

June 28, 2006

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Re: Permissibility of an FCU Developing Residential Property to  
Lease to Employees for Housing.

Dear Mr. Lozoff:

You have asked if a federal credit union (FCU) can convert excess credit union property into residential housing that it would lease to its employees. No, FCUs have neither express authority nor is it within their incidental powers to engage in this activity.

The background for your inquiry is that an FCU would like to offer residential housing to its employees due to high area real estate prices in the area where the FCU has its offices. The FCU wants to develop excess credit union property by converting it into residential rental units. It would then lease units to employees and charge below market rates. The intent of the proposal is to attract employees to positions at the FCU by making affordable rental housing available near the FCU.

You believe the activity might be permissible by knitting together certain provisions in the FCU Act and NCUA's regulations, but we disagree. An FCU may only engage in activities that the FCU Act expressly authorizes or that fall within an FCU's incidental powers.

In support of your contention, you note the provision in the FCU Act expressly authorizing an FCU "to purchase, hold, and dispose of property necessary or incidental to its operations." 12 U.S.C. §1757(4). FCUs are financial institutions and, by its terms, this express, statutory authority only permits FCUs to own property related to an FCU's "operations," which is providing financial products and services to members. We conclude this express power does not authorize FCUs to engage in the business of developing property it owns into residential rental property or to be in the business of leasing residential property, even where the property is leased on a subsidized basis to its employees.

Further, the activity is not contemplated as a category of incidental powers. Although the proposed activity involves excess property, it is not within the preapproved incidental powers category of excess capacity. 12 C.F.R. §721.3(d) ("Excess capacity is the excess use or capacity remaining in facilities . . . invested in or established, in good faith, with the intent of serving your members . . . [and] will be taken up by the future expansion of services to members"). We

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have also considered if the proposed activity could be considered with the general, regulatory definition of an incidental powers activity.

An activity meets the definition of an incidental power activity if the activity: (a) Is convenient or useful in carrying out the mission or business of credit unions consistent with the [FCU] Act; (b) Is the functional equivalent or logical outgrowth of activities that are part of the mission or business of credit unions; and (c) Involves risks similar in nature to those already assumed as part of the business of credit unions.

12 C.F.R. §721.2. The FCU's proposal to develop and maintain residential property for lease to its employees is not part of the mission or business of credit unions. Residential real estate development and leasing is a separate, unrelated business line from the mission of FCUs to provide financial products and services to members. In addition, the rental real estate business has different risks and liabilities than those credit unions assume as part of their business. As proposed, the FCU would be its employees' landlord, resulting in financial and legal obligations separate from the employment relationship and with very different risks and liabilities.

You identified two NCUA regulations you believe support the permissibility of the proposed activity; however, since the FCU Act does not authorize developing and leasing residential property as either an express or incidental power, it likewise would not be permissible under NCUA's regulations. Nevertheless, we considered your contention that residential rental property might be considered "premises," as used in the fixed asset rule and, also, that the CUSO rule provides a permissible basis for the activity.

NCUA's fixed asset rule permits FCUs to invest in real property used or is intended to be used as premises, but residential rental units for FCU employees do not fall within the definition of "premises." 12 C.F.R. §701.36(e)(4)(i). The regulation defines premises to mean "any office, branch office, suboffice, service center, parking lot, other facility, or real estate where the credit union transacts or will transact business." 12 C.F.R. §701.36(e)(6). Rental housing for employees would not be property where the FCU conducts business and the fixed asset rule provides no support for the proposal.

Likewise, the NCUA's credit union service organization (CUSO) rule does not provide a regulatory basis or means for an FCU to engage in residential real estate leasing to provide housing for its employees. You identified the provision in the CUSO rule permitting CUSOs to engage in "real estate leasing of excess CUSO property" as basis for the proposal. 12 C.F.R. §712.5(i)(2). First, we note that each identified preapproved activity and service in the CUSO rule must be

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one “related to the routine daily operations of credit unions.” 12 C.F.R. §712.5. As discussed above, we do not consider leasing residential real estate to employees as part of the daily operations of credit unions. In addition, the preamble to the CUSO rule when NCUA adopted the provision on leasing excess real estate indicates the proposed activity is not within the rule’s scope:

This covers real estate leasing only of premises acquired for CUSO business, and otherwise mainly used in CUSO business, that may later be used for future CUSO expansion. CUSOs are still otherwise obligated to demonstrate that the purchase of any real property will be used for CUSO purposes. NCUA expects that any real property purchased by a CUSO for future expansion should have a future benefit to the CUSO as evidenced by a business plan discussing future use of the real property.

63 Fed. Reg. 10743, 10751 (March 9, 1998).

As an alternative to the FCU’s proposal, we note NCUA’s regulations specifically permit an FCU to provide employee benefits. 12 C.F.R. §701.19. To address the problem of affordable housing close to FCU offices for employees, we suggest the FCU consider providing an employee benefit such housing stipends or special loan rates to qualifying FCU employees. If you have further questions about these or other options, please feel free to contact me or Staff Attorney Regina Metz at 703-518-6540.

Sincerely,

Sheila A. Albin  
Associate General Counsel

GC/RMM/SAA:bhs  
06-0545  
cc: Region III