NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

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JUN 21 1985

Mr. Stephen M. Endaya
General Manager
Aerospace Federal Credit Union
P.O. Box 90735
Los Angeles, CA 90009

Dear Mr. Endaya:

This is in reply to your letter dated May 28, 1985, concerning the Franklin U.S. Government Securities Fund ("Fund"). Specifically, you have asked for a current legal opinion with respect to the legality of the Fund as an FCU investment.

The last legal opinion written about the Fund was a letter dated March 22, 1985. We have enclosed a copy of that letter for your review. We should point out that, since the time of writing that opinion, NCUA's position on the accounting treatment of the sales charge has been revised. The present position is contained in NCUA Letter No. 79 dated May 29, 1985 (we have enclosed a copy for your review).

I hope that we have been of assistance.

Sincerely,

/S/

STEVEN R. BISKER
Assistant General Counsel

Enclosures

FOIA Vol I Part E.2.

NCUA LETTER TO CREDIT UNIONS

NCUA LETTER NO. 79

DATE: May 29, 1985

TO THE BOARD OF DIRECTORS OF THE FEDERALLY INSURED CREDIT UNION ADDRESSED:

Recently, there has been an increase in the credit union purchase of mutual funds. Since the mutual fund market is relatively new to credit unions and the market functions somewhat differently from other traditional investment vehicles, I would like to take this opportunity to briefly discuss these funds and to provide you with NCUA's position on accounting procedures.

WHAT IS A MUTUAL FUND?

Mutual funds permit investors to acquire a pro-rata share of a diversified portfolio of securities. Part of the popularity of mutual funds is their ability to offer small investors some of the advantages otherwise limited to large investors: diversification of the portfolio and professional portfolio management. An investment in a mutual fund is actually the purchase of shares in a fund. The shares are purchased at a public offering price, which is the net asset value of a share in the fund at the time of purchase, plus, in some cases, a sales charge or commission. It should be noted that a common trust plan is a mutual fund.

Mutual funds and common trusts are usually open-end investment companies because they stand ready to sell the public as large a volume of shares as it wishes to buy. Whatever volume of money is drawn in is invested according to the formula or policy of the particular fund. When investors wish to cash in their shares, the fund sells a part of its portfolio to raise the money. It then pays off the investor on the basis of the value of its assets at the date of liquidation. In effect, you buy $1,000 worth of shares in the fund and, when you sell your interest, you receive your proportionate share of the value of the fund's assets at the time of the sale. Therefore, you may realize a gain or a loss on your original investment.

WHICH MUTUAL FUNDS CAN A FEDERALLY INSURED CREDIT UNION INVEST IN?

Section 107(7) and (8) of the Federal Credit Union Act (12 U.S.C. section 1757 (7) and (8)) and Part 703 of the NCUA Rules and Regulations (12 C.F.R. Part 703) specify the types of investments, investment activities, and deposits that are legal for federal credit unions. NCUA has taken the position that federal credit unions can invest in a mutual fund or a common trust if its portfolio is limited to investments, investment activities, and deposits authorized for federal credit unions. Federally insured state-chartered credit unions should determine the legality of a mutual fund investment by reviewing state statutes and regulations and, where necessary, by consultation with your state regulator. Prior to making any investment, you should obtain a prospectus and determine that all investments, investment activities and deposits are legal for your credit union. As with any investment, you should take into consideration both safety and soundness and the appropriateness of the investment for your credit union.

ACCOUNTING PROCEDURES

Unlike a direct investment in government securities, shares in a mutual fund or a common trust do not have a stated value at maturity or a specific maturity date. The value of shares changes based on the portfolio and market conditions. Therefore, market conditions play a more significant role in determining the ultimate recoverable value of an investment in a mutual fund or a common trust than in an investment with a specific maturity date.