

prospective homeowners do not contract to reside in a property. They asked, therefore, that this wording be removed. The Board agrees and amended the final rule accordingly. These commenters also asked the Board to expand the exclusion to one-to-four family dwellings. The final rule maintains the more restrictive provision as proposed, limiting the exclusions to single-family residences. The Board has determined not to extend the exclusion to multi-family dwellings as these dwellings have an investment component for the purchaser.

*Direct Experience Requirement, Section 723.5*

The final rule amends this section by requiring that the person meeting the rule's mandatory two years of direct experience requirement have sufficient experience given the complexity and risk exposure of the credit union's MBLs. It also requires that a third party meeting the experience requirement be independent from the transaction, but establishes three exceptions from this standard.

Seventy-four commenters supported the agency's intent for this proposal. Most of these commenters stated that the rule would make it easier to find individuals qualified to act as an MBL officer by allowing credit unions to engage the services of a third party with direct experience in MBLs under certain conditions so as to avoid potential conflict of interest. They also stated that it allows credit unions to make MBLs without creating a costly infrastructure to meet the experience requirement. The Board wants to clarify that credit unions have been able to use third parties to meet the experience requirement since the 1991 final MBL rule. 56 FR 48421, Sept. 25, 1991. This rulemaking bolsters the experience requirement by ensuring that the individual's experience is relevant to the types of MBLs the credit union makes and that the individual does not have interests that conflict with the credit union's interests.

Six commenters asked for clarification regarding the agency's standard for the requisite lending experience. In 1999, the Board stated that the "experience requirement can be met by either general business lending experience or experience with granting loans for a particular purpose or secured by a particular collateral." 64 FR 28721, 28723, May 27, 1999. The final rule has a more specific standard requiring a credit union to obtain the services of someone with experience tailored to the credit union's needs. Individuals who meet the requirements of this section must have lending experience directly

related to the type of MBLs the credit union intends to offer. These individuals must be familiar with the proper underwriting, analysis, and origination of loans of a particular type in order to understand their complexity and risk exposure. For example, an individual with experience solely in taxi cab loans does not have the requisite experience necessary to underwrite a loan to the taxi company for a gas station, because the individual will be unfamiliar with related issues that may impact the loan, such as environmental laws applicable to underground storage tanks. Likewise, an individual who only has experience with financing residential real estate for homebuilders does not have sufficient lending experience for the land development and construction, or purchase, of a commercial strip center.

Thirty-three commenters found the prohibition against a third party having an interest or involvement in the transaction too restrictive. Most of these commenters stated that the proposal limited a credit union's ability to use third-party service providers and should not be adopted in the final rule. They stated that, while improper personal financial gain cannot be tolerated, a paid third party's interest and involvement is necessary to provide the assistance many credit unions need to make MBLs. One commenter opposed the requirement stating that it would preclude smaller credit unions from having agreements with larger credit unions that have experience underwriting MBLs and then selling participations to that credit union. Two commenters suggested that, in any transaction in which a third party is retained, a credit union should obtain written disclosures of actual or potential relationships and fee arrangements the third party may have in the transaction. Another commenter stated that the proposal was worded too broadly. The Board agrees that the proposal required some revision. The final rule amends the proposed language to more accurately reflect the Board's concerns by establishing a general conflicts of interest standard and exceptions to the standard.

In order for a credit union to engage in business lending in a safe and sound manner, it is crucial for the credit union to maintain strong internal controls and to have independent, experienced personnel involved in making lending decisions that are in the best interests of the credit union. The credit union must perform its own due diligence, both when the credit union makes MBLs and when it purchases MBLs or MBL participation interests, through the

services of an individual who meets the requirements in § 723.5. The final rule does not prevent a third party who has the direct experience necessary for a credit union to make MBLs from providing services to the credit union such as document preparation, annual reviews, or loan servicing.

The final rule generally prevents a credit union from relying on a seller's due diligence and experience when the credit union is purchasing MBLs or participation interests in MBLs from the seller. Regardless of whether the seller is, for instance, another credit union or CUSO, the purchasing credit union cannot meet the direct experience requirements of § 723.5 by depending on the advice of the experienced individual(s) who performed the underwriting for the originating lender unless: (1) Staff for the purchasing credit union performed the loan analysis for the originating credit union; or (2) the CUSO exception in § 723.5(b)(3) applies. The final rule bars a credit union from using a third party who has an interest in either the sale of the loan or the collateral securing the loan. It does not bar a smaller credit union from subsequently selling participations to a larger credit union that had advised the credit union when it originated the MBL.

Under the CUSO exception in paragraph (b)(3), a credit union may comply with § 723.5 when purchasing a participation interest or eligible obligation from a CUSO, if the experienced individual is employed by a CUSO in which the credit union has a "controlling financial interest" as determined under the Generally Accepted Accounting Principles, even though the CUSO is both the originator and underwriter of the loan.

*Member Business Loan Policy, Section 723.6*

This section is amended to require credit unions to adopt analysis and documentation requirements within their MBL policies that are consistent with appropriate underwriting and due diligence standards for the types of MBLs the credit union makes, without detailing required documents. Documentation and underwriting criteria for an MBL may vary depending on the type of business requesting the loan and type of loan requested. The final rule also makes a technical amendment to 12 CFR 704.11(c) to reflect the redesignation of paragraphs in § 723.6.

One hundred and twelve commenters supported the proposal. The vast majority of these commenters noted it would greatly expedite the MBL process