



NATIONAL CREDIT UNION ADMINISTRATION  
Washington, D.C. 20456

GC/JS:sg  
3600

July 19, 1988

Office of General Counsel

Mr. Daniel P. Bradley  
DM Federal Credit Union  
P.O. Box 15115  
Tucson, Arizona 85708

Re: Subventive Auto Financing (Your June 14, 1988, Letter)

Dear Mr. Bradley:

The Federal Credit Union ("FCU") Act and NCUA's Rules and Regulations do not prohibit FCU's from participating in "subventive" (manufacturer or dealer subsidized) auto financing, even up to 100 percent of the finance charges. However, certain aspects of such a plan may create concerns under the FCU Act and our Regulations. Without reviewing your particular plan, we cannot comment further than to say that an FCU should carefully review its financing plan in light of the finance charge ceilings in Section 701.21(7) of the NCUA Rules and Regulations; the Holder-in-Due-Course Rule, 16 C.F.R. §433.2(b); and the disclosure requirements of Regulation Z.

FACTS

Your FCU proposes participating in a subventive auto financing arrangement. Such an arrangement would entail an automobile dealer's or manufacturer's subsidizing credit union financing by paying the FCU the difference between their normal rate of interest and the lower contract rate. One such arrangement would allow a dealer or manufacturer to subsidize 100 percent of the finance charges.

ANALYSIS

FCU Power

FCU's are empowered to make loans and extend lines of credit pursuant to Section 107(5) of the FCU Act [12 U.S.C. §1757(5)]. Section 107(16) of the FCU Act [12 U.S.C. §1757(16)] grants FCU's

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the authority to exercise such incidental powers necessary or requisite to carry out their express powers. It has been our opinion that Sections 107(5) and 107(16) of the FCU Act provide the statutory authority enabling an FCU to participate in a subventive financing arrangement, even up to 100 percent of the finance charges.

#### Finance Charge Ceilings

You have stated that, for purposes of Regulation Z, the Federal Reserve Board would consider the subventive financing subsidies to be seller's points. Points are considered "finance charges" in Regulation Z [12 C.F.R. §226.4(b)(3)], and since the NCUA Board has adopted the regulation Z definition of "finance charge" to flesh out the term as it appears in the FCU Act [45 Fed. Reg. 22,890 (1980)], you must assure that your proposed plan complies with the usury provisions of the FCU Act [12 U.S.C. §1757(5)(A)(vi)] and NCUA Rules and Regulations [12 U.S.C. §701.21(c)(7)].

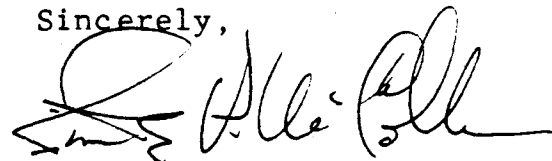
#### Holder-in-Due-Course

In drafting the plan, care should be taken to determine whether there is a working relationship between the dealer or manufacturer and the credit union which would constitute a "business arrangement" under the Holder-in-Due-Course Rule, 16 C.F.R. §433.2(b). Although the FCU has no liability under the rule unless the dealer or manufacturer directs the FCU to place the Holder notice in its loan contracts, the FCU would be subject to any claims or defenses that the borrowing member could assert against the dealer if the "business arrangement" exists.

#### Disclosure Requirements

Upon completion of your written plan, you should consult the Federal Reserve Board to determine the requisite disclosure requirements under Regulation Z.

Sincerely,



TIMOTHY P. McCOLLUM  
Assistant General Counsel

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cc:Region V