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Participation loans spark lawsuit

ORLANDO, Fla. (8/25/10)--A lawsuit that focuses on what happens to participation loans when the credit union that sold them is absorbed by another credit union has been filed in a U.S. District Court for the Middle District of Florida.

Sperry Associates FCU, a \$372.3 million asset credit union based in New Hyde Park, N.Y., filed the lawsuit Friday in Orlando. It alleges that it had bought nearly \$4.5 million in participation loans from the now defunct Miami-based Eastern Florida Financial CU. It also alleges that the credit union that assumed Eastern Financial last year--the \$3.2 billion asset Space Coast CU, Melbourne, Fla.--is responsible for the loans.

Also named in the lawsuit are Eastern Financial's credit union service organization, CU Business Capital (CUBC) of Miramar, Fla., and its successor, Small Business America of Linthicum, Md.

The complaint filed in court alleges that Eastern Financial FCU and South Florida Properties entered into a loan agreement on Oct. 18, 2006 for \$22.4 million in a speculative land deal involving 120.7 acres appraised at \$40 million in St. Lucie, Fla. in 2007. Sperry Associates FCU was sold an undivided participation totaling nearly \$3 million in the SFP loan.

Sperry also entered into a participation loan with Eastern Financial involving a \$15 million credit agreement with King Credit Facility, the court documents said. Sperry paid \$1.5 million for the King participation loan. The loans were underwritten by CU Business Capital.

In early 2009, regulators placed Eastern Financial into conservatorship, and on June 23, 2009, Eastern Financial was merged into the Space Coast CU.

The participation agreements "were in full force and effect as of the merger," said the complaint filed. "As a result of the merger, Space Coast succeeded to the rights, interests, obligations, duties, responsibilities, representations, warranties and liabilities of Eastern Financial under" the participation agreements, the suit alleged.

The complaint also alleged that the National Credit Union Administration, as conservator of the failed credit union, made a payment to Space Coast on the participation loans, which were in default at the time of the merger. Sperry contends that Space Coast is required to turn over the portion of the participation loan allocations to the plaintiff.