

## Environmental Evaluation

It has been determined by an environmental evaluation that this action will not have a significant impact on the quality of the human environment. Therefore, neither an Environmental Assessment nor an Environmental Impact Statement is needed.

## Executive Order 12778

This final rule has been reviewed in accordance with Executive Order 12778. The provisions of the final rule do not preempt State laws, are not retroactive, and do not involve administrative appeals.

## Executive Order 12372

This program/activity is not subject to the provisions of Executive Order 12372, which requires intergovernmental consultation with State and local officials. See notice related to 7 CFR part 3015, subpart V, published at 48 FR 29115 (June 24, 1983).

## Paperwork Reduction Act

The amendments to 7 CFR part 1443 set forth in this final rule do not contain information collections that require clearance by the Office of Management and Budget under the provisions of 44 U.S.C. 35.

## Background

This final rule removes 7 CFR part 1443 pertaining to the cottonseed purchase program. The cottonseed purchase program has not been in effect since 1969 and the regulations are obsolete.

## List of Subjects in 7 CFR Part 1443

Cottonseed, Price support and purchase programs, Cotton ginneries, Reporting and recordkeeping requirements, Warehouses.

Accordingly, under the authority of 7 U.S.C. 2202 and 7 CFR 2.65 (a)(14), 7 CFR part 1443 is removed:

Signed at Washington, DC, on September 28, 1995.

Bruce R. Weber,

*Acting Executive Vice President, Commodity Credit Corporation.*

[FR Doc. 95-24625 Filed 10-3-95; 8:45 am]

BILLING CODE 3410-05-P

## NATIONAL CREDIT UNION ADMINISTRATION

### 12 CFR Part 701

#### Organization and Operations of Federal Credit Unions

**AGENCY:** National Credit Union Administration (NCUA).

**ACTION:** Final rule

**SUMMARY:** Currently, NCUA Rules and Regulations prohibit officials and certain employees of federally insured credit unions from receiving either incentive pay or outside compensation for certain activities related to credit union lending. To reduce regulatory burden, the NCUA Board is amending the regulations to give member-elected credit union boards more flexibility to determine compensation policies, including the use of incentive pay.

**EFFECTIVE DATE:** October 4, 1995.

**ADDRESSES:** National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314-3428.

**FOR FURTHER INFORMATION CONTACT:** Lisa Henderson, Staff Attorney, (703) 518-6561, at the above address.

#### SUPPLEMENTARY INFORMATION:

##### Background

Section 701.21(c)(8) of the NCUA Rules and Regulations, 12 CFR 701.21(c)(8), prohibits federal credit unions from making a loan if, either directly or indirectly, any commission, fee, or other compensation is to be received by the credit union's directors, committee members, senior management employees, loan officers, or any immediate family members of such individuals, in connection with underwriting, insuring, servicing, or collecting the loan. However, non-commission salary may be paid to employees. As a condition of federal insurance pursuant to § 741.3(a) of the Regulations, 12 CFR 741.3(a), the prohibition applies to federally insured state-chartered credit unions. As a consequence of the regulation, federally insured credit unions may not provide incentive compensation to officials and loan officers.

Noting that credit union management had become increasingly interested in implementing lending-related incentive pay programs, the NCUA Board, on March 9, 1994, issued a Request for Comment on whether § 701.21(c)(8) should be amended to permit loan officers and/or senior management to receive incentive pay for underwriting and insuring loans. 59 FR 11937 (March 15, 1994). A total of 252 comments was received, 177 of which expressed

support for allowing incentive pay for loan officers.

On April 13, 1995, the Board issued a proposed regulation which would amend § 701.21(c)(8) to authorize lending-related compensation in certain situations where it is currently prohibited. 60 FR 19690 (April 20, 1995). A total of 105 comments was received, 48 from federal credit unions, 29 from state-chartered credit unions, 19 from national and state credit union leagues, 3 from insurance companies, 2 from state credit union regulators, and 1 each from a banking trade association, Member of Congress, law firm, and individual.

Seventy-four commenters felt that the proposed regulation was too restrictive. Seven commenters expressed unqualified support for the proposed regulation and nine expressed qualified support. Seven commenters stated that credit unions should not be permitted to pay incentives, period. Six commenters urged that the current regulation be retained, expressing concern that additional authority to pay incentives could create safety and soundness problems.

#### Final Rule

In response to the comments, and to reduce regulatory burden, the Board has determined to give member-elected boards of directors more flexibility in determining compensation policies for lending-related activities, including the use of incentive pay. Accordingly, the final rule will allow federal credit unions to pay: (1) To any employee, *including* a senior management employee, an incentive or bonus based on the overall financial performance of the credit union; and (2) to any employee, *except* a senior management employee, an incentive based on a loan made by the credit union, provided that the board of the credit union has established written policies and internal controls in connection with the incentive or bonus and monitors compliance with them at least annually. In addition, the final rule will allow a credit union's volunteer officials and non senior management employees, and family members of officials and all employees, to receive compensation from an outside party for a service or activity performed outside the credit union, provided that neither the credit union nor the official, employee, or family member has "steered" anyone to the other party. This will allow for "incidental" situations resulting from the fact that volunteer officials, non senior management employees, such as part-time employees, and family members of employees, may have jobs

outside the credit union in areas such as insurance or real estate, where customers of the outside business choose to obtain loans from the credit union.

The Board wishes to make clear that this action is not intended to encourage lending-related incentives. In the preamble to the proposed rule, the Board expressed some of its concerns regarding incentive pay, particularly for lending activities. However, this liberalization and deregulation reflects the recognition that there are good arguments and strongly held beliefs on both sides of the incentive pay issue. It is the Board's determination, in light of those considerations and the comments received, that NCUA should structure a rule that involves basic controls and safety and soundness standards and that, beyond that, allows a member-elected board of directors to decide whether to use incentives. Of course, NCUA reserves the right to take exception to any compensation plan for safety and soundness reasons.

#### Analysis

The supplementary information section of the preamble stated that the structure of the regulation had been changed to make it easier to interpret and administer. The preamble noted that it had been difficult to determine, in the current regulation, whether an activity was part of "underwriting, insuring, servicing, or collecting" a loan. The proposed regulation only required that an activity be "in connection with" a loan. The preamble stated that NCUA would take a reasonableness approach to that determination.

In an effort to illustrate the distinction between activities in connection and not in connection with lending, the preamble provided examples. The following were presented as being not in connection with lending: (1) Purchasing loan application forms from a company owned by an official; and (2) Financing a home (already) built by a construction company owned by an official. In contrast, the following were presented as being in connection with lending: (1) Obtaining a credit report from a credit bureau owned by an official; and (2) Referring a member to a construction company owned by an official to have a home built and financing the construction of the home.

Eleven commenters stated that the phrase "in connection with" was too broad or too vague. Two commenters stated that the examples provided did little to clarify the scope of coverage of the regulation.

The Board continues to believe that the proposed prohibition would be easier to administer than the current regulation and has therefore retained it in the final rule. The Board acknowledges, however, that the examples provided were not helpful. Rather than trying to determine whether an activity is significant enough to be considered "in connection with" a loan, the Board has concluded that any activity that is directly linked to lending should be considered to be "in connection with" a loan. Under that analysis, each of the four examples discussed above involves an activity that is in connection with a loan.

Proposed paragraph (8)(ii) set forth definitions, only three of which elicited comment. The proposed regulation defined "compensation" as including non monetary items, and a few commenters stated that items of nominal value should be excluded. The Board agrees, and has changed the definition accordingly. Items of nominal value are those with a value so small as to make accounting for them unreasonable or administratively impracticable. The board of directors of a credit union may look to Internal Revenue Service law regarding income and de minimus fringe benefits, 26 USC 132, for guidance in this area.

The proposed regulation defined "employee" to include independent contractor. The intent was to prevent credit unions from evading the rule by calling an individual who is essentially an employee an independent contractor. Several commenters objected to including independent contractors in the definition of employee. They said that it would have the effect of prohibiting any lending-related compensation to any independent contractors or third parties. The Board agrees and has deleted the term "independent contractor" from the final rule. The Board notes, however, that NCUA will treat an individual functioning as an employee as such for the purposes of § 701.21(c)(8).

The proposed regulation defined "senior management employee" as it is defined elsewhere in the NCUA regulations (the chief executive officer, any assistant chief executive officers, and the chief financial officer) but added the phrase, "and any other employee who sets policy for the credit union." Several commenters objected to this addition, arguing that it was too broad and muddied the distinction between senior management and other employees. The Board agrees and has deleted the phrase from the final rule.

Finally, in the final rule the Board has deleted the definition of "workout loan"

as unnecessary and added a definition for "volunteer official." A volunteer official is a director or committee member who is not compensated as such. Federal credit unions are permitted to compensate one director solely for his or her service on the board, and many state-chartered credit unions are permitted by state law to compensate one or more directors for such service. Under the final rule, a director so compensated would not be considered a volunteer official.

Paragraph (8)(iii) of the proposed regulation set forth five exceptions to the prohibition against lending-related compensation. Exception (A), salary for employees, was met with universal approval from the commenters. Exception (B) was an incentive or bonus to an employee, including a senior management employee, based on the credit unions overall financial performance. This codified a position that had been taken in an opinion letter from NCUA and also was supported by the commenters. Accordingly, exceptions (A) and (B) have been retained in the final rule.

Exceptions (C), (D), and (E) authorized payment of an incentive to an employee in connection with processing a loan, making a decision to approve or disapprove a loan, and collecting a loan, respectively, provided that no incentive or bonus was paid to a supervisor of the employee, a senior management employee, or an immediate family member of a supervisor or senior management employee. Exception (D) additionally required that an incentive paid in connection with making a loan decision not be based on the number or dollar amount of loans approved and be structured in a manner that demonstrably protected against an increase in problem loans.

Sixteen commenters said that non senior management should be permitted to receive incentives. Many said that the prohibition against payment of incentives to supervisors would disproportionately affect large credit unions. They argued that lower level supervisors would be caught between senior management, who receive bonuses based on overall performance, and front-line employees, who are eligible for incentive pay. In response to the comments, the Board has removed the prohibition against supervisors receiving incentive pay from the final rule.

Thirty-eight commenters objected to the prohibition against basing incentives on the number or dollar amount of loans approved. Most said there were no other reasonable measures on which to base incentives for loan officers. As

discussed above, the Board has determined to deregulate this issue and allow credit unions to structure their own incentive plans. This is provided for in Exception (C) in the final rule, which simply provides that a federal credit union may pay an incentive or bonus to a non senior management employee in connection with a loan made by the credit union. This includes incentives for any activity connected with lending, including processing and collecting loans, making credit decisions, and selling credit life, credit disability, and mechanical breakdown insurance. The only limitation is that the board of directors of the credit union must have established written policies and internal controls in connection with the incentive or bonus and must monitor those policies and controls annually.

The final rule's requirement of annual monitoring of policies and controls is a change from paragraph (8)(iv) of the proposed regulation, which required quarterly monitoring. Thirteen commenters said that quarterly review was too frequent, arguing that it would put the board of the credit union in the role of micro-managing the credit union. In response to the comments, the change was made. The Board notes, however, that the supervisory committee, or internal auditor in larger credit unions, should consider reviewing the effectiveness of incentive pay policies and controls more frequently than annually.

Paragraph 8(iv) of the proposed rule also required that documentation of the monitoring be made available to the supervisory committee and NCUA. There was some confusion about this requirement. Several commenters asked whether documentation should be made available to examiners during exams or sent to NCUA. There also was a question as to whether state-chartered credit unions should provide documentation to the state regulator. The Board has deleted this requirement as unnecessary. Under the final rule, a credit union wishing to provide incentive pay must establish written policies. These are by definition part of the books and records of the credit union, which are open to the supervisory committee of the credit union and to NCUA examiners.

The preamble to the proposed rule discussed a number of policy changes the regulation would make. It first noted that the current regulation had been interpreted to permit a credit union official or employee to receive compensation for acting as an agent in the sale of property securing a loan made by a credit union, on the rationale

that listing or selling a property on which a loan is granted is not included in underwriting, insuring, servicing, or collecting the loan. Since listing or selling property financed by the credit union is "in connection with" the loan, however, the proposed rule would prohibit compensation for such activity.

The preamble also noted that the current regulation had been interpreted to prohibit a credit union official or employee from, for example, owning an insurance company that sells car insurance to members who finance their cars at the credit union. An argument had been made, however, that the regulatory language prohibited the receipt of compensation in connection with insuring the loan but not in connection with insuring collateral securing the loan. The preamble stated that NCUA was concerned about the opportunity for credit union officials and employees to steer members to a particular insurance agency and that the proposed regulation therefore would prohibit all officials and employees from receiving compensation for insuring collateral securing a loan made by the credit union.

A number of commenters stated that the prohibition against receiving compensation for outside activities might restrict members from volunteering to serve on a credit unions board. The NCUA Board shares that concern and has determined to permit volunteer officials and non senior management employees of a federal credit union, and the family members of officials and all employees, to receive compensation from an outside party for an activity performed outside the credit union, as long as neither the credit union nor the official, employee, or family member refers any person to the other party. Thus, the borrower's receipt of a loan from the credit union should be unconnected to his or her participation in the outside activity of the official, employee, or family member. The Board believes the prohibition should remain in effect for senior management employees in order to prevent situations where subordinate employees feel pressure to make loans to customers of the outside business interest of the senior management employee. The exception will ensure, at the same time, that NCUA's rules do not interfere with the livelihoods of volunteer officials, non senior management employees, such as part-time employees, and the family members of officials and employees. This is set forth in Exception (D) of the final rule.

## Regulatory Procedures

### *Regulatory Flexibility Act*

The NCUA Board certifies that this rule will not have a significant impact on a substantial number of small credit unions (those under \$1 million in assets). Accordingly, a Regulatory Flexibility Analysis is not required.

### *Paperwork Reduction Act*

NCUA has determined that the requirement to establish a written policy in connection with the payment of lending-related incentives does constitute a collection of information under the Paperwork Reduction Act. The Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget (OMB) require that the public be provided an opportunity to comment on information collection requirements, including an agency's estimate of the burden of the collection of information. NCUA estimates that no more than 1000 federally insured credit unions will seek to implement lending-related incentive compensation policies. It is NCUA's view that the time a credit union spends developing a responsible policy is not a burden created by this regulation but rather is necessary to the safe and sound payment of lending-related incentives. The paperwork burden created by this rule is the requirement that such policy be put in writing. NCUA estimates that it should take at most one hour to put an incentive policy in written form. Therefore, 1000 total burden hours are required to comply with the collection requirement.

The NCUA Board invites comment on: (1) Whether the collection of information is necessary for the proper performance of the functions of NCUA, including whether the information will have practical utility; (2) The accuracy of NCUA's estimate of the burden of the collection of information; (3) Ways to enhance the quality, utility, and clarity of the information to be collected; and (4) Ways to minimize the burden of the collection of information. Send comments to Suzanne Beauchesne, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314-3428. Comments should be postmarked by December 4, 1995.

After 60 days, NCUA will submit the paperwork requirement to OMB for review under the Paperwork Reduction Act and will publish a notice to that effect in the Federal Register. NCUA will also publish a notice in the Federal Register once OMB takes action on the submitted request. Until NCUA receives an OMB control number indicating approval of the requirement that

incentive policies be put in writing, a credit union is not required to comply with that requirement.

**Regulatory Burden**

Section 302 of the Riegle Community Development and Regulatory Improvement Act of 1994 requires the federal regulators of banks and savings associations to make all regulations that impose new requirements take effect on the first date of the calendar quarter following publication of the rule unless good reason exists for some other effective date. Although NCUA is not formally subject to this requirement, Letter to Credit Unions #158 stated that the requirement would be beneficial to credit unions and that NCUA planned to implement it whenever practicable. NCUA believes that an immediate effective date is appropriate since the final rule relieves a regulatory burden on credit unions that wish to implement lending-related incentive compensation programs by permitting them to do so. Although the final rule also imposes a recordkeeping requirement, the primary effect of the rule is to relieve regulatory burden.

**Executive Order 12612**

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. The preamble to the proposed rule acknowledged that the proposed rule would impose some requirements on state-chartered, federally insured credit unions but stated that any effect on the distribution of power and responsibilities among the various levels of government was justified by the potential risk to the NCUSIF. Several commenters argued that no risk to the NCUSIF had been demonstrated and that, for state-chartered credit unions, the matter should be left to state regulators to determine.

The final rule imposes significantly less regulatory burden on credit unions than either the proposed rule or the currently effective rule. Therefore, the effect on state regulatory authority is considerably diminished. The Board continues to believe, however, that any remaining effect on that authority is justified by the potential risk to the NCUSIF without such a rule.

The Board notes that this rule is not intended to expand the authority of state-chartered credit unions. If state law imposes greater restrictions on lending-related compensation than does this rule, state-chartered credit unions must comply with state law.

**List of Subjects in 12 CFR Part 701**

Federal credit unions, Organization and operations.

By the National Credit Union Administration Board on September 28, 1995.

Becky Baker,

*Secretary of the Board.*

For the reasons set forth in the preamble, NCUA amends 12 CFR part 701 as follows:

**PART 701—ORGANIZATION AND OPERATION OF FEDERAL CREDIT UNIONS**

1. The authority citation for part 701 continues to read as follows:

Authority: 12 USC 1752(5), 1755, 1756, 1757, 1759, 1761a, 1761b, 1766, 1767, 1782, 1784, 1787, 1789, and Pub. L. 101-73. Section 701.6 is also authorized by 31 USC 3717. Section 701.31 is also authorized by 15 USC 1601, *et seq.*, 42 USC 1981, and 42 USC 3601-3610. Section 701.35 is also authorized by 12 USC 4311-4312.

**§ 701.21 [Amended]**

2. Section 701.21(c)(8) is revised to read as follows:

\* \* \* \* \*

(c) \* \* \*

(8)(i) Except as otherwise provided herein, no official or employee of a Federal credit union, or immediate family member of an official or employee of a Federal credit union, may receive, directly or indirectly, any commission, fee, or other compensation in connection with any loan made by the credit union.

(ii) For the purposes of this section: *Compensation* includes non monetary items, except those of nominal value.

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

*Loan* includes line of credit.

*Official* means any member of the board of directors or a volunteer committee.

*Person* means an individual or an organization.

*Senior management employee* means the credit union's chief executive officer (typically, this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (e.g., Assistant President, Vice President, or Assistant Treasurer/Manager), and the chief financial officer (Comptroller).

*Volunteer official* means an official of a credit union who does not receive compensation from the credit union solely for his or her service as an official.

(iii) This section does not prohibit:

(A) Payment, by a Federal credit union, of salary to employees;

(B) Payment, by a Federal credit union, of an incentive or bonus to an employee based on the credit union's overall financial performance;

(C) Payment, by a Federal credit union, of an incentive or bonus to an employee, other than a senior management employee, in connection with a loan or loans made by the credit union, provided that the board of directors of the credit union establishes written policies and internal controls in connection with such incentive or bonus and monitors compliance with such policies and controls at least annually.

(D) Receipt of compensation from a person outside a Federal credit union by a volunteer official or non senior management employee of the credit union, or an immediate family member of a volunteer official or employee of the credit union, for a service or activity performed outside the credit union, provided that no referral has been made by the credit union or the official, employee, or family member.

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[FR Doc. 95-24688 Filed 10-3-95; 8:45 am]

BILLING CODE 7535-01-P

**12 CFR Part 722**

**Appraisals**

**AGENCY:** National Credit Union Administration (NCUA).

**ACTION:** Final amendments.

**SUMMARY:** The NCUA Board is issuing final amendments to its regulation regarding the appraisal of real estate, adopted pursuant to Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989. The final amendments simplify compliance with regulatory requirements for credit unions by changing provisions of the appraisal regulation that govern: the publication of the Uniform Standards of Professional Appraisal Practice (USPAP); minimum appraisal standards; appraisals to address safety and soundness concerns; unavailable information; additional appraisal standards developed by credit unions; and appraiser independence. The final amendments should reduce costs without affecting the reliability of appraisals used in connection with federally related transactions.

**EFFECTIVE DATE:** October 1, 1995.

**FOR FURTHER INFORMATION CONTACT:** Herbert Yolles, Director, Department of Risk Management, Office of Examination and Insurance, (703) 518-6360 or Michael McKenna, Staff