

Division of Securities
Utah Department of Commerce
160 East 300 South
P.O. Box 146760
Salt Lake City, Utah 84114-6760
Telephone: 801 530-6600
Facsimile: 801 530-6980

**BEFORE THE DIVISION OF SECURITIES
OF THE DEPARTMENT OF COMMERCE
OF THE STATE OF UTAH**

IN THE MATTER OF:

**XCU Capital Corporation, Inc.,
CRD#19899**

Respondent.

**STIPULATION AND CONSENT
ORDER**

Docket No. SD-07-0027

The Utah Division of Securities (“Division”), by and through its Director of Licensing, George Robison, and Respondent XCU Capital Corporation, Inc. (“XCU”), CRD#19899, hereby stipulate and agree as follows:

1. XCU was the subject of an examination conducted by the Division into allegations that it violated the Utah Uniform Securities Act (“Act”), Utah Code Ann. § 61-1-1, *et seq.*
2. In lieu of the Division filing an administrative action for sanctions, XCU and the Division have agreed to settle this matter by way of this Stipulation and Consent Order (“Order”). If entered, the Order will fully resolve all claims the Division has against XCU pertaining to this matter.
3. XCU admits the jurisdiction of the Division over it and over the subject matter of this

action.

4. XCU waives any right to a hearing to challenge the Division's evidence and present evidence on its behalf.
5. XCU has read the Order, understands its contents and submits to this Order voluntarily. No promises or threats have been made by the Division, nor by any representative of the Division, to induce XCU to enter into this Order, other than as described in this Order.
6. XCU is represented by attorneys Christine A. Bruenn and Hope M. Jarkowski and is satisfied with the legal representation received.

I. FINDINGS OF FACT

7. XCU Capital Corporation, Inc. ("XCU") is a California corporation located in Carlsbad, California and has been a licensed broker-dealer in Utah since October 28, 1992.
8. XCU Corporation, Inc. ("XCU Corporation") is a California corporation that operates as a Credit Union Service Organization ("CUSO")¹ primarily for the purpose of providing services to credit unions and their members through its wholly-owned subsidiaries. XCU and Focus Insurance Services Corporation, Inc. ("Focus") are wholly-owned subsidiaries of XCU Corporation.
9. On February 10, 2006, XCU applied for an investment adviser license in Utah. The application is currently pending.
10. XCU previously filed an investment adviser application in Utah in 2002. On September

¹A Credit Union Service Organization ("CUSO") provides operational and financial services primarily to credit unions and their members. CUSOs are permitted to earn a profit and therefore credit unions have, pursuant to National Credit Union Administration Rules and Regulations, invested in CUSOs for various business purposes.

6, 2002, in Division action SD-02-0128, the Division entered an order denying the application because it was incomplete and XCU failed to respond to a reasonable request for information from the Division.

11. XCU subsequently filed investment adviser applications in 2003 and 2004. XCU withdrew each of those applications after the Division expressed concerns that the applications were incomplete.
12. On January 31, 2002, a Utah state-chartered credit union² (“Credit Union” or “the credit union”) purchased a 6.66% interest in XCU Corporation, and Credit Union’s wholly-owned CUSO (“Utah CUSO”) entered into a Financial Institution Master Service Agreement (“Service Agreement”) with XCU.
13. On December 31, 2004, Utah CUSO assigned the Service Agreement to Credit Union. The Service Agreement between Credit Union and XCU is still in effect.
14. The Service Agreement is a “networking” arrangement whereby XCU, through its registered representatives, provides securities brokerage services to Credit Union’s members on Credit Union’s premises.
15. Credit Union used this networking arrangement to act as an unlicensed broker-dealer.
16. During the period relevant to this action, XCU registered representatives have been designated as “dual employees,” which means they are employees of Credit Union and are also independent contractors of XCU³.

²On May 2, 2003, the credit union became a federal-chartered credit union.

³Generally, an employer must withhold income taxes, withhold and pay Social Security and Medicare taxes, and pay unemployment tax on wages paid to employees. An independent contractor has more independence in completing contracted work and is responsible for his

17. Dual employees must disclose to credit union members that the employee is acting solely on behalf of the broker-dealer when dealing with investment products.⁴
18. In March 2006, the Division received a call from a Utah resident who indicated she had a financial adviser at Credit Union. The caller was concerned about a clause in the prospectus of an investment she had recently made through her Credit Union financial adviser in the Aquila Group of Funds.
19. An initial review of the Division's records revealed no registration filing for the Aquila Group of Funds. After meeting with Credit Union, the Division learned the fund the customer invested in is the Tax Free Fund for Utah, which is a part of the Aquila Group of Funds and is properly registered with the Division.
20. The Division contacted Credit Union to inquire about the Aquila fund and the call was transferred to various people. None of them could answer the Division's questions.
21. The Division thereafter reviewed Credit Union's website, which contained a list of financial advisors. The Central Registration Depository ("CRD")⁵ showed that the financial advisors listed on Credit Union's website were licensed with XCU.
22. The Division contacted XCU and was again transferred to various people before reaching a manager of XCU's Office of Supervisory Jurisdiction ("OSJ").
23. The manager told the Division that XCU provides clearing services to Credit Union and

taxes.

⁴See National Credit Union Administration Office of General Counsel Letter OGC 01-0742.

⁵CRD is a computerized database maintained by the National Association of Securities Dealers ("NASD"). CRD contains employment, licensing and disciplinary information on broker-dealers, investment advisers and investment adviser representatives.

that licensed agents are employees of Credit Union, not of XCU.

24. The manager also stated that compliance duties and OSJ supervision are performed by Credit Union employees.
25. Credit Union's Senior Vice President and Chief Risk Officer later returned the Division's earlier call to Credit Union. She told the Division that Credit Union is licensed and gave the Division the name and CRD number of XCU.
26. Division auditors conducted on-site exams at XCU's office in Carlsbad, California and of the OSJ branch office on Credit Union's premises in Utah.

Examination Findings

27. Credit Union's name and logo were prominently displayed on all investment services promotional materials, including business cards that the Division reviewed during its XCU audit.
28. On promotional materials, dual employees used the title, "Investment Representative" followed by the name of Credit Union.
29. Dual employees sent out letters stating, "[t]ime for a free annual review! Now is a good time to review your investments! [Credit Union] would like to thank you again for your business and I look forward to continuing our relationship."
30. Credit Union's "Non-Solicitation and Confidentiality Agreement" for its dual employees, who are registered representatives of XCU, states that Credit Union "engages in and operates, among other things, a business which offers 'Investment Products.'"
31. The Non-Solicitation and Confidentiality Agreement defines "Investment Products" as, among other things, "securities products of every kind and nature including, but not

limited to, mutual funds, stocks, variable annuities, bonds, and related products which are regulated by the Securities and Exchange Commission or applicable state regulatory entities.”

32. XCU registered representatives received transaction-based commissions but these commissions were not paid to the registered representatives directly by XCU. Instead, pursuant to the Service Agreement, XCU paid between 85 and 93% of the transaction-based commissions to Credit Union. Credit Union determined the percentage that ultimately was paid to the registered representatives and retained the remaining commissions.
33. Credit Union used the commissions received from XCU to pay the dual employees and to pay Credit Union’s expenses that were related to the XCU brokerage services offered on Credit Union’s premises.

CUSOs and Networking Arrangements

34. The National Credit Union Administration (“NCUA”) is the federal agency that charters and supervises federal credit unions (“FCUs”) and insures deposits in FCUs through the National Credit Union Share Insurance Fund (“NCUSIF”).
35. NCUA issues regulations (“NCUA Rules and Regulations”)⁶ to interpret and enforce the Federal Credit Union Act (“FCUA”)⁷, which governs federally chartered credit unions.
36. CUSOs are permitted to earn profits and therefore credit unions have, pursuant to NCUA Rules and Regulations, invested in CUSOs for various business purposes.

⁶Codified at 12 C.F.R. §700 (2006) *et seq.*

⁷Codified at 12 U.S.C. §1751 (1998) *et seq.*

37. Section 712.5(1) of the NCUA Rules and Regulations, lists brokerage services as one of the enumerated pre-approved activities in which CUSOs may engage.
38. Section 712.4 of the NCUA Rules and Regulations sets forth what a CUSO and a FCU must do to maintain separate identities. One of the requirements is that CUSOs and their investing FCUs must be held out to the public as separate enterprises and that the CUSO cannot be treated as a department of the FCU.
39. Networking arrangements allow broker-dealers to offer investment services on credit union premises to credit union members. Broker-dealers and credit unions often use dual employees to provide the investment services.
40. In April 2002, XCU's then-president and CEO was quoted on the website, www.CreditUnions.com, as describing credit unions' purchases of interests in XCU Corporation as:

...credit unions becoming their own broker-dealer, rather than doing business with a third-party. For an ownership level of 6.66% each, it means the credit unions are no longer "basically renting" their financial investment services from other entities...

Splitting Transaction-Based Commissions

41. Pursuant to the Service Agreement, XCU paid Credit Union between 85% and 93% of the annualized gross commissions XCU received from transactions made by dual employees.
42. From this amount, Credit Union paid dual employees commissions based on a commission payout grid. Under the terms of the Service Agreement, Credit Union determined the commission payout grid.
43. From its percentage of the annualized gross commissions, Credit Union also paid its

expenses related to the services provided to its members by the XCU registered representatives.

44. In 2004 and 2005, after paying its dual employees and paying expenses, Credit Union's income statements reported income from XCU of over \$60,000 each year.
45. Since January 2002, Credit Union has received compensation for effecting transactions in securities with Utah residents. Credit Union also participated in broker-dealer presentations to the public, representing that it is in the business of effecting securities business. Credit Union marketed itself as the entity effecting transactions in securities.

Approval of Misleading Marketing Materials

46. XCU approved the use of promotional materials that prominently display Credit Union's logo and include the names of dual employees who use the title, "Investment Representative" followed by Credit Union's name. Only at the bottom of the promotional materials, in fine print, was the required disclosure that securities are offered through XCU.
47. XCU approved the use of letters written on Credit Union's letterhead sent by dual employees using the title, "Investment Representative" followed by Credit Union's name. The bottom of the letter contained the XCU disclosure in small print.
48. XCU approved marketing materials for seminars that were mailed to Credit Union's members in Credit Union envelopes. The marketing materials prominently displayed Credit Union's logo and listed the seminar presenters with the titles of "Investment Representative" followed by Credit Union's name.
49. XCU approved investment related portions of Credit Union's website. Under the "Products and Services" portion of the website, Credit Union had a web page for

investment services. The page stated that Credit Union’s “mission is to provide financial peace of mind through sound investment advice.”

50. This XCU-approved page, included a link that included the tab, “Financial Advisors,” which listed five individuals as investment representatives of XCU Capital.
51. The page also had a tab, “Refer-a-Friend” that states, “yes, I’d like to refer a friend to an advisor with [Credit Union.]”
52. Another example of XCU-approved promotional materials is a January 30, 2006, letter from an XCU/Credit Union dual employee to a client. In part, the letter read:

With the portfolio I have presented I really believe that you can get even better money management with improved risk adjusted returns while having a financial advisor on your side. I would be your contact person going forward and can provide increased depth of service for your portfolio.

II. CONCLUSIONS OF LAW

53. XCU willfully⁸ engaged in the following misconduct:

Dishonest and Unethical Business Practices Under § 61-1-6(2)(g) of the Act

- a. XCU approved advertisements that emphasized Credit Union and held Credit Union out as a provider of investment advice. XCU’s use of advertising or sales presentations in such a fashion as to be deceptive or misleading constitutes dishonest and unethical conduct under Utah Admin. Code R164-6-1(C)(18), warranting sanctions under Section 61-1-6(2)(g) of the Act. Moreover, through its approval of Credit Union’s advertising materials, XCU held itself out as a

⁸To act willfully in this context means to act deliberately and purposefully, as distinguished from merely accidentally or inadvertently. Willful, when applied to the intent with which an act is done or omitted, implies a willingness to commit the act, and does not require an intent to violate the law or to injure another or acquire any advantage.

provider of investment advice, which under Utah Admin. Code R164-4-2(G)(4)(a)(i), constitutes an act or practice that requires licensing as an investment adviser. XCU's failure to license as an investment adviser is a violation of Section 61-1-3(3) of the Act.

- b. XCU published, circulated, or distributed public communications that it knew or should have known contained false or misleading statements of material fact, which conduct constitutes dishonest or unethical practices, warranting disciplinary sanctions under Section 61-1-6(2)(g) of the Act.
- c. XCU aided an unlicensed entity in effecting securities transactions, split transaction-based commissions with a non-NASD member, and implied that the sale of interests in the broker-dealer enabled the broker-dealer shareholders to act as a broker-dealer. Such conduct constitutes dishonest or unethical practices warranting sanctions under Section 61-1-6(2)(g) of the Act.

Failure to Supervise Under § 61-1-6(2)(j) of the Act

- d. XCU's registered representatives used numerous misleading promotional materials. XCU failed to implement and enforce policies and procedures reasonably designed to detect and prevent agents' securities law violations, and therefore failed to reasonably supervise its agents, warranting disciplinary sanctions under Section 61-1-6(2)(j) of the Act.

III. REMEDIAL ACTIONS/SANCTIONS

- 54. XCU neither admits nor denies the Division's investigative findings and conclusions, but consents to the entry of an Order requiring XCU to pay a fine of \$40,000 within thirty (30) days of the entry of this Order.

55. XCU represents that information provided to the Division in connection with this matter is accurate and complete.
56. XCU agrees to corrective action in the State of Utah, some of which may already have been implemented, as set forth herein. Within 60 days following entry of this Order, XCU shall amend contracts and procedures as necessary to ensure compliance with this Order.
57. XCU shall cease splitting commissions with Credit Union, and will not split commissions with any unlicensed entity in Utah.
58. XCU may enter into networking arrangements with credit unions wherein XCU pays the credit union a reasonable up-front fee for services. The fee may be used to cover the credit union's reasonable expenses, for example, rent for the space on the credit union's premises. Payroll for dual employees may run through the credit union as it would in a temporary employee agency or payroll services company, and a reasonable charge for such service may be included in the up-front fee. A reasonable fee for access to credit union members and member information may also be paid to the credit union. There will, however, be no charge-backs, no bonuses, and no transaction-based portion of the fee, but such can be passed through to the registered representatives who are dual employees. No portion of the fee may be related to the volume of securities business that occurs. Payment of the up-front fee may be paid in monthly installments.
59. XCU shall approve all advertisements, correspondence, letterhead, web sites, web pages, business cards, seminar materials, presentations and any similar communications with the public. XCU shall ensure that the brand which is marketed is that of XCU and not that of Credit Union. Marketing materials shall only reference Credit Union for the purpose of

identifying where XCU's services are located, and may describe the existence of a networking arrangement between the credit union and XCU. Any use of the Credit Union name and logo on marketing materials must not be greater than 1/2 the size of XCU's name and logo. These requirements apply equally to communications with the public that offer or discuss investment advisory services.

60. If a seminar is to be held on Credit Union premises, a written disclaimer will be made to participants which clearly indicates that services and products offered are made by XCU and not by Credit Union.
61. XCU shall send a letter to all Utah clients (current and past) since 2002 explaining that XCU is the broker-dealer, that XCU provides broker-dealer services on Credit Union premises, and that these broker-dealer services are not provided by the credit union.
62. XCU shall ensure that all XCU business that is conducted on a credit union's premises is done so in an area that is physically separate from the credit union's regular business activities, and that proper XCU signage is clearly visible.
63. XCU shall ensure that any dual employee's business cards include the name and logo of XCU, a toll-free number for XCU, and XCU's home office address. Any identification of the credit union shall be not greater than 1/2 of the size of the XCU name and logo, and shall only refer to the location and the existence of the networking arrangement. Alternatively, dual employees may have separate credit union business cards that identify the individual's role as a credit union employee.
64. XCU will control, properly supervise, and be responsible for its registered representatives.
65. During 2007, XCU will conduct an on-site examination of all business locations in Utah,

located on credit union properties, to ensure compliance with all terms set forth herein.

XCU will provide the results of these audits to the Division.

66. For 2007 and 2008, XCU will, on a quarterly basis, send the Division copies of all Utah customer complaints, written or verbal, and all memoranda relating to all Utah customer complaints. XCU will include documents detailing the resolution of the complaints.
67. Including the items above, XCU will also comply with the provisions of the SEC Chubb letter⁹ and the Utah Uniform Securities Act.
68. If the Division changes its interpretation of compensation arrangements allowed between broker-dealers and credit unions such that sharing of commissions is permitted, XCU may approach the Division to modify this agreement.

IV. FINAL RESOLUTION

69. XCU acknowledges that this Order, upon approval by the Division Director and the Securities Advisory Board shall be the final compromise and settlement of this matter. XCU further acknowledges that if the Division Director and Securities Advisory Board do not accept the terms of the Order, it shall be deemed null and void and without any force or effect whatsoever.
70. XCU acknowledges that the Order does not affect any civil or arbitration causes of action that third-parties may have against it arising in whole or in part from XCU's actions, and that the Order does not affect any criminal cause of action that a prosecutor might bring.
71. This Order constitutes the entire agreement between the parties herein and supersedes and cancels any and all prior negotiations, representations, understandings, or agreements

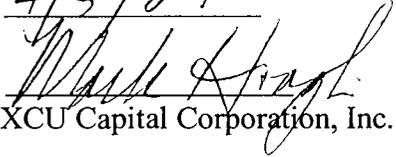
⁹See SEC Letter re: Chubb Securities Corp. (November 24, 1993).

between the parties. There are no verbal agreements which modify, interpret, construe, or otherwise affect this Order in any way.

Date: 04/11/07

By: 
George Robison
Director of Licensing
Utah Division of Securities

Date: 4/5/07

By: 
XCU Capital Corporation, Inc.

Its: PRESIDENT/CEO

Approved:


Laurie L. Noda
Assistant Attorney General

Approved:


Christine A. Bruenn
Hope M. Jarkowski
Counsel for XCU Capital Corporation, Inc.

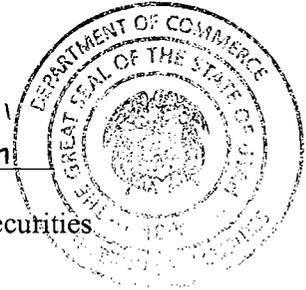
ORDER

IT IS HEREBY ORDERED THAT:

1. The Division has made a sufficient showing of Findings of Fact and Conclusions of Law to form a basis for this settlement.
2. Respondent pay a fine of \$40,000 within thirty (30) days of entry of this Order.
3. Respondent comply with the obligations set forth in Section III of this Order and the requirements of the Utah Uniform Securities Act in all future business in this state.

DATED this 16th day of April, 2007.


WAYNE KLEIN
Director, Utah Division of Securities



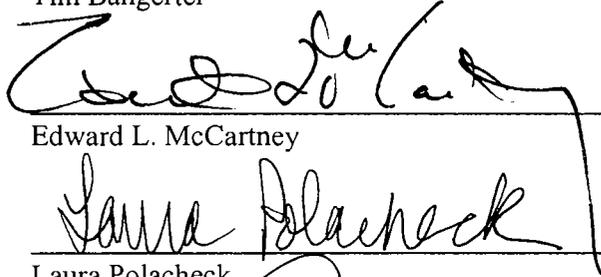
BY THE UTAH SECURITIES ADVISORY BOARD:

The foregoing Order is hereby accepted, confirmed and approved by the Utah Securities
Advisory Board.

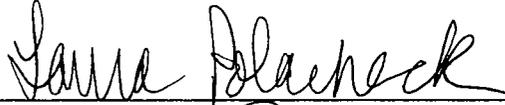
DATED this 16~~th~~ day of April, 2007.



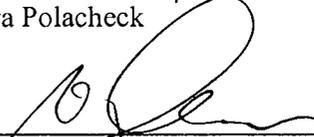
Tim Bangerter



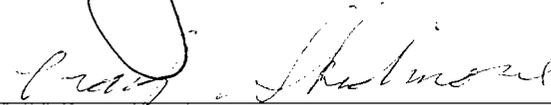
Edward L. McCartney



Laura Polacheck



Mark Pugsley



Craig Skidmore

Certificate of Mailing

I certify that on the 19TH day of APRIL, 2007, I mailed a true and correct copy of the Stipulation and Consent Order to:

Christine A. Bruenn
Bingham McCutchen LLP
121 Middle Street, Ste. 400
Portland, ME 04101
Counsel for XCU Capital Corporation, Inc.


Ramona Radzinski
Executive Secretary