

December 27, 2000

James F. Kanaley, Vice President of Financial Services  
Empire Federal Credit Union  
P.O. Box 11127  
Syracuse, New York 13218-1127

Re: Application of the Member Business Loan Rule to Loans Secured by Stock.

Dear Mr. Kanaley:

Thank you for your recent memorandum concerning NCUA's member business loan regulation, in which you asked that the Office of General Counsel consider adding stock-secured loans to the list of loans excepted from the definition of member business loan. The definition of member business loan and the exceptions to the definition are set out in the Federal Credit Union Act (the Act). 12 U.S.C. §1757a(c)(1). NCUA does not have the authority to issue a regulation that contradicts the Act.

In your memorandum, you state that your credit union originated two loans collateralized by a member's stock. The member indicated that the purpose of the loans was partially or completely for business. The general rule, as stated in NCUA's member business loan regulation, is that loans made for commercial, corporate, other business investment property or venture, or agricultural purposes are member business loans. 12 C.F.R. §723.1(a). Loans made for these purposes carry greater risk and necessitates the limitation imposed by the member business loan regulation. Only certain types of loans specified in the Act are excepted from the definition in the NCUA regulation. 12 C.F.R. 723.1(b). The exceptions include loans deemed to be less risky because of the type of security given by the borrower, for example a mortgage on the borrower's primary residence or a lien on shares in the credit union or deposits in other financial institutions.

You contend that the purpose of a loan should not be considered pertinent if it is secured by a member's stock. You further contend that a loan secured by stock is similar to those excepted from the member business loan definition in the regulation because the value of the collateral would be as safe as real estate and more easily liquidated. We believe that there is an additional risk associated with loans secured by stock as compared to loans secured by real estate. In any case, the Act directs us to look solely at the purpose of the loan to determine if it should be classified as a member business loan, unless it falls within one of the statutory exceptions. 12 U.S.C. §1757a(c)(1)(A).

A loan secured by stock would not be considered a member business loan if it were not made for a business purpose. For your information, loans for the purpose of purchasing or carrying margin stock are considered commercial loans subject to the provisions of the member business loan rule. Such loans are also subject to the credit restrictions and requirements of the Board of Governors of the Federal

Reserve System regulation entitled, "Credit by Banks and Persons Other Than Brokers or Dealers for the Purpose of Purchasing or Carrying Margin Stock (Regulation U)." 12 C.F.R. Part 221. Further, any loan secured by an equity security registered or traded on a national securities exchange, even if not for the purpose of purchasing stock, is subject to some of the filing requirements of Regulation U. 12 C.F.R. §221.3(c)(ii).

Sincerely,

Sheila A. Albin  
Associate General Counsel

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