



CREDIT UNION DEPARTMENT

DATE: **March 8, 2012**

TO: **State Chartered Credit Unions**

SUBJECT: **Change 31 to Update the Texas Rules for Credit Unions**

The attached pages constitute changes to the Texas Rules for Credit Unions. Your book of rules should be updated as follows:

REMOVE PAGES

Index – pages iii and iv

91-19 thru 91-22-b

91-59 thru 91-70

INSERT

Index – pages iii and iv

91-19 thru 91-22-b

91-59 thru 91-70-b

AMENDMENTS OR NEW RULES

Updated Index

Readopted Rules 91.301, 91.302, 91.310,
and 91.315 with no changes

Amended Rule 91.801

FOR YOUR RECORDS - Please keep this letter of transmittal behind the **Update Tab** of the Rules Section of your binder as a record to show your rules are up to date.

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CHARTERING, OPERATIONS, MERGERS, LIQUIDATIONS

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Subchapter C. Members

§91.301. Field of Membership.

(a) General. Membership in a credit union shall be limited to one or more groups, each of which (the Group) has its own community of interest and is within the credit union's local service area. In this section, local service area shall mean an area that is within reasonable proximity of a credit union's office, and allows members to be realistically served from that office. For purposes of field of membership, the Group as a whole will be considered to be within the local service area when:

(1) A majority of the persons in the Group live, work, or gather regularly within the local service area;

(2) The Group's headquarters is located within the local service area; or

(3) The persons in the Group are "paid from" or "supervised from" an office or facility located within the local service area.

The commissioner may impose a geographical limitation on any Group if the commissioner reasonably determines that the applicant credit union does not have the facilities and staffing to serve a larger group or there are other operational or management concerns.

(b) Other persons eligible for membership. A number of persons by virtue of their close relationship to a Group may be included in the field of membership at the option of the applicant credit union. These include:

(1) members of the family or household of a member of the Group;

(2) volunteers performing services for or on behalf of the Group;

(3) organizations owned or controlled by a member or members of the Group, and any employees and members of those organizations;

(4) spouses of persons who died while in the Group;

(5) employees of the credit union;

(6) subsidiaries of the credit union and their employees; and businesses and other organizations whose employees or members are within the Group.

(c) Multiple-groups.

(1) The commissioner may approve a credit union's original articles of incorporation and bylaws or a request for approval of an amendment to a credit union's bylaws to serve one or more communities of interest or a combination of types of communities of interest.

(2) In addition to general requirements, special requirements pertaining to multiple-Group applications may be required before the commissioner will grant such a certificate or approve such an amendment.

(A) Each Group to be included in the proposed field of membership of the credit union must have its own community of interest.

(B) Each associational or occupational Group must individually request inclusion in the proposed credit union's field of membership.

(d) Overlap protection.

(1) The commissioner will only consider the financial effect of an overlap proposed by an application to expand a credit union's field of membership or when a charter application proposes an overlap for a Group of 3,000 members or more.

(2) The commissioner will weigh the information in support of the application and any information provided by a protesting or affected credit union. If the applicant has the financial capacity to serve the financial needs of the proposed members, demonstrates economic feasibility,

complies with the requirements of this rule, and no protestant reasonably establishes a basis for denying the request, it shall be approved.

(3) If a finding is made that overlap protection is warranted, the commissioner shall reject the application or require the applicant to limit or eliminate the overlap by adding exclusionary language to the text of the amendment, e.g., "excluding persons eligible for primary membership in any occupation or association based credit union that has an office within a specified proximity of the applicant credit union at the time membership is sought." Exclusionary clauses are rarely appropriate for inclusion on a geographic community of interest.

(4) Generally, if the overlapped credit union does not submit a notice of protest form, and the department determines that there is no safety and soundness problem, an overlap will be permitted. If, however, a notice of protest is filed, the commissioner will consider the following in performing an overlap analysis:

(A) whether the overlap is incidental in nature, ie., the group(s) in question is so small as to have no material effect on the overlapped credit union;

(B) whether there is limited participation by members of the group(s) in the overlapped credit union after the expiration of a reasonable period of time;

(C) whether the overlapped credit union provides requested service;

(D) the financial effect on the overlapped credit union;

(E) the desires of the group(s); and

(F) the best interests of the affected group(s) and the credit union members involved.

(5) Where a sponsor organization expands its operations internally, by acquisition or otherwise, the credit union may serve these new entrants to its field of membership if they are part of the community of interest described in the credit union's bylaws. Where acquisitions are made which add a new subsidiary or affiliate, the group cannot be served until the entity is included in the field of membership through the application process.

(6) Credit unions affected by the organizational restructuring or merger of a group within its field of membership must apply for a modification of their fields of membership to reflect the group to be served.

(e) Underserved communities.

(1) All credit unions may include underserved areas in their fields of membership, without regard to location. More than one credit union can serve the same underserved area.

(2) Once an underserved area has been added to a credit union's field of membership, the credit union must establish and maintain an office or facility in the community. For the purposes of this subsection, service facility is defined as a place where shares are accepted for members' accounts, loan applications are accepted and loan proceeds are disbursed. This definition includes a credit union owned branch, a shared branch, a mobile branch, and an office operated on a regularly scheduled weekly basis, or a credit union owned electronic facility that meets, at a minimum, these requirements. This definition does not include an ATM or a credit union's Internet website.

(3) A credit union desiring to add an underserved area must document that the community meets the definition. In addition, the credit union must develop a business plan specifying how it will serve the community. The business plan, at a minimum, must identify the credit and depository needs of the community and detail how the credit union plans to serve those needs. The credit union will be expected to regularly review the business plan to determine if the community is being adequately served. The commissioner may require periodic service status reports from a credit union pertaining to the underserved area to ensure that the

needs of the area are being met, as well as requiring such reports before allowing a credit union to add an additional underserved area.

(f) Parity with Federal Credit Unions.

Credit unions will be allowed to have, at a minimum, at least as much flexibility as federal credit unions have in field of membership regulation. If a credit union proposes a type of Group that the National Credit Union Administration has previously determined meets the Federal requirements, the commissioner shall approve the application unless the commissioner finds that the credit union has not demonstrated sufficient managerial and financial capacity to safely and soundly serve such expanded membership.

(g) Application.

In order to request the approval of the commissioner to add a Group to its bylaws, a credit union must submit a written application to the Department. The applicant credit union shall have the burden to show to the Department such facts and data that support the requirements and considerations in this rule. In reviewing such application, the commissioner shall consider:

(1) Whether the Group has adequate unifying characteristics or a mutual interest such that the safety and soundness of the credit union is maintained;

(2) The ability of credit unions to maintain parity and to compete fairly with their counterparts;

(3) Service by the credit union that is responsive to the convenience and needs of prospective members;

(4) Protection for the interest of current and future members of the credit union; and

(5) The encouragement of economic progress in this State by allowing opportunity to expand services and facilities.

Source: The provisions of this §91.301 adopted to be effective February 11, 2001, 26 TexReg 1132; adopted to be effective January 7, 2004, 29 TexReg 82; readopted to be effective June 22, 2004, 29 TexReg 6423; reviewed and amended to be effective July 13, 2008, 33 TexReg 5294; reviewed and readopted to be effective February 17, 2012, 37 TexReg 1518.

§91.302. Election or Other Membership Vote By Electronic Balloting, Early Voting, Absentee Voting, or Mail Balloting.

(a) All credit unions should actively promote member participation in elections and other membership votes as long as the costs are reasonable and the integrity of the vote is not compromised. Any credit union instituting alternative procedures or systems to benefit members who find it difficult or inconvenient to vote at annual or special meetings must ensure that the alternative is thoroughly explained and publicized so that all members will be able to take advantage of those procedures or systems.

(b) The board of directors, before holding an election or other membership vote that uses electronic balloting, early voting, absentee voting, or mail balloting, shall establish written election rules, including procedures to: control, tabulate and retain ballots; identify invalid ballots; and handle disputed election results and tie votes.

(c) Any elections or other membership vote using electronic balloting, early voting, absentee voting, or mail balloting are subject to the following conditions:

(1) The election tellers shall be appointed by the board of directors;

(2) At least 30 days prior to the annual or special meeting, the board of directors will cause either a printed ballot or notice of a ballot, along with appropriate instructions, to be mailed to all members eligible to vote;

(3) Completed electronic or mail ballots cast during early or absentee voting must be received prior to convening the annual or special meeting;

(4) The votes will be tallied by the tellers and the results of the vote will be made public at the annual or special meeting.

(d) In the event of a malfunction of the electronic balloting system, the board of directors may in its discretion order elections or other vote to be held by mail ballot only. The board may make reasonable adjustments to the voting time frames in subsection (c) of this section, or postpone the annual or special meeting if necessary, to complete the elections prior to the annual or special meeting.

Source: The provisions of this §91.302 adopted to be effective November 13, 2000, 25 TexReg 11278; amended to be effective November 14, 2004, 29 TexReg 10253, reviewed and amended to be effective July 13, 2008, 33 TexReg 5295; reviewed and readopted to be effective February 17, 2012, 37 TexReg 1518.

§91.310. Annual Report to Membership.

(a) Every credit union shall provide to its membership an annual written report, as prescribed below. The report must be updated before the credit union's annual meeting and shall be available on the credit union's website throughout the year. Any credit union that does not maintain a website shall distribute the report at its annual meeting and must notify members at least annually that copies of the report are available upon request.

(b) The annual report shall cover the credit union's operations during the preceding calendar year and shall contain, at a minimum, the following information:

(1) the names and dates of expiration of the terms of office for each director on the credit union's board;

(2) the names of any honorary or advisory directors appointed by the board;

(3) a brief description of any changes, since the last report, to the credit union's:

A. senior management staff;

B. bylaws or articles of incorporation;

C. financial condition and operating results;

D. membership size and services offered; and

(4) the credit union's year end balance sheet and income/expense statement.

(c) For purposes of this rule, senior management staff shall include the chief executive officer, any assistant chief executive officers, including any vice-presidents and above, and the chief financial officer.

Source: The provisions of this §91.310 adopted to be effective November 8, 2009, 34 TexReg 7625; reviewed and readopted to be effective February 17, 2012, 37 TexReg 1518.

§91.315. Members' Access to Credit Union Documents.

(a) Required Notice. Every credit union shall provide notice to its membership of the availability of certain documents related to the credit union's finances and management.

(b) Delivery of Required Notice. A credit union shall post a copy of the required notice on its website throughout the year. The notice required by this section shall be published in the credit union's newsletter twice a year. If a credit union does not maintain a website and distribute a newsletter at least semiannually, the credit union shall provide the notice at least semiannually with each member's account statement.

(c) Documents Available to Members. Upon request, a member is entitled to review or receive a copy of the most recent version of the following credit union documents:

1. balance sheet and income statement (the non-confidential pages of the latest call report may be given to meet this requirement);
2. a summary of the most recent annual audit completed in accordance with §91.516 of this chapter (relating to Audits and Verifications);
3. written board policy regarding access to the articles of incorporation, bylaws, rules, guidelines, board policies, and copies thereof; and
4. Internal Revenue Service Form 990.

Source: The provisions of this §91.315 adopted to be effective November 8, 2009, 34 TexReg 7627; reviewed and readopted to be effective February 17, 2012, 37 TexReg 1518.

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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 make a material change to a CUSO's organizational structure, or perform new 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 Determination 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 or will be 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 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 as he deems appropriate.

(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.

Source: The provisions of this §91.801 adopted to be effective August 14, 2000, 25 TexReg 7635; adopted to be effective January 7, 2004, 29 TexReg 83; amended to be effective July 11, 2004, 29 TexReg 6630; amended to be effective July 10, 2005, 30 TexReg 3863; amended to be effective November 11, 2007, 32 TexReg 7921; amended to be effective March 4, 2009, 34 TexReg 1400; reviewed and amended to be effective March 8, 2012, 37 TexReg 1506.

§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.

(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) 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.

(5) 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.

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

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

(8) 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.

(9) 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 §124.351(a)(1) of the Act.

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

(11) 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.

(12) 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.

(13) 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.

(14) 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.

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

(18) 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.

(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 the Act, 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) Government-sponsored enterprises. A credit union may invest in government-sponsored enterprise obligations such as Federal Home Loan Banks, the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, the Federal Farm Credit Bank, and the Student Loan Marketing Association.

(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 five 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 five years or less.

(14) Mortgage-related securities. With the exception of "accrual bonds" (or Z-bonds) or 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.

(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.

(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.

Source: The provisions of this §91.802 adopted to be effective February 11, 2001, 26 TexReg 1135; amended to be effective August 11, 2002, 27 TexReg 6835; amended to be effective November 14, 2004, 29 TexReg 10254; amended to be effective November 11, 2007, 32 TexReg 7922; amended to be effective July 12, 2009, 34 TexReg 4512; reviewed and amended to be effective November 13, 2011, 36 TexReg 7540.

§91.803. Investment Limits and Prohibitions.

(a) Limitations. A credit union may invest no more than 50% of its net worth with any single obligor or related obligors. This limitation does not apply to investments issued by, or fully guaranteed as to principal and interest by, the United States or an agency, enterprise, corporation, or instrumentality of the United States, 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) Fair value--the price at which a security can be bought or sold in a current, arms length transaction between willing parties, other than in a forced or liquidation sale.

(D) 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.

(E) 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.

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

(G) Stripped mortgage-backed security (SMBS)--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. Some mortgage-backed securities represent essentially principal-only cash flows with nominal interest cash flows or essentially interest-only cash flows with nominal principal cash flows. These securities are considered SMBSs for the purposes of this rule.

(H) 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) Purchase or sell financial derivatives, such as futures, options, interest rate swaps, or forward rate agreements;

(B) Engage in adjusted trading or short sales;

(C) Purchase stripped mortgage backed securities, residual interests in CMOs/REMICs, mortgage servicing rights, commercial mortgage related securities, or small business related securities;

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

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

(F) Purchase securities used as collateral by a safekeeping concern.

(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.

Source: The provisions of this §91.803 adopted to be effective July 9, 2001, 26 TexReg 5001; amended to be effective July 11, 2004, 29 TexReg 6632; amended to be effective November 11, 2007, 32 TexReg 7922; reviewed and amended to be effective November 13, 2011, 36 TexReg 7544.

§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.

Source: The provisions of this §91.804 adopted to be effective August 14, 2000, 25 TexReg 7636; amended to be effective July 11, 2004, 29 TexReg 6632; amended to be effective March 6, 2005, 30 TexReg 1065; amended to be effective November 11, 2007, 32 TexReg 7922; reviewed and amended to be effective November 13, 2011, 36 TexReg 7544.

§91.805. Loan Participation Investments.

(a) A credit union may purchase a participation interest in a non-member loan from a corporation, credit organization, or financial organization, as permitted by §124.351(a)(8) of the Act, provided the credit union:

(1) is specifically empowered to purchase such investments in the board's written investment policy;

(2) does not obtain an interest greater than 90% of the face amount of each individual loan, if the borrower is not a member of the credit union or a member of another participating credit union;

(3) uses the same underwriting standards for loan participation investments as it does for loans originated by the credit union; and

(4) limits its aggregate investment in loan participation investments to an amount no greater than 50% of the credit union's net worth.

(b) Financial Reporting. A participation interest in a non-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.

Source: The provisions of this §91.805 adopted to be effective August 14, 2000, 25 TexReg 7636; readopted to be effective February 24, 2004, 29 TexReg 2393; amended to be effective November 11, 2007, 32 TexReg 7923; reviewed and amended to be effective November 13, 2011, 36 TexReg 7544.

§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 designated depositories, in other institutions that are not fully insured by the Federal Deposit Insurance Corporation, National Credit Union Administration, or federal or state governments or their agencies.

(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) 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.

Source: The provisions of this §91.808 adopted to be effective February 11, 2001, 26 TexReg 1137; readopted to be effective February 24, 2004, 29 TexReg 2393; amended to be effective November 11, 2007, 32 TexReg 7923; reviewed and readopted to be effective June 20, 2011, 36 TexReg 4152.

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