



NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

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Office of General Counsel

Bruce D. Patner, President
Potomac Community Federal Credit Union
10220 River Road
Potomac, MD 20854

Dear Mr. Patner:

Senator Jepsen referred your recent letter to this Office for response. Your letter sets forth your thoughts and those of your board on how credit unions may be better able to compete in today's economic environment. The issues that you raise and suggestions that you make are addressed below.

1. Decline in traditional loan sources.
 - (a) Automobile loans.

We are aware that credit unions have lost some of their traditional share of the market in domestic automobile lending due to below-market financing available through automobile manufacturers' financing subsidiaries. You suggest that Federal credit unions (FCU's) are further burdened in that they cannot participate in dealer reserve programs whereby an FCU would reimburse an automobile dealer for efforts and expenses in initiating loans. Be advised that FCU's can participate in such programs. In addition, there are other automobile financing options available to FCU's. Many FCU's are offering automobiles to their members at fleet purchasing prices, either through a credit union service organization (CUSO) or directly. FCU's are financing such purchases. FCU's are also leasing vehicles to their members themselves (pursuant to Interpretive Ruling and Policy Statement 83-3) or through their CUSO's. Although there is great competition in the automobile financing market, these alternatives present options for FCU's.

- (b) Real estate loans

You state that FCU's are highly restricted in charging points and in the manner in which they are able to account for this income. The NCUA Rules and Regulations do not limit the amount of points that an FCU may charge. Of course, the points are calculated into the interest being charged and FCU's cannot charge more than the current interest ceiling of 21%. The accounting treatment for buyer's and seller's points is addressed

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in the Accounting Manual for FCU's. See Section 6110 of the Accounting Manual (Accounts 886 and 887). We note that the accounting treatment in the Manual is in line with the recent FASB position on the issue.

(c) Student Loans

You note that you have lost your market for student loans due to changes in Federal law. This is regrettable. Unfortunately, we have little control over such laws.

(d) Home equity loans

You note that your FCU has been making home equity loans for several years but now faces greater competition from banks and savings associations. FCU home equity loans are subject to Section 701.21 of the NCUA Rules and Regulations. The lending provision has been deregulated for the most part and does not subject FCU's to any greater restrictions than those imposed on banks and savings associations making home equity loans.

You state further that other lending institutions have an edge on FCU's because they can lend to the general public and can also offer other services that FCU's are not permitted to offer. What sets credit unions apart from other institutions is that they are member-owned and -operated institutions. Because of their special role, they have been afforded privileges (e.g., tax exempt status) not afforded to other financial institutions. A soundly managed FCU should be more than able to compete in the financial services market and keep their members as customers of the credit union.

You note that, in conjunction with making loans, other financial institutions are able to "cross sell" services and products that provide income to the institution. FCU's may offer a variety of services to their members through their CUSO's (e.g., brokerage services, trust services, etc., see Section 701.27 of the NCUA Regulations) or as a conduit for a third-party vendor (e.g. insurance, group purchasing) under Part 721 of the NCUA Regulations. In the case of the sale of insurance related to loans or shares at the FCU, pursuant to Part 721, an FCU can derive income beyond its administrative costs.

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(e) Consumer loans

You note that banks can appeal to a wider market of consumers and can "cross sell" other services. As noted above, FCU's may offer most services offered by banks to their members either with the use of a CUSO (Section 701.27) or through a third-party vendor pursuant to Part 721.

2. Some possible solutions and new competitive tools.
(a) Loan Participations and (b) Loan Pools

FCU's can participate in both the purchase and sale of loan participations. These activities are authorized for FCU's pursuant to Section 107(5)(E) and 107(13) of the FCU Act and Sections 701.22 and 701.23 of the NCUA Regulations.

3. Investment Authority

(a) Loans to nonprofit organizations.

You state that FCU's should be able to make loans to certain non-profit organizations, for instance a mortgage loan to a church. You reason that repayment on such loans is excellent and that loans of this nature are important to the community. Such loans are not precluded by the FCU Act. As long as the borrowing entity (church) is a member of the FCU (in a community-based FCU, a church would qualify for membership if within the geographic boundaries), a loan to a church would be permitted. The church could be eligible to obtain a construction loan and/or mortgage loan within the limitations contained in the Act and Regulations relating to such loans.

(b) Loans to State and Local Governmental Agencies

As noted previously, an FCU can only make loans to its members. However, FCU's do have the authority to invest in issuances of state and political subdivisions. (See Section 107(7)(K) of the FCU Act.)

I hope that we have been able to shed a little more light on the issues raised in your letter.

Sincerely,



STEVEN R. BISKER
Assistant General Counsel

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