



NATIONAL CREDIT UNION ADMINISTRATION
Washington, D.C. 20456

November 9, 1989

Office of General Counsel

GC\RRD:sg
SSIC 4650
89-0928

Mr. Ashok Roy
Compliance Officer
Chattanooga TVA Employees Federal Credit Union
P.O. Box 11146
Chattanooga, TN 37401-2146

Re: Guaranteed Student Loans (Your September 25,
1989, Letter)

Dear Mr. Roy:

Your Federal credit union ("FCU") wants to offer guaranteed student loans to nonmembers because the volume of student loans made to members only is not enough to make your operations economically feasible. You argue that such activity is permissible for your FCU. We do not agree. The activity you describe is impermissible for FCU's.

ANALYSIS

The first step in your analysis is correct. FCU's can make loans only to members. (See Section 107(5) of the FCU Act, 12 U.S.C. 1757(5), and Section 701.21(a) of the NCUA Regulations, 12 C.F.R. §701.21(a).) You then attempt to classify guaranteed student loans to nonmembers as investments since the loans will be sold before they are repaid. FCU investment authority is found in Sections 107(7), (8) and (15) of the FCU Act (12 U.S.C. §1757(7), (8) and (15) (enclosed).) The activity you describe is not authorized under these sections. In addition, we do not believe the activity you describe is authorized under any provision of the FCU Act or NCUA Rules and Regulations.

FOIA

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There is one regulatory provision which may assist you. Section 701.23(b)(1) of the NCUA Rules and Regulations (12 C.F.R. §701.23(b)(1) enclosed) provides, in part:

A Federal credit union may purchase, in whole or in part, within the limitations of the [FCU's] board of directors' written purchase policies:

* * *

(iii) Student loans, from any source, if the purchaser is granting student loans on an ongoing basis and if the purchase will facilitate the purchasing credit union's packaging of a pool of such loans to be sold or pledged on the secondary market;

This authorized activity is intended to assist FCU's participation in the student loan secondary market. As discussed above, FCU's are not permitted to directly fund student loans to nonmembers; however, nonmember student loans may be purchased from any source pursuant to 701.23, if such purchase will facilitate sale on the secondary market.

Sincerely,

Hattie M. Ulan

HATTIE M. ULAN
Assistant General Counsel

Enclosures

(3) the names and addresses of the subscribers to the certificate and the number of shares subscribed by each;

(4) the initial par value of the shares;

(5) the proposed field of membership, specified in detail;

(6) the term of the existence of the corporation, which may be perpetual; and

(7) the fact that the certificate is made to enable such persons to avail themselves of the advantages of this chapter.

Such organization certificate may also contain any provisions approved by the Board for the management of the business of the association and for the conduct of its affairs and relative to the powers of its directors, officers, or stockholders.

§ 1754

§ 104

Approval of organization certificate.—The organization certificate shall be presented to the Board for approval. Before any organization certificate is approved, an appropriate investigation shall be made for the purpose of determining (1) whether the organization certificate conforms to the provisions of this chapter; (2) the general character and fitness of the subscribers thereto; and (3) the economic advisability of establishing the proposed Federal credit union. Upon approval of such organization certificate by the Board it shall be the charter of the corporation, and one of the originals thereof shall be delivered to the corporation after the payment of the fee required therefor. Upon such approval the Federal credit union shall be a body corporate and as such, subject to the limitations herein contained, shall be vested with all of the powers and charged with all of the liabilities conferred and imposed by this chapter upon corporations organized hereunder.

§ 1755

§ 105

Fees.—(a) In accordance with rules prescribed by the Board, each Federal credit union shall pay to the Administration an annual operating fee which may be composed of one or more charges identified as to the function or functions for which assessed.

(b) The fee assessed under this section shall be determined according to a schedule, or schedules, or other method determined by the Board to be appropriate, which gives due consideration to the expenses of the Administration in carrying out its responsibilities under this Act and to the ability of Federal credit unions to pay the fee. The Board shall, among other things, determine the periods

for which the fee shall be assessed and the date or dates for the payment of the fee or increments thereof.

(c) If the annual operating fee is composed of separate charges, no supervision charge shall be payable by a Federal credit union, and the Board may waive payment of any or all other charges comprising the fee, with respect to the year in which its charter is issued, or in which final distribution is made in its liquidation or the charter canceled.

(d) All operating fees shall be deposited with the Treasurer of the United States for the account of the Administration and may be expended by the Board to defray the expenses incurred in carrying out the provisions of this Act including the examination and supervision of Federal credit unions.

(e)(1) Upon request of the Board, the Secretary of the Treasury shall invest and reinvest such portions of the annual operating fees deposited under subsection (d) as the Board determines are not needed for current operations.

(2) Such investments may be made only in interest bearing securities of the United States with maturities requested by the Board bearing interest at rates determined by the Secretary of the Treasury, taking into consideration current market yields on outstanding marketable obligations of the United States of comparable maturities.

(3) All income derived from such investments and reinvestments shall be deposited to the account of the Administration described in subsection (d).

§ 1756

§ 106

Reports and examinations.—Federal credit unions shall be under the supervision of the Board, and shall make financial reports to it as and when it may require, but at least annually. Each Federal credit union shall be subject to examination by, and for this purpose shall make its books and records accessible to, any person designated by the Board.

§ 1757

§ 107

Powers.—A Federal credit union shall have succession in its corporate name during its existence and shall have power—

(1) to make contracts;

(2) to sue and be sued;

(3) to adopt and use a common seal and alter the same at pleasure;

(4) to purchase, hold, and dispose of property necessary or incidental to its operations;

(5) to make loans, the maturities of which shall not exceed twelve years except as otherwise provided herein, and extend lines of credit to its members, to other credit unions, and to credit union organizations and to participate with other credit unions, credit union organizations, or financial organizations in making loans to credit union members in accordance with the following:

(A) Loans to members shall be made in conformity with criteria established by the board of directors: *Provided, That—*

(i) a residential real estate loan on a one-to-four-family dwelling, including an individual cooperative unit, that is or will be the principal residence of a credit union member, and which is secured by a first lien upon such dwelling, and may have a maturity not exceeding thirty years or such other limits as shall be set by the National Credit Union Administration Board (except that a loan on an individual cooperative unit shall be adequately secured as defined by the Board), subject to the rules and regulations of the Board;

(ii) a loan to finance the purchase of a mobile home, which shall be secured by a first lien on such mobile home, to be used by the credit union member as his residence, a loan for the repair, alteration, or improvement of a residential dwelling which is the residence of a credit union member, or a second mortgage loan secured by a residential dwelling which is the residence of a credit union member, shall have a maturity not to exceed 15 years or any longer term which the Board may allow.

(iii) a loan secured by the insurance or guarantee of, or with advance commitment to purchase the loan by, the Federal Government, a State government or any agency of either may be made for the maturity and under the terms and conditions specified in the law under which such insurance, guarantee, or commitment is provided;

(iv) a loan or aggregate of loans to a director or member of the supervisory or credit committee of the credit union making the loan which exceeds \$10,000 plus pledged shares, be approved by the board of directors;

(v) loans to other members for which directors or members of the supervisory or credit committee act as guarantor or endorser be approved by the board of directors when such loans standing alone or when added to any outstanding loan or loans of the guarantor or endorser exceeds \$10,000;

(vi) the rate of interest may not exceed 15 per centum per annum on the unpaid balance inclusive of all finance charges, except that the Board may establish—

(I) after consultation with the appropriate committees of the Congress, the Department of Treasury, and the Federal financial institution regulatory agencies, an interest rate ceiling exceeding such 15 per centum per annum rate, for periods not to exceed 18 months, if it determines that money market interest rates have risen over the preceding six-month period and that prevailing interest rate levels threaten the safety and soundness of individual credit unions as evidenced by adverse trends in liquidity, capital, earnings, and growth; and

(II) a higher interest rate ceiling for Agent members of the Central Liquidity Facility in carrying out the provisions of title III for such periods as the Board may authorize,

(vii) the taking, receiving, reserving, or charging of a rate of interest greater than is allowed by this paragraph, when knowingly done, shall be deemed a forfeiture of the entire interest which the note, bill, or other evidence of debt carries with it, or which has been agreed to be paid thereon. If such greater rate of interest has been paid, the person by whom it has been paid, or his legal representatives, may recover back from the credit union taking or receiving the same, in an action in the nature of an action of debt, the entire amount of interest paid; but such action must be commenced within two years from the time the usurious collection was made;

(viii) a borrower may repay his loan, prior to maturity in whole or in part on any business day without penalty, except that on a first or second mortgage loan a Federal credit union may require that any partial prepayments (I) be made on the date monthly installments are due and (II) be in the amount of that part of one or more monthly installments which would be applicable to principal;

(ix) loans shall be paid or amortized in accordance with rules and regulations prescribed by the Board after taking into account the needs or conditions of the borrowers, the amounts and duration of the loans, the interests of the members and the credit unions, and such other factors as the Board deems relevant;

(x) loans must be approved by the credit committee or a loan officer, but no loan may be made to any member if, upon the making of that loan, the member would be indebted to the Federal

credit union upon loans made to him in an aggregate amount which would exceed 10 per centum of the credit union's unimpaired capital and surplus.

(B) A self-replenishing line of credit to a borrower may be established to a stated maximum amount on certain terms and conditions which may be different from the terms and conditions established for another borrower.

(C) Loans to other credit unions shall be approved by the board of directors.

(D) Loans to credit union organizations shall be approved by the board of directors and shall not exceed 1 per centum of the paid-in and unimpaired capital and surplus of the credit union. A credit union organization means any organization as determined by the Board, which is established primarily to serve the needs of its member credit unions, and whose business relates to the daily operations of the credit unions they serve.

(E) Participation loans with other credit unions, credit union organizations, or financial organizations shall be in accordance with written policies of the board of directors. *Provided*, That a credit union which originates a loan for which participation arrangements are made in accordance with this subsection shall retain an interest of at least 10 per centum of the face amount of the loan.

(6) To receive from its members, from other credit unions, from an officer, employee, or agent of those nonmember units of Federal, Indian Tribal, State, or local governments and political subdivisions thereof enumerated in section 207 of this Act and in the manner so prescribed, from the Central Liquidity Facility, and from nonmembers in the case of credit unions serving predominantly low-income members (as defined by the Board) payments, representing equity, on—(A) shares which may be issued at varying dividend rates; (B) share certificates which may be issued at varying dividend rates and maturities; and (C) share draft accounts authorized under Section 205(f); subject to such terms, rates, and conditions as may be established by the board of directors, within limitations prescribed by the Board.

(7) To invest its funds (A) in loans exclusively to members; (B) in obligations of the United States of America, or securities fully guaranteed as to principal and interest thereby; (C) in accordance with rules and regulations prescribed by the Board, in loans to other credit unions in the total amount not exceeding 25 per centum of its paid-in and unimpaired capital and surplus; (D) in shares or accounts of savings and loan associations or mutual savings banks, the accounts of which are

insured by the Federal Savings and Loan Insurance Corporation or the Federal Deposit Insurance Corporation; (E) in obligations issued by banks for cooperatives, Federal land banks, Federal intermediate credit banks, Federal home loan banks, the Federal Home Loan Bank Board, or any corporation designated in section 846 of Title 31 as a wholly owned Government corporation; or in obligations, participations, or other instruments of or issued by, or fully guaranteed as to principal and interest by, the Federal National Mortgage Association or the Government National Mortgage Association; or in mortgages, obligations, or other securities which are or ever have been sold by the Federal Home Loan Mortgage Corporation pursuant to Section 305 or Section 306 of the Federal Home Loan Mortgage Corporation Act; or in obligations or other instruments or securities of the Student Loan Marketing Association; or in obligations, participations, securities, or other instruments of, or issued by, or fully guaranteed as to principal and interest by any other agency of the United States and a Federal credit union may issue and sell securities which are guaranteed pursuant to section 306(g) of the National Housing Act; (F) in participation certificates evidencing beneficial interests in obligations, or in the right to receive interest and principal collections therefrom, which obligations have been subjected by one or more Government agencies to a trust or trusts for which any executive department, agency, or instrumentality of the United States (or the head thereof) has been named to act as trustee; (G) in shares or deposits of any central credit union in which such investments are specifically authorized by the board of directors of the Federal credit union making the investment; (H) in shares, share certificates, or share deposits of federally insured credit unions; (I) in the shares, stocks, or obligations of any other organization, providing services which are associated with the routine operations of credit unions, up to 1 per centum of the total paid in and unimpaired capital and surplus of the credit union with the approval of the Board: *Provided, however*, That such authority does not include the power to acquire control directly or indirectly, of another financial institution, nor invest in shares, stocks or obligations of an insurance company, trade association, liquidity facility or any other similar organization, corporation, or association, except as otherwise expressly provided by this Act; (J) in the capital stock of the National Credit Union Central Liquidity Facility; and (K) investments in obligations of, or issued by, any State or political subdivision thereof (including any agency, corporation, or instrumentality of a State or political subdivision), except that no credit

union may invest more than 10 per centum of its unimpaired capital and surplus in the obligations of any one issuer (exclusive of general obligations of the issuer).

(8) to make deposits in national banks and in State banks, trust companies, and mutual savings banks operating in accordance with the laws of the State in which the Federal credit union does business, or in banks or institutions the accounts of which are insured by the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation, and for Federal credit unions or credit unions authorized by the Department of Defense operating suboffices on American military installations in foreign countries or trust territories of the United States to maintain demand deposit accounts in banks located in those countries or trust territories, subject to such regulations as may be issued by the Board and provided such banks are correspondents of banks described in this paragraph;

(9) to borrow in accordance with such rules and regulations as may be prescribed by the Board, from any source, in an aggregate amount not exceeding, except as authorized by the Board in carrying out the provisions of title III, 50 per centum of its paid-in and unimpaired capital and surplus: *Provided*, That any Federal credit union may discount with or sell to any Federal intermediate credit bank any eligible obligations up to the amount of its paid-in and unimpaired capital;

(10) to levy late charges, in accordance with the bylaws, for failure of members to meet promptly their obligations to the Federal credit union;

(11) to impress and enforce a lien upon the shares and dividends of any member, to the extent of any loan made to him and any dues or charges payable by him;

(12) in accordance with rules and regulations prescribed by the Board, to sell to members negotiable checks (including travelers checks), money orders and other similar money transfer instruments; and to cash checks and money orders for members, for a fee;

(13) in accordance with rules and regulations prescribed by the Board, to purchase, sell, pledge, or discount or otherwise receive or dispose of, in whole or in part, any eligible obligations (as defined by the Board) of its members and to purchase from any liquidating credit union notes made by individual members of the liquidating credit union at such prices as may be agreed upon by the board of directors of the liquidating credit union

and the board of directors of the purchasing credit union, but no purchase may be made under authority of this paragraph if, upon the making of that purchase, the aggregate of the unpaid balances of notes purchased under authority of this paragraph would exceed 5 per centum of the unimpaired capital and surplus of the credit union; and

(14) to sell all or a part of its assets to another credit union, to purchase all or part of the assets of another credit union and to assume the liabilities of the selling credit union and those of its members subject to regulations of the Board;

(15) to invest in securities that—

(A) are offered and sold pursuant to section 4(5) of the Securities Act of 1933 (15 U.S.C. 77d(5)); or

(B) are mortgage related securities (as that term is defined in section 3(a)(41) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(41)), subject to such regulations as the Board may prescribe, including regulations prescribing minimum size of the issue (at the time of initial distribution) or minimum aggregate sales prices, or both;

(16) to exercise such incidental powers as shall be necessary or requisite to enable it to carry on effectively the business for which it is incorporated.

§ 1758

§ 108

Bylaws.—In order to simplify the organization of Federal credit unions the Board shall from time to time cause to be prepared a form of organization certificate and a form of bylaws, consistent with this chapter, which shall be used by Federal credit union incorporators, and shall be supplied to them on request. At the time of presenting the organization certificate the incorporators shall also submit proposed bylaws to the Board for its approval.

§ 1759

§ 109

Membership.—Federal credit union membership shall consist of the incorporators and such other persons and incorporated and unincorporated organizations, to the extent permitted by rules and regulations prescribed by the Board, as may be elected to membership and as such shall each subscribe to at least one share of its stock and pay the initial installment thereon and a uniform entrance fee if required by the board of directors; except that Federal credit union membership shall be limited to groups having a common bond of occupation or association, or to groups within a well-defined neighborhood, community, or rural district.

§701.22 Loan Participation.

(a) For purposes of this section:

(1) "participation loan" means a loan made in participation with one or more eligible organizations, where the written commitment to participate in the loan precedes final disbursement.

(2) "Eligible organizations" means a credit union, credit union organization, or financial organization.

(3) "Credit union" means any Federal or state chartered credit union.

(4) "Credit union organization" means any organization as determined by the Board, established primarily to serve the daily operational needs of its member credit unions. The term does not include trade associations, membership organizations principally composed of credit unions, or corporations or other businesses which principally provide services to credit union members as opposed to corporations or businesses whose business relates to the daily in-house operation of credit unions.

(5) "Financial organization" means any federally chartered or federally insured financial institution.

(6) "Originating lender" means the participant with which the member contracts.

(b) Subject to the provisions of this section any Federal credit union may participate in making loans with eligible organizations within the limitations of the board of directors' written participation loan policies, PROVIDED:

(1) no Federal credit union shall obtain an interest in a participation loan if the sum of that interest and any (other) indebtedness owing to the Federal credit union by the borrower exceeds 10 per centum of the Federal credit union's unimpaired capital and surplus;

(2) prior to final disbursement, a written participation agreement shall be properly executed, acted upon by the Federal credit union's board of directors or the investment committee and retained in the Federal credit union's office. The agreement shall include provisions which identify the participation loan or loans.

(3) A Federal credit union may sell to or purchase from any participant the servicing of any loan in which it owns a participation interest.

(c) An originating lender which is a Federal credit union shall:

(1) originate loans only to its members;

(2) retain an interest of at least 10 per centum of the face amount of each loan;

(3) retain the original or copies of the loan documents; and

(4) obtain approval of the loan from the credit committee or loan officer.

(d) A participant Federal credit union that is not an originating lender shall:

(1) participate only in loans it is empowered to grant;

(2) participate in participation loans only if made to its own members or members of another participating credit union;

(3) retain the original or a copy of the written participation loan agreement and a schedule of the loans covered by the agreement; and

(4) obtain the approval of the board of directors or investment committee of the disbursement of proceeds to the originating lender.

§701.23 Purchase, Sale, and Pledge of Eligible Obligations.

(a) For purposes of this Section:

(1) "Eligible obligation" means a loan or group of loans;

(2) "Student loan" means a loan granted to finance the borrower's attendance at an institution of higher education or at a vocational school, which is secured by and on which payment of the outstanding principal and interest has been deferred in accordance with the insurance or guarantee of the Federal Government, of a State government, or any agency of either.

(b) Purchase.

(1) A Federal credit union may purchase, in whole or in part, within the limitations of the board of directors' written purchase policies:

(i) Eligible obligations of its members, from any source, if either (A) they are loans it is empowered to grant or (B) they are refinanced with the consent of the borrowers, within 60 days after they are purchased, so that they are loans it is empowered to grant;

(ii) Eligible obligations of a liquidating credit union's individual members, from the liquidating credit union;

(iii) Student loans, from any source, if the purchaser is granting student loans on an ongoing basis and if the purchase will facilitate the purchasing credit union's packaging of a pool of such loans to be sold or pledged on the secondary market; and

(iv) Real estate-secured loans, from any source, if the purchaser is granting real estate-secured loans pursuant to Section 701.21 on an on-

§701.22 Loan Participation.

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(1) "participation loan" means a loan made in participation with one or more eligible organizations, where the written commitment to participate in the loan precedes final disbursement.

(2) "Eligible organizations" means a credit union, credit union organization, or financial organization.

(3) "Credit union" means any Federal or state chartered credit union.

(4) "Credit union organization" means any organization as determined by the Board, established primarily to serve the daily operational needs of its member credit unions. The term does not include trade associations, membership organizations principally composed of credit unions, or corporations or other businesses which principally provide services to credit union members as opposed to corporations or businesses whose business relates to the daily in-house operation of credit unions.

(5) "Financial organization" means any federally chartered or federally insured financial institution.

(6) "Originating lender" means the participant with which the member contracts.

(b) Subject to the provisions of this section any Federal credit union may participate in making loans with eligible organizations within the limitations of the board of directors' written participation loan policies, PROVIDED:

(1) no Federal credit union shall obtain an interest in a participation loan if the sum of that interest and any (other) indebtedness owing to the Federal credit union by the borrower exceeds 10 per centum of the Federal credit union's unimpaired capital and surplus:

(2) prior to final disbursement, a written participation agreement shall be properly executed, acted upon by the Federal credit union's board of directors or the investment committee and retained in the Federal credit union's office. The agreement shall include provisions which identify the participation loan or loans.

(3) A Federal credit union may sell to or purchase from any participant the servicing of any loan in which it owns a participation interest.

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(b) Purchase.

(1) A Federal credit union may purchase, in whole or in part, within the limitations of the board of directors' written purchase policies:

(i) Eligible obligations of its members, from any source, if either (A) they are loans it is empowered to grant or (B) they are refinanced with the consent of the borrowers, within 60 days after they are purchased, so that they are loans it is empowered to grant;

(ii) Eligible obligations of a liquidating credit union's individual members, from the liquidating credit union;

(iii) Student loans, from any source, if the purchaser is granting student loans on an ongoing basis and if the purchase will facilitate the purchasing credit union's packaging of a pool of such loans to be sold or pledged on the secondary market; and

(iv) Real estate-secured loans, from any source, if the purchaser is granting real estate-secured loans pursuant to Section 701.21 on an on-