



## Regulatory Interpretation 2024-RI-01

**Subject:** Classification of Cooperativas for Purposes of Determining Eligibility for Federal Home Loan Bank (FHLBank) Membership

**Issue:** Under the Federal Housing Finance Agency’s (FHFA) regulation on FHLBank membership at 12 CFR part 1263 (membership regulation), how are Puerto Rican cooperativas to be classified for purposes of determining eligibility for FHLBank membership?

**Conclusion:** Like other state-chartered credit unions without federal share insurance, cooperativas that are certified as community development financial institutions (CDFIs) by the United States Department of the Treasury’s CDFI Fund (CDFI Fund) are to be classified as “CDFI credit unions” under the membership regulation, while those that are not certified as CDFIs are to be classified as “non-federally insured credit unions.”

### **Background:**

Cooperativas are a type of state-chartered credit union organized under the laws of the Commonwealth of Puerto Rico.<sup>1</sup> Member shares (i.e., deposits) in cooperativas are not insured by the National Credit Union Administration’s (NCUA) Share Insurance Fund but are insured by the Public Corporation for the Supervision and Insurance of Cooperatives of Puerto Rico (COSSEC). COSSEC, which also serves as the regulator of cooperativas, was created under Puerto Rican law and its assets are guaranteed by the Government of Puerto Rico.<sup>2</sup> As of May 18, 2023, there exist 102 cooperativas, most of which are certified as CDFIs.<sup>3</sup>

To date, no cooperativas are members of any FHLBank. During the development of the *FHLBank System at 100: Focusing on the Future* report released on November 7, 2023, FHFA received input highlighting potential confusion about the proper classification of cooperativas under the membership regulation. This Regulatory Interpretation clarifies how FHLBanks are to classify cooperativas and other state-chartered credit unions without federal share insurance for purposes of determining their eligibility for FHLBank membership under the membership regulation.

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<sup>1</sup> See Laws of Puerto Rico, Title Seven, Chapter 86 (Cooperative Savings and Credit Associations Act of 2002).

<sup>2</sup> See Laws of Puerto Rico, Title Seven, Chapter 84 (Public Corporation for the Supervision and Insurance of Cooperatives).

<sup>3</sup> By law, credit unions, including state-chartered credit unions without federal share insurance, may be certified as CDFIs. See 12 U.S.C. 4701-4719; 12 CFR part 1805. COSSEC is considered equivalent to a state credit union regulator by the CDFI Fund.

## *Analysis:*

### I. Overview of Membership Regulation

Eligibility for membership in an FHLBank is limited to the types of financial institutions specified in section 4(a) of the Federal Home Loan Bank Act (Bank Act), each of which must also meet several other eligibility requirements to become an FHLBank member.<sup>4</sup> When the statute was originally enacted in 1932, eligible entities included only thrift institutions and insurance companies. Federally insured credit unions first became eligible for FHLBank membership in 1989 when Congress amended the Bank Act to add “insured depository institutions” (defined as any depository institution the accounts of which are insured by the Federal Deposit Insurance Corporation (FDIC) or by the National Credit Union Share Insurance Fund<sup>5</sup>) to the list of eligible entity types. Congress further amended the Bank Act in 2008 to add CDFIs as an eligible entity type, and again in 2015 to provide that credit unions without federal share insurance may be eligible for membership as insured depository institutions, provided certain prerequisites are met.<sup>6</sup>

Among other things, the membership regulation implements the statutory membership eligibility requirements, extends to all members and applicants several eligibility requirements that expressly apply only to insured depository institutions under the statute, and specifies how and when an institution must demonstrate compliance with each of the requirements. Although the regulation requires each institution, regardless of type, to meet the same six general eligibility requirements, for some requirements it specifies different methods of demonstrating compliance for different entity types. For purposes of determining eligibility for membership, the regulation groups members and applicants into three general categories—insured depository institutions, insurance companies, and CDFIs—with some further variation among sub-types within those categories.

The membership regulation provides that, regardless of type, an institution is eligible for membership only if:

- (1) It is duly organized under tribal law, or under the laws of any state or of the United States;
- (2) It is subject to inspection and regulation under the banking laws, or under similar laws, of any state or of the United States or, in the case of a non-depository CDFI, is certified by the CDFI Fund;
- (3) It makes long-term home mortgage loans;
- (4) Its financial condition is such that advances may be safely made to it;
- (5) The character of its management is consistent with sound and economical home financing; and
- (6) Its home financing policy is consistent with sound and economical home financing.<sup>7</sup>

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<sup>4</sup> See 12 U.S.C. 1424(a).

<sup>5</sup> See 12 U.S.C. 1422(9).

<sup>6</sup> See 12 U.S.C. 1424(a)(5); 12 CFR 1263.19.

<sup>7</sup> See 12 CFR 1263.6(a).

In addition to those six generally applicable requirements, the regulation parallels the Bank Act by requiring that an insured depository institution that is not a “community financial institution” (CFI) also have at least 10 percent of its total assets in residential mortgage loans in order to be eligible for membership (the “10 percent” requirement).<sup>8</sup> The regulation imposes an alternative mission eligibility requirement on entities that are not insured depository institutions, requiring them to have “mortgage-related assets” that “reflect a commitment to housing finance,” as determined by the FHLBank in its discretion.<sup>9</sup>

## II. Approach to State-Chartered Credit Unions Without Federal Share Insurance Under the Regulation

As mentioned, the membership regulation treats federally insured credit unions—including those certified as CDFIs—as insured depository institutions in all respects. In addition, the regulation expressly addresses two types of State-chartered credit unions without federal share insurance: a “CDFI credit union,” which is “a State-chartered credit union that does not have Federal share insurance and that has been certified as a CDFI by the CDFI Fund”; and a “non-federally insured credit union” (NFICU), which is “a State-chartered credit union that does not have Federal share insurance and *that has not been certified as a CDFI* by the CDFI Fund.”<sup>10</sup> In most respects, CDFI credit unions are treated as CDFIs and NFICUs are treated as insured depository institutions for purposes of determining eligibility for membership under the regulation.

The “CDFI credit union” concept was added to the membership regulation as part of the 2010 final rule promulgated by FHFA to implement the 2008 statutory amendments permitting FHLBank membership for CDFIs. That final rule revised the regulation to address membership eligibility and application requirements for CDFIs and to clarify the types of entities to be treated as CDFIs for membership purposes.<sup>11</sup> The rule defined “CDFI” to mean any entity that the CDFI Fund has certified as a community development financial institution, except for federally insured banks, thrifts, and credit unions.<sup>12</sup>

As insured depository institutions under the Bank Act, federally insured banks, thrifts, and credit unions had already been eligible for FHLBank membership prior to the enactment of the statutory provisions authorizing membership for CDFIs. By excluding federally insured depository institutions from the definition of “CDFI,” FHFA effectively required that such institutions continue to be treated solely as insured depository institutions under the membership regulation even if they are certified as CDFIs. In explaining its decision, FHFA cited its conclusion that, while Congress adopted the 2008 amendments to provide a new avenue to membership for CDFIs that had not previously been eligible, it did not intend to provide an additional avenue to membership for federally insured depository institutions that had already been eligible under prior law.<sup>13</sup> Conversely, CDFI credit unions are included within the

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<sup>8</sup> See 12 CFR 1263.6(b).

<sup>9</sup> See 12 CFR 1263.6(c). The regulation does not define the term “mortgage-related assets.”

<sup>10</sup> See 12 CFR 1263.1 (emphasis added).

<sup>11</sup> See 75 FR 678 (Jan. 5, 2010).

<sup>12</sup> See 12 CFR 1263.1.

<sup>13</sup> 75 FR at 681.

definition of “CDFI” and (with the exceptions discussed below) are therefore generally treated as CDFIs for membership eligibility purposes under the regulation.

The “NFICU” concept was added to the membership regulation as part of the 2017 final rule promulgated to implement the 2015 statutory amendments expressly addressing credit unions without federal share insurance.<sup>14</sup> The statutory amendment provided that such a credit union must be treated as an insured depository institution for membership eligibility purposes if its state regulator either determines that it meets all eligibility requirements for federal share insurance (notwithstanding its lack of such insurance) or fails to make such a determination within six months of being asked to do so.<sup>15</sup>

In developing the 2017 final rule, FHFA considered whether it should remove the “CDFI credit union” category from the membership regulation and treat all state-chartered credit unions without federal share insurance as NFICUs. FHFA ultimately decided to retain the CDFI credit union concept because failing to do so would have caused entities that would have been classified as CDFI credit unions to become subject to the “10 percent” requirement, in addition to imposing upon them the requirement to seek state regulator confirmation of their eligibility for federal share insurance. FHFA viewed that result as contrary to Congress’s apparent intent to expand eligibility for FHLBank membership through its 2008 and 2015 amendments to the Bank Act.

### III. Cooperativa Membership Eligibility

Cooperativas that are certified as CDFIs, as well as any other state-chartered credit unions without federal share insurance that are certified as CDFIs, are to be classified as “CDFI credit unions” under the membership regulation. Cooperativas and other state-chartered credit unions without federal share insurance that *are not* certified as CDFIs are to be classified as NFICUs.

As a prerequisite to being considered for membership, any cooperativa classified as an NFICU will need to follow the procedures described in 12 CFR 1263.19 to demonstrate that it meets the eligibility requirements for federal share insurance. A cooperativa classified as a CDFI credit union will not need to meet that prerequisite. In addition, a cooperativa classified as an NFICU must meet the “10 percent” requirement to be eligible for membership. While a cooperativa classified as a CDFI credit union need not meet the “10 percent” requirement, it must satisfy the alternative mission requirement by having mortgage-related assets that reflect a commitment to housing finance, as determined by the FHLBank.

For purposes of determining compliance with the general membership eligibility requirements, a cooperativa that is an NFICU and has met the prerequisites of 1263.19 will be treated as an insured depository institution, while a cooperativa that is a CDFI credit union will, with two important exceptions, be treated as a CDFI. Those two exceptions are with respect to determining compliance with the requirements that an applicant be in a financial condition such that advances may be safely made to it (the “financial condition” requirement), and that the character of its management be consistent with sound and economical home financing (the

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<sup>14</sup> See 82 FR 25716 (June 5, 2017); 12 CFR 1263.19.

<sup>15</sup> See 12 U.S.C. 1424(a)(5).

“character of management” requirement), in which cases it is to be treated in the same manner as an insured depository institution.

In evaluating applications from insured depository institutions (including NFICUs) and CDFI credit unions, an FHLBank must review: (1) regulatory financial reports filed by the applicant with its appropriate regulator for the last six calendar quarters and three year-ends; (2) the applicant’s most recent audited financial statements; (3) the applicant’s most recent available report of examination, as well as summaries of strengths and weaknesses cited in the report and of actions taken by the applicant to respond to examination weaknesses; (4) a description of any outstanding enforcement actions against the applicant and supporting materials regarding the applicant’s compliance with the terms of the enforcement action; and (5) any other relevant information concerning the applicant’s financial condition.<sup>16</sup> The regulation provides that an insured depository institution or CDFI credit union shall be deemed to be in compliance with the “financial condition” requirement if it: (1) has received a composite regulatory examination rating from its appropriate regulator within the preceding two years; (2) meets all of its minimum statutory and regulatory capital requirements; and (3) meets a “minimum performance standard.”<sup>17</sup>

An insured depository institution applicant is considered to meet the minimum performance standard if its most recent composite regulatory examination rating within the past two years was “1”, or if its most recent such rating was “2” or “3” and it satisfies certain “performance trend criteria” relating to earnings, nonperforming assets, and allowance for loan and lease losses.<sup>18</sup> Under the regulation, both CDFI credit unions and NFICUs are treated differently from insured depository institutions with respect to the minimum performance standard in that they must satisfy the performance trend criteria irrespective of their composite regulatory examination rating.<sup>19</sup> In the both the 2010 and 2017 final rules, FHFA explained this difference as a prudential measure warranted by the fact that those types of credit unions are not subject to oversight by the NCUA and that FHLBanks may be less familiar with state examination processes and ratings.<sup>20</sup>

To satisfy the “character of management” requirement, insured depository institution (including NFICU) and CDFI credit union (as well as insurance company) applicants must provide to the FHLBank an unqualified written certification that: (1) neither the applicant nor any of its directors or senior officers is subject to, or operating under, any enforcement action instituted by its appropriate regulator; (2) neither the applicant nor any of its directors or senior officers has been the subject of any criminal, civil or administrative proceedings reflecting upon creditworthiness, business judgment, or moral turpitude since the most recent report of examination; and (3) there are no known potential criminal, civil or administrative monetary liabilities, material pending lawsuits, or unsatisfied judgments against the applicant or any of its

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<sup>16</sup> See 12 CFR 1263.11(a).

<sup>17</sup> See 12 CFR 1263.11(b). In contrast, the membership regulation provides that a CDFI applicant, other than a CDFI credit union, shall be deemed to comply with the “financial condition” requirement if it meets certain minimum financial standards relating to net asset ratio, earnings, loan loss reserves, and liquidity. See 12 CFR 1263.16(b)(2).

<sup>18</sup> See 12 CFR 1263.11(b)(3)(i).

<sup>19</sup> See 12 CFR 1263.11(b)(3)(iii).

<sup>20</sup> See 82 FR 25716, 25721 (June 5, 2017).

directors or senior officers since the most recent report of examination, that are significant to the applicant's operations.<sup>21</sup>

A cooperativa that is a de novo institution (one chartered within the three years prior to the date of application) may apply for FHLBank membership if it is classified as an NFICU,<sup>22</sup> while (like other CDFIs), one classified as a CDFI credit union must have been in operation for at least three years before applying. Finally, whether classified as an NFICU or a CDFI credit union, a cooperativa that has become an FHLBank member will thereafter need to submit a biennial Community Support Statement (a requirement that does not apply to non-depository CDFIs).<sup>23</sup>

### ***Congressional Review Act***

FHFA has determined that this Regulatory Interpretation does not constitute a major rule under the Congressional Review Act (5 U.S.C. 801 et seq.).

### ***Effective Date:***

This Regulatory Interpretation is effective immediately upon issuance.

By: \_\_\_\_\_

Clinton Jones  
General Counsel

This Regulatory Interpretation is issued pursuant to 12 CFR 1211.5 and is subject to modification or rescission by the Director of the Federal Housing Finance Agency.

<sup>21</sup> See 12 CFR 1263.12(a). Because they are not subject to regulatory examination or enforcement actions, CDFIs other than CDFI credit unions need only certify as to the latter two points, with the applicable time period being the preceding three years. See 12 CFR 1263.12(b).

<sup>22</sup> See 12 CFR 1263.14.

<sup>23</sup> See 12 CFR 1290.2(d).