

July 29, 2003

Steven D. Eimert, Esquire
Sherin and Lodgen, LLP
100 Summer Street
Boston, MA 02110

Re: Federal Credit Union (FCU) and Credit Union Service Organization (CUSO) Participation in New Markets Tax Credits Program.

Dear Mr. Eimert:

You have asked if an FCU or a CUSO may become certified as a Community Development Entity (CDE) and then participate in the New Markets Tax Credit Program (NMTC) sponsored by the U.S. Department of Treasury (Treasury). As explained below, we have no legal concerns with an FCU or CUSO receiving certification and participating in the program with the caveat that an FCU's participation is limited to the activities described below and a CUSO's participation is contingent on a change in the CUSO rule to permit CUSOs to originate business loans.

You have described the process to participate in the NMTC as a two-step procedure. First, an applicant must be certified as a CDE by Treasury. To qualify for certification, the applicant must demonstrate a commitment to making loans to or equity investments in low-income communities and establish a mechanism for community input on these loans and investments. You suggest an FCU or CUSO satisfy the community involvement requirement through the appointment of an informal advisory board of low-income community representatives. You indicate there are currently about 15 federal and state chartered credit unions designated as CDEs but you are not aware of any CUSOs designated as CDEs.

Second, once an entity is designated as a CDE it may: 1) buy loans from and sell loans to other CDEs; 2) borrow from and receive equity investments from other CDEs; 3) if it is a for-profit entity with the power to issue stock or other traditional equity ownership interests to investors, apply for, receive and sell NMTCs and apply the proceeds from the sale of the NMTCs to business lending or investment under the NMTC program rules; and 4) if it is a not-for-profit entity, apply for, receive and sell NMTCs on behalf of its for-profit CDE approved subsidiaries.

Your first question is whether an FCU has the authority to seek certification as a CDE and upon certification exercise its CDE powers to buy loans from and sell loans to other CDEs and to borrow from other CDEs. You acknowledge that an FCU does not have the authority to receive equity investments from other CDEs or the authority to sell NMTCs for its own account.

An FCU may seek certification as a CDE and engage in CDE activities to the extent they are authorized under the FCU Act and NCUA's regulations. As you have discussed with Staff Attorney Mary Rupp, although an FCU is authorized to buy and sell loans, this authority is limited by 12 C.F.R. §701.23. An FCU's borrowing is permitted to the extent it is authorized under §107(9) of the FCU Act. 12 U.S.C. §1757(9).

Second, assuming CUSOs are authorized to originate business loans, you ask whether an FCU as part of its incidental powers, may apply for, receive and sell NMTCs on behalf of its CUSO subsidiary. We do not believe the activity of applying for, obtaining and selling NMTCs on behalf of its CUSO subsidiary is within an FCU's incidental powers. An incidental powers activity is one that is necessary or requisite to enable an

FCU to carry on the business for which it is incorporated. 12 C.F.R. §721.2. Activities on behalf of a CUSO, do not meet this test. An FCU is incorporated to serve its members, not its CUSOs. In addition, you note that this activity may be performed directly by the CUSO, rather than the FCU, and so we are not certain what purpose would be served by having the FCU perform this activity.

Third, you ask if a CUSO, assuming the CUSO regulation is amended to permit CUSOs to originate business loans, may become a certified CDE and apply for and sell NMTCs. The CUSO would use the proceeds from the sale of the NMTCs to make business loans. We have no legal concerns with a CUSO engaging in this activity as long as it complies with the other requirements of the CUSO regulation, including the requirement that it primarily serve credit unions and their members. 12 C.F.R. §712.3(b).

Fourth, you ask if a “Federal CUSO certified as a CDE, may as part of a conforming loan prohibit payment of the loan before the stated maturity date.” You correctly note that §701.21(c)(6), the provision in NCUA’s lending regulation that prohibits FCUs from charging prepayment penalties, only applies to FCUs and not to their CUSOs. We want to clarify that although you have referred to the CUSO as a “Federal CUSO,” CUSOs are in fact incorporated under state law and look to state law for their regulatory requirements. Although an FCU may only invest in a CUSO that meets the requirements of Part 712, NCUA does not regulate CUSOs.

Sincerely,

Sheila A. Albin
Associate General Counsel

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