Total investments in and total loans to CUSOs shall not, in the aggregate, exceed 10% of the total unconsolidated assets of the credit union, unless the credit union receives the prior written approval of the commissioner. The amount of loans to CUSOs, cosigned, endorsed, or otherwise guaranteed by the credit union, shall be included in the aggregate for the purpose of determining compliance with the limitations of this section.

(e) Prohibitions. No credit union may invest in or make loans to a CUSO:

(1) if any officer, director, committee member, or employee of the credit union or any member of the immediate family of such persons owns or makes an investment in or has made or makes a loan to the CUSO;

(2) unless the organization is structured as a corporation, limited liability company, registered limited liability partnership, or limited partnership;

(3) unless the credit union has obtained written legal advice that the CUSO has been designed in a manner that will limit the credit union's potential exposure to no more than the amount of funds invested in or loaned to the CUSO;

(4) if the CUSO engages in any revenue-producing activity other than the performance of services for credit unions or members of credit unions, and such activity equals or exceeds one half (1/2) of the CUSO's total revenue;

(5) unless prior to investing in or making a loan to a CUSO the credit union obtains a written agreement which requires the CUSO to follow GAAP, render financial statements to the credit union at least quarterly, and provide the department, or its representatives, complete access to the CUSO's books and records at reasonable times without undue interference with the business affairs of the CUSO;

(6) unless the CUSO is adequately bonded or insured for its operations;

(7) unless the CUSO obtains an annual opinion audit, by a licensed Certified Public Accountant, on its financial statements in accordance with generally accepted auditing standards, unless the investment in or loan to the CUSO by any one or more credit unions does not exceed \$100,000, or the CUSO is wholly owned and the CUSO is included in the annual consolidated financial statement audit of its parent credit union; or

(8) if any director of the credit union is an employee of the CUSO, or anticipates becoming an employee of the CUSO upon its formation.

(f) Permissible activities and services. The commissioner may, based upon supervisory, legal, or safety and soundness reasons, limit any CUSO activities or services, or refuse to permit any CUSO activities or services. Otherwise, a credit union may invest in or loan to a CUSO that is engaged in providing products and services that include, but are not limited to:

(1) operational services including credit and debit card services, cash services, wire transfers, audits, ATM and other EFT services, share draft and check processing and related services, shared service center operations, electronic data processing, development, sale, lease, or servicing of computer hardware and software, alternative methods of financing and related services, other lending related services, and other services or activity, including consulting, related to the routine daily operations of credit unions;

(2) financial services including financial planning and counseling, securities brokerage and dealer activities, estate planning, tax services, insurance services, administering retirement, or deferred compensation and other employee or business benefit plans;

(3) internet-based or related services including sale and delivery of products to credit unions or members of credit unions; or

(4) any other product, service or activity deemed economically beneficial or attractive to credit unions or credit union members if approved, in writing, by the commissioner.

(g) Compensation. A credit union director, senior management employee, or committee member or immediate family member of any such person may not receive any salary, commission, or other income or compensation, either directly or indirectly, from a CUSO affiliated with their credit union, unless received in accordance with a written agreement between the CUSO and the credit union. The agreement shall describe the services to be performed, the rate of compensation (or a description of the method of determining the amount of compensation) and any other provisions deemed desirable by the CUSO and the credit union. The agreement, and any amendments, must be approved by the board of directors of the credit union and the board of directors (or equivalent governing body) of the CUSO prior to any performance of service or payment and annually thereafter. For purposes of this section, senior management employee shall include the chief executive officer, any assistant chief executiveofficers (vice presidents and

above), and the chief financial officer. Immediate family shall include a person's spouse or any other person living in the same household.

(h) Examination fee. If the commissioner requests a CUSO to make its books and records available for inspection and examination, the CUSO shall pay a supplemental examination fee as prescribed in §97.113(e) of this title (relating to Supplemental examination fees). The commissioner may waive the supplemental examination fee or reduce the fee.

(i) Exception. A credit union which has a net worth ratio greater than six percent (6%) and is deemed adequately capitalized by its insuring organization may make an investment in or make loans to a CUSO that is not limited by the restriction set forth in subsection (e)(4) of this section, provided the activities of the CUSO are limited to activities which could be conducted directly by a credit union or are incidental to the conduct of the business of a credit union. Notwithstanding this exception, all other provisions of the act and this chapter applicable to a CUSO apply. In the event a credit union's net worth declines below the required thresholds, the credit union may not renew, extend the maturity of, or restructure an existing loan, advance additional funds, or increase the investment in the CUSO without the prior written approval of the commissioner.

(j) Change in Valuation. If the limitations established by this section are reached or exceeded solely because of the profitability of the CUSO and the related GAAP valuation of the investment under the equity method, divestiture is not required. A credit union may continue to invest up to the limitation without regard to the increase in the GAAP valuation resulting from a CUSO's profitability.

§91.802. Other Investments.

(a) Definitions. Unless the context clearly indicates otherwise, these words and terms, when used in this section, shall have the following meanings. Any technical words, terms, or phrases that are not specifically defined in this section shall be construed in a manner consistent with the Texas Code of Construction Act (*Tex. Govt. Code §311.001*).

(1) Asset-backed security--A bond, note, or other obligation issued by a financial institution, trust, insurance company, or other corporation secured by either a pool of loans, extensions of credit which are unsecured or secured by personal property, or a pool of personal property leases.

(2) Bailment for hire contract--A contract whereby a third party, bank, or other financial institution, for a fee, agrees to exercise ordinary care in protecting the securities held in safekeeping for its customers; also known as a custodial agreement.

(3) Bankers' acceptance--A time draft that is drawn on and accepted by a bank, and that represents an irrevocable obligation of the bank.

(4) Borrowing repurchase transaction--A transaction whereby a credit union either:

(A) agrees to sell a security to a counterparty and to repurchase the same or any identical security from that counterparty at a future date and at a specified price; or (B) borrows funds from a counterparty and collateralizes the loan with securities owned by the credit union.

(5) Cash forward agreement--An agreement to purchase or sell a security with delivery and acceptance being mandatory and at a future date in excess of 30 days from the trade date.

(6) Counterparty--An entity with which a credit union conducts investment-related activities in such a manner as to create a credit risk exposure for the credit union to the entity.

(7) Eurodollar deposit--A deposit denominated in U. S. dollars in a foreign branch of a United States financial institution.

(8) Federal funds transaction--A short-term or open-ended transfer of funds to a financial institution.

(9) Financial institution--A bank or savings association, the deposits of which are insured by the Federal Deposit Insurance Corporation, a federal or state-chartered credit union, or the National Credit Union Central Liquidity Facility.

(10) Investment--Any security, obligation, account, deposit, or other item authorized for investment by the Act or this section. For the purposes of this section, the term does not include an investment authorized by $\frac{124.351(a)(1)}{10}$ of the Texas Finance Code.

(11) Investment repurchase transaction--A transaction in which a credit union agrees to purchase a security from a counterparty and to resell the same or any identical security to that counterparty at a later date and at a specified price.

(12) Mortgage related security--A security which meets the definition of mortgage related security in United States Code Annotated, Title 15, §78c(a)(41).

(13) Nationally recognized statistical rating organization (NRSRO)--A rating organization such as Standard and Poor's, Moody's, or Fitch which is recognized by the Securities and Exchange Commission

(14) Ordinary care--The degree of care, which an ordinarily prudent and competent person engaged in the same line of business or endeavor should exercise under similar circumstances.

(15) Security--An investment that has a CUSIP number or that is represented by a share, participation, or other interest in property or in an enterprise of the issuer or an obligation of the issuer that:

(A) either is represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer;

(B) is of a type commonly traded on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or traded as a medium for investment; and

(C) either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

(16) Settlement date--The date originally agreed to by a credit union and a vendor for settlement of the purchase or sale of a security.

(17) Small business-related securities -- is a security as defined in Section 3(a)(53) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(53). This definition does not include Small Business Administration securities permissible under section 107(7) of the Federal Credit Union Act.

(18) Trade date--The date a credit union originally agrees, whether orally or in writing, to enter into the purchase or sale of a security.

(19) Yankee dollar deposit--A deposit in a United States branch of a foreign bank, the deposits of which are insured by the Federal Deposit Insurance Corporation, that is licensed to do business in the state in which it is located, or a deposit in a state chartered, foreign controlled bank.

(b) Policy. A credit union may invest funds not used in loans to members, subject to the conditions and limitations of the written investment policy of the board of directors. The investment policy may be part of a broader, asset-liability management policy. The board of directors must review and approve the investment policy at least annually to ensure that the policies adequately address the following issues:

(1) The types of investments that are authorized to be purchased.

(2) The aggregate limit on the amount that may be invested in any single investment or investment type, set as a percentage of net worth. This requirement does not apply to certificates of deposit or other accounts issued by a financial institution that are fully insured (including accumulated interest) by either the Federal Deposit Insurance Corporation or the National Credit Union Administration. (3) The delegation of investment authority to the credit union's officials or employees, including the person or persons authorized to purchase or sell investments, and a limit of the investment authority for each individual or committee.

(4) The authorized broker-dealers or other third-parties that may be used to purchase or sell investments, and the internal process for assessing the credentials and previous record of the individual or firm.

(5) The risk management framework given the level of risk in the investment portfolio. This will include specific methods for evaluating, monitoring, and managing the credit risk, interest-rate risk, and liquidity risk from the investment activities.

(6) The authorized third-party safekeeping agents.

(7) If the credit union operates a trading account, the policy shall specify the persons authorized to engage in trading account activities, trading account size limits, stop loss and sale provisions, time limits on inventoried trading account investments, and internal controls that specify the segregation of risk-taking and monitoring activities related to trading account activities.

(8) The procedure for reporting to the board of directors investments and investment activities that become noncompliant with the credit union's investment policy subsequent to the initial purchase.

(c) Authorized activities.

(1) General authority. A credit union may contract for the purchase or sale of a security provided that delivery of the security is by regular-way settlement. Regular-way settlement means delivery of a security from a seller to a buyer within the time frame that the securities industry has established for that type of security. All purchases and sales of investments must be delivery versus payment (i.e., payment for an investment must occur simultaneously with its delivery).

(2) Cash forward agreements. A credit union may enter into a cash forward agreement to purchase or sell a security, provided that:

(A) the period from the trade date to the settlement date does not exceed 90 days;

(B) if the credit union is the purchaser, it has written cash flow projections evidencing its ability to purchase the security;

(C) if the credit union is the seller, it owns the security on the trade date; and

(D) the cash forward agreement is settled on a cash basis at the settlement date.

(3) Investment repurchase transactions. A credit union may enter an investment repurchase transaction provided:

(A) the purchase price of the security obtained in the transaction is at or below the market price;

(B) the repurchase securities are authorized investments under Texas Finance Code §124.351 or this section;

(C) the credit union has entered into signed contracts with all approved counterparties;

(D) the counterparty is rated in one of the three highest long-term or counterparty rating categories by a NRSRO; and

(E) the credit union receives a daily assessment of the market value of the repurchase securities, including accrued interest, and maintains adequate margin that reflects a risk assessment of the repurchase securities and the term of the transaction.

(4) Borrowing repurchase transactions. A credit union may enter into a borrowing repurchase transaction, which is a borrowing transaction subject to §123.201 of the Texas Finance Code, provided:

(A) any investments purchased by the credit union with either borrowed funds or cash obtained by the credit union in the transaction are authorized investments under Texas Finance Code §124.351 and this section;

(B) the credit union has entered into signed contracts with all approved counterparties; and

(C) investments referred to in subparagraph (A) of this paragraph mature no later than the maturity date of the borrowing repurchase transaction; and

(D) the counterparty is rated in one of the three highest long-term or counterparty rating categories by a NRSRO.

(5) Federal funds. A credit union may enter into a federal funds transaction with a financial institution, provided that the interest or other consideration received from the financial institution is at the market rate for federal funds transactions and that the transaction has a maturity of one or more business days or the credit union is able to require repayment at any time.

(6) Yankee dollars. A credit union may invest in yankee dollar deposits.

(7) Eurodollars. A credit union may invest in eurodollar deposits.

(8) Bankers' acceptance. A credit union may invest in bankers' acceptances.

(9) Open-end Investment Companies (Mutual Funds). A credit union may invest funds in an open-end investment company established for investing directly or collectively in any investment or investment activity that is authorized under Texas Finance Code §124.351 and this section, including qualified money market mutual funds as defined by Securities and Exchange Commission regulations.

(10) U.S. Government-sponsored enterprises. A credit union may invest in obligations of U.S. Government sponsored enterprises such as, for example: the Federal Home Loan Bank System, the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, and the Federal Farm Credit Bank.

(11) Commercial paper. A credit union may invest in commercial paper issued by a corporation domiciled within the United States and having a short-term or commercial paper rating of no less than A1 or P1 by Standard & Poor's or Moody's, respectively, or an equivalent rating by a NRSRO.

(12) Corporate bonds. A credit union may invest in corporate bonds issued by a corporation domiciled in the United States. The bonds must be rated by a NRSRO in one of the two highest long-term rating categories and have remaining maturities of seven years or less.

(13) Municipal bonds. A credit union may invest in municipal bonds rated by a NRSRO in one of the two highest long-term rating categories with remaining maturities of seven years or less.

(14) Mortgage-related securities. With the exception of the residual interest of the mortgage-related security, a credit union may invest in mortgage-related securities backed by mortgages secured by real estate upon which is located a residential dwelling, a mixed residential and commercial structure, or a residential manufactured home. The security must be rated by a NRSRO in one of the two highest long-term rating categories.

(15) Asset-backed securities. Provided the underlying collateral is domestic- and consumer-based, a credit union may invest in asset-backed securities which are rated by a NRSRO in one of the two highest long-term rating categories.

(16) Small business-related securities. A credit union may invest in small business-related securities that represent an interest in one or more promissory notes or leases of personal property evidencing the obligation of a domestic small business concern and originated by a financial institution, insurance company, or similar institution which is regulated and supervised by a Federal or State authority. The securities must be rated by a NRSRO in one of the two highest long-term rating categories and have remaining maturities of seven years or less.

(17) Derivative authority. A credit union may enter into certain derivative transactions exclusively for the purpose of decreasing interest rate risk. The transaction is used to manage risk arising from otherwise permissible credit union activities and not entered into for speculative purposes. Permissible derivatives include interest rate swaps, options on swaps, interest rate caps,

interest rate floors, and Treasury futures. Derivative authority is restricted to the provisions outlined under Subpart B of Part 703 of the National Credit Union Administration Rules and Regulations.

(d) Documentation. A credit union shall maintain files containing credit and other information adequate to demonstrate evidence of prudent business judgment in exercising the investment powers under the Act and this rule including:

(1) Except for investments that are issued, insured or fully guaranteed as to principal and interest by the U.S. Government or its agencies, enterprises, or corporations or fully insured (including accumulated interest) by the National Credit Union Administration or the Federal Deposit Insurance Corporation, a credit union must conduct and document a credit analysis of the issuing entity and/or investment before purchasing the investment. The credit union must update the credit analysis at least annually as long as the investment is held.

(2) Credit and other due diligence documentation for each investment shall be maintained as long as the credit union holds the investment and until it has been both audited and examined. Before purchasing or selling a security, a credit union must obtain either price quotations on the security (or a similarly-structured security) from at least two broker-dealers or a price quotation on the security (or similarly-structured security) from an industry-recognized information provider. If a credit union is unable to obtain a price quotation required by this subsection for a particular security, then it can compare prices using nominal or option-adjusted spreads, or spreads to TBA (to-beannounced) mortgage backed securities. This requirement to obtain a price quotation does not apply to new issues purchased at par or at original issue discount.

(3) The reference to and use of NRSRO credit ratings in this rules provides a minimum threshold and is not an endorsement of the quality of the ratings. Credit unions must conduct their own independent credit analyses to determine that each security purchased presents an acceptable credit risk, regardless of the rating.

(e) Classification. A credit union must classify a security as hold-to-maturity, available-for-sale, or trading, in accordance with generally accepted accounting principles and consistent with the credit union's documented intent and ability regarding the security.

(f) Purchase or Sale of Investments Through a Third-Party.

(1) A credit union may purchase and sell investments through a broker-dealer as long as the broker-dealer is registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) or is a financial institution whose broker-dealer activities are regulated by a federal or state regulatory agency.

(2) Before purchasing an investment through a broker-dealer, a credit union must analyze and annually update the following information.

(A) The background of the primary sales representative and the local broker-dealer firm with whom the credit union is doing business, using information available from federal or state securities regulators and securities industry self-regulatory organizations, such as the Financial Industry Regulatory Authority and the North American Securities Administrators Association, about any enforcement actions against the broker-dealer firm, its affiliates, or associated personnel.

(B) If the broker-dealer is acting as the credit union's counterparty, the ability of the broker-dealer and its subsidiaries or affiliates to fulfill commitments, as evidenced by capital strength, liquidity, and operating results. The credit union should consider current financial data, annual reports, long-term or counterparty ratings that have been assigned by NRSROs, reports of NRSROs, relevant disclosure documents such as annual independent auditor reports, and other sources of financial information.

(3) Paragraphs (1) and (2) of this subsection do not apply when a credit union purchases a certificate of deposit or share certificate directly from a bank, credit union, or other financial institution.

(g) Discretionary Control Over Investments and Investment Advisers.

(1) Except as provided in paragraph (2) of this subsection, a credit union must retain discretionary control over its purchase and sale of investments. A credit union has not delegated discretionary control to an investment adviser when the credit union reviews all recommendations from the investment adviser and is required to authorize a recommended purchase or sale transaction before its execution.

(2) A credit union may delegate discretionary control over the purchase and sale of investments in an aggregate amount not to exceed 100% of its net worth at the time of delegation to persons other than the credit union's officials or employees, provided each such person is an investment adviser registered with the Securities and Exchange Commission under the Investment Advisers Act of 1940 (15 U.S.C. 80b).

(3) Before transacting business with an investment adviser to which discretionary control has been granted, and annually thereafter, a credit union must analyze the adviser's background and information available from federal and state securities regulators and securities industry self-regulatory organizations, including any enforcement actions against the adviser, associated personnel, and the firm for which the adviser works.

(4) A credit union may not compensate an investment adviser with discretionary control over the purchase and sale of investments on a per transaction basis or based on capital gains, capital appreciation, net income, performance relative to an index, or any other incentive basis.

(5) A credit union must obtain a report from its investment adviser at least monthly that details the investments under the adviser's control and their performance.

(h) Investment Practice Permitted to Federal Credit Unions.

If an applicant credit union proposes to make the same type of investment which a federally chartered credit union has been granted permission to make, the commissioner shall grant the application unless the commissioner finds that due to the financial position or the state of management of the applicant credit union, the proposed investments or deposits would not be sound or prudent investment practices for the applicant credit union. The commissioner may instead grant the application conditionally, grant in modified form, or deny the application.

(i) Modification or Revocation of Investment Authority.

If the commissioner finds that due to the financial condition or management of a credit union, an investment practice authorized by this section has ceased to be a safe and prudent practice, the commissioner shall inform the board of directors of the credit union, in writing, that the authority to engage in the practice has been revoked or modified. The credit union's directors and management shall immediately take steps to begin liquidating the investments in question or make the modification required by the commissioner. The commissioner for cause shown may grant the credit union a definite period of time to comply with the commissioner's orders. Credit unions which continue to engage in investment practices after their authority to do so has been revoked or modified will be treated as if the authority to engage in the practice had never been granted, and their actions may be deemed an unsound practice and a willful violation of an order of the commissioner and may be grounds for appropriate supervisory action against the credit union, its directors or officers.

(j) Waivers.

(1) The commissioner in the exercise of discretion may grant a written waiver, consistent with safety and soundness principles, of a requirement or limitation imposed by this subchapter. A decision to deny a waiver is not subject to appeal. A waiver request must contain the following:

- (A) A copy of the credit union's investment policy;
- (B) The higher limit or ratio sought;
- (C) An explanation of the need to raise the limit or ratio; and
- (D) Documentation supporting the credit union's ability to manage this activity;

(2) In determining action on a waiver request made under this subsection, the commissioner will consider the:

(A) Credit union's financial condition and management, including compliance with regulatory net worth requirements. If significant weaknesses exist in these financial and managerial factors, the waiver normally will be denied.

(B) Adequacy of the credit union's policies, practices, and procedures. Correction of any deficiencies may be included as conditions, as appropriate, if the waiver is approved.

(C) Credit union's record of investment performance. If the credit union's record of performance is less than satisfactory or otherwise problematic, the waiver normally will be denied.

(D) Credit union's level of risk. If the level of risk poses safety and soundness problems or material risks to the insurance fund, the waiver normally will be denied.

§91.803. Investment Limits and Prohibitions.

(a) Limitations. With the exception of deposits held by a Federal Reserve Bank, a credit union may invest no more than 50% of its net worth with any single obligor or related obligors. This limitation also does not apply to the extent that the investment is insured or guaranteed by the United States government, or an agency, sponsored enterprise, corporation, or instrumentality of the United States government, or to any trust or trusts established for investing, directly or collectively, in such securities, obligations, or instruments. For the purposes of this section, obligor is defined as an issuer, trust, or originator of an investment, including the seller of a loan participation.

(b) Designated Depository. As a single exception to subsection (a) of this section, a credit union's board of directors may establish the maximum aggregate deposit limit for a single financial institution approved by the board as the credit union's designated depository. This deposit limit shall be a percentage of net worth and must be based on the credit union's liquidity trends and funding needs as documented by its asset/liability management policy. This authority is contingent upon the credit union appropriately documenting its due diligence to demonstrate that the investments in this designated depository do not pose a safety and soundness concern. The credit union's board of directors shall review and approve at least annually the maximum aggregate deposit limit for its designated depository. The review shall include a current due diligence analysis of the financial institution.

- (c) Prohibited Activities.
 - (1) Definitions.

(A) Adjusted trading--selling an investment to a counterparty at a price above its current fair value and simultaneously purchasing or committing to purchase from the counterparty another investment at a price above its current fair value.

(B) Collateralized mortgage obligation (CMO)--a multi-class bond issue collateralized by mortgages or mortgage-backed securities.

(C) Commercial mortgage related security--a mortgage related security except that it is collateralized entirely by commercial real estate, such as a warehouse or office building, or a multi-family dwelling consisting of more than four units.

(D) Fair value--the price at which a security can be bought or sold in a current, arm's length transaction between willing parties, other than in a forced or liquidation sale.

(E) Real estate mortgage investment conduit (REMIC)--a nontaxable entity formed for the sole purpose of holding a fixed pool of mortgages secured by an interest in real property and issuing multiple classes of interests in the underlying mortgages.

(F) Residual interest--the remainder cash flows from a CMO/REMIC, or other mortgage-backed security transaction, after payments due bondholders and trust administrative expenses have been satisfied.

(G) Short sale--the sale of a security not owned by the seller.

(H) Stripped mortgage-backed security--a security that represents either the principal-only or the interest-only portion of the cash flows of an underlying pool of mortgages or mortgage-backed securities.

(I) Zero coupon investment--an investment that makes no periodic interest payments but instead is sold at a discount from its face value. The holder of a zero coupon investment realizes the rate of return through the gradual appreciation of the investment, which is redeemed at face value on a specified maturity date.

(2) A credit union may not:

(A) Use financial derivatives for replication, or for any purposes other than hedging;

(B) Engage in adjusted trading or short sales;

(C) Purchase stripped mortgage backed securities;

(D) Purchase residual interests in CMOs/REMICs, or other structured mortgage backed securities;

(E) Purchase mortgage servicing rights as an investment but may retain mortgage servicing rights on a loan originated by the credit union and sold on the secondary market;

(F) Purchase commercial mortgage related securities of an issuer other than a U.S. Government sponsored enterprise;

(G) Purchase any security that has the capability of becoming a first credit loss piece which supports another more senior security;

(H) Purchase a zero coupon investment with a maturity date that is more than 10 years from the settlement date;

(I) Purchase investments whereby the underlying collateral consists of foreign receivables or foreign deposits;

(J) Purchase securities used as collateral by a safekeeping concern;

(K) Purchase exchangeable mortgage backed securities, unless they are fully compliant with the provisions outlined in Part 703 of the National Credit Union Administration Rules and Regulations; or

(L) Purchase securities convertible into stock at the option of the issuer.

(d) Investment pilot program.

(1) The commissioner may authorize a limited number of credit unions to engage in other types of investment activities under an investment pilot program. A credit union wishing to participate in an investment pilot program shall submit a request that addresses the following items:

(A) Board policies approving the activities and establishing limits on them;

(B) A complete description of the activities, with specific examples of how the credit union will conduct them and how they will benefit the credit union;

(C) A demonstration of how the activities will affect the credit union's financial performance, risk profile, and asset-liability management strategies;

(D) Examples of reports the credit union will generate to monitor the activities;

(E) A projection of the associated costs of the activities, including personnel, computer, audit, etc.;

(F) A description of the internal systems to measure, monitor, and report the activities, and the qualifications of the staff and/or official(s) responsible for implementing and overseeing the activities; and

(G) The internal control procedures that will be implemented, including audit requirements.

(2) In connection with a request to participate in an investment pilot program, the commissioner will consider the general nature and functions of credit unions, as well as the specific

financial condition and management of the applicant credit union, as revealed in the request, examinations, or such other information as may be available to the commissioner. The commissioner may approve the request, approve the request conditionally, approve it in modified form, or deny it in whole or in part. A decision by the commissioner concerning participation in an investment pilot program is not appealable.

(3) The commissioner may find that an investment pilot program previously authorized is no longer a safe and prudent practice for credit unions generally to engage in, or has become inconsistent with applicable state or federal law, or has ceased to be a safe and prudent practice for one or more particular credit unions in light of their financial condition or management. Upon such a finding, the commissioner will send written notice informing the board of directors of any or all of the credit unions engaging in such a practice that the authority to engage in the practice has been revoked or modified. When the commissioner so notifies any credit union, its directors and officers shall forthwith take steps to liquidate the investments in question or to make such modifications as the commissioner requires. Upon demonstration of good cause, the commissioner may grant a credit union some definite period of time in which to arrange its affairs to comply with the commissioner's direction. Credit unions which continue to engage in investment practices where their authority to do so has been revoked or modified will be deemed to be engaging in an unsound practice.

§91.804. Custody And Safekeeping.

(a) A credit union's purchased investments and repurchased collateral must be in its possession, recorded as owned by the credit union through the federal reserve book-entry system, or be held by a board-approved safekeeper under a bailment for hire contract or a custodial arrangement subject to regulation by the Securities and Exchange Commission. Any safekeeper used by a credit union must be regulated and supervised by either the Securities and Exchange Commission or a federal or state financial institution regulatory agency. For the purposes of this section a bailment for hire contract has the same meaning as in §91.802 (relating to Other Investments). Annually, a credit union must analyze the ability of any safekeeper used by the credit union to fulfill its custodial responsibilities, as evidenced by capital strength and financial conditions. The credit union should consider current financial data, annual reports, reports of nationally-recognized statistical rating organizations (NRSROs), relevant disclosure documents such as annual independent auditor reports, and other sources of financial information. At least monthly, a credit union must obtain and reconcile a statement of purchased investments and repurchased collateral held in safekeeping.

(b) A credit union that invests funds in a certificate of deposit in a financial institution as defined in §91.802 (relating to Other Investments) shall hold such certificate of deposit in the name of the credit union or, if held by a safekeeper or registered broker-dealer, in the safekeeper's or registered broker-dealer's name as custodial nominee for a credit union. Any certificate of deposit held by a safekeeper or registered broker-dealer as custodial nominee for a credit union or the credit union's registered broker or dealer must be eligible for extended or flow-through insurance coverage to the credit union through either the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund.

§91.805. Loan Participation Investments.

(a) A credit union may purchase a participation interest in a loan, where the borrower is neither a member of the credit union or a member of another participating credit union, as permitted by \$124.351(a)(8) of the Texas Finance Code, provided the following conditions are satisfied:

(1) the purchase complies with all regulatory requirements to the same extent as if the credit union had originated the loan;

(2) the originating lender retains at least 10 percent of the outstanding balance of the loan through the life of the loan;

(3) the purchase complies with the credit union's investment policy, which, at a minimum, must:

(A) establish the same degree of independent credit and collateral analysis as if the credit union was the originator; and

(B) establish commitment limits for aggregate purchased participations, out-ofarea participations, and loans originated by individual lead institutions.

(4) the written loan participation agreement fully describes the lead institution's responsibilities, establishes requirements for obtaining timely borrower credit information, addresses remedies upon default, and outlines dispute resolution procedures.

(b) Financial Reporting. A participation interest in a non-credit union member loan purchased under this section shall be reported in accordance with generally accepted accounting principles.

(c) Other Requirements. A credit union purchasing a loan participation investment must also comply with applicable requirements contained within Part 741 of the National Credit Union Administration Rules and Regulations.

§91.808. Reporting Investment Activities to the Board of Directors.

(a) A credit union shall provide its board of directors a monthly comprehensive report of investment activities, including:

(1) investments purchased and sold during the month;

(2) unrealized market gains or losses compared to book value for each security at month's end;

- (3) fair or market value of each security;
- (4) total book value of investments outstanding at month's end;
- (5) unrecorded and unreported obligations to buy or sell investments; and

(6) amount of investments, other than deposits and investments in designated depositories, that are not either issued by, or fully guaranteed as to principal and interest by, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the United States or any agency, enterprise, corporation, or instrumentality of the United States, or in any trust or trusts established for investing, directly or collectively, in such securities, obligations or instruments.

(b) The credit union shall also provide a quarterly report to the board of directors that summarizes the volatility of the entire security portfolio, if the aggregate amount of securities with one or more of the features included below exceeds the credit union's net worth:

- (1) embedded options;
- (2) remaining maturities greater than three years; or

(3) coupon formulas that are related to more than one index or are inversely related to, or multiples of, an index.

(c) The report described in subsection (b) of this section must provide a reasonable and supportable estimate of the potential impact, in percentage and dollar terms, of an immediate and sustained parallel shift in market interest rates of plus and minus 300 basis points on the:

- (1) fair value of each security in the entire portfolio;
- (2) fair value of the entire security portfolio as a whole; and
- (3) credit union's net worth.

(d) For the purposes of this section, an embedded option means a characteristic of an investment that gives the issuer or holder the right to alter the level and timing of the cash flows of the investment. Embedded options include call and put provisions and interest rate caps and floors. Since a prepayment option in a mortgage is a type of call provision, a mortgage-backed security composed of mortgages that may be prepaid is an example of an investment with an embedded option.

INVESTMENTS IN CREDIT UNION SERVICE ORGANIZATIONS

E. (d) Proposed Amendments to 7 TAC Section 91.801 Concerning Investments in Credit Union Service Organizations.

BACKGROUND: The proposed amendment would authorize investments in certain CUSOs to the extent they are providing property management services. The language is presented to clearly document state credit union authority to invest in CUSOs providing property management services. The authority is provided through parity provisions found within TFC Section 123.003, as that authority is available to federal credit unions under NCUA Rules and Regulations 12 C.F.R. Part 712(g).

RECOMMENDED ACTION: The Department recommends that the Commission approve for publication and comment the proposed amendments to 7 TAC Section 91.801.

RECOMMENDED MOTION: I move that we approve for publication and comment in the *Texas Register* the proposed amendments to 7 TAC Section 91.801.

TITLE 7.	BANKING AND SECURITIES
Part 6.	Credit Union Department
Chapter 91.	Chartering, Operations, Mergers, Liquidations
Subchapter H.	Investments
Rule §91.801	Investments in Credit Union Service Organizations

The Credit Union Commission (the Commission) proposes amendments to Section 91.801, relating to Investments in Credit Union Service Organizations. The proposed amendment would make state rules consistent with the federal regulations governing the authority of Credit Union Service Organizations (CUSOs) that provide property management services. The federal regulations are found at 12 C.F.R. Part 712.5(g). The amendment complies with the parity provisions of Texas Finance Code (TFC) Section 123.003.

The Commission proposes the following amendment to Section 91.801. The language is presented to clearly document state credit union authority to invest in CUSOs providing property management services. The authority is provided through parity provisions found within TFC Section 123.003, as that authority is available to federal credit unions under NCUA Rules and Regulations 12 C.F.R. Part 712.5(g).

The commissioner finds, in accordance with Texas Finance Code section 123.003(b), that exercise of those powers or authorities is convenient for and affords an advantage to the credit union's members and maintains the fairness of competition and parity between the credit union and any foreign credit union.

FISCAL NOTE ON STATE AND LOCAL GOVERNMENTS. John J. Kolhoff, Commissioner, has determined that for the first five-year period the proposed amendments are in effect, there are no reasonably foreseeable implications relating to cost or revenues of state or local governments, under Government Code §2001.024(a)(4), as a result of enforcing or administering these amendments, as proposed.

PUBLIC BENEFIT/COST NOTE. Mr. Kolhoff has determined, under Government Code §2001.024(a)(5) that for the first five-year period the amended rules are in effect, the public benefit of rule clarity will provide improved guidance to the industry. He further has determined there will be no probable economic cost to the credit union system or to persons required to comply with the rule.

IMPACT ON LOCAL EMPLOYMENT OR ECONOMY. There is no reasonably forecasted effect on local economy for the first five years that the proposed amendments are in effect. Therefore, no economic impact statement, local employment impact statement, nor regulatory flexibility analysis is required under Texas Government Code §§2001.022 or 2001.024(a)(6).

COST TO REGULATED PERSONS (COST-IN/COST-OUT). This rule proposal is not subject to Texas Government Code §2001.0045, concerning increasing costs to regulated persons, because this agency is a Self-Directed Semi-Independent (SDSI) agency under Finance Code Chapter 16 and is exempt from that cost provision.

ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS FOR SMALL BUSINESSES, MICROBUSINESSES, AND RURAL COMMUNITIES. Mr. Kolhoff

has also determined that for each year of the first five years the proposed amendment is in effect, there will be no reasonably forecasted adverse economic effect on small businesses, microbusinesses, or rural communities as a result of implementing these amendments, and, therefore, no regulatory flexibility analysis, as specified in Texas Government Code §2006.002 is required.

GOVERNMENT GROWTH IMPACT STATEMENT. In compliance with Texas Government Code §2001.0221, the Board has prepared a government growth impact statement.

Unless indicated below, for each year of the first five years that the rule will be in effect, the rule will not:

- create or eliminate a government program;
- require the creation of new employee positions or the elimination of existing employee positions;
- require an increase or decrease in future legislative appropriations to the agency;
- lead to an increase or decrease in the fees paid to the department;
- create new regulations;
- expand, limit or repeal existing regulation
- increase or decrease the number of individuals subject to the rule's applicability;
- positively or adversely affect this state's economy.

TAKINGS IMPACT ASSESSMENT. No private real property interests are affected by this proposal, and the proposal does not restrict or limit an owner's right to his or her property that would otherwise exist in the absence of government action. Therefore, the rule does not constitute a taking under Texas Government Code §2007.043.

REQUEST FOR PUBLIC COMMENT. Written comments on the proposed amendments may be submitted in writing to John J. Kolhoff, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register*.

STATUTORY AUTHORITY. The amendments are proposed pursuant to Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Texas Finance Code, Title 2, Chapter 15 and Title 3, Subtitle D.

STATUTORY SECTIONS AFFECTED. The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Chapter 15 and Title 3, Subtitle D.

LEGAL REVIEW. The Commission certifies that the proposed rule has been reviewed by legal counsel and has been found to be within the agency's authority to adopt.

Subchapter H. Investments

§91.801. Investments in Credit Union Service Organizations.

(a) Definitions. As used in this section:

(1) A credit union service organization (CUSO) is an organization whose primary purpose is to strengthen or advance the credit union movement, serve or otherwise assist credit unions or their operations, and provide products or services authorized by this section to credit unions and their members.

(2) An investment in a CUSO includes the following:

(A) an investment in the stock, bonds, debentures, or other equity ownership interest of the CUSO; and

(B) loans granted by a third party to the CUSO which are guaranteed in writing by the credit union.

(3) A financing program is a plan, approved by the credit union's board of directors, that provides for multiple extensions of credit to a CUSO during the regular course of business.

(b) Authority. A credit union by itself, or with other parties, may organize, invest in or make loans to a CUSO only if it is structured and operated in a manner that demonstrates to the public that it maintains a legal existence separate from the credit union. A credit union and a CUSO must operate so that:

(1) their respective business transactions, accounts, and records are not intermingled;

(2) each observes the formalities of its separate corporate or other organizational procedures;

(3) each is adequately capitalized as a separate unit in light of normal obligations reasonably foreseeable in a business of its size and character;

(4) each is held out to the public as a separate and distinct enterprise;

(5) all transactions between them are at arm's length and consistent with sound business practices as to each of them;

(6) unless the credit union has guaranteed a loan to the CUSO, all borrowings by the CUSO indicate that the credit union is not liable; and

(7) their respective activities are in compliance with any licensing or registration requirements imposed by applicable federal or state law.

(c) Notice; Authorization; Supplemental Information; Written Objection.

(1) Required Notice. Before committing to any aggregate investment or loan to a CUSO in an amount greater than 15% of the credit union's net worth, a credit union shall provide at least thirty days' written notice to the commissioner of its intent to make or increase its investment in a CUSO, or make a loan to or enter into a financing program with a CUSO. Subject to the net worth threshold, a credit union shall also provide notice of its intent to engage in additional or substitute activities in an existing CUSO or its intent to materially alter an existing loan or financing program with a CUSO. The written notice shall include as applicable:

(A) a description of the organizational and legal structure of the CUSO and the proposed method of capitalizing the organization;

(B) a description of the loan, including the purpose, terms, guarantors, and collateral;

(C) a description of the products or services to be offered by the CUSO and the customer base it will serve;

(D) an explanation of how the CUSO will primarily serve credit unions or members of credit unions, or how the activities of the CUSO could be conducted directly by a credit union or are incidental to the conduct of the business of a credit union; and

(E) a representation that the activities will be conducted in accordance with applicable law, the requirements of this section, and in a manner that will limit exposure of the credit union to no more than the loss of funds invested in, or loaned to, the CUSO.

(2) Authorization to Proceed. If the commissioner issues a non-objection letter, the credit union may proceed with the proposed transaction when it receives the letter. Otherwise, a credit union may proceed with the proposed transaction or the CUSO may engage in the new activities 30 days after the department receives the required notice, unless the commissioner takes one of the following actions before the expiration of that time period:

(A) the commissioner notifies the credit union that it must file additional information supplementing the required notice. If a credit union is required to file additional information, it may proceed with the proposed transaction or the CUSO may engage in the new activities 30 days after the department receives the requested information, unless the commissioner issues a written objection before the expiration of that time period; or

(B) the commissioner notifies the credit union of an objection to the proposed transaction or new activity.

(3) Request for Supplemental Information. A credit union shall provide any additional information reasonably requested by the commissioner.

(4) Action on a Notice. The commissioner shall object to a proposed transaction or activity if the commissioner finds that:

(A) there is inadequate capital to support the proposed transaction or activity;

(B) the proposed transaction or activity does not comply with this section;

(C) the credit union's concentrated exposures to the CUSO give rise to safety and soundness issues; or

(D) the credit union has regulatory or operational deficiencies which would materially affect its ability to properly and effectively manage and monitor the risk associated with the CUSO.

(5) Written Objection. If the commissioner determines that an objection should be interposed, the commissioner will notify the credit union in writing of the determination and the actions the credit union must take to proceed with the proposed transaction or activity. A credit union receiving notification of an objection may appeal the commissioner's finding to the commission in the manner provided by Chapter 93, Subchapter C of this title (relating to Appeals of Preliminary Determinations on Applications).

(d) Limitations. The board of directors of a credit union that organizes, invests in, or lends to any CUSO shall adopt and maintain written policies, which establish appropriate limits and standards for this type of investment including the maximum amount relative to the credit union's net worth, that will be invested in or loaned to any one CUSO. The maximum amount invested in any one CUSO may not exceed the statutory limit established by Texas Finance Code §124.352(b). Total investments in and total loans to CUSOs shall not, in the aggregate, exceed 10% of the total unconsolidated assets of the credit union, unless the credit union receives the prior written approval of the commissioner. The amount of loans to CUSOs, cosigned, endorsed, or otherwise guaranteed by the credit union, shall be included in the aggregate for the purpose of determining compliance with the limitations of this section.

(e) Prohibitions. No credit union may invest in or make loans to a CUSO:

(1) if any officer, director, committee member, or employee of the credit union or any member of the immediate family of such persons owns or makes an investment in or has made or makes a loan to the CUSO;

(2) unless the organization is structured as a corporation, limited liability company, registered limited liability partnership, or limited partnership;

(3) unless the credit union has obtained written legal advice that the CUSO has been designed in a manner that will limit the credit union's potential exposure to no more than the amount of funds invested in or loaned to the CUSO;

(4) if the CUSO engages in any revenue-producing activity other than the performance of services for credit unions or members of credit unions, and such activity equals or exceeds one half (1/2) of the CUSO's total revenue;

(5) unless prior to investing in or making a loan to a CUSO the credit union obtains a written agreement which requires the CUSO to follow GAAP, render financial statements to the credit union at least quarterly, and provide the department, or its representatives, complete access to the CUSO's books and records at reasonable times without undue interference with the business affairs of the CUSO;

(6) unless the CUSO is adequately bonded or insured for its operations;

(7) unless the CUSO obtains an annual opinion audit, by a licensed Certified Public Accountant, on its financial statements in accordance with generally accepted auditing standards, unless the investment in or loan to the CUSO by any one or more credit unions does not exceed \$100,000, or the CUSO is wholly owned and the CUSO is included in the annual consolidated financial statement audit of its parent credit union; or

(8) if any director of the credit union is an employee of the CUSO, or anticipates becoming an employee of the CUSO upon its formation.

(f) Permissible activities and services. The commissioner may, based upon supervisory, legal, or safety and soundness reasons, limit any CUSO activities or services, or refuse to permit any CUSO activities or services. Otherwise, a credit union may invest in or loan to a CUSO that is engaged in providing products and services that include, but are not limited to:

(1) operational services including credit and debit card services, cash services, wire transfers, audits, ATM and other EFT services, share draft and check processing and related services, shared service center operations, electronic data processing, development, sale, lease, or servicing of computer hardware and software, alternative methods of financing and related services, other lending related services, and other services or activity, including consulting, related to the routine daily operations of credit unions;

(2) financial services including financial planning and counseling, securities brokerage and dealer activities, estate planning, tax services, insurance services, administering retirement, or deferred compensation and other employee or business benefit plans;

(3) internet-based or related services including sale and delivery of products to credit unions or members of credit unions; [or]

(4) Property management services; or

[(4)] (5) any other product, service or activity deemed economically beneficial or attractive to credit unions or credit union members if approved, in writing, by the commissioner.

(g) Compensation. A credit union director, senior management employee, or committee member or immediate family member of any such person may not receive any salary, commission, or other income or compensation, either directly or indirectly, from a CUSO affiliated with their credit union, unless received in accordance with a written agreement between the CUSO and the credit union. The agreement shall describe the services to be performed, the rate of compensation (or a description of the method of determining the amount of compensation) and any other provisions deemed desirable by the CUSO and the credit union. The agreement, and any amendments, must be approved by the board of directors of the credit union and the board of directors (or equivalent governing body) of the CUSO prior to any performance of service or payment and annually thereafter. For purposes of this section, senior

management employee shall include the chief executive officer, any assistant chief executive officers (vice presidents and above), and the chief financial officer. Immediate family shall include a person's spouse or any other person living in the same household.

(h) Examination fee. If the commissioner requests a CUSO to make its books and records available for inspection and examination, the CUSO shall pay a supplemental examination fee as prescribed in §97.113(e) of this title (relating to Supplemental examination fees). The commissioner may waive the supplemental examination fee or reduce the fee.

(i) Exception. A credit union which has a net worth ratio greater than six percent (6%) and is deemed adequately capitalized by its insuring organization may make an investment in or make loans to a CUSO that is not limited by the restriction set forth in subsection (e)(4) of this section, provided the activities of the CUSO are limited to activities which could be conducted directly by a credit union or are incidental to the conduct of the business of a credit union. Notwithstanding this exception, all other provisions of the act and this chapter applicable to a CUSO apply. In the event a credit union's net worth declines below the required thresholds, the credit union may not renew, extend the maturity of, or restructure an existing loan, advance additional funds, or increase the investment in the CUSO without the prior written approval of the commissioner.

(j) Change in Valuation. If the limitations established by this section are reached or exceeded solely because of the profitability of the CUSO and the related GAAP valuation of the investment under the equity method, divestiture is not required. A credit union may continue to invest up to the limitation without regard to the increase in the GAAP valuation resulting from a CUSO's profitability.

INVESTMENT LIMITS AND PROHIBTIONS

E. (e) Proposed Amendments to 7 TAC Section 91.803 Concerning Investment Limits and Prohibitions.

BACKGROUND: The proposed amendment would authorize investments in certain CUSOs to the extent they are providing property management services. The language is presented to clearly document state credit union authority to invest in CUSOs providing property management services. The authority is provided through parity provisions found within TFC Section 123.003, as that authority is available to federal credit unions under NCUA Rules and Regulations 12 C.F.R. Part 712(g).

RECOMMENDED ACTION: The Department recommends that the Commission approve for publication and comment the proposed amendments to 7 TAC Section 91.803.

RECOMMENDED MOTION: I move that we approve for publication and comment in the *Texas Register* the proposed amendments to 7 TAC Section 91.803.

TITLE 7.	BANKING AND SECURITIES
Part 6.	Credit Union Department
Chapter 91.	Chartering, Operations, Mergers, Liquidations
Subchapter H.	Investments
Rule §91.803	Investment Limits and Prohibitions

The Credit Union Commission (the Commission) proposes amendments to Section 91.803, relating to Investment Limits and Prohibitions. The proposed amendment would make state rules consistent with the federal regulations governing the authority of Credit Union Organizations (CUSOs) that provide property management services. The federal regulations are found at 12 C.F.R. Part 712.5(g).

The Commission proposes the following amendment to Section 91.803. The language is presented to clearly document state credit union authority to invest in CUSOs providing property management services. The authority is provided to comply with parity provisions found within TFC Section 123.003, as that authority to invest in certain CUSOs is available to federal credit unions under NCUA Rules and Regulations 12 C.F.R. Part 712.5(g).

The commissioner finds, in accordance with Texas Finance Code section 123.003(b), that exercise of those powers or authorities is convenient for and affords an advantage to the credit union's members and maintains the fairness of competition and parity between the credit union and any foreign credit union.

FISCAL NOTE ON STATE AND LOCAL GOVERNMENTS. John J. Kolhoff, Commissioner, has determined that for the first five-year period the proposed amendments are in effect, there are no reasonably foreseeable implications relating to cost or revenues of state or local governments, under Government Code §2001.024(a)(4), as a result of enforcing or administering these amendments, as proposed.

PUBLIC BENEFIT/COST NOTE. Mr. Kolhoff has determined, under Government Code §2001.024(a)(5) that for the first five-year period the amended rules are in effect, the public benefit of rule clarity and parity with federal regulations will provide improved guidance to the industry. He further has determined there will be no probable economic cost to the credit union system or to persons required to comply with the rule.

IMPACT ON LOCAL EMPLOYMENT OR ECONOMY. There is no reasonably forecasted effect on local economy for the first five years that the proposed amendments are in effect. Therefore, no economic impact statement, local employment impact statement, nor regulatory flexibility analysis is required under Texas Government Code §§2001.022 or 2001.024(a)(6).

COST TO REGULATED PERSONS (COST-IN/COST-OUT). This rule proposal is not subject to Texas Government Code §2001.0045, concerning increasing costs to regulated persons, because this agency is a Self-Directed Semi-Independent (SDSI) agency under Finance Code Chapter 16 and is exempt from that cost provision.

ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS FOR SMALL BUSINESSES, MICROBUSINESSES, AND RURAL COMMUNITIES. Mr. Kolhoff has also determined that for each year of the first five years the proposed amendment is in effect, there will be no reasonably forecasted adverse economic effect on small businesses, microbusinesses, or rural communities as a result of implementing these amendments, and, therefore, no regulatory flexibility analysis, as specified in Texas Government Code §2006.002 is required.

GOVERNMENT GROWTH IMPACT STATEMENT. In compliance with Texas Government Code §2001.0221, the Board has prepared a government growth impact statement.

Unless indicated below, for each year of the first five years that the rule will be in effect, the rule will not:

- create or eliminate a government program;
- require the creation of new employee positions or the elimination of existing employee positions;
- require an increase or decrease in future legislative appropriations to the agency;
- lead to an increase or decrease in the fees paid to the department;
- create new regulations;
- expand, limit or repeal existing regulation
- increase or decrease the number of individuals subject to the rule's applicability;
- positively or adversely affect this state's economy.

TAKINGS IMPACT ASSESSMENT. No private real property interests are affected by this proposal, and the proposal does not restrict or limit an owner's right to his or her property that would otherwise exist in the absence of government action. Therefore, the rule does not constitute a taking under Texas Government Code §2007.043.

REQUEST FOR PUBLIC COMMENT. Written comments on the proposed amendments may be submitted in writing to John J. Kolhoff, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register*.

STATUTORY AUTHORITY. The amendments are proposed pursuant to Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Texas Finance Code, Title 2, Chapter 15 and Title 3, Subtitle D.

STATUTORY SECTIONS AFFECTED. The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Chapter 15 and Title 3, Subtitle D, specifically, Finance Code, Sections 124.351, and 124.352.

LEGAL REVIEW. The Commission certifies that the proposed rule has been reviewed by legal counsel and has been found to be within the agency's authority to adopt.

§91.803. Investment Limits and Prohibitions.

(a) Limitations. [With the exception of] <u>Except for</u> deposits [held by] <u>placed in</u> a Federal Reserve Bank, a credit union may invest no more than 50% of its net worth with any single obligor or related obligors. This limitation [also] does not apply to the extent that the investment is insured or guaranteed by the United States government, or an agency, sponsored enterprise, corporation, or instrumentality, of the United States government, or to any trust or trusts established for investing, directly or collectively, in such securities, obligations, or instruments. For the purposes of this section, obligor is defined as an issuer, trust, or originator of an investment, including the seller of a loan participation investment.

(b) Designated Depository. As a single exception to subsection (a) of this section, a credit union's board of directors may establish the maximum aggregate deposit limit for a single financial institution approved by the board as the credit union's designated depository. This deposit limit shall be a percentage of net worth and must be based on the credit union's liquidity trends and funding needs as documented by its asset/liability management policy. This authority is contingent upon the credit union appropriately documenting its due diligence to demonstrate that the investments in this designated depository do not pose a safety and soundness concern. The credit union's board of directors shall review and approve at least annually the maximum aggregate deposit limit for its designated depository. The review shall include a current due diligence analysis of the financial institution.

(c) Prohibited Activities.

(1) Definitions.

(A) Adjusted trading--selling an investment to a counterparty at a price above its current fair value and simultaneously purchasing or committing to purchase from the counterparty another investment at a price above its current fair value.

(B) Collateralized mortgage obligation (CMO)--a multi-class bond issue collateralized by mortgages or mortgage-backed securities.

(C) Commercial mortgage related security--a mortgage related security except that it is collateralized entirely by commercial real estate, such as a warehouse or office building, or a multi-family dwelling consisting of more than four units.

(D) Fair value--the price at which a security can be bought or sold in a current, arm's length transaction between willing parties, other than in a forced or liquidation sale.

(E) Real estate mortgage investment conduit (REMIC)--a nontaxable entity formed for the sole purpose of holding a fixed pool of mortgages secured by an interest in real property and issuing multiple classes of interests in the underlying mortgages.

(F) Residual interest--the remainder cash flows from a CMO/REMIC, or other mortgage-backed security transaction, after payments due bondholders and trust administrative expenses have been satisfied.

(G) Short sale--the sale of a security not owned by the seller.

(H) Stripped mortgage-backed security--a security that represents either the principal-only or the interest-only portion of the cash flows of an underlying pool of mortgages or mortgage-backed securities.

(I) Zero coupon investment--an investment that makes no periodic interest payments but instead is sold at a discount from its face value. The holder of a zero coupon investment realizes the rate of return through the gradual appreciation of the investment, which is redeemed at face value on a specified maturity date.

(2) A credit union may not:

(A) Use financial derivatives for replication, or for any purposes other than

hedging;

(B) Engage in adjusted trading or short sales;

(C) Purchase stripped mortgage backed securities;

(D) Purchase residual interests in CMOs/REMICs, or other structured mortgage backed securities;

(E) Purchase mortgage servicing rights as an investment but may retain mortgage servicing rights on a loan originated by the credit union and sold on the secondary market;

(F) Purchase commercial mortgage related securities of an issuer other than a U.S. Government sponsored enterprise;

(G) Purchase any security that has the capability of becoming a first credit loss piece which supports another more senior security;

(H) Purchase a zero coupon investment with a maturity date that is more than 10 years from the settlement date;

(I) Purchase investments whereby the underlying collateral consists of foreign receivables or foreign deposits;

(J) Purchase securities used as collateral by a safekeeping concern;

(K) Purchase exchangeable mortgage backed securities, unless they are fully compliant with the provisions outlined in Part 703 of the National Credit Union Administration Rules and Regulations; or

(L) Purchase securities convertible into stock at the option of the issuer.

(d) Investment pilot program.

(1) The commissioner may authorize a limited number of credit unions to engage in other types of investment activities under an investment pilot program. A credit union wishing to participate in an investment pilot program shall submit a request that addresses the following items:

(A) Board policies approving the activities and establishing limits on them;

(B) A complete description of the activities, with specific examples of how the credit union will conduct them and how they will benefit the credit union;

(C) A demonstration of how the activities will affect the credit union's financial performance, risk profile, and asset-liability management strategies;

(D) Examples of reports the credit union will generate to monitor the activities;

(E) A projection of the associated costs of the activities, including personnel, computer, audit, etc.;

(F) A description of the internal systems to measure, monitor, and report the activities, and the qualifications of the staff and/or official(s) responsible for implementing and overseeing the activities; and

(G) The internal control procedures that will be implemented, including audit requirements.

(2) In connection with a request to participate in an investment pilot program, the commissioner will consider the general nature and functions of credit unions, as well as the specific financial condition and management of the applicant credit union, as revealed in the request, examinations, or such other information as may be available to the commissioner. The commissioner may approve the request, approve the request conditionally, approve it in modified

form, or deny it in whole or in part. A decision by the commissioner concerning participation in an investment pilot program is not appealable.

(3) The commissioner may find that an investment pilot program previously authorized is no longer a safe and prudent practice for credit unions generally to engage in, **[or]** that it has become inconsistent with applicable state or federal law, or that it has ceased to be a safe and prudent practice for one or more **[particular]** credit unions in light of their financial condition or management. Upon such a finding, the commissioner will send written notice informing the board of directors of any or all of the credit unions engaging in such a practice that the authority to engage in the practice has been revoked or modified. When the commissioner so notifies any credit union, its directors and officers shall forthwith take steps to liquidate the investments in question or to make such modifications as the commissioner requires. Upon demonstration of good cause, the commissioner may grant a credit union some definite period of time in which to arrange its affairs to comply with the commissioner's direction. The commissioner deems credit [Credit] unions **[which]** that continue to engage in investment practices **[where]** after their authority to do so has been revoked or modified [will be deemed] to be engaging in an unsound practice.

MANDATORY RULE REVIEW

E. (f) Adoption of the Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter I (Relating to Reserves and Dividends), Sections 91.901, and 91.902, and Readoption of Rules.

BACKGROUND: Section 2001.039, Government Code, requires that a state agency review and consider for readoption each rule not later than the fourth anniversary of the date on which the rule took effect and every four years after that date. As provided in the noted section, the reviews must include, at a minimum, an assessment by the agency as to whether the reason for adopting the rule continues to exist. At its July 2016 meeting, the Commission approved a plan which establishes a date for the required review for each of the affected rules. In accordance with that plan, staff has reviewed 7 TAC, Part 6, Chapter 91, Subchapter I (reserves and dividends) and believes certain revisions are appropriate and necessary. Amendments to the noted chapter is being separately presented for proposal.

Notice of the review and a request for comments on the rules in this chapter was published in the March 15, 2019 issue of the *Texas Register*. No comments were received regarding the review. The Department believes that the reasons for adopting the noted rules continue to exist.

RECOMMENDED ACTION: The Department recommends that the Commission adopt these rules.

RECOMMENDED MOTION: I move that we adopt Rules 91.901, and 91.902 without changes to the proposed text as published in the *Texas Register*.

E. (f) Adoption of the Rule Review of 7 TAC, Part 6, Chapter 91, Subchapter I (Relating to Reserves and Dividends), Sections 91.901, and 91.902, and Readoption of Rules.

BACKGROUND: Section 2001.039, Government Code, requires that a state agency review and consider for readoption each rule not later than the fourth anniversary of the date on which the rule took effect and every four years after that date. As provided in the noted section, the reviews must include, at a minimum, an assessment by the agency as to whether the reason for adopting the rule continues to exist. At its July 2016 meeting, the Commission approved a plan which establishes a date for the required review for each of the affected rules. In accordance with that plan, staff has reviewed 7 TAC, Part 6, Chapter 91, Subchapter I (reserves and dividends) and believes certain revisions are appropriate and necessary. Amendments to the noted chapter is being separately presented for proposal.

Notice of the review and a request for comments on the rules in this chapter was published in the March 15, 2019 issue of the *Texas Register*. No comments were received regarding the review. The Department believes that the reasons for adopting the noted rules continue to exist.

RECOMMENDED ACTION: The Department recommends that the Commission adopt these rules.

RECOMMENDED MOTION: I move that we adopt Rules 91.901, and 91.902 without changes to the proposed text as published in the *Texas Register*.

The Credit Union Commission (Commission) has completed its review of Chapter 91, Subchapter I (relating to Reserves and Dividends), of the Texas Administrative Code, Title 7, Part 6, consisting §§91.901 and 91.902.

The rules were reviewed as a result of the Department's general rule review under Texas Government Code Section 2001.039.

Notice of the review of 7 TAC, Part 6, Chapter 91, Subchapter I, was published in the March 15, 2019, issue of the *Texas Register* (44 TexReg 1449) as required. The Department received no comments on the notice of intention to review.

As a result of the internal review by the Department, the Commission has determined that no revisions are appropriate and necessary. The Commission finds that the reasons for initially adopting these rules continue to exist, and readopts Chapter 91, Subchapter I, §§91.902 in accordance with the requirements of Texas Government Code, Section 2001.039. This concludes the review of 7 TAC, Part 6, Chapter 91, Subchapter I.

The Department hereby certifies that the proposal has been reviewed by legal counsel and found to be within the agency's legal authority to readopt.

Subchapter I. Reserves and Dividends

§91.901. Reserve Requirements.

(a) Definitions. The words and terms, when used in this chapter, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Net worth means the retained earnings balance of the credit union as determined under generally accepted accounting principles. Retained earnings consist of undivided earnings, regular reserves, and any other appropriations designated by management, the insuring organization, or the commission. This means that only undivided earnings and appropriations of undivided earnings are included in net worth. Net worth does not include the allowance for loan and lease losses account.

(2) Net worth ratio means, with respect to a credit union, the ratio of the net worth of the credit union to the total assets of the credit union.

(3) Total assets means the average of the total assets as measured using one of the following methods:

(A) average quarterly balance. The average of quarter-end balances of the four most recent calendar quarters; or

(B) average monthly balance. The average of month-end balances over the three calendar months of the calendar quarter; or

(C) average daily balance. The average daily balance over the calendar quarter; or

(D) quarter-end balance. The quarter-end balance of the calendar quarter as reported on the credit union's call report.

(b) In accordance with the requirements of §122.104 of the Act, state-chartered credit unions shall set aside a portion of their current gross income, prior to the declaration or payment of dividends, as follows:

(1) A credit union with a net worth ratio below 7.0% shall increase the dollar amount of its net worth reserves by the following amounts at the indicated intervals until its net worth ratio equals 7.0% of total assets:

(A) in the case of a monthly dividend period, net worth must increase monthly by an amount equivalent to at least 0.0334% of its total assets; and

(B) in the case of a quarterly, semi-annual or annual dividend period, net worth must increase quarterly by an amount equivalent to at least 0.1% per quarter of its total assets.

(2) For a credit union in operation less than ten years and having assets of less than \$10 million, a business plan must be developed that reflects, among other items, net worth projections consistent with the following:

(A) 2.0% net worth ratio by the end of the third year of operation;

(B) 3.5% net worth ratio by the end of the fifth year of operation;

(C) 6.0% net worth ratio by the end of the seventh year of operation; and

(D) 7.0% net worth ratio by the time it reaches \$10 million in total assets or by the end of the tenth year of operation, whichever is shorter.

(3) Whenever the net worth ratio falls below 7.0%, the credit union shall transfer a portion of its current period net income to its regular reserve in such amounts as described in paragraph (1) of this subsection.

(4) Special reserves. In addition to the regular reserve, special reserves to protect the interest of members may be established by board resolution or by order of the commissioner, from current income or from undivided earnings. In lieu of establishing a special reserve, the commissioner may direct that all or a portion of the undivided earnings and any other reserve fund be restricted. In either case, such directives must be given in writing and state with reasonable specificity the reasons for such directives.

(5) Insuring organization's capital requirements. As applicable, a credit union shall also comply with any and all net worth or capital requirements imposed by an insuring organization as a condition to maintaining insurance on share and deposit accounts. For federally-insured credit unions this includes all prompt corrective action requirements contained within Part 702 of the NCUA Rules and Regulations.

(6) Decrease in Required Reserve Transfer. The commissioner, on a case-by-case basis, and after receipt of a written application, may permit a credit union to transfer an amount that is less than the amount required under paragraph (1) of this subsection. A credit union shall submit such statements and reports as the commissioner may, in his discretion, require in support of a decreased transfer request. The application must be received no later than 10 days before the quarter end and shall include but not be limited to:

- (A) An explanation of the need for the reduced transfer amount;
- (B) Financial statement reflecting the fiscal impact of the required transfer; and

(C) Documentation supporting the credit union's ability to resume the required transfer at a future date certain.

(7) Financial Plan. A credit union that is not capable of making the prescribed reserve transfer under paragraph (1) of this subsection for three consecutive quarters, shall file a written financial plan detailing a quarterly timetable of steps the credit union will take to increase its net worth ratio and fully comply with this section in the future. A credit union shall file and implement the financial plan within 45 days of the triggering quarter end date. A credit union may, after prior written notice to the Department, amend its financial plan to reflect a change in circumstances. Failure to meet the terms of the financial plan may be considered a violation of a written agreement with the commissioner under §122.255 of the Finance Code.

(c) Revised business plan for new credit unions. A credit union that has been in operation for less than ten years and has assets of less than \$10 million shall file a written revised business plan within 30 calendar days of the date the credit union's net worth ratio has failed to increase consistent with its current business plan. Failure to submit a revised business plan, or submission of a plan not adequate to either increase net worth or increase net worth within a reasonable time; or failure of the credit union to implement its revised business plan, may trigger the regulatory actions described in subsection (b)(4) of this section.

(d) Unsafe practice. Any credit union which has less than a 6.0% net worth ratio may be deemed to be engaged in an unsafe practice pursuant to §122.255 of the Finance Code. The determination may be abated if, the credit union has entered into and is in compliance with a written agreement or order with the department or is in compliance with a net worth restoration or revised business plan approved by the department to increase its net worth ratio. If a credit union has a net worth ratio below 6.0% or is otherwise engaged in an unsafe practice, the department may impose the following administrative sanctions in addition to, or in lieu of, any other authorized supervisory action:

(1) all unencumbered reserves, undivided earnings, and current earnings are encumbered as special reserves;

(2) dividends and interest refunds may not be declared, advertised, or paid without the prior written approval of the commissioner; and

(3) any changes to the credit union's board of directors or senior management staff must receive the prior written approval of the commissioner.

(e) Supervisory action. Notwithstanding any requirements in this section, the department may take enforcement action against a credit union with capital above the minimum requirement if the credit union's circumstances indicate such action would be appropriate.

§91.902. Dividends.

(a) Dividend eligibility shall be prescribed by written board policy.

(b) When a credit union is subject to a cease and desist order or is otherwise notified that it is deemed to be in a troubled condition or engaged in an unsafe practice, the credit union must obtain prior written approval of the commissioner before it declares or pays any dividend or interest refund. A request for approval to pay a dividend or interest refund under this section must be in writing and must include the following supporting information:

(1) the proposed dividend and/or interest refund rate and the estimated total dollar amount of payment;

(2) an analysis of the credit union's ability to make the payment from current earnings without incurring an operating loss for the period; and

(3) an explanation of the progress in resolving the areas of concern detailed in the cease and desist order or the examiner's findings schedule of the most recent report of examination.

RESERVE REQUIREMENTS

E. (g) Proposed Amendments to 7 TAC Section 91.901 Concerning Reserve Requirements.

BACKGROUND: The proposed amendment would match deadlines for waiver applications contained in NCUA 12 C.F.R. Part 702.201, relating to Prompt Corrective Action (PCA) requirements for waiver applications. The language is presented to ensure deadline uniformity between the state and federal regulatory agencies in a waiver process.

RECOMMENDED ACTION: The Department recommends that the Commission approve for publication and comment the proposed amendments to 7 TAC Section 91.901.

RECOMMENDED MOTION: I move that we approve for publication and comment in the *Texas Register* the proposed amendments to 7 TAC Section 91.901.

TITLE 7.	BANKING AND SECURITIES
Part 6.	Credit Union Department
Chapter 91.	Chartering, Operations, Mergers, Liquidations
Subchapter I.	Reserves and Dividends
Rule §91.901	Reserve Requirements

The Credit Union Commission (the Commission) proposes amendments to Section 91.901, relating to Reserve Requirements. The proposed amendment would match deadlines for waiver applications contained in NCUA 12 C.F.R. Part 702.201, relating to Prompt Corrective Action (PCA) requirements for waiver applications.

The Commission proposes the following amendment to Section 91.901. The language is presented to ensure deadline uniformity between the state and federal regulatory agencies in a waiver process.

FISCAL NOTE ON STATE AND LOCAL GOVERNMENTS. John J. Kolhoff, Commissioner, has determined that for the first five-year period the proposed amendments are in effect, there are no reasonably foreseeable implications relating to cost or revenues of state or local governments, under Government Code §2001.024(a)(4), as a result of enforcing or administering these amendments, as proposed.

PUBLIC BENEFIT/COST NOTE. Mr. Kolhoff has determined, under Government Code §2001.024(a)(5) that for the first five-year period the amended rules are in effect, the public benefit of rule clarity and parity with federal regulations will provide improved guidance to the industry. He further has determined there will be no probable economic cost to the credit union system or to persons required to comply with the rule.

IMPACT ON LOCAL EMPLOYMENT OR ECONOMY. There is no reasonably forecasted effect on local economy for the first five years that the proposed amendments are in effect. Therefore, no economic impact statement, local employment impact statement, nor regulatory flexibility analysis is required under Texas Government Code §§ 2001.022 or 2001.024(a)(6).

COST TO REGULATED PERSONS (COST-IN/COST-OUT). This rule proposal is not subject to Texas Government Code §2001.0045, concerning increasing costs to regulated persons, because this agency is a Self-Directed Semi-Independent (SDSI) agency under Finance Code Chapter 16 and is exempt from that cost provision.

ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS FOR SMALL BUSINESSES, MICROBUSINESSES, AND RURAL COMMUNITIES. Mr. Kolhoff has also determined that for each year of the first five years the proposed amendment is in effect, there will be no reasonably forecasted adverse economic effect on small businesses, microbusinesses, or rural communities as a result of implementing these amendments, and, therefore, no regulatory flexibility analysis, as specified in Texas Government Code §2006.002 is required.

GOVERNMENT GROWTH IMPACT STATEMENT. In compliance with Texas Government Code §2001.0221, the Board has prepared a government growth impact statement. Unless indicated below, for each year of the first five years that the rule will be in effect, the rule will not:

- create or eliminate a government program;
- require the creation of new employee positions or the elimination of existing employee positions;
- require an increase or decrease in future legislative appropriations to the agency;
- lead to an increase or decrease in the fees paid to the department;
- create new regulations;
- expand, limit or repeal existing regulation
- increase or decrease the number of individuals subject to the rule's applicability;
- positively or adversely affect this state's economy.

TAKINGS IMPACT ASSESSMENT. No private real property interests are affected by this proposal, and the proposal does not restrict or limit an owner's right to his or her property that would otherwise exist in the absence of government action. Therefore, the rule does not constitute a taking under Texas Government Code §2007.043.

REQUEST FOR PUBLIC COMMENT. Written comments on the proposed amendments may be submitted in writing to John J. Kolhoff, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register*.

STATUTORY AUTHORITY. The amendments are proposed pursuant to Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Texas Finance Code, Title 2, Chapter 15 and Title 3, Subtitle D.

STATUTORY SECTIONS AFFECTED. The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Chapter 122 and Subchapter C, specifically, Finance Code, Section 122.104.

LEGAL REVIEW. The Commission certifies that the proposed rule has been reviewed by legal counsel and has been found to be within the agency's authority to adopt.

Subchapter I. Reserves and Dividends

§91.901. Reserve Requirements.

(a) Definitions. The words and terms, when used in this chapter, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Net worth means the retained earnings balance of the credit union as determined under generally accepted accounting principles. Retained earnings consist of undivided earnings, regular reserves, and any other appropriations designated by management, the insuring organization, or the commission. This means that only undivided earnings and appropriations of undivided earnings are included in net worth. Net worth does not include the allowance for loan and lease losses account.

(2) Net worth ratio means, with respect to a credit union, the ratio of the net worth of the credit union to the total assets of the credit union.

(3) Total assets means the average of the total assets as measured using one of the following methods:

(A) average quarterly balance. The average of quarter-end balances of the four most recent calendar quarters; or

(B) average monthly balance. The average of month-end balances over the three calendar months of the calendar quarter; or

or

(C) average daily balance. The average daily balance over the calendar quarter;

(D) quarter-end balance. The quarter-end balance of the calendar quarter as reported on the credit union's call report.

(b) In accordance with the requirements of §122.104 of the Act, state-chartered credit unions shall set aside a portion of their current gross income, prior to the declaration or payment of dividends, as follows:

(1) A credit union with a net worth ratio below 7.0% shall increase the dollar amount of its net worth reserves by the following amounts at the indicated intervals until its net worth ratio equals 7.0% of total assets:

(A) in the case of a monthly dividend period, net worth must increase monthly by an amount equivalent to at least 0.0334% of its total assets; and

(B) in the case of a quarterly, semi-annual or annual dividend period, net worth must increase quarterly by an amount equivalent to at least 0.1% per quarter of its total assets.

(2) For a credit union in operation less than ten years and having assets of less than \$10 million, a business plan must be developed that reflects, among other items, net worth projections consistent with the following:

(A) 2.0% net worth ratio by the end of the third year of operation;

(B) 3.5% net worth ratio by the end of the fifth year of operation;

(C) 6.0% net worth ratio by the end of the seventh year of operation; and

(D) 7.0% net worth ratio by the time it reaches \$10 million in total assets or by the end of the tenth year of operation, whichever is shorter.

(3) Whenever the net worth ratio falls below 7.0%, the credit union shall transfer a portion of its current period net income to its regular reserve in such amounts as described in paragraph (1) of this subsection.

(4) Special reserves. In addition to the regular reserve, special reserves to protect the interest of members may be established by board resolution or by order of the commissioner, from current income or from undivided earnings. In lieu of establishing a special reserve, the commissioner may direct that all or a portion of the undivided earnings and any other reserve fund be restricted. In either case, such directives must be given in writing and state with reasonable specificity the reasons for such directives.

(5) Insuring organization's capital requirements. As applicable, a credit union shall also comply with any and all net worth or capital requirements imposed by an insuring organization as a condition to maintaining insurance on share and deposit accounts. For federally-insured credit unions this includes all prompt corrective action requirements contained within Part 702 of the NCUA Rules and Regulations.

(6) Decrease in Required Reserve Transfer. The commissioner, on a case-by-case basis, and after receipt of a written application, may permit a credit union to transfer an amount that is less than the amount required under paragraph (1) of this subsection. A credit union shall submit such statements and reports as the commissioner may, in his discretion, require in support of a decreased transfer request. The application must be received no later than [10] <u>14</u> days before the quarter end and shall include but not be limited to:

(A) An explanation of the need for the reduced transfer amount;

(B) Financial statement reflecting the fiscal impact of the required transfer; and

(C) Documentation supporting the credit union's ability to resume the required transfer at a future date certain.

(7) Financial Plan. A credit union that is not capable of making the prescribed reserve transfer under paragraph (1) of this subsection for three consecutive quarters, shall file a written financial plan detailing a quarterly timetable of steps the credit union will take to increase its net worth ratio and fully comply with this section in the future. A credit union shall file and implement the financial plan within 45 days of the triggering quarter end date. A credit union may, after prior written notice to the Department, amend its financial plan to reflect a change in circumstances. Failure to meet the terms of the financial plan may be considered a violation of a written agreement with the commissioner under §122.255 of the Finance Code.

(c) Revised business plan for new credit unions. A credit union that has been in operation for less than ten years and has assets of less than \$10 million shall file a written revised business plan within 30 calendar days of the date the credit union's net worth ratio has failed to increase consistent with its current business plan. Failure to submit a revised business plan, or submission of a plan not adequate to either increase net worth or increase net worth within a reasonable time; or failure of the credit union to implement its revised business plan, may trigger the regulatory actions described in subsection (b)(4) of this section.

(d) Unsafe practice. Any credit union which has less than a 6.0% net worth ratio may be deemed to be engaged in an unsafe practice pursuant to §122.255 of the Finance Code. The determination may be abated if, the credit union has entered into and is in compliance with a written agreement or order with the department or is in compliance with a net worth restoration or revised business plan approved by the department to increase its net worth ratio. If a credit union has a net worth ratio below 6.0% or is otherwise engaged in an unsafe practice, the department may impose the following administrative sanctions in addition to, or in lieu of, any other authorized supervisory action:

(1) all unencumbered reserves, undivided earnings, and current earnings are encumbered as special reserves;

(2) dividends and interest refunds may not be declared, advertised, or paid without the prior written approval of the commissioner; and

(3) any changes to the credit union's board of directors or senior management staff must receive the prior written approval of the commissioner.

(e) Supervisory action. Notwithstanding any requirements in this section, the department may take enforcement action against a credit union with capital above the minimum requirement if the credit union's circumstances indicate such action would be appropriate.

MERGERS/CONSOLIDATIONS

E. (h) Proposed Amendments to 7 TAC Section 91.1003 Concerning Mergers/Consolidations.

BACKGROUND: The proposed amendments would reference the Hart-Scott Rodino Act (HSRA) requirements of proposed mergers instead of repeating specific thresholds within the HSRA that change over time. The language is presented to refer institutions directly to the federal HSRA language and its specific requirements and thresholds instead of duplicating all, or part of the federal provision, within the state rule. Currently the rule refers to an outdated dollar threshold for measurement of HSRA applicability. This improves the current rule, which does not refer to all of the tests used to determine if HSRA applies to a merger transaction.

RECOMMENDED ACTION: The Department recommends that the Commission approve for publication and comment the proposed amendments to 7 TAC Section 91.1003.

RECOMMENDED MOTION: I move that we approve for publication and comment in the *Texas Register* the proposed amendments to 7 TAC Section 91.1003.

TITLE 7.	BANKING AND SECURITIES
Part 6.	Credit Union Department
Chapter 91.	Chartering, Operations, Mergers, Liquidations
Subchapter J.	Changes in Corporate Status
Rule §91.1003	Mergers/Consolidations

The Credit Union Commission (the Commission) proposes amendments to Section 91.1003, relating to Mergers and Consolidations. The proposed amendments would reference Hart-Scott Rodino Act (HSRA) requirements of proposed mergers instead of repeating specific thresholds within the HSRA that change over time.

The Commission proposes the following amendment to Section 91.1003. The language is presented to refer institutions directly to the federal HSRA language and its specific requirements and thresholds instead of duplicating all, or part of the federal provision, within the state rule. Currently the Rule refers to an outdated dollar threshold for measurement of HSRA applicability. This improves the current rule, which does not refer to all of the tests used to determine if HSRA applies to a merger transaction.

FISCAL NOTE ON STATE AND LOCAL GOVERNMENTS. John J. Kolhoff, Commissioner, has determined that for the first five-year period the proposed amendments are in effect, there are no reasonably foreseeable implications relating to cost or revenues of state or local governments, under Government Code §2001.024(a)(4), as a result of enforcing or administering these amendments, as proposed.

PUBLIC BENEFIT/COST NOTE. Mr. Kolhoff has determined, under Government Code §2001.024(a)(5) that for the first five-year period the amended rules are in effect, the public benefit of rule clarity will provide improved guidance to the industry. He further has determined there will be no probable economic cost to the credit union system or to persons required to comply with the rule.

IMPACT ON LOCAL EMPLOYMENT OR ECONOMY. There is no reasonably forecasted effect on local economy for the first five years that the proposed amendments are in effect. Therefore, no economic impact statement, local employment impact statement, nor regulatory flexibility analysis is required under Texas Government Code §§2001.022 or 2001.024(a)(6).

COST TO REGULATED PERSONS (COST-IN/COST-OUT). This rule proposal is not subject to Texas Government Code §2001.0045, concerning increasing costs to regulated persons, because this agency is a Self-Directed Semi-Independent (SDSI) agency under Finance Code Chapter 16 and is exempt from that cost provision.

ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS FOR SMALL BUSINESSES, MICROBUSINESSES, AND RURAL COMMUNITIES. Mr. Kolhoff has also determined that for each year of the first five years the proposed amendment is in effect, there will be no reasonably forecasted adverse economic effect on small businesses, microbusinesses, or rural communities as a result of implementing these amendments, and, therefore, no regulatory flexibility analysis, as specified in Texas Government Code §2006.002 is required.

GOVERNMENT GROWTH IMPACT STATEMENT. In compliance with Texas Government Code §2001.0221, the Board has prepared a government growth impact statement.

Unless indicated below, for each year of the first five years that the rule will be in effect, the rule will not:

- create or eliminate a government program;
- require the creation of new employee positions or the elimination of existing employee positions;
- require an increase or decrease in future legislative appropriations to the agency;
- · lead to an increase or decrease in the fees paid to the department;
- create new regulations;
- expand, limit or repeal existing regulation
- increase or decrease the number of individuals subject to the rule's applicability;
- positively or adversely affect this state's economy.

TAKINGS IMPACT ASSESSMENT. No private real property interests are affected by this proposal, and the proposal does not restrict or limit an owner's right to his or her property that would otherwise exist in the absence of government action. Therefore, the rule does not constitute a taking under Texas Government Code §2007.043.

REQUEST FOR PUBLIC COMMENT. Written comments on the proposed amendments may be submitted in writing to John J. Kolhoff, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register*.

STATUTORY AUTHORITY. The amendments are proposed pursuant to Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Texas Finance Code, Title 2, Chapter 15 and Title 3, Subtitle D. Authority to adopt these amendments is found also in Texas Finance Code Sections 122.1531 and 122.156.

STATUTORY SECTIONS AFFECTED. The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Chapter 15 and Title 3, Subtitle D, specifically, Finance Code, Sections 122.005, 122.151 – .156, and 124.003.

LEGAL REVIEW. The Commission certifies that the proposed rule has been reviewed by legal counsel and has been found to be within the agency's authority to adopt.

Subchapter J. Changes in Corporate Status

§91.1003. Mergers/Consolidations.

(a) Definitions. The following words and terms, when used in this section, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Acquirer credit union - The credit union that will continue in operation after the merger/consolidation.

(2) Acquiree credit union - The credit union that will cease to exist as an operating credit union at the time of the merger/consolidation.

(3) Merger inducement -A promise by a credit union to pay to the members of another credit union a sum of money or other material benefit upon the successful completion of a merger of the two credit unions.

(4) Substantial – An amount that is large in size, value, or importance. For purposes of this section, an amount is substantial if it exceeds \$1,000.00 in total.

(b) Two or more credit unions organized under the laws of this state, another state, or the United States, may merge/consolidate, in whole or in part, with each other, or into a newly incorporated credit union to the extent permitted by applicable law, subject to the requirements of this rule. A credit union may not offer a merger inducement to another credit union's members as a means of promoting a merger of the two credit unions.

(c) Notice of Intent to Merge/Consolidate. The credit unions shall notify the commissioner in writing of their intent to merge/consolidate within ten days after the credit unions' boards of directors formally agree in principle to merge/consolidate.

(d) Plan for Merger/Consolidation. Upon approval of a proposition for merger/consolidation by the boards of directors, the credit unions must prepare a plan for the proposed merger/consolidation. The plan shall include:

(1) The terms and conditions of the merger/consolidation including a detailed description of any substantial remuneration, such as bonuses, deferred compensation, early payout of retirement benefits, severance packages, retainers, services agreements, or other substantial financial rewards or benefits that any board member or senior management employee of the acquiree credit union may receive in connection with the merger/consolidation;

(2) the current financial reports of each credit union;

(3) the combined financial reports of the two or more credit unions;

(4) an analysis of the adequacy of the combined Allowance for Loan and Lease Losses account;

(5) an explanation of any proposed adjustments to the members' shares, or provisions for reserves, dividends, or undivided profits;

(6) a summary of the products and services proposed to be available to the members of the acquirer credit union, with an explanation of any changes from the current products and services provided to the members;

(7) a summary of the advantages and disadvantages of the merger/consolidation;

(8) the projected location of the main office and any branch location(s) after the merger/consolidation and whether any existing office locations will be permanently closed; and

(9) any other items deemed critical to the merger/consolidation agreement by the boards of directors.

(e) Submission of an Application to Merge/Consolidate to Department.

(1) An application for approval of the merger/consolidation will be complete when the following information is submitted to the commissioner:

(A) the merger/consolidation plan, as described in this rule;

(B) a copy of the corporate resolution of each board of directors approving the merger/consolidation plan;

(C) the proposed Notice of Special Meeting of the members;

(D) a copy of the ballot form to be sent to the members;

(E) the current delinquent loan summaries for each credit union;

(F) [if the acquiree credit union has \$65.2 million or more in assets on its latest call report,] a statement as to whether the transaction is subject to the Hart-Scott Rodino Act premerger notification filing requirements; and

(G) a request for a waiver of the requirement that the plan be approved by the members of any of the affected credit unions, in the event the board(s) seek such a waiver, together with a statement of the reason(s) for the waiver(s).

(2) If the acquirer credit union is organized under the laws of another state or of the United States, the commissioner may accept an application to merge or consolidate that is prescribed by the state or federal supervisory authority of the acquirer credit union, provided that the commissioner may require additional information to determine whether to deny or approve the merger/consolidation. The application will be deemed complete upon receipt of all information requested by the commissioner.

(3) Notice of the proposed merger must be published in the *Texas Register* and Department Newsletter as prescribed in §91.104 (relating to Notice of Applications).

(f) Commissioner Action on the Application.

(1) The commissioner may grant preliminary approval of an application for merger/consolidation conditioned upon specific requirements being met, but final approval shall not be granted unless such conditions have been met within the time specified in the preliminary approval.

(2) The commissioner shall deny an application for merger/consolidation if the commissioner finds any of the following:

(A) the financial condition of the acquirer credit union before the merger/consolidation is such that it will likely jeopardize the financial stability of the merging credit union or prejudice the financial interests of the members, beneficiaries or creditors of either credit union;

(B) the plan includes a change in the products or services available to members of the acquiree credit union that substantially harms the financial interests of the members, beneficiaries or creditors of the acquiree credit union;

(C) the merger/consolidation would probably substantially lessen the ability of the acquirer credit union to meet the reasonable needs and convenience of members to be served;

(D) the credit unions do not furnish to the commissioner all information requested by the commissioner which is material to the application;

(E) the credit unions fail to obtain any approval required from a federal or state supervisory authority; or

(F) the merger/consolidation would be contrary to law.

(3) For applications to merge/consolidate in which the products and services of the acquirer credit union after merger/consolidation are proposed to be substantially the same as those of the acquiree and acquirer credit unions, the commissioner will presume that the merger/consolidation will not significantly change or affect the availability and adequacy of financial services in the local community.

(g) Procedures for Approval of Merger/Consolidation Plan by the Members of Each Credit Union.

(1) The credit unions have the option of allowing their members to vote on the plan in person at a meeting of the members, by mail ballot, or both. With prior approval of the commissioner, a credit union may accept member votes by an alternative method that is reasonably calculated to ensure each member has an opportunity to vote.

(2) Members shall be given advance notice of the meeting in accordance with the credit union's bylaws. The notice of the meeting shall:

(A) specify the purpose of the meeting and state the date, time, and place of the special meeting;

(B) state the reasons for the proposed merger/consolidation;

(C) contain a summary of the merger plan and state that any interested person may obtain more detailed information about the merger from the credit union at its principal place of business, or by any method approved in advance by the commissioner;

- (D) provide the name and location of the acquirer credit union;
- (E) specify the methods permitted for casting votes; and
- (F) if applicable, be accompanied by a mail ballot.

(h) Completion of Merger/Consolidation.

(1) Upon approval of the merger/consolidation plan by the membership, if applicable, the Certificate of Merger/Consolidation shall be completed, signed and submitted to the commissioner for final authority to combine the records. Necessary amendments to the acquirer credit union's articles of incorporation or bylaws shall also be submitted at this time.

(2) Upon receipt of the commissioner's written authorization, the records of the credit unions shall be combined as of the effective date of the merger/consolidation. The board of the directors of the acquirer credit union shall certify the completion of the merger/consolidation to the commissioner within 30 days after the effective date of the merger/consolidation.

(3) Upon receipt by the commissioner of the completion of the merger/consolidation certification, any article of incorporation or bylaw amendments will be approved and the charter of the acquiree credit union will be canceled.

LEGISLATIVE ISSUES AND ACTIVITIES

E. (i) Legislative Issues and Activities Relating to the 86th Regular Session that may impact the Department.

BACKGROUND: Monday May 27th was the last day of the 86th Regular Session (sine die); only corrections may be considered in the House and Senate after that date. Sunday June 16th was the last day the governor could sign, or veto bills passed. Currently there is no significant legislation noted impacting the operation of the Department.

<u>RECOMMENDED ACTION:</u> No formal action is anticipated.

RESOLUTION FOR CARY L. CABE

E. (j) Resolution of Appreciation for Retiring Field Supervisor Cary L. Cabe.

BACKGROUND: Cary Cabe, Field Supervisor, will be retiring on September 30, 2019 after a long and distinguished career with the Department. Mr. Cabe progressed to various positions within the department. In recognition of the leadership he has provided in helping to develop the Department into a strong organization it is today, the staff has drafted this resolution for the Commission's consideration.

<u>RECOMMENDED ACTION:</u> I move that we approve the Resolution of Appreciation for retiring Field Supervisor Cary L. Cabe as presented and that the resolution be given to him as a token of our appreciation.



RESOLUTION

The Credit Union Commission, State of Texas, hereby recognizes and expresses its gratitude for the significant contributions made to the Credit Union Department and the State's credit unions by

Cary L. Cabe

WHEREAS, Cary L. Cabe has served the Department with distinction since 1993, first as an Examiner, then as a Principal Examiner, and most recently as Field Supervisor VII; and

WHEREAS, Cary L. Cabe has been diligent in safeguarding the public interest, protecting the interests of credit union members, and promoting public confidence in credit unions; and

WHEREAS, Cary L. Cabe has demonstrated leadership and skills which have contributed to the strengthening of the Credit Union Department's examination and supervision capabilities; and

WHEREAS, Cary L. Cabe is now retiring from the staff of the Credit Union Department after 25 years of dedicated service to credit unions; now therefore,

NOW THEREFORE BE IT RESOLVED, that the Credit Union Commission thanks Cary L. Cabe for his service, interest, and devotion to the Department and credit unions; and

BE IT FURTHER RESOLVED, that a copy of this Resolution be entered in the minutes of the Commission with the original given to him.

READ, ADOPTED, AND APPROVED unanimously by the Credit Union Commission, State of Texas, this twelve day of July 2019.

SUNSET REVIEW

E. (k) Status of the Department's Sunset Review.

BACKGROUND: The Sunset Commission provided us with the selfevaluation questionnaire on May 9th and we've begun preparing our response. The response is due to the Sunset Commission by September 1st. Department staff attended an orientation on June 3rd. I'm working closely with Deputy Commissioner Etheridge and Executive Assistant Velasquez as well as referencing Commissioner Feeney's past self-evaluations.

RECOMMENDED ACTION: No formal action is anticipated.

CYBERNANCE COMMISSION STUDY

E. (m) Cybernance Rquest to Commission Study.

BACKGROUND: Cybernance is an Austin startup that is seeking to collect cybersecurity related risk profile assessments of Texas Credit Unions and consolidate that data with the intent of reviewing the level of aggregate risk statewide and providing peer assessments to institutions on how they perform relative to similar institutions. The cyber risk profile information that Cybernance collects is the Cyber Assessment Tool (CAT) which was created by the Federal Financial Institutions Examination Council (FFIEC) as an examination standard throughout the depository industries (banks and credit unions). According to Cybernance staffers, the Texas Bankers Association has initiated a similar study for Texas banks and they wanted to talk to the Department about doing the same for the Texas credit union industry.

After doing some online research regarding the company and its products I attended conference call with Cybernance executives to discuss broadly the concept of their work.

After they provided additional background information I provided the following points to them.

- The Department does not require the use of CAT. Many institutions may use CAT, but there are other acceptable methodologies used by the industry to measure and monitor cybersecurity risk and mitigation techniques. CAT is an examination process, and as such is confidential by our statute. Therefore, it would not be appropriate for the Department to share that data with a vendor, nor recommend any particular vendor's product or service.
- I recommended that the company contact the Cornerstone League, the credit union industry's equivalent to the banking industry's TBA. Given their similar goals, Cornerstone presented as the most likely partner to Cybernance on this endeavor.
- Cybernance could also reach out to NCUA's Deputy Director of Examination and Insurance Tim Segerson. Mr. Segerson oversees the development and deployment of NCUA's implementation of the CAT and may be interested in their product and how it works.
- The Department only directly regulates state-chartered institutions operating in Texas. Even if the Department was interested in participating in the study only Texas chartered credit unions would

make up the sample. Given Cybernance's stated intent it would seem a broader pool of state and federal credit unions should be incorporated in the study.

I hope this short summary is appropriately informative to give you a general idea of the vendor and their query with the Department. As always, if you have any questions please let me know.

<u>RECOMMENDED ACTION:</u> No formal action is anticipated.