

Proposed Rules

Federal Register

Vol. 63, No. 151

Thursday, August 6, 1998

This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Organization and Operations of Federal Credit Unions

AGENCY: National Credit Union Administration (NCUA).

ACTION: Notice of proposed rulemaking and request for comment.

SUMMARY: The proposed rule clarifies certain provisions in NCUA's regulation that sets forth the requirements for the purchase, sale and pledge of eligible obligations. Currently, the regulation provides that a federal credit union (FCU) may purchase real estate loans from any source if it is granting real estate loans on an ongoing basis and the purchase will facilitate the packaging of a pool of loans for sale on the secondary market. The proposal clarifies that a pool must include a substantial portion of the FCU's own loans and must be sold promptly. Further, the proposed rule explains when the purchase of a member's loan is not the purchase of an eligible obligation, but rather the making of a direct loan.

DATES: Comments must be received by October 5, 1998.

ADDRESSES: Comments should be directed to Becky Baker, Secretary of the Board. Mail or hand-deliver comments to: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314-3428. Fax comments to (703) 518-6319. E-mail comments to boardmail@ncua.gov. Please send comments by one method only.

FOR FURTHER INFORMATION CONTACT: Mary F. Rupp, Staff Attorney, Office of General Counsel, National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314-3428 or telephone: (703) 518-6553.

SUPPLEMENTARY INFORMATION:

Background

On May 3, 1979, the NCUA Board adopted a final rule that allowed an

FCU to purchase real estate loans from any source if it is granting real estate loans on an ongoing basis and the purchase will facilitate the packaging of a pool of loans to be sold on the secondary market. 44 FR 27068 (May 9, 1979). The rule was based on three sections of the Federal Credit Union Act (the Act): §§ 107(5)(A)(i), 107(13) and 107(15). Section 107(13) authorizes an FCU to purchase, sell, pledge, discount, or otherwise receive or dispose of in whole or in part, any eligible obligations of its members. The proposed rule explained that, although on its face § 107(13) does not authorize the purchase of nonmember real estate loans, "[c]onsidering the Congressional intent to allow credit unions to take advantage of secondary mortgage market facilities, the Administration does not believe that Congress intended 107(13) to be an express prohibition on such purchases provided they are authorized by other sections of the Act." 44 FR 60, 61 (January 2, 1979). The Board found this authority in the incidental powers clause, § 107(15), and the long term real estate lending power, § 107(5)(A)(i) of the Act. The Board believed that an FCU's power to purchase nonmember real estate loans was incident to its power to make long term real estate loans, because "[i]n order to operate a successful real estate program an FCU must have access to the secondary market. This can best be done by pooling loans." 44 FR at 61. The Board recognized that, for an FCU to pool loans to sell in the secondary market, it would sometimes need to purchase nonmember loans to complete its pool. The proposed rule restricted the purchase of nonmember loans to the loans of other credit unions because the Board was mindful of the "restrictions placed on real estate lending by Congress." 44 FR at 61. Although the final rule removed the restriction that the nonmember loans be purchased from credit unions, the Board remained concerned that this incidental power not be interpreted too broadly and that the focus remain on making loans to members.

The Board balanced "the need for efficient access to the secondary market against Congressional intent in restricting the real estate loans" of FCUs. 44 FR at 22070. The preamble to the final rule stated that the FCU's "board of directors must have adopted

a policy of granting long term real estate loans" and must be granting them "on an on-going basis"; an FCU "must include a substantial portion of its own loans in the pool"; once a particular pool is sold, an FCU must "grant more loans before a second pool can be assembled"; and "Federal credit unions will be expected to sell or pledge obligations purchased to package a pool of loans promptly. Arrangements to dispose of such loans should generally be made in advance of their purchase by obtaining a commitment from a buyer to purchase the pool of loans before the pool is actually assembled." 44 FR at 27070.

Although the preamble to the final rule discusses the requirements that a pool must include a substantial portion of the credit union's own loans and must be sold promptly, questions on these points have arisen from time to time. NCUA has responded, through legal opinion letters and provisions in the Accounting Manual for Credit Unions, that FCUs must meet these conditions. Accounting Manual for Federal Credit Unions, § 6030.4. The Board believes it will be helpful to FCUs to clarify these existing requirements by having them set out in the regulation, itself. FCUs and persons involved in advising them often review regulations pertaining to particular activities and, with this amendment, it will be easier for FCUs to be informed about the requirements for the purchase of eligible obligations without consulting other sources for guidance.

The Act and NCUA's regulations limit the aggregate unpaid balance of eligible obligations purchased to 5% of the unimpaired capital and surplus of the purchaser. 12 U.S.C. 1757(13) and 12 CFR 701.23(b)(3). The current regulation specifically exempts from the 5% limitation student and real estate loans purchased under paragraphs (b)(1)(iii) and (iv) and eligible obligations purchased under paragraph (b)(1)(i) that are refinanced by the purchasing credit union so that they are loans it is empowered to grant. 12 CFR 701.23(b)(3). There has been some confusion as to whether FCUs participating in indirect lending and leasing must account for these as eligible obligations subject to the 5% limitation or if they may treat them as loans.

General Counsel opinion letters have stated that indirect lending and indirect leasing arrangements may be treated as loans if certain conditions are met. The proposed rule lists the conditions, so that FCUs can determine if a transaction qualifies as a loan or the purchase of an eligible obligation.

Proposal

The Board proposes to amend § 701.23(b)(1)(iv) by clarifying that a pool of loans, as used in that subsection, must include a substantial portion of the FCU's own loans and must be sold promptly. This clarification mirrors what is currently stated in the Accounting Manual. Accounting Manual for Federal Credit Unions, § 6030.4. To provide a more concrete measure for compliance, the Board has considered substituting specific numbers to measure what is meant by "substantial" and "promptly" in the proposed rule. Agency staff with expertise in the secondary market has suggested that, in order for an FCU's pool of loans to be considered to contain a "substantial portion of its own loans," a reasonable measure would be at least 75%. Staff believes this figure represents current practice amongst FCUs participating in the secondary market. FCUs participating in the secondary market normally only need a small percentage of nonmember loans to complete the pool. Further, because FCUs do not have the express statutory authority to purchase nonmember loans, the Board continues to interpret this provision narrowly. It should only be used by an FCU that is granting member real estate loans on an ongoing basis, pooling the loans and selling them on the secondary market, as a mechanism to complete a pool. It should not be a mechanism for FCUs to circumvent the lending restrictions on loans to nonmembers.

Regarding the period that FCUs can hold the pool of loans, FCUs will be expected to sell them "promptly" because they will be purchasing loans of nonmembers, loans they could not grant. The 1979 preamble states that "[a]rrangements should generally be made in advance of their purchase by obtaining a commitment from a buyer to purchase the pool of loans before the pool is actually assembled." 44 FR at 27070. Agency staff has suggested that 120 days is adequate time given the commitment period from purchasers in the secondary market.

Although specific numbers provide a more definitive measure, they remove flexibility which may be useful in certain circumstances. The Board is interested in receiving comments on

whether specific numbers should be used and, if so, what numbers are reasonable.

The Board proposes amending § 701.23(b)(3) by reorganizing it so that the current exceptions to the 5% limit are listed in separate subsections and the indirect lending and leasing exception is added to the list. The new provision sets forth the conditions for classifying an indirect lending or leasing arrangement as a loan. First, the FCU must make the final underwriting decision. This means that the FCU must actually review the application and determine that the transaction conforms to its lending or leasing policies. Second, the sales or lease contract must be assigned to the FCU very soon after it is signed by the member and the dealer or leasing company. In some programs, the assignment will occur immediately. In others, the assignment will occur the next business day. The longer the time between the formation of the contract and its assignment, the more likely the program will be viewed as involving the purchase of an eligible obligation rather than the making of a loan. The NCUA Board is interested in receiving comment on whether a specific number of days should be substituted for "very soon" and, if so, what number is reasonable.

Request for Additional Comment

Section 701.23(b)(1)(iii) and (iv), with certain restrictions, allows an FCU to purchase student and real estate loans from any source if the FCU is pooling them for sale on the secondary market. The NCUA Board is also interested in receiving comment on whether the types of loans that can be purchased from any source for purposes of creating pools for sale should be expanded to include auto and credit card loans. Comments on this issue will assist the Board in determining whether to propose regulatory changes to include auto and credit card loans.

REGULATORY PROCEDURES

Regulatory Flexibility Act

The Regulatory Flexibility Act requires the NCUA to prepare an analysis to describe any significant economic effect any regulation may have on a substantial number of small credit unions, meaning those under \$1 million in assets. The NCUA Board has determined and certifies that the proposed rule if adopted will not have a significant economic impact on a substantial number of small credit unions. The reason for this determination is that it is highly unlikely that small credit unions would

be engaged in pooling real estate loans for sale on the secondary market. Accordingly, the NCUA Board has determined that a Regulatory Flexibility Analysis is not required.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. The proposed amendments will only apply to federal credit unions. Section 741.8(b)(1) specifically exempts state chartered federally insured credit unions from 701.23(b)(1)(iv). Proposed § 701.23(b)(v) only applies to FCUs.

Paperwork Reduction Act

The proposal does not impose any additional paperwork requirements on FCUs.

List of Subjects in 12 CFR Part 701

Credit unions, Eligible obligations.

By the National Credit Union Administration Board on July 30, 1998.

Becky Baker,

Secretary of the Board.

Accordingly, NCUA proposes to amend 12 CFR part 701 as follows:

PART 701—ORGANIZATION AND OPERATIONS OF FEDERALLY-INSURED CREDIT UNIONS

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

Authority: 12 U.S.C. 1752(5), 1755, 1756, 1757, 1759, 1761a, 1761b, 1766, 1767, 1782, 1784, 1787, 1789 and 1798. Section 701.6 is also authorized by 31 U.S.C. 3717. Section 701.31 is also authorized by 15 U.S.C. 1601 *et seq.*; 42 U.S.C. 1981 and 3601-3610. Section 701.35 is also authorized by 42 U.S.C. 4311-4312.

2. Amend § 701.23 by adding a sentence to the end of paragraph (b)(1)(iv) and by revising paragraph (b)(3) to read as follows:

§ 701.23 Purchase, sale and pledge of eligible obligations.

* * * * *

(b) * * *

(1) * * *

(iv) * * * A pool must include a substantial portion of the credit union's own loans and must be sold promptly.

* * * * *

(3) The aggregate of the unpaid balance of eligible obligations purchased under paragraph (b) of this section cannot exceed 5% of the unimpaired capital and surplus of the purchaser. The following can be excluded in calculating this 5% limitation:

(i) Student loans purchased in accordance with paragraph (b)(1)(iii) of this section;

(ii) Real estate loans purchased in accordance with paragraph (b)(1)(iv) of this section;

(iii) Eligible obligations purchased in accordance with paragraph (b)(1)(i) of this section that are refinanced by the purchaser so that it is a loan it is empowered to grant; and

(iv) An indirect lending or indirect leasing arrangement that is classified as a loan and not the purchase of an eligible obligation because the federal credit union makes the final underwriting decision and the sales or lease contract is assigned to the federal credit union very soon after it is signed by the member and the dealer or leasing company.

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[FR Doc. 98-20952 Filed 8-5-98; 8:45 am]

BILLING CODE 7535-01-P

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Organization and Operations of Federal Credit Unions

AGENCY: National Credit Union
Administration (NCUA).

ACTION: Notice of proposed rulemaking.

SUMMARY: The NCUA is proposing to incorporate into its regulations the agency's longstanding interpretation that federal credit unions can permit a nonmember to assume a member's long-term residential real estate loan in conjunction with the nonmember's purchase of the member's principal residence.

DATES: Comments must be received on or before October 5, 1998.

ADDRESSES: Direct comments to Becky Baker, Secretary of the Board. Mail or hand-deliver comments to: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314-3428. Fax comments to (703) 518-6319. *Please send comments by one method only.*

FOR FURTHER INFORMATION CONTACT: Michael J. McKenna, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518-6540.

SUPPLEMENTARY INFORMATION: Since 1977, federal credit unions have had the authority to offer long-term real estate loans to finance a member's principal residence. 12 U.S.C. 1757(A)(i). NCUA's implementing regulation for this authority is set forth at 12 CFR 701.21(g).

In 1985, the NCUA Board issued Interpretive Ruling and Policy

Statement 85-3 (IRPS 85-3). 50 FR 51840 (December 20, 1985). IRPS 85-3 stated that, incidental to a federal credit union's authority to make long-term real estate loans to members, a federal credit union may permit assumptions, by either members or nonmembers, under the terms and conditions specified in the loan agreement and consistent with the Federal Credit Union Act and NCUA's Regulations. The Board also stated that, in the case of a nonmember assumption, there must be no new money lent to the borrower and no extension of the original maturity date specified in the loan agreement with the member.

NCUA has a policy of periodically reviewing its regulations to "update, clarify and simplify existing regulations and eliminate redundant and unnecessary provisions." IRPS 87-2, Developing and Reviewing Government Regulations. As part of its regulatory review program, NCUA reviewed its IRPS to determine their current effectiveness. As a result of that review, the NCUA Board stated that it planned to incorporate IRPS 85-3 into NCUA's Regulations. 62 FR 11773 (March 13, 1997) and 62 FR 50245 (September 25, 1997). The Board's goal is to increase regulatory effectiveness by making it easier for credit unions to locate applicable rules regarding real estate lending. Accordingly, the Board is proposing to add a new paragraph to Section 701.21(g) that will incorporate IRPS 85-3 so that this provision on nonmember assumption of loans will be in the same place with the other regulatory provisions regarding real estate lending. Although the language is slightly different, the policy set forth in the proposed amendment is, for all practical purposes, identical to the policy set forth in IRPS 85-3.

This proposal does not authorize a refinancing by a nonmember. Further, this proposal, just as IRPS 85-3, does not permit a federal credit union to grant an assumption of a loan to a nonmember if the underlying intent of the original loan to the member was to grant an assumption by a nonmember immediately or soon after making the original loan. NCUA would view such a transaction as a sham and will not permit federal credit unions to circumvent the restriction on lending to nonmembers. NCUA will review assumptions by nonmembers during the examination process. Federal credit unions engaging in such sham transactions will be subject to NCUA's administrative enforcement process.

This proposal does not require a federal credit union to permit nonmember assumption of real estate

loans. A federal credit union's loan agreements can provide that a loan is immediately due and payable if the member's residence securing the loan is sold.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact any proposed regulation may have on a substantial number of small entities (primarily those under \$1 million in assets). The NCUA Board has determined and certifies that the proposed amendment, if adopted, will not have a significant economic impact on a substantial number of small credit unions.

Accordingly, the Board has determined that a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

NCUA has determined that the proposed amendments do not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. The proposal only applies to federal credit unions. NCUA has determined that the proposed amendment does not constitute a significant regulatory action for the purposes of the Executive Order.

List of Subjects in 12 CFR Part 701

Credit, Credit unions, Insurance, Mortgages, Reporting and recordkeeping requirements, Surety bonds.

By the National Credit Union
Administration Board on July 30, 1998.

Becky Baker,
Secretary of the Board.

For the reasons set forth in the preamble, it is proposed that 12 CFR Part 701 be amended 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 U.S.C. 1752(5), 1755, 1756, 1757, 1759, 1761a, 1761b, 1766, 1767, 1782, 1784, 1787, and 1789. Section 701.6 is also authorized by 31 U.S.C. 3717. Section 701.31 is also authorized by 15 U.S.C. 1601 *et seq.*, 42 U.S.C. 1861 and 42 U.S.C. 3601-3610. Section 701.35 is also authorized by 42 U.S.C. 4311-4312.