

PART 723—MEMBER BUSINESS LOANS

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AUTHORITY: 12 U.S.C. 1756, 1757, 1757A, 1766, 1785, 1789.

SOURCE: 64 FR 28729, May 27, 1999, unless otherwise noted.

§ 723.1 What is a member business loan?

(a) *General rule.* A member business loan includes any loan, line of credit, or letter of credit (including any unfunded commitments) where the borrower uses the proceeds for the following purposes:

- (1) Commercial;
- (2) Corporate;
- (3) Other business investment property or venture; or
- (4) Agricultural.

(b) *Exceptions to the general rule.* The following are not member business loans:

- (1) A loan fully secured by a lien on a 1 to 4 family dwelling that is the member's primary residence;

(2) A loan fully secured by shares in the credit union making the extension of credit or deposits in other financial institutions;

(3) Loan(s) to a member or an associated member which, when the net member business loan balances are added together, are equal to less than \$50,000;

(4) A loan where a federal or state agency (or its political subdivision) fully insures repayment, or fully guarantees repayment, or provides an advance commitment to purchase in full; or

(5) A loan granted by a corporate credit union to another credit union.

(c) *Loans to credit unions and credit union service organizations.* This part does not apply to loans made by federal credit unions to credit unions and credit union service organizations. This part does not apply to loans made by a federally insured, state-chartered credit union to credit unions and credit union service organizations if the credit union's supervisory authority determines that state law grants authority to lend to these entities other than the general authority to grant loans to members.

(d) *Purchase of member loans and member loan participations.* Any interest a credit union obtains in a loan that was made by another lender to the credit union's member is a member business loan, for purposes of this rule and the risk weighting standards of part 702 of this chapter to the same extent as if made directly by the credit union to its member.

(e) *Purchases of nonmember loans and nonmember loan participations.* Any interest a credit union obtains in a nonmember loan, pursuant to § 701.22 or part 742 of this chapter or other authority, is treated the same as a member business loan for purposes of this rule and the risk weighting standards under part 702 of this chapter, except that the effect of such interest on a credit union's aggregate member business loan limit will be as set forth in § 723.16(b) of this part.

[64 FR 28729, May 27, 1999, as amended at 64 FR 57365, Oct. 25, 1999; 68 FR 56551, Oct. 1, 2003]

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§ 723.2 What are the prohibited activities?

(a) *Who is ineligible to receive a member business loan?* You may not grant a member business loan to the following:

(1) Your chief executive officer (typically this individual holds the title of President or Treasurer/Manager);

(2) Any assistant chief executive officers (e.g., Assistant President, Vice President, or Assistant Treasurer/Manager);

(3) Your chief financial officer (Comptroller); or

(4) Any associated member or immediate family member of anyone listed in paragraphs (a) (1) through (3) of this section.

(b) *Equity agreements/joint ventures.* You may not grant a member business loan if any additional income received by the credit union or senior management employees is tied to the profit or sale of the business or commercial endeavor for which the loan is made.

(c) *Loans to compensated directors.* A credit union may not grant a member business loan to a compensated director unless the board of directors approves granting the loan and the compensated director is recused from the decision making process.

§ 723.3 What are the requirements for construction and development lending?

Except as provided in § 723.4 or unless your Regional Director grants a waiver, loans granted for the construction or development of commercial or residential property are subject to the following additional requirements.

(a) The aggregate of the net member business loan balances for all construction and development loans must not exceed 15% of net worth. In determining the aggregate balances for purposes of this limitation, a credit union may exclude any loan made to finance the construction of a single-family residence if a prospective homeowner has contracted to purchase the property and may also exclude a loan to finance the construction of one single-family residence per member-borrower or group of associated member-borrowers, irrespective of the existence of a contractual commitment from a prospec-

tive homeowner to purchase the property.

(b) The borrower must have a minimum of 25% equity interest in the project being financed, the value of which is determined by the market value of the project at the time the loan is made, except that this requirement will not apply in the case of a loan made to finance the construction of a single-family residence if a prospective homeowner has contracted to purchase the property and in the case of one loan to a member-borrower or group of associated member-borrowers to finance the construction of a single-family residence, irrespective of the existence of a contractual commitment from a prospective homeowner to purchase the property. Instead, the collateral requirements of § 723.7 will apply; and

(c) The funds may be released only after on-site, written inspections by qualified personnel and according to a preapproved draw schedule and any other conditions as set forth in the loan documentation.

[64 FR 28729, May 27, 1999, as amended at 68 FR 56551, Oct. 1, 2003; 69 FR 62565, Oct. 27, 2004]

§ 723.4 What other regulations apply to member business lending?

(a) The provisions of § 701.21(a) through (g) and part 702 of this chapter apply to member business loans granted by credit unions to the extent they are consistent with this part. Except as required by part 741 of this chapter, federally insured State-chartered credit unions are not required to comply with the provisions of § 701.21(a) through (g) of this chapter.

(b) If a federal credit union makes a member business loan as part of a Small Business Administration guaranteed loan program with loan requirements that are less restrictive than those required by NCUA, then the federal credit union may follow the loan requirements of the relevant Small Business Administration guaranteed loan program to the extent they are consistent with this part. A federally insured State-chartered credit union that is subject to this part and makes a member business loan as part of a

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Small Business Administration guaranteed loan program with loan requirements that are less restrictive than those required by NCUA may follow the loan requirements of the relevant Small Business Administration guaranteed loan program to the extent they are consistent with this part if its state supervisory authority has determined that the credit union has authority to do so under State law.

(c) The collateral and security requirements of § 723.3 and § 723.7 do not apply to member business loans made as part of a Small Business Administration guaranteed loan program.

[69 FR 62565, Oct. 27, 2004]

§ 723.5 How do you implement a member business loan program?

(a) *Generally.* The board of directors must adopt specific business loan policies and review them at least annually. The board must also use the services of an individual with at least two years direct experience with the type of lending the credit union will be engaging in. The experience must provide the credit union sufficient expertise given the complexity and risk exposure of the loans in which the credit union intends to engage. Credit unions do not have to hire staff to meet the requirements of this section but must ensure that the expertise is available. A credit union can meet the experience requirement through various approaches. For example, a credit union can use the services of a credit union service organization (CUSO), an employee of another credit union, an independent contractor, or other third parties. However, the actual decision to grant a loan must reside with the credit union.

(b) *Conflicts of Interest.* Any third party used by a credit union to meet the requirements of paragraph (a) of this section must be independent from the transaction and is prohibited from having a participation in the loan or an interest in the collateral securing the loan that the third party is responsible for reviewing, with the following exceptions:

- (1) The third party may provide a service to the credit union related to the transaction, such as loan servicing;
- (2) The third party may provide the requisite experience to the credit union

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and purchase a loan or a participation interest in a loan originated by the credit union that the third party reviewed; or

(3) A credit union may use the services of a CUSO that otherwise meets the requirements of paragraph (a) of this section even though the CUSO is not independent from the transaction, provided the credit union has a controlling financial interest in the CUSO as determined under Generally Accepted Accounting Principles.

[68 FR 56551, Oct. 1, 2003]

§ 723.6 What must your member business loan policy address?

At a minimum, your policy must address the following:

- (a) The types of business loans you will make;
- (b) Your trade area;
- (c) The maximum amount of your assets, in relation to net worth, that you will invest in secured and unsecured business loans;
- (d) The maximum amount of your assets, in relation to net worth, that you will invest in a given category or type of business loan;
- (e) The maximum amount of your assets, in relation to net worth, that you will loan to any one member or group of associated members, subject to § 723.7(c)(2) and § 723.8;
- (f) The qualifications and experience of personnel (minimum of 2 years) involved in making and administering business loans;
- (g) A requirement to analyze and document the ability of the borrower to repay the loan consistent with appropriate underwriting and due diligence standards, which also addresses the need for periodic financial statements, credit reports, and other data when necessary to analyze future loans and lines of credit, such as, borrower's history and experience, balance sheet, cash flow analysis, income statements, tax data, environmental impact assessment, and comparison with industry averages, depending upon the loan purpose;
- (h) The collateral requirements must include:
 - (1) Loan-to-value ratios;
 - (2) Determination of value;
 - (3) Determination of ownership;

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(4) Steps to secure various types of collateral; and

(5) How often the credit union will re-evaluate the value and marketability of collateral;

(i) The interest rates and maturities of business loans;

(j) General loan procedures which include:

(1) Loan monitoring;

(2) Servicing and follow-up; and

(3) Collection;

(k) Identification of those individuals prohibited from receiving member business loans.

[64 FR 28729, May 27, 1999, as amended at 68 FR 56551, Oct. 1, 2003]

§ 723.7 What are the collateral and security requirements?

(a) Except as provided in § 723.3 or unless your Regional Director grants a waiver, all member business loans, except those made under paragraphs (c), (d), and (e) of this section, must be secured by collateral as follows:

(1) The maximum loan-to-value ratio for all liens must not exceed 80% unless the value in excess of 80% is covered through private mortgage insurance or equivalent type of insurance, or insured, guaranteed, or subject to advance commitment to purchase by an agency of the federal government, an agency of a state or any of its political subdivisions, but in no case may the ratio exceed 95%;

(2) A borrower may not substitute any insurance, guarantee, or advance commitment to purchase by any agency of the federal government, a state or any political subdivision of such state for the collateral requirements of this paragraph.

(b) Principals, other than a not for profit organization as defined by the Internal Revenue Service Code (26 U.S.C. 501) or those where the Regional Director grants a waiver, must provide their personal liability and guarantee.

(c) You may make unsecured member business loans under the following conditions:

(1) You are a natural person credit union that is well capitalized as defined by § 702.102(a)(1) of this chapter or you are a corporate credit union that maintains a minimum capital ratio as required by § 704.3(d) of this chapter or

a different ratio as permitted under § 704.3(e) of this chapter;

(2) The aggregate of the unsecured outstanding member business loans to any one member or group of associated members does not exceed the lesser of \$100,000 or 2.5% of your net worth; and

(3) The aggregate of all unsecured outstanding member business loans does not exceed 10% of your net worth.

(d) You are exempt from the provisions of paragraphs (a), (b), and (c) of this section with respect to credit card line of credit programs offered to non-natural person members that are limited to routine purposes normally made available under those programs.

(e) You may make vehicle loans under this part without complying with the loan-to-value ratios in this section, provided that the vehicle is a car, van, pick-up truck, or sports utility vehicle and not part of a fleet of vehicles.

[68 FR 56551, Oct. 1, 2003, as amended at 69 FR 62565, Oct. 27, 2004; 70 FR 75722, Dec. 21, 2005; 72 FR 30247, May 31, 2007; 75 FR 66298, Oct. 28, 2010]

§ 723.8 How much may one member or a group of associated members borrow?

Unless your Regional Director grants a waiver for a higher amount, the aggregate amount of net member business loan balances to any one member or group of associated members must not exceed the greater of:

(a) 15% of the credit union's net worth; or

(b) \$100,000.

[68 FR 56552, Oct. 1, 2003]

§ 723.9 [Reserved]

§ 723.10 What waivers are available?

You may seek a waiver for a category of loans in any of the following areas:

(a) Appraisal requirements under § 722.3;

(b) Aggregate construction and development loans limits under § 723.3(a);

(c) Minimum borrower equity requirements for construction and development loans under § 723.3(b);

(d) Loan-to-value ratio requirements for business loans under § 723.7(a);

(e) Requirement for personal liability and guarantee under § 723.7(b);

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(f) Maximum unsecured business loans to one member or group of associated members under § 723.7(c)(2);

(g) Maximum aggregate unsecured member business loan limit under § 723.7(c)(3); and

(h) Maximum aggregate net member business loan balance to any one member or group of associated members under § 723.8.

[68 FR 56552, Oct. 1, 2003, as amended at 69 FR 62565, Oct. 27, 2004]

§ 723.11 How do you obtain a waiver?

To obtain a waiver, a federal credit union must submit a request to the Regional Director (a corporate federal credit union submits the waiver request to the Director of the Office of Corporate Credit Unions). A state chartered federally insured credit union must submit the request to its state supervisory authority. If the state supervisory authority approves the request, the state regulator will forward the request to the Regional Director (or if appropriate the Director of the Office of Corporate Credit Unions). A waiver is not effective until it is approved by the Regional Director (or in the case of a corporate federal credit union the Director of the Office of Corporate Credit Unions). The waiver request must contain the following:

(a) A copy of your business lending policy;

(b) The higher limit sought (if applicable);

(c) An explanation of the need to raise the limit (if applicable);

(d) Documentation supporting your ability to manage this activity; and

(e) An analysis of the credit union's prior experience making member business loans, including as a minimum:

(1) The history of loan losses and loan delinquency;

(2) Volume and cyclical or seasonal patterns;

(3) Diversification;

(4) Concentrations of credit to one borrower or group of associated borrowers in excess of 15% of net worth;

(5) Underwriting standards and practices;

(6) Types of loans grouped by purpose and collateral; and

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(7) The qualifications of personnel responsible for underwriting and administering member business loans.

§ 723.12 What will NCUA do with my waiver request?

Your Regional Director (or the Director of the Office of Corporate Credit Unions) will:

(a) Review the information you provided in your request;

(b) Evaluate the level of risk to your credit union;

(c) Consider your credit union's historical CAMEL composite and component ratings when evaluating your request; and

(d) Notify you whenever your waiver request is deemed complete. Notify you of the action taken within 45 calendar days of receiving a complete request from the federal credit union or the state supervisory authority. If you do not receive notification within 45 calendar days of the date the complete request was received by the regional office, the credit union may assume approval of the waiver request.

§ 723.13 What options are available if the NCUA Regional Director denies my waiver request, or a portion of it?

You may appeal the Regional Director's (or the Director of the Office of Corporate Credit Unions) decision in writing to the NCUA Board. Your appeal must include all information requested in § 723.11 and why you disagree with your Regional Director's (or the Office of Corporate Credit Union Director's) decision.

§§ 723.14–723.15 [Reserved]

§ 723.16 What is the aggregate member business loan limit for a credit union?

(a) *General.* The aggregate limit on a credit union's net member business loan balances is the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets. Loans that are exempt from the definition of member business loans are not counted for the purpose of the aggregate loan limit.

(b) *Effect of nonmember loans and nonmember participations.* If a credit union

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holds any nonmember loans or nonmember loan participation interests that would constitute a member business loan if made to a member, those loans will affect the credit union's aggregate limit on net member business loan balances as follows:

(1) The total of the credit union's net member business loan balances and the nonmember loan balances must not exceed the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets, unless the credit union has first received approval from the NCUA regional director.

(2) To request approval from the NCUA regional director, a credit union must submit an application that:

(i) Includes a current copy of the credit union's member business loan policies;

(ii) Confirms that the credit union is in compliance with all other aspects of this rule;

(iii) States the credit union's proposed limit on the total amount of nonmember loans and participation interests that the credit union may acquire if the application is granted; and

(iv) Attests that the acquisition of nonmember loans and participations is not being used, in conjunction with one or more other credit unions, to have the effect of trading member business loans that would otherwise exceed the aggregate limit.

(3) A federal credit union must submit its request for approval to the regional director (a corporate federal credit union submits its request to the Director of the Office of Corporate Credit Unions). A state chartered federally insured credit union must submit the request to its state supervisory authority. If the state supervisory authority approves the request, the state regulator will forward the application and its decision to the regional director (or if appropriate, the Director of the Office of Corporate Credit Unions). An approved application is not effective until it is approved by the regional director (or in the case of a corporate federal credit union the Director of the Office of Corporate Credit Unions). The regional director will issue a decision within 30 days of receipt of a federal credit union's completed application or within 30 days of receipt of a completed

application and the state supervisory authority's approval for a state chartered federally insured credit union.

[68 FR 56552, Oct. 1, 2003, as amended at 70 FR 75722, Dec. 21, 2005]

§ 723.17 Are there any exceptions to the aggregate loan limit?

There are three circumstances where a credit union qualifies for an exception from the aggregate limit. Loans that are excepted from the definition of member business loans are not counted for the purpose of the exceptions. The three exceptions are:

(a) Credit unions that have a low-income designation or participate in the Community Development Financial Institutions program;

(b) Credit unions that were chartered for the purpose of making member business loans and can provide documentary evidence (such evidence includes but is not limited to the original charter, original bylaws, original business plan, original field of membership, board minutes and loan portfolio);

(c) Credit unions that have a history of primarily making member business loans, meaning that either member business loans comprise at least 25% of the credit union's outstanding loans (as evidenced in any call report filed between January 1995 and September 1998 or any equivalent documentation including financial statements) or member business loans comprise the largest portion of the credit union's loan portfolio (as evidenced in any call report filed between January 1995 and September 1998 or any equivalent documentation including financial statements). For example, if a credit union makes 23% member business loans, 22% first mortgage loans, 22% new automobile loans, 20% credit card loans, and 13% total other real estate loans, then the credit union meets this exception.

§ 723.18 How do I obtain an exception?

To obtain the exception, a federal credit union must submit documentation to the Regional Director, demonstrating that it meets the criteria of one of the exceptions. A state chartered federally insured credit union must submit documentation to its state supervisory authority. The state

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supervisory authority will forward its decision to NCUA. The exception does not expire unless revoked by the state supervisory authority for a state chartered federally insured credit union or the Regional Director for a federal credit union. If an exception request is denied for a federal credit union, it may be appealed to the NCUA Board within 60 days of the denial by the Regional Director. Until the NCUA Board acts on the appeal, the credit union can continue to make new member business loans.

§ 723.19 What are the recordkeeping requirements?

You must separately identify member business loans in your records and in the aggregate on your financial reports.

§ 723.20 How can a state supervisory authority develop and enforce a member business loan regulation?

(a) The NCUA Board may exempt federally insured state chartered credit unions in a given state from NCUA's member business loan rule if NCUA approves the state's rule for use for state chartered federally insured credit unions. In making this determination, the Board is guided by safety and soundness considerations and reviews whether the state regulation minimizes the risk and accomplishes the overall objectives of NCUA's member business loan rule in this part. Specifically, the Board will focus its review on:

- (1) The definition of a member business loan;
- (2) Loan to one borrower limits;
- (3) Written loan policies;
- (4) Collateral and security requirements;
- (5) Construction and development lending; and
- (6) Loans to senior management.

(b) To receive NCUA's approval of a state's member business loan rule, the state supervisory authority must submit its rule to the NCUA regional office. After reviewing the rule, the region will forward the request to the NCUA Board for a final determination.

(c) A state supervisory authority that administers a state member business loans rule, approved by NCUA under §§ 723.20(a) and (b), may rescind

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its rule without NCUA approval. A state supervisory authority should notify NCUA if it anticipates rescinding its rule to foster regulatory continuity and cooperation.

[64 FR 28729, May 27, 1999, as amended at 69 FR 27828, May 17, 2004; 70 FR 75722, Dec. 21, 2005]

§ 723.21 Definitions.

For purposes of this part, the following definitions apply:

Associated member is any member with a shared ownership, investment, or other pecuniary interest in a business or commercial endeavor with the borrower.

Construction or development loan is a financing arrangement for acquiring property or rights to property, including land or structures, with the intent to convert it to income-producing property such as residential housing for rental or sale; commercial use; industrial use; or similar uses. Construction or development loan includes a financing arrangement for the major renovation or development of property already owned by the borrower that will convert the property to income producing property or convert the use of income producing property to a different use from its use before the major renovation or development or is a major expansion of its current use. Construction or development loan does not include loans to finance maintenance, repairs, or improvements to an existing income producing property that do not change its use. Examples to illustrate when a loan is or is not a construction or development loan follow.

Example 1. If a member borrows money to repair a roof on a barn on an existing farming operation, this is a member business loan but is not a construction or development loan. A construction or development loan does not include a loan for routine maintenance of a borrower's existing business or a loan to enhance or expand a borrower's existing business unless those renovations convert the property to a different use or are so major as to be considered the equivalent of converting the use of the property.

Example 2. A loan to convert a movie theater into a restaurant is a construction or development loan. A loan to convert a large Victorian home used for residential purposes

into a six-room inn also would be a construction or development loan. In both instances, the loans are for the purpose of converting the use of the properties. By contrast, a loan to repair the roof or replace the carpet and wallpaper of an operating inn would not be a construction or development loan as it neither converts the use of the property, nor is so major a renovation to be considered the equivalent of converting the use of the property.

Example 3. A loan to expand the parking lot of a small strip shopping center would not be a construction or development loan, but a loan to renovate the small strip shopping center into a mega-mall would be a construction or development loan as it would be viewed as a major renovation that converts the use of the property.

Example 4. A hotel with a fair market value of \$10 million borrows \$1 million to build an exercise facility in the hotel to enhance the property. The loan amount is 10% of the fair market value of the property. This is not a construction or development loan. It is a member business loan to improve or renovate an existing income producing property, but it is not so major a renovation as to be considered the equivalent of converting the use of the property. In another scenario, a hotel with a fair market value of \$10 million borrows \$5 million to build a luxury health spa on the hotel grounds. The loan amount is 50% of the fair market value of the property. This is a construction or development loan, even if the use of the property has not been converted, as the renovation is so major as to be considered the equivalent of converting the use of the property.

Immediate family member is a spouse or other family member living in the same household.

Loan-to-value ratio is the aggregate amount of all sums borrowed including outstanding balances plus any unfunded commitment or line of credit from all sources on an item of collateral divided by the market value of the collateral used to secure the loan.

Net member business loan balance means the outstanding loan balance plus any unfunded commitments, reduced by any portion of the loan that is secured by shares in the credit union, or by shares or deposits in other financial institutions, or by a lien on the member's primary residence, or insured or guaranteed by any agency of the federal government, a state or any political subdivision of such state, or subject to an advance commitment to purchase by any agency of the federal government, a state or any political

subdivision of such state, or sold as a participation interest without recourse and qualifying for true sales accounting under generally accepted accounting principles.

Net worth means the retained earnings balance of the credit union at quarter end as determined under generally accepted accounting principles. Retained earnings consists of undivided earnings, regular reserves, and any other appropriations designated by management or regulatory authorities. This means that only undivided earnings and appropriations of undivided earnings are included in net worth. For low-income designated credit unions, net worth also includes secondary capital accounts that are uninsured and subordinate to all other claims, including claims of creditors, shareholders and the NCUSIF. For any credit union, net worth does not include the allowance for loan and lease losses account.

[64 FR 28729, May 27, 1999, as amended at 68 FR 56552, Oct. 1, 2003; 69 FR 27828, May 17, 2004; 70 FR 75722, Dec. 21, 2005; 73 FR 30478, May 28, 2008]

PART 724—TRUSTEES AND CUSTODIANS OF CERTAIN TAX-ADVANTAGED SAVINGS PLANS

Sec.

724.1 Federal credit unions acting as trustees and custodians of certain tax-advantaged savings plans.

724.2 Self-directed plans.

724.3 Appointment of successor trustee or custodian.

AUTHORITY: 12 U.S.C. 1757, 1765, 1766 and 1787.

SOURCE: 55 FR 30211, July 25, 1990, unless otherwise noted.

§ 724.1 Federal credit unions acting as trustees and custodians of certain tax-advantaged savings plans.

A federal credit union is authorized to act as trustee or custodian, and may receive reasonable compensation for so acting, under any written trust instrument or custodial agreement created or organized in the United States and forming part of a tax-advantaged savings plan which qualifies or qualified for specific tax treatment under sections 223, 401(d), 408, 408A and 530 of the Internal Revenue Code (26 U.S.C. 223,