

December 13, 1999

Linda J. Lehnertz, Associate General Counsel
CUNA Mutual Group
P.O. Box 391
5910 Mineral Point Road
Madison, WI 53701-0391

Re: Mechanical Breakdown Coverage.

Dear Ms. Lehnertz:

You have asked that we reconsider our interpretation of insurance sales under the group purchasing regulation, as discussed in a letter from me to Susan Brandon, dated August 18, 1997. 12 C.F.R. §721.2(b)(1). In that letter, we stated that a federal credit union (FCU) could receive unlimited compensation from a third-party vendor for offering mechanical breakdown service agreements, if state law deemed the agreement to be insurance. Otherwise, an FCU could recover only reimbursement of its cost amount. 12 C.F.R. §721.2(b)(3). On reconsideration, our view is that FCUs may receive unlimited compensation for offering third-party mechanical breakdown insurance, regardless of whether the product constitutes insurance under state law. The general restriction on compensation in Part 721 would still apply. 12 C.F.R. 0167721.2(b)(1). FCUs may receive unlimited compensation only if the sale is directly related to an extension of credit or the opening or maintenance of share accounts.

The 1985 amendments to the insurance and group purchasing regulation permit FCUs to accept compensation in excess of administrative costs when offering vendors' insurance products to members. 12 C.F.R. §721.2(b). The preamble to the final rule notes that certain types of insurance products are incidental to providing an extension of credit. 50 Fed. Reg. 16,463 (1985). Mechanical breakdown insurance on motor vehicles is among the list of insurance products deemed incidental to providing credit. *Id.* As such, it may be offered in connection with member automobile loans. The preamble also warns that an FCU could be subject to state insurance laws, including individual agent licenses for FCU employees. *Id.* at 16,464. The preamble and regulation do not require that state law regulate the product as insurance before an FCU can receive unlimited compensation from its sale.

Tying FCU compensation limits to state insurance laws results in treating FCUs inconsistently throughout the nation. To avoid this disparity, FCUs should determine whether the product constitutes insurance under basic principles of insurance. The product or agreement should undertake to indemnify the insured against loss, damages, or liability arising from a contingency or act to occur in the future. Therefore, generally, FCUs may receive unlimited compensation from

vendors for selling permissible insurance products, whether or not state law deems them to be insurance. However, state insurance regulators may impose laws on FCUs requiring agency licenses and restricting income.

Please note that the NCUA Board recently issued an advance notice of proposed rulemaking on changes to Part 721, the insurance and group purchasing regulations. We have proposed defining the phrase "insurance products" to provide clarity on this issue. While these regulations are under review, NCUA welcomes comment and suggestions for improving this Part.

Sincerely,

Sheila A. Albin
Associate General Counsel

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