

December 23, 2002

Guy Messick, Esquire
Lastowka & Messick P.C.
The Madison Building
108 Chesley Drive
Media, PA 19063-1712

Re: Debt Cancellation Programs.

Dear Mr. Messick:

You have asked if a federal credit union (FCU) must obtain stop-loss insurance coverage if it institutes a debt cancellation or debt suspension program. No, the Federal Credit Union Act and NCUA's regulations do not require that an FCU obtain such insurance, although this insurance can mitigate an FCU's risk of loss from these programs.

This office has previously addressed an FCU's authority to offer debt cancellation products in a legal opinion to Irwin A. Thomas, OGC 97-0632, dated September 12, 1997, which is available on our website. The NCUA Board codified this authority when it adopted the incidental powers regulation, which expressly noted debt cancellation and debt suspension agreements as permissible loan-related products. 12 C.F.R. §721.3(g). In the Thomas letter, we stated that an FCU could offer debt cancellation products if it obtained insurance to cover its risk of loss so that the FCU did not act as a self-insurer. We have reconsidered this position relating to self-insurance, an inherent aspect of debt cancellation and suspension agreements, and do not view stop-loss insurance coverage as a legal requirement for offering these loan-related products.

Similarly, national banks may offer debt cancellation products without any legal prerequisite that they obtain third-party insurance to cover any expected losses. 12 C.F.R. §7.1013. We note that a rule recently issued by the Office of the Comptroller of the Currency (OCC) will continue to allow national banks to offer these products without requiring that they establish a reserve or obtain stop-loss insurance coverage. 67 Fed. Reg. 58,962 (Sept. 19, 2002) (to be codified at 12 C.F.R. pt. 37). The OCC rule, however, recognizes the necessity for banks to establish and maintain effective risk management and control processes over their debt cancellation and debt suspension programs. 67 Fed. Reg. 58,962, 58,978 (Sept. 19, 2002) (to be codified at 12 C.F.R. §37.8).

An FCU must manage the risk involved in debt cancellation and debt suspension programs in accordance with safety and soundness principles. Effective risk management and control processes include appropriate recognition and financial reporting of income, expenses, assets and liabilities, and appropriate treatment of all expected and unexpected losses associated with these products. In addition, the FCU should assess the adequacy of its internal control and risk mitigation activities in accordance with the nature and scope of its program. While stop-loss insurance coverage is not legally required, an FCU may determine that obtaining insurance from a third-party provider to cover expected losses may be an appropriate means for the FCU to manage its risk.

You have also asked us if debt cancellation contracts or debt suspension agreements are insurance products under state law. As we stated in the Thomas letter, and as discussed in the preamble to the OCC rule, a

federal appellate court concluded, in essence, that debt cancellation products do not constitute the business of insurance under state regulation. See *First National Bank of Eastern Arkansas v. Taylor*, 907 F.2d 775, 780 (8th Cir. 1990), cert. denied, 498 U.S. 972 (1990). An FCU, therefore, may offer debt cancellation and debt suspension products under its powers incidental to its express lending authority granted by the Federal Credit Union Act without engaging in the business of insurance.

Sincerely,

Sheila A. Albin
Associate General Counsel

GC/CJL:bhs
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