

NCUA-IR - 81-3 STATE CHARTERED FEDERALLY INSURED CREDIT
UNIONS AS "MOST FAVORED LENDERS" 04/81

NATIONAL CREDIT UNION ADMINISTRATION
INTERPRETIVE RULING AND POLICY STATEMENT

IRPS 81-3; DATE: April 30, 1981

12 C.F.R. Part 741

[IRPS 81-3]

Statement of Interpretation and Policy

State Chartered Federally Insured Credit Unions As "Most Favored Lenders"

AGENCY: National Credit Union Administration.

ACTION: Statement of Interpretation and Policy.

SUMMARY: In IRPS 80-11 NCUA stated that it would interpret Section 205(g)(1) of the Federal Credit Union Act to accord "most favored lender" status to a state chartered federally insured credit union. This status would be triggered only when the interest rate the credit union could normally charge on a loan was less than the discount rate plus one percent. If triggered, this status would apply only when the credit union granted a loan other than a first mortgage loan, a business loan of \$1000 or more, or an agricultural loan of \$1000 or more. This document replaces IRPS 80-11. It removes the trigger mechanism and states that the "most favored lender" status will apply to any loan the credit union grants.

EFFECTIVE DATE: April 1, 1980 (the effective date of P.L. 96-221).

FOR FURTHER INFORMATION CONTACT: John L. Culhane, Jr., Senior Attorney, or Barbara A. Burrows, Attorney-Advisor, Office of General Counsel, National Credit Union Administration, 1776 G Street, N.W., Washington, D.C. 20456. Telephone: (202) 357-1030.

SUPPLEMENTARY INFORMATION:

P.L. 96-221, the Depository Institutions Deregulation and Monetary Control Act of 1980, added Section 205(g)(1) to the Federal Credit Union Act. Section 205(g)(1), reads as follows:

If the applicable rate prescribed in this subsection exceeds the rate an insured credit union would be permitted to charge in the absence of this subsection, such credit union may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this subsection, take, receive, reserve, and charge on any loan, interest at a rate of not more than 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve bank in the Federal Reserve District where such insured credit union is located or at the rate allowed by the laws of the State, territory, or district where such credit union is located, whichever may be greater.

In IRPS 80-11 NCUA stated that it would interpret this Section to grant "most favored lender" status to state chartered federally insured credit unions. This status would be triggered whenever one per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve bank in the Federal Reserve District where a credit union was located was higher than the rate the credit union could normally charge on a loan other than a first mortgage loan, a business loan of \$1000 or more, or an agricultural loan of \$1000 or more. Once triggered, the credit union would have two options. It could charge up to one per centum in excess of that discount rate or it could charge any rate any other lender could charge on that loan under state law, whichever would be greater. 45 F.R. 78624 (1980).

After the IRPS was published, credit unions and credit union trade associations requested that NCUA reconsider certain aspects of its interpretation. While the commenters agreed with NCUA that Section 205(g)(1) grants "most favored lender" status to state chartered federally insured credit unions, they argued for certain changes in the interpretation. Two of the commenters' arguments are being addressed in this IRPS. First, they argued that the statute could be interpreted in such a way as to eliminate the trigger mechanism. Second, they argued that the statute could be interpreted in such a way as to accord "most favored lender" status regardless of the type of loan being granted.

The trigger mechanism was imposed based on NCUA's interpretation of the phrase, "the applicable rate prescribed in this subsection." Although noting that the phrase was not entirely clear, NCUA interpreted the phrase to refer to one percent over the discount rate for ninety-day commercial paper, as that rate was the only rate specifically set out in Section 205(g)(1). In addition, this interpretation seemed to be consistent with certain references in the legislative history of P.L. 96-221. See Conf. Rep. No. 842, 96th Cong., 2d Sess. 78 (1980).

The commenters argued that an equally supportable reading of the phrase would be that "the applicable rate prescribed in this subsection" refers both to one percent over the discount rate for ninety-day commercial paper and to the rate allowed by the laws of the state, territory, or district where the credit union is located. It was further argued that this interpretation would be more consistent with the Congressional intent of placing state chartered federally insured credit unions in parity with national banks. And it was also argued that this interpretation would avoid the operational problems associated with a trigger mechanism. The NCUA Board is persuaded by these arguments and has revised its interpretation accordingly.

The limitation on the loans that could be granted by a credit union as a "most favored lender" was imposed based on NCUA's interpretation of the structure of Title V of P.L. 96-221. Title V contained three parts. Part A was entitled, "Mortgage Usury Laws." Part B was entitled, "Business and Agricultural Loans." Part C was entitled, "Other Loans." Section 205(g)(1) was added by Part C; hence it appeared that it applied only to loans that were not covered by Parts A or B.

The commenters argued that an equally supportable reading would be that a loan could be made at the greatest rate permissible under either Parts A, B, or C. It was further argued that this interpretation would be more consistent with the

Congressional intent of placing state chartered federally insured credit unions in parity with national banks. And it was also argued that this interpretation was supported by Section 528 of P.L. 96-221 which, in pertinent part, states that: "In any case in which one or more provisions of, or amendments made by ... this title (.i.e. Title V,) ... apply with respect to the same loan, mortgage, credit sale, or advance, such loan, mortgage, credit sale, or advance may be made at the highest possible rate." The NCUA Board finds these arguments persuasive and has revised its interpretive ruling accordingly.

However, the Board once again cautions state chartered federally insured credit unions that Section 525 of P.L. 96-221 permits a state to elect not to have Section 205(g)(1) of the Federal Credit Union Act apply in that state. Before granting loans under the authority of Section 205(g)(1) and this interpretive ruling, a state credit union should contact its state supervisory agency to determine whether or not Section 205(g)(1) has been superceded.

According the NCUA Board cancels IRPS No. 80-11 and in its place adopts the following.

Text of Statement of Interpretation and Policy [IRPS 81-3]

Section 205(g)(1) of the Federal Credit Union Act states that:

If the applicable rate prescribed in this subsection exceeds the rate an insured credit union would be permitted to charge in the absence of this subsection, such credit union may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this subsection, take, receive, reserve, and charge on any loan, interest at a rate of not more than 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve Bank in the Federal Reserve District where the insured credit union is located or at the rate allowed by the laws of the State, territory, or district where such credit union is located, whichever may be greater.

NCUA interprets this Section to grant "most favored lender" status to state chartered federally insured credit unions. On any particular class of loans, state chartered federally insured credit unions may charge interest at a rate not to exceed the greater of one percent over the discount rate on ninety-day commercial paper or the rate allowed to the "most favored lender" on the particular class of loans under state law, provided the greater of either of these rates exceeds the rate state chartered federally insured credit unions are normally permitted to charge under state law.

ROSEMARY BRADY
Secretary, NCUA Board

April 24, 1981