

July 1, 2004

John J. Wohadlo, President/CEO
Inland Employees Federal Credit Union
31 West Lincoln Highway
Scherverville, IN 46375

Re: Permissibility of Loan Participation or Purchase of an Eligible Obligation.

Dear Mr. Wohadlo:

You have asked if a federal credit union (FCU) may “participate” in a bank’s indirect automobile lending program by purchasing a one hundred percent interest in automobile loans originated by the bank and made to individuals who are not members of the FCU. No, an FCU cannot participate in the program because the purchase is not a permissible loan participation or permissible purchase of an eligible obligation. An FCU cannot purchase automobile loans originated by a bank unless the loans are to its members.

Your letter indicates your FCU has signed a contract to purchase a minimum of \$500,000 per month in loans made by a bank located approximately fifty miles from your offices. You have indicated that, “more than likely,” the borrowers are not eligible for membership in your credit union. The contract calls for your credit union to purchase one hundred percent of the loans, without recourse, with the bank retaining the servicing rights. In your judgment, the loans represent a sound investment for the credit union.

NCUA’s regulations permit an FCU to purchase loans from any source, provided the borrower is a member and the loan is either of a type the FCU is empowered to grant or the loan is refinanced by the FCU within 60 days of its purchase. 12 C.F.R. §701.23(b)(1)(i). The rule imposes other restrictions as well, including an aggregate limitation on the amount of loans that may be purchased. 12 C.F.R. §701.23(b)(3). The rule excepts certain types of loans from these requirements, for example, where the seller is a liquidating credit union or for student loans or real estate loans if the purchase will facilitate an FCU’s sale of a pool of such loans in the secondary market. 12 C.F.R. §§701.23(b)(1)(ii) – (iv). As these exceptions are not applicable here, and the borrowers are not members of your credit union, the purchase is prohibited §701.23.

Because the credit union’s contract with the bank calls for the purchase of one hundred percent of the loans, we do not view the transaction as a loan participation. 12 C.F.R. 701.22. Even if it were governed by NCUA’s loan participation rule, however, the transaction would not be permissible. Our rule requires, among other things, that an FCU may participate in a loan only if it is made to one of its own members, or to someone who is a member of another credit union that is also participating in the transaction. 12 C.F.R. §701.22(d)(2). Under the facts you have presented, the loans will not meet this requirement.

You have asked if the contract between your credit union and the Bank can or should be voided. The contract is not in compliance with our regulation, and the credit union must take steps to extricate itself from its obligations. We recommend you confer with personnel in our Regional Office in Atlanta on the logistical considerations of doing so, and we suggest you consult with private counsel to advise you on matters that involve questions of state law.

You have also asked if NCUA can waive these requirements. Certain well-capitalized FCUs are exempt from some of the restrictions contained in the rule, but only where the purchase is from a federally insured credit union. 12 C.F.R. §742.5.

Sincerely,

Sheila A. Albin
Associate General Counsel

cc: Timothy Hornbrook, Associate Regional Director

OGC/RPK:bhs
04-0528