Part 723 Member Business Loans

§ 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 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.

§ 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?

Unless the 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 all construction and development loans must not exceed 15% of net worth. To determine the aggregate, you may exclude any portion of a loan:
   (1) Secured by shares in the credit union;
   (2) Secured by deposits in another financial institution;
   (3) Fully or partially insured or guaranteed by any agency of the federal government, state, or its political subdivisions; or
   (4) Subject to an advance commitment to purchase by any agency of the federal government, state, or its political subdivisions;

(b) The borrower must have a minimum of 35% equity interest in the project being financed; 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.

§ 723.4 What are the Other Applicable Regulations?

The provisions of § 701.21(a) through (g) of this chapter apply to member business loans granted by federal 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.

§ 723.5 How do you Implement a Member Business Loan Program?

The board of directors must adopt specific business loan policies and review them at least annually. The board must also utilize the services of an individual with at least two years direct experience with the type of lending the credit union will be engaging in. Credit unions do not have to hire staff to meet the requirements of this section; however, credit unions 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, 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.

§ 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 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 § 723.8;

(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;

(h) Receipt and periodic updating of financial statements and other documentation, including tax returns;
(i) A requirement for sufficient documentation supporting each request to extend credit, or increase an existing loan or line of credit (except where the board of directors finds that the documentation requirements are not generally available for a particular type of business loan and states the reasons for those findings in the credit union's written policies). At a minimum, your documentation must include the following:
  (1) Balance sheet;
  (2) Cash flow analysis;
  (3) Income statement;
  (4) Tax data;
  (5) Analysis of leveraging; and
  (6) Comparison with industry average or similar analysis;
(j) The collateral requirements must include:
  (1) Loan-to-value ratios;
  (2) Determination of value;
  (3) Determination of ownership;
  (4) Steps to secure various types of collateral; and
  (5) How often the credit union will reevaluate the value and marketability of collateral;
(k) The interest rates and maturities of business loans;
(l) General loan procedures which include:
  (1) Loan monitoring;
  (2) Servicing and follow-up; and
  (3) Collection;
(m) Identification of those individuals prohibited from receiving member business loans.

§ 723.7 What are the Collateral and Security Requirements?

(a) Unless your Regional Director grants a waiver, all member business loans must be secured by collateral as follows:

Lien	*Minimum loan to value requirements*
All	LTV ratios for all liens cannot exceed 80% unless the value in excess of 80% is covered through private mortgage or equivalent insurance but in no case can it exceed 95%.
First with PMI or similar type of insurer	You may grant a LTV ratio in excess of 80% only where the value in excess of 80% is covered through: acquisition of private mortgage or equivalent type insurance provided by an insurer acceptable to the credit union (where available); insurance or guarantees by, or subject to advance commitment to purchase by, an agency of the federal government; or insurance or guarantees by, or subject to advance commitment to purchase by, an agency of a state or any of its political subdivisions.
First	LTV ratios up to 80%
Second	LTV ratios up to 80%

(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) Federally insured credit unions are exempt from the provisions of paragraphs (a) and (b) of this section with respect to credit card line of credit programs offered to nonnatural person members that are limited to routine purposes normally made available under those programs.

§ 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 out-standing member business loans (including any unfunded commitments) 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.

§ 723.9 How Do You Calculate the Aggregate 15% Limit?

(a) *Step* 1. Calculate the numerator by adding together the total outstanding balance of member business loans to any one member, or group of associated members. From this amount, subtract any portion:
   (1) Secured by shares in the credit union;
   (2) Secured by deposits in another financial institution;
   (3) Fully or partially insured or guaranteed by any agency of the Federal government, state, or its political subdivisions;
   (4) Subject to an advance commitment to purchase by any agency of the Federal government, state, or its political subdivisions.
(b) *Step* 2. Divide the numerator by net worth.

§ 723.10 What Waivers are Available?

You may seek a waiver for a category of loans in the following areas:
(a) Loan-to-value ratios under § 723.7;
(b) Maximum loan amount to one borrower or associated group of borrowers under §723.8;
(c) Construction and development loan limits under § 723.3;
(d) Requirement for personal liability and guarantee under § 723.7; and
(e) Appraisal requirements under § 722.3.

§ 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
    (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 How do I classify loans so as to reserve for potential losses?

Non-delinquent member business loans may be classified based on factors such as the adequacy of analysis and supporting documentation. You must classify potential loss loans as either substandard, doubtful, or loss. The criteria for determining the classification of loans are:

(a) Substandard. Loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of debt. They are characterized by the distinct possibility that the credit union will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in individual loans classified substandard.

(b) Doubtful. A loan classified doubtful has all the weaknesses inherent in one classified substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the loan, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include: proposed merger, acquisition, or liquidation actions; capital injection; perfecting liens on collateral; and refinancing plans.

(c) Loss. Loans classified loss are considered uncollectible and of such little value that their continuance as loans is not warranted. This classification does not necessarily mean that the loan has absolutely no recovery or salvage value, but rather, it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may occur in the future.

§ 723.15 How Much Must I Reserve for Potential Losses?

The following schedule sets the minimum amount you must reserve for classified loans:

Classification	*Amount Required*
Substandard	10% of outstanding amount unless other factors (for example, history of such loans at the credit union) indicate a greater or lesser amount is appropriate.
Doubtful	50% of the outstanding amount.
Loss	100% of the outstanding amount.

§ 723.16 What is the Aggregate Member Business Loan Limit for a Credit Union?

The aggregate limit on a credit union’s outstanding member business loans (including any unfunded commitments) is the lesser of 1.75 times the credit union’s net worth or 12.25% of the credit union’s total assets. Net worth is all of the credit union’s retained earnings. Retained earnings normally includes undivided earnings, regular reserves and any other appropriations designated by management or regulatory authorities. Loans that are exempt from the definition of member business loans are not counted for the purpose of the aggregate loan limit.

§ 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 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 members 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.

§ 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.

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 worth is retained earnings as defined under Generally Accepted Accounting Principles. Retained earnings normally includes undivided earnings, regular reserves and any other appropriations designated by management or regulatory authorities.