NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

December 17, 1991

Deborah B. Ellingwood,
Executive Director
Minnesota Association of Credit Unions
1821 University Avenue
Suite S-207
St. Paul, Minnesota 55104

Re: State Law on Tax Escrow Accounts (Your November 14, 1991, Letter)

Dear Ms. Ellingwood:

You asked whether federal credit unions ("FCUs") are subject to a Minnesota statute requiring financial institutions to establish escrow accounts for personal property taxes for loans granted on manufactured homes. FCUs must comply with the law in question.

Background

You forwarded a copy of a letter from the Minnesota Department of Revenue, describing a recently enacted statute, Chapter 291, Article 15, Section 1 of the Minnesota Laws of 1991, which has an effective date of January 1, 1992. According to that letter, the new law requires the establishment of escrow accounts for the payment of personal property taxes by lenders who finance purchases of manufactured homes. The law also requires lenders to make the required payments of personal property taxes to the taxing authority on two scheduled dates. Credit unions are listed among the institutions subject to the new statute. You asked whether FCUs are subject to the new law.

Analysis

FCUs must comply with state laws, unless a particular state law is preempted by federal law. The Federal Credit Union

Act (the "FCU Act") and NCUA's Rules and Regulations ("the Regulations") preempt state law only when there is a conflict, or when the state law interferes with an FCU's exercise of its statutory powers. We do not believe that any conflict exists. Neither the FCU Act nor the Regulations addresses establishment of escrow accounts or collection and payment of personal property taxes. Nor does it appear that the Minnesota law would prevent FCUs from exercising any of their statutory powers. In our opinion, the Minnesota statute does not meet the standards for preemption.

We have reviewed the FCU Act and the Regulations with particular attention to three sections which, in our opinion, could conceivably have preempted the Minnesota law. Although we do not believe that any of those sections actually does preempt the Minnesota statute, we will discuss them briefly.

Section 122 of the FCU Act, 12 U.S.C. 1768, generally exempts FCUs from taxation. With regard to member holdings in FCUs, Section 122 provides that such holdings may be "included in the valuation of the personal property of the owners or holders thereof in assessing taxes imposed by authority of the State or political subdivision thereof in which the Federal credit union is located." Section 122 goes on to state that "the duty or burden of collecting or enforcing the payment of such a tax shall not be imposed upon any such Federal credit union . . . ." Pursuant to Section 122, FCUs may not be required to collect any tax on member holdings in the FCU. However, the Section 122 exemption extends only to that narrow class of taxes. Section 122 does not relieve FCUs from state-imposed requirement for the collection of other types of taxes.

Section 701.21(b)(1) of the Regulations, 12 C.F.R. §701.21(b)(1), provides that federal law preempts any state law purporting to regulate the rates, terms of repayment and other conditions of FCU loans and lines of credit. Section 701.21(b)(2) makes clear that state laws affecting other aspects of FCU loans and lines of credit are not preempted. In our view, the Minnesota statute does not affect the rates, terms of repayment or other terms similar to those specified in Section 701.21(b)(1), of FCU loans and lines of credit. Therefore, Section 701.21(b)(1) does not preempt the Minnesota law.

Lastly, Section 701.35(c) of the Regulations, 12 C.F.R. §701.35(c), allows an FCU to determine "all . . . matters affecting the opening, maintaining or closing of a share, share draft or share certificate account." Section 701.35(c) goes on to state, "State laws regulating such activities are not applicable to Federal credit unions." The Minnesota law is preempted if it attempts to regulate the opening, maintaining, or closing of an FCU account.

Section 701.35(c) does not define the phrase "matters affecting the opening, maintaining or closing" of accounts, nor does its regulatory history (49 Fed. Reg. 46552, 11/27/84; 50 Fed. Reg. 4636, 2/1/85) explain the phrase. However, the preamble to the 1982 revision of Section 701.35 provides some insight into the meaning of those terms. See, 47 Fed. Reg. 17979, 4/27/82. The 1982 revision deregulated Section 701.35, placing the responsibility for determining the terms and conditions governing share accounts on an FCU's board of directors. The 1985 revision, which added Section 701.35(c), was intended to carry out what the Board had intended when it deregulated Section 701.35; that is, to give FCUs the authority to determine for themselves matters affecting member accounts that had previously been controlled by regulation. Prior to the deregulation, Section 701.35 included rate and maturity limitations and other requirements for share and share certificate accounts. The NCUA Board stated, in the preamble to the 1982 revision, that under the new rule, an FCU's board of directors "would be responsible for determining the classes of accounts to be offered, maturities, dividend rates, minimum denominations, premature withdrawal penalty provisions, and any other terms and conditions governing the account." Those are the types of conditions that the NCUA Board had in mind when it granted FCUs the express power, in Section 701.35(c), to determine matters affecting the opening, maintaining and closing of accounts, and preempted state laws regulating such areas. Based on that analysis, it is our opinion that the Minnesota law does not impermissibly attempt to govern the opening, maintaining or closing of FCU accounts, and is not preempted by Section 701.35. We also note that, although the Minnesota law affects accounts in that it requires the creation of escrow accounts, its chief effect is to impose additional requirements on FCU lending. For that reason, the Minnesota statute should properly be considered in relation to Section 701.21, rather than Section 701.35.

In summary, we find no basis in the FCU Act or the Regulations for preempting Chapter 291, Article 15, Section 1 of the Minnesota Laws of 1991. In our opinion, FCUs must comply with the statute.

We note, however, that while Minnesota may require FCUs to establish escrow accounts for their manufactured home loans, it may not regulate the rates, terms or conditions of such accounts. Any state law attempting to set interest rates payable on such accounts, to require payment of interest on such accounts by FCUs, or otherwise to affect the terms or conditions of FCU accounts would be preempted by Section 701.21(b)(1) of the Regulations.

Sincerely,

Hattie M. Ulan

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Associate General Counsel

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