

credit union members, particularly small businesses, will have a greater opportunity to obtain loans that their credit union may not be able to grant.

## B. Section-by-Section Analysis

### *Outstanding Loan Balance, Sections 723.1, 723.3, 723.8, 723.16, 723.21*

The Board proposes to adopt the phrase "outstanding member business loan balance" as a new definition in § 723.21 and use it in various sections in the rule, including §§ 723.1, 723.3, 723.8, and 723.16. The proposed definition for "outstanding member business loan balance" is:

[T]he outstanding loan balance and any unfunded commitments, excluding 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 fully or partially 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.

This definition reflects NCUA's interpretation of various provisions in the MBL rule since the current rule was issued and incorporates several exclusions derived from CUMAA. This definition is key to determining: whether a loan qualifies as an MBL; which portion of an MBL is included in the calculation of the loans to one borrower limit; and which portion of an MBL is included in the calculation of a credit union's total aggregate MBL limit.

One example of an interpretation that the Board proposes to include in the definition of outstanding MBL balance concerns participation interests sold without recourse. The Board addressed this issue during the agency's 1999 MBL rulemaking in the final rule's preamble, rather than in the regulation's text. In the preamble, the Board agreed with a commenter that, when participating out loan interests, an originating credit union should count only the amount of the loan it holds towards its aggregate loan limit, provided that the loan participation sold is without recourse. 64 FR 28721, 28727, May 27, 1999. The Board has determined that the proposed rule should include this interpretation, as well as other interpretations and CUMAA exclusions, so that credit unions can easily ascertain the factors that are involved in calculating outstanding MBL balances.

The Board believes the rule should use outstanding MBL balance throughout the rule for uniformity and to avoid confusion. Clarifying the use of

outstanding MBL balances in the rule incorporates the Board's positions stated in past rulemakings and interpretations provided in NCUA legal opinions.

As part of the proposal to adopt the definition of "outstanding MBL balance," the Board also proposes to delete and reserve § 723.9, which addresses calculation of the limit on loans to one borrower. The proposed definition of "outstanding MBL balance" contains all of the rule's exclusions from this calculation, making § 723.9 unnecessary.

### *Loan Participations*

The Board has reconsidered its position regarding the treatment of loan participations by purchasing credit unions and proposes to exclude participation interests from the calculation of the aggregate MBL limit. The Federal Credit Union Act expressly requires a credit union to include only MBLs it makes to its members in calculating its statutory aggregate MBL limit. 12 U.S.C. 1757a(a). Participation interests purchased by a credit union from an originating eligible organization are not loans made by the participating credit union. The Board, therefore, proposes that these loans need not be included in calculating the participating credit union's aggregate loan limits.

The Board believes CUMAA's legislative history supports this interpretation as consistent with the congressional goal that credit unions fulfill their mission of meeting the credit and savings needs of consumers. Selling MBL participations without recourse permits an originating credit union to obtain additional liquidity enabling it to meet the demand for both consumer and small business loans to members. A credit union that purchases participation interests in loans from other originating lenders does so as a means of investing its excess funds and bases its participation decision on normal investment considerations, including safety and return. As a member-owned and controlled lender, a credit union will purchase participation interests only after meeting its members' own lending needs. The due diligence analysis by the purchasing credit union enhances the overall creditworthiness process in credit union business lending. In addition, these participations diversify the risk of MBLs within the credit union system, ultimately making credit unions safer and better able to meet the needs of both consumer and small business members.

While the Board believes that purchased MBL participation interests need not be included in the aggregate loan limit, a purchased participation

interest is a business loan asset and carries the associated risks. A participating credit union, therefore, must otherwise comply with part 723 and subject these loans to the PCA risk-weighting standards under part 702 as though the credit union had originated the MBLs. This means that a participating credit union must have an MBL policy, employ an individual or use the services of an independent third-party with the requisite lending experience, perform the appropriate due diligence, and comply with the collateral requirements and loans to one borrower limit in part 723, in addition to all other provisions of the MBL rule when purchasing a MBL participation interest from any eligible organization.

Finally, the Board notes that, in order for a participating credit union to exclude participation interests it has purchased, the purchase must be a *bona fide* transaction to fulfill a business purpose. The sale and purchase of participation interests in MBLs among credit unions cannot be used as a means to circumvent the regulation's aggregate loan limit. For example, credit unions may not enter into participation agreements that, in effect, permit them to swap portions or all of their MBL portfolios and, thereby, claim that the participation interests are excluded from the aggregate loan limit.

### *Loans to Credit Unions and CUSOs, Section 723.1*

The Board proposes to amend § 723.1 to clarify that loans made by Federal, natural person credit unions to other natural person credit unions and CUSOs are not MBLs. The Federal Credit Union Act grants federal credit unions (FCUs) distinct, express authority to lend to credit unions and CUSOs, independent from their authority to make MBLs. 12 U.S.C. 1757(5)(C), (D). While CUMAA placed limitations on a federally insured credit union's authority to make MBLs to members, 12 U.S.C. 1757a, the law did not alter an FCU's authority to lend to credit unions or CUSOs and did not impose limits on the amount an FCU could lend to these entities beyond the statutory conditions that pre-dated CUMAA. 12 U.S.C. 1757(5)(C), (D).

The proposed rule also permits FISCUs to exclude loans to credit unions and CUSOs in calculating their aggregate MBL limit if the state supervisory authority determines that state law grants distinct authority to lend to credit unions and CUSOs separately from the authority to make MBLs. In the absence of authority similar to that in the Federal Credit Union Act, a FISCUs loans to credit