

1 ~~04 NCAC 06C .0407 is amended as a temporary rule as follows:~~ is amended as published in 31:19 NCR 1862 as
2 follows

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4 **04 NCAC 06C .0407 BUSINESS LOANS Commercial Lending and Member Business Loans**

5 (a) ~~Prohibited fees.~~ A North Carolina credit union shall not make any loan or extend any line of credit if, either
6 directly or indirectly, any commission, fee or other compensation is to be received by the Credit Union's directors,
7 committee members, senior management employees, loan officers, or any immediate family members of such
8 individuals, in connection with underwriting, insuring, servicing or collecting the loan or line of credit. However,
9 salary (except commissions) for employees is not prohibited by this Section. For purposes of this Section, "senior
10 management employees" means the Credit Union's chief executive officer (typically this individual holds the title of
11 President or Treasurer/Manager), any assistant chief executive officers (e.g., Assistant President, Vice President or
12 Assistant Treasurer/Manager), and the chief financial officer (Comptroller), and "immediate family member" means
13 a spouse or other family member living in the same household.

14 (b) ~~Member Business Loans.~~

15 (1) ~~Definitions:~~

16 (A) ~~Member business loans mean any loan, line of credit, or letter of credit, the proceeds of which will be used for~~
17 ~~commercial, corporate, business, investment property or venture, or agriculture purpose, except that the following~~
18 ~~shall not be considered member business loans for purposes of this Section:~~

19 (i) ~~A loan or loans fully secured by a lien on a one to four family dwelling that is the member's primary residence.~~

20 (ii) ~~A loan that is fully secured by shares in the credit union or deposits in other financial institutions.~~

21 (iii) ~~A loan meeting the general definition of member business loans under Part (b)(1)(A) of this Rule, and, made to~~
22 ~~a borrower or an associated member, which, when added to other such loans to the borrower or associated member,~~
23 ~~is less than fifty thousand dollars (\$50,000).~~

24 (iv) ~~A loan, the repayment of which is fully insured or fully guaranteed by, or where there is an advance~~
25 ~~commitment to purchase in full by, any agency of the federal government or of a state or any of its political~~
26 ~~subdivisions.~~

27 (v) ~~A loan granted by a corporate credit union operating under the provisions of the North Carolina General Statutes~~
28 ~~to another credit union.~~

29 (B) ~~Reserves means reserve fund, undivided earnings, current earnings, and excludes the Allowance for Loan~~
30 ~~Losses.~~

31 (C) ~~Associated Member means any member with a shared ownership, investment or other pecuniary interest in a~~
32 ~~business or commercial endeavor with the borrower.~~

33 (D) ~~Immediate Family Member means a spouse, or other family member living in the same household.~~

34 (E) ~~Loan to Value (LTV) ratio means the quotient of the aggregate amount of all sums borrowed from all sources on~~
35 ~~an item of collateral divided by the market value of the collateral used to secure the loan.~~

1 ~~(F) Construction or development loan means a financing arrangement for the purpose of acquisition of property or~~
2 ~~rights to property or rights to property including land or structures with the intent of conversion into income-~~
3 ~~producing property including residential housing for rental or sale, commercial or industrial use, or a similar use.~~
4 ~~(2) Requirements. Member business loans, as defined in Part (b)(1)(A) of this Rule may be made by credit unions~~
5 ~~only in accordance with the applicable provisions of Rule .0409 and .0205(d) and the following additional~~
6 ~~requirements:~~
7 ~~(A) Written loan policies. The Board of Directors must adopt specific business loan policies and review them at least~~
8 ~~annually. The policies shall, at a minimum, address the following:~~
9 ~~(i) Types of business loans that will be made;~~
10 ~~(ii) The credit union's trade area for business loans;~~
11 ~~(iii) Maximum amount of credit union assets, in relation to reserves, that will be invested in business loans;~~
12 ~~(iv) Maximum amount of credit union assets, in relation to reserves, that will be invested in a given category or type~~
13 ~~of business loan;~~
14 ~~(v) Maximum amount of credit union assets, in relation to reserves, that will be loaned to any one member or group~~
15 ~~of associated members, subject to Subpart (b)(2)(C)(i) of this Rule;~~
16 ~~(vi) Qualifications and experience of personnel involved in making and administering business loans with a~~
17 ~~minimum of two years direct experience with this type of lending;~~
18 ~~(vii) Analysis of the ability of the borrower to repay the loan;~~
19 ~~(viii) Documentation supporting each request for an extension of credit or an increase in an existing loan or line of~~
20 ~~credit shall (except where the Board of Directors finds that such documentation requirements are not generally~~
21 ~~available for a particular type of business loan and states the reasons for those findings in the credit union's written~~
22 ~~policies) include the following: balance sheet, cash flow analysis, income statement, tax data, leveraging;~~
23 ~~comparison with industry averages; receipt and periodic updating of financial statements and other documentation;~~
24 ~~including tax returns;~~
25 ~~(ix) Collateral requirements, including loan to value ratios; appraisal, title search and insurance requirements; steps~~
26 ~~to be taken to secure various types of collateral; and how often the value and marketability of collateral is~~
27 ~~reevaluated;~~
28 ~~(x) Appropriate interest rates and maturities of business loans;~~
29 ~~(xi) Loan monitoring, servicing and follow up procedures, including collection procedures;~~
30 ~~(xii) Provision for periodic disclosure to the credit union's members of the number and aggregate dollar amount of~~
31 ~~member business loans;~~
32 ~~(xiii) Identification, by position, of those senior management employees prohibited by Rule .0205(d) of this Chapter~~
33 ~~from receiving member business loans.~~
34 ~~(B) Other policies. The following minimum limits and policies shall also be established in writing and reviewed at~~
35 ~~least annually for loans granted under this Section:~~
36 ~~(i) Loans shall be granted on a fully secured basis by collateral as follows:~~
37 ~~(f) Second lien for LTV ratios of up to 70 percent;~~

1 ~~(II) First lien for LTV ratios of up to 80 percent;~~

2 ~~(III) First lien with a LTV ratio in excess of 80 percent shall be granted only where the value in excess of 80 percent~~
3 ~~is covered through acquisition of private mortgage, or equivalent type insurance provided by an insurer acceptable to~~
4 ~~the credit union or insurance or guarantees by or subject to advance commitment to purchase by, an agency of the~~
5 ~~federal government or of a state or any of its political subdivisions, and in no event shall the LTV ratio exceed 95~~
6 ~~percent;~~

7 ~~(ii) Loans shall not be granted without the personal liability and guarantees of the principals (natural person~~
8 ~~members) except where the borrower is a not for profit organization as defined by the Internal Revenue Service~~
9 ~~Code (26 U.S.C. 501);~~

10 ~~(iii) All loans to non natural persons, except to other credit unions, must be secured as required in Chapter 54-~~
11 ~~109.27 of the North Carolina General Statutes.~~

12 ~~(C) Loan Limits.~~

13 ~~(i) Unless a greater amount is approved by the Administrator based on the factors set out in Subpart (b)(2)(C)(ii) of~~
14 ~~this Rule with the concurrence of the Regional Director of the National Credit Union Administration, the aggregate~~
15 ~~amount of outstanding member business loans to any one member or group of associated members shall not exceed~~
16 ~~15 percent of the credit union's reserves (less the Allowance for Loan Losses account), or seventy five thousand~~
17 ~~dollars (\$75,000) whichever is higher. If any portion of a member business loan is secured by shares in the credit~~
18 ~~union, or deposits in another financial institution, or fully or partially insured or guaranteed by, or subject to an~~
19 ~~advance commitment to purchase by, any agency of the federal government or of a state or any of its political~~
20 ~~subdivisions, such portion shall not be calculated in determining the 15 percent limit.~~

21 ~~(ii) Exceptions. Credit unions seeking an exception from the limits of Subpart (b)(2)(C)(i) or Subparagraph (b)(3) of~~
22 ~~this Rule must present the Administrator of Credit Unions and the Regional Director of the National Credit Union~~
23 ~~Administration with, at a minimum; the higher limit sought; an explanation of the need by the members to raise the~~
24 ~~limit and ability of the credit union to manage this activity; an analysis of the credit union's prior experience making~~
25 ~~member business loans; and a copy of its business lending policy. The analysis of credit union experience in making~~
26 ~~member business loans shall document the history of loan losses, loan delinquency, volume and cyclical or seasonal~~
27 ~~patterns, diversification, concentrations of credit to one borrower or group of associated borrowers in excess of 15~~
28 ~~percent of reserves (less the Allowance of Loan Losses account), underwriting standards and practices, types of~~
29 ~~loans grouped by purpose and collateral and qualifications of personnel responsible for underwriting and~~
30 ~~administering member business loans. The credit union must have written approval of the Administrator of Credit~~
31 ~~Unions and the Regional Director of the National Credit Union Administration to exceed the limitations contained in~~
32 ~~this Rule.~~

33 ~~(iii) Maturity. Member business loans shall be granted for periods consistent with the purpose, security,~~
34 ~~creditworthiness of the borrower and sound lending policies.~~

35 ~~(iv) Monitoring requirement. Credit unions with member business loans in excess of 100 percent of reserves (less~~
36 ~~the Allowance for Loan Losses account) shall submit the following information regarding member business loans to~~
37 ~~the Administrator on a quarterly basis: the aggregate total of loans outstanding; the amount of loans delinquent in~~

1 excess of 30 days; the balance of the allowance for member business loan losses; the aggregate total of all
2 concentrations of credit to one borrower or group of associated borrowers in excess of 15 percent of reserves (less
3 the Allowance for Loan Losses account); the total number and amount of all construction, development or
4 speculative loans; and any other information pertinent to the safe and sound condition of the member business loan
5 portfolio.

6 (D) Allowance for loan losses.

7 (i) The determination whether a member business loan will be classified as substandard, doubtful, or loss, for
8 purposes of the valuation allowance for loan losses, will rely on factors not limited to the delinquency of the loan.
9 Non-delinquent loans may be classified depending on an evaluation of factors, including but not limited to, the
10 adequacy of analysis and documentation.

11 (ii) Loans classified shall be reserved as follows:

12 (I) Substandard loans at ten percent of outstanding amount unless other factors (e.g. history of such loans at the
13 Credit Union) indicate a greater or lesser amount is appropriate. Loans classified as substandard loans are
14 inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if
15 any. Loans classified must have a well defined weakness or weaknesses that jeopardize the liquidation of the debt.
16 They are characterized by the distinct possibility that the Credit Union will sustain some loss if the deficiencies are
17 not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in
18 individual loans classified substandard.

19 (II) Doubtful loans at 50 percent of outstanding amount. Loans classified as doubtful loans have all the weaknesses
20 inherent in ones classified substandard, with the added characteristic that the weaknesses make collection or
21 liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and
22 improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific
23 pending factors which may work to the advantage and strengthening of the loan its classification as an estimated loss
24 is deferred until its more exact status is determined. Pending factors include: proposed merger, acquisition, or
25 liquidation actions, capital injection, perfecting liens on additional collateral, and refinancing plans.

26 (III) Loss loans at 100 percent of outstanding amount. Loans classified as loss loans are considered uncollectible and
27 of such little value that their continuance as loans is not warranted. This classification does not necessarily mean that
28 the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this
29 basically worthless asset even though partial recovery may occur in the future.

30 (3) Construction and development lending. Loans granted under this Section to finance the construction or
31 development of commercial or residential property shall be subject to the following additional provisions:

32 (A) The aggregate of all such loans, excluding any portion of a loan secured by shares in the credit union, or
33 deposits in another financial institution, or fully or partially insured or guaranteed by, or subject to an advance
34 commitment to purchase by, any agency of the Federal Government or of a State or any of its political subdivisions,
35 shall not exceed 15 percent of reserves (less the Allowance for Loan Losses account);

36 (B) The borrower shall have a minimum of 35 percent equity interest in the project being financed;

1 ~~(C) Funds for such projects shall be released following on-site inspections by independent credit union personnel,~~
2 ~~qualified as in Subpart (b)(2)(A)(vi) of this Rule in accordance with a draw schedule preapproved by the credit~~
3 ~~union.~~

4 ~~(4) Prohibitions.~~

5 ~~(A) Senior management employees. A credit union may not make member business loans to the following:~~

6 ~~(i) Any member of the Board of Directors who is compensated as such;~~

7 ~~(ii) The credit union's chief executive officer (typically this individual holds the title of President or~~
8 ~~Treasurer/Manager);~~

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

10 ~~(iv) The chief financial officer (Comptroller);~~

11 ~~(v) Any associated member or immediate family member of the senior management employees listed in~~
12 ~~Subparagraphs (b)(4)(A)(i) thru (iv) of this Rule.~~

13 ~~(B) Equity kickers/joint ventures. A credit union shall not grant a member business loan where a portion of the~~
14 ~~amount of income to be received by the credit union in conjunction with such loan is tied to the profit or sale of the~~
15 ~~business or commercial endeavor for which the loan is made.~~

16 ~~(5) Recordkeeping. All loans, lines of credit, or letters of credit, the proceeds of which will be used for a~~
17 ~~commercial, corporate, business, investment property or venture, or agriculture purpose, shall be separately~~
18 ~~identified in the records of the credit union and reported as such in financial and statistical reports required by the~~
19 ~~Administrator in Subpart (b)(2)(C)(iv) of this Rule or the Regional Director of the National Credit Union~~
20 ~~Administration.~~

21 (a) Commercial lending and member business loans. State chartered federally insured credit unions shall adhere to
22 the federal regulations prescribed by the National Credit Union Administration relating to commercial lending and
23 member business loan program pursuant to 12 C.F.R. Part 723, and this Rule, and any subsequent amendments, are
24 incorporated by reference and can be found at no cost on the Code of Federal Regulations website www.ecfr.gov.

25 (b) Written loan policies. The Board of Directors shall give notification to the Administrator of Credit Unions prior
26 to initiating a commercial lending and member business loan program and adopt specific commercial lending and
27 member business loan policies and review them at least annually. The Board of Directors shall review its commercial
28 lending and member business loan policies prior to any material change in the credit union's commercial lending and
29 member business loan program or related organizational structure, and in response to any material change in portfolio
30 performance or change in economic conditions. Credit unions with an asset size of two hundred fifty million dollars
31 (\$250,000,000) or below shall have commercial lending and member business loan polices submitted to the
32 Administrator of Credit Unions 30 days prior to initiating a commercial lending and member business loan program.

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34 *History Note:* Authority G.S. 54-109.12; 54-109.21(25); 54-109.78; 12 C.F.R. Part 741.3; 12 C.F.R. Part 723; 12
35 C.F.R. Part 741.203;
36 Eff. January 1, 1988;
37 Amended Eff. August 1, 1998; March 2, 1992;

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