

November 7, 2008

Mary Dunn, Sr. Vice President and Deputy General Counsel
Credit Union National Association
601 Pennsylvania Avenue, N.W.
Suite 600, South Building
Washington, DC 20004

Re: Prepayment Penalty in the Member Business Loans (MBL) Context.

Dear Ms. Dunn:

You have asked if a federal credit union (FCU) may recoup waived settlement costs and fees associated with an MBL without that being considered a prohibited prepayment penalty. Yes, it may as long as the recoupment period is reasonable in terms of the size and type of fees being waived.

The Federal Credit Union Act states:

[A] borrower may repay his loan, prior to maturity in whole or in part on any business day without penalty, except that on a first or second mortgage loan a Federal credit union may require that any partial prepayments (I) be made on the date monthly installments are due and (II) be in the amount of that part of one or more monthly installments which would be applicable to principal.

12 U.S.C. §1757(5)(A)(viii). This statutory mandate prohibiting an FCU from charging a borrower a prepayment penalty is reiterated in NCUA's general lending rule.¹ 12 C.F.R. §701.21(c)(6); 12 C.F.R. §701.21(g)(4). Also, the MBL rule, Part 723, states that the provisions of §§701.21(a)-(g) apply to MBLs to the extent they are consistent with Part 723 and subject to certain exceptions for state chartered credit unions. 12 C.F.R. §723.4(a).

In OGC Legal Op. 93-0206, we addressed the question whether an FCU's marketing program offering a conditional waiver of appraisal and title fees violated the prohibition against prepayment penalties. The FCU was concerned that the waived fees would not be offset by interest income in the first year of repayment and wanted to require the borrower to pay the waived fees if the borrower prepaid the loan in the first year.

¹ The prohibition against prepayment penalties applies only to natural person FCUs. It does not apply to corporate credit unions. 12 U.S.C. §1766(a); 12 C.F.R. §704.7(g).

We determined the conditional waiver program did not violate the prohibition against prepayment penalties. Specifically, we stated:

In our view, an agreement that a borrower will pay the FCU for fees initially waived if he closes his HELOC within one year does not constitute a prepayment penalty. When an FCU pays loan settlement costs, such as appraisal and title fees, it confers a benefit on the borrower. If a borrower closes his HELOC within a year and has to reimburse the FCU for the appraisal and title fees, he has simply lost the benefit. This is not the same as imposition of a prepayment penalty.

OGC Legal Op. 93-0206 (March 9, 1993). In OGC Legal Op. 96-0522, we took the same position based on similar facts. OGC Legal Op. 96-0522 (June 13, 1996). These prior opinions indicate the loan agreements specifically disclosed to borrowers the conditional nature of the fee waiver. Although these two opinions are based on circumstances surrounding non-business loans, we believe the analysis is equally applicable in the MBL context. We note the conditional waiver programs addressed in those opinions specifically limited the recoupment periods to one year and two years, respectively. You have not suggested a particular time period that an FCU will use as a recoupment period so we do not express a specific opinion but note that, in the MBL context, as in the circumstances addressed in our prior opinions, the recoupment period should be disclosed to the borrower and should be no longer than that reasonably necessary to offset expenses associated with waived fees.

You also have suggested this analysis should apply to costs and fees regardless of when they are due, meaning you believe a fee due at loan payoff, a so-called back-end fee, should be treated the same as a fee due at or before loan closing. In principle, we agree but only if the back-end fee is one that is charged regardless of whether the MBL is paid early or at maturity.

Please contact Staff Attorney Frank Kressman or me with any questions or if we can be of further assistance.

Sincerely,

/S/

Sheila A. Albin
Associate General Counsel