

October 24, 1996

Stephen B. Mitchell  
Burbridge And Mitchell  
139 East South Temple, Suite 200  
Salt Lake City, Utah 54111

Re: Construction and Development Lending (Your July 17, 1996 Letter)

Dear Mr. Mitchell:

We apologize for the delay in our response but we did not receive your letter until September 26, 1996. You have asked whether a loan made to a member for the purpose of purchasing raw land to be held for investment purposes without the present intent of converting the land into income producing property qualifies as a construction and development loan under NCUA Regulation Section 701.21(h)(1)(vi). The loan does not fall within the definition if the member has no intent to convert the land into income producing property during the life of the loan.

#### **ANALYSIS**

Section 701.21(h)(1)(vi) defines a construction and development loan as a "financing arrangement for the purpose of acquisition of property or rights to property, including land or structures, with the intent of conversion into income-producing property including residential housing for rental or sale, commercial, or industrial use, or a similar use." The preamble to this rule as published in the Federal Register elaborates on this definition and states in part that:

Construction or development loans are for the acquisition of land or property upon which improvements are planned. Examples of these types of loans included: (1) The purchase of raw land to be developed for resale as building lots; (2) the purchase of raw or developed land for the purpose of constructing housing or a commercial building; and (3) the purchase of an existing structure for rehabilitation in order to improve the economic value for resale or to improve income-producing potential. This term does not include loans for the construction of a member's residence. Loans for construction of a member's residence are normally consumer loans granted under other provisions of these rules and regulations.

56 Fed. Reg. 48421, 48423 (September 25, 1991).

A loan to a member to acquire raw land with the intent of holding it for price speculation does not fall within the rule's definition of a construction or development loan. It is important that the credit union determine the intention of the member when the loan application is submitted. The member must be able to show that he has the income stream to repay the loan and is not relying on income from the property for repayment. Balloon payment loans might also serve as partial evidence that the member intends to improve the property.

Sincerely,

Richard S. Schulman  
Associate General Counsel

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96-0937