NATIONAL CREDIT UNION ADMINISTRATION

RULES AND REGULATIONS

TRANSMITTAL SHEET **CHANGE 4**

NCUA 8006 (M3500) DATE: November 2005

TO: THE BOARD OF DIRECTORS OF THE FEDERAL CREDIT UNION OR THE FEDERALLY INSURED CREDIT UNION ADDRESSED:

This is Change 4 to the National Credit Union Administration Rules and Regulations (Revised April 2004).

1. **PURPOSE.** To update the April 2004 edition of the National Credit Union Administration Rules and Regulations in the following manner:

   a. **Part 701—Organization and Operation of Federal Credit Unions.**

   § 701.21—Loans to members and lines of credit to members. Revised paragraphs (e), (f), and (g)(1).

   b. **Part 717—Fair Credit Reporting.**

   Subpart A—General Provisions.

   § 717.1—Purpose. New.

   § 717.2—Examples. New.

   § 717.3—Definitions. Revised paragraphs (a) and (b); (d); (i); (k) and (l).

   Subpart D—Medical Information. New.

   § 717.30—Obtaining or using medical information in connection with a determination of eligibility for credit. New.

   § 717.31—Limits on redisclosure of information. New.

   § 717.32—Sharing medical information with affiliates. New.

   c. **Part 748—Security Program, Report of Crime and Catastrophic Act and Bank Secrecy Act Compliance.**

   § 748.0—Security Program. Revised paragraph (b).

   Appendix B to Part 748—Guidance on Response Programs for Unauthorized Access to Member Information and Member Notice. Added new Appendix B.

2. This revision also corrects typing and printing errors.
3. **INSTRUCTIONS:**
   a. Your April 2004 NCUA Rules and Regulations should be updated as follows:

REMOVE OLD PAGES	INSERT NEW PAGES
i–xv	i–xv
701–7 thru 701–10	701–7 thru 701–10
708a–3 thru 708a–4	708a–3 thru 708a–4
717–1 thru 717–2	717–1 thru 717–7
748–1 thru 748–2	748–1 thru 748–2
748–5 thru 748–6	748–5 thru 748–9
792–5 thru 792–8	792–5 thru 792–8
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4. **PREAMBLES.** Enclosed with Change 4 are Federal Register published preambles. Although not part of the rules, you may find them useful for explanatory purposes.

NATIONAL CREDIT UNION ADMINISTRATION

RULES AND REGULATIONS

TRANSMITTAL SHEET **CHANGE 3**

NCUA 8006 (M3500) DATE: June 2005

TO: THE BOARD OF DIRECTORS OF THE FEDERAL CREDIT UNION OR THE FEDERALLY INSURED CREDIT UNION ADDRESSED:

This is Change 3 to the National Credit Union Administration Rules and Regulations (Revised April 2004).

1. **PURPOSE.** To update the April 2004 edition of the National Credit Union Administration Rules and Regulations in the following manner:
   a. **Part 701—Organization and Operation of Federal Credit Unions.**

      § 701.21—Loans to members and lines of credit to members. Revised paragraph (c)(7)(ii)(C).

   b. **Part 708a—Conversion of Insured Credit Unions to Mutual Savings Banks.**

      § 708a.4—Voting procedures. Revised by adding three sentences at the end of paragraph (a) and adding new paragraph (e).

      § 708a.5—Notice to NCUA. Revised by redesignating paragraph (b) as paragraph (b)(1), added a sentence at the end of paragraph (b)(1), and added paragraph (b)(2).

      § 708a.11—Voting guidelines. New section added.

   c. **Part 708b—Mergers of Federally-Insured Credit Unions; Voluntary Termination or Conversion of Insured Shares.**

      Revised the Table of Contents and the entire part.

2. This revision also corrects typing and printing errors.
3. **INSTRUCTIONS:**
   a. Your April 2004 NCUA Rules and Regulations should be updated as follows:

REMOVE OLD PAGES	INSERT NEW PAGES
i–xv	i–xv
701–7 thru 701–8	701–7 thru 701–8
701–11 thru 701–12	701–11 thru 701–12
708a–1 thru 708a–3	708a–1 thru 708a–4
708b–1 thru 708b–8	708b–1 thru 708b–15

4. **PREAMBLES.** Enclosed with Change 3 are Federal Register published preambles. Although not part of the rules, you may find them useful for explanatory purposes.

NATIONAL CREDIT UNION ADMINISTRATION

RULES AND REGULATIONS

TRANSMITTAL SHEET **CHANGE 2**

NCUA 8006 (M3500) DATE: January 2005

TO: THE BOARD OF DIRECTORS OF THE FEDERAL CREDIT UNION OR THE FEDERALLY INSURED CREDIT UNION ADDRESSED:

This is Change 2 to the National Credit Union Administration Rules and Regulations (Revised April 2004).

1. **PURPOSE.** To update the April 2004 edition of the National Credit Union Administration Rules and Regulations in the following manner:

   a. **Part 701—Organization and Operation of Federal Credit Unions.**

   § 701.14—Change in Official or Senior Executive Officer in Credit Unions that are Newly Chartered or are in Troubled Condition. Removed paragraphs (c), (d), and (e). Also added new paragraphs (c) and (d), and redesignated paragraph (f) as paragraph (e).

   § 701.36—Federal Credit Union Ownership of Fixed Assets. Revised the entire section.

   b. **Part 717—Fair Credit Reporting.** New part added.

   c. **Part 723—Member Business Loans.**

   § 723.3—What are the requirements for construction and development lending? Revised the introductory sentence.

   § 723.4—What other regulations apply to member business lending? Revised the entire section.

   § 723.7—What are the collateral and security requirements? Revised paragraph (a) introductory text.

   § 723.10—What waivers are available? Revised paragraph (h).

   d. **Part 742—regulatory Flexibility Program.**

   § 742.4—From what NCUA regulations will I be exempt? Revised paragraph (a).

   e. **Part 747—Administrative Actions, Adjudicative Hearings, Rules of Practice and Procedure, and Investigations.**

   Subpart K—Inflation Adjustment of Civil Money Penalties.

   § 747.1001—Adjustment of civil money penalties by the rate of inflation. Revised paragraph (a).

f. **Part 748—Security Program, Report of Crime and Catastrophic Act and Bank Secrecy Act Compliance.**

Appendix A to Part 748—Guidelines for Safeguarding Member Information Added sentence to the end of paragraph I; added sentence to the end of paragraph I.A.; redesignated paragraphs I.B.2. a. through d. as I.B.2.c. through f.; added new paragraphcs 1.B.2.a. and b.; Removed the word "and" after the word "information" in paragraph II.B. Added a phrase after the word "member" at the end of the sentence. Added new paragraphs III.G.3. and III.G.4.

2. This revision also corrects typing and printing errors.
3. **INSTRUCTIONS:**
   a. Your April 2004 NCUA Rules and Regulations should be updated as follows:

REMOVE OLD PAGES	INSERT NEW PAGES
i–xv	i–xv
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701–21 thru 701–24	701–21 thru 701–24
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748–1 thru 748–5	748–1 thru 748–5
792–9 thru 792–10	792–9 thru 792–10

4. **PREAMBLES.** Enclosed with Change 2 are Federal Register published preambles. Although not part of the rules, you may find them useful for explanatory purposes.

NATIONAL CREDIT UNION ADMINISTRATION

RULES AND REGULATIONS

TRANSMITTAL SHEET **CHANGE 1**

NCUA 8006 (M3500) DATE: September 2004

TO: THE BOARD OF DIRECTORS OF THE FEDERAL CREDIT UNION OR THE FEDERALLY INSURED CREDIT UNION ADDRESSED:

This is Change 1 to the National Credit Union Administration Rules and Regulations (Revised April 2004).

1. **PURPOSE.** To update the April 2004 edition of the National Credit Union Administration Rules and Regulations in the following manner:

   a. **Part 701—Organization and Operation of Federal Credit Unions.**

   § 701.21—Loans to members and lines of credit to members. Revised paragraph (i)(4).

   b. **Part 703—Investment and Deposit Activities.**

   § 703.1—Purpose and scope. Revised paragraph (b)(6).

   § 703.2—Definitions. Revised the definitions of *Call, Custodial Agreement, Derivatives, and Put,* and added definitions of *Collateralized Mortgage Obligation and Exchangeable Collateralized Mortgage Obligation.*

   § 703.4—Recordkeeping and documentation requirements. Removed the last sentence of paragraph (a).

   § 703.8—Broker-dealers. Revised the second sentence of paragraph (b)(3).

   § 703.9—Safekeeping of investments. Revised the second sentence of paragraph (d).

   § 703.14—Permissible Investments. Revised paragraph (g)(4) and paragraph (g)(13) introductory text.

   § 703.16—Prohibited Investments. Revised paragraphs (a) and (e) and added paragraph (f).

   § 703.19—Investment Pilot Program. Revised introductory language of paragraph (c).

   c. **Part 704—Corporate Credit Unions.**

   § 704.2—Definitions. Revised to add definitions of *Derivatives* and *Exchangeable collateralized mortgage obligation,* and revised the

definitions of *Small business related security* and *Weighted average life*.

§ 704.5—Investments. Revised paragraphs (h)(1) and (h)(4) and added paragraph (h)(5).

§ 704.8—Asset and liability management. Revised paragraph (a)(4).

d. **Part 705—Community Development Revolving Loan Program for Credit Unions.**

§ 705.3—Definitions. Removed from paragaph (b), the parenthetical clause "(excluding student credit unions)".

e. **Part 708a—Conversion of Insured Credit Unions to Mutual Savings Banks.**

Replaced page 708a–3 due to printing error.

f. **Part 708b—Merger of Federally-Insured Credit Unions; Voluntary Termination or Conversion of Insured Status.**

Replaced the entire part due to printing error.

g. **Part 709—Involuntary Liquidation of Federal Credit Unions in Adjudication of Creditor Claims Involving Federally Insured Credit Unions in Liquidation.**

§ 709.1—Definitions. Revised paragaph (c).

h. **Part 715—Supervisory Committee Audits and Verifications.**

§ 715.3—General responsibilities of the Supervisory Committee. Revised paragraphs (a)(1) and (a)(2).

i. **Part 721—Incidental Powers.**

§ 721.3—What categories of activities are preapproved as incidental powers necessary or requisite to carry on a credit union's business? Revised paragraph (l).

j. **Part 723—Member Business Loans.**

§ 723.20—How can a state supervisory authority develop and enforce a member business loan regulation? Revised the first sentence of paragraph (b).

§ 723.21—Definitions. Revised the definition of "Net Member Business Loan Business".

k. **Part 724—Trustees and Custodians of Pension Plans.**

§ 724.1—Federal credit unions acting as trustees and custodians of certain tax-advantaged savings plans. Revised the section heading and the first two sentences.

§ 724.2—Self-Directed Plans. Revised the section heading and the introductory text.

l. **Part 725—Central Liquidity Facility.**

§ 725.18—Creditworthiness. Revised the first sentence of paragraph (c).

m. **Part 745—Share Insurance; Living Trusts.**

Reflects the finalization of § 745.4, without change, the interim final rule published on February 26, 2004, concerning share insurance coverage for beneficial interests in living trust accounts.

2. This revision also corrects typing and printing errors.

3. **INSTRUCTIONS:**

a. Your April 2004 NCUA Rules and Regulations should be updated as follows:

REMOVE OLD PAGES	INSERT NEW PAGES
i–xv	i–xv
701–9 thru 701–10	701–9 thru 701–10
702–1 thru 702–2	702–1 thru 702–2
703–1 thru 703–10	703–1 thru 703–10
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715–1 thru 715–2	715–1 thru 715–2
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723–5 thru 723–6	723–5 thru 723–6
724–1	724–1
725–5 thru 725–6	725–5 thru 725–6

4. **PREAMBLES.** Enclosed with Change 1 are Federal Register published preambles. Although not part of the rules, you may find them useful for explanatory purposes.

NATIONAL CREDIT UNION ADMINISTRATION

RULES AND REGULATIONS

TRANSMITTAL SHEET

NCUA 8006 (M3500) Revised April 2004

TO: THE BOARD OF DIRECTORS OF THE FEDERAL CREDIT UNION OR THE FEDERALLY INSURED CREDIT UNION ADDRESSED:

This is a revision to the National Credit Union Administration Rules and Regulations.

1. PURPOSE. To revise the National Credit Union Administration Rules and Regulations to reflect recent final rules, and to incorporate Changes 1 through 6 of the November 2001 edition. The following changes were made in this revision:

   a. **Part 701—Organization and Operations of Federal Credit Unions.**

      § 701.20—Suretyship and guaranty. New section added.

      § 701.22—Loan participation. Revised paragraphs (a)(4) and (a)(5).

   b. **Part 708a—Conversion of Insured Credit Unions to Mutual Savings Banks.**

      § 708a.4—Voting procedures. Added paragraph (d).

   c. **Part 741—Requirement for Insurance.**

      § 741.2—Maximum borrowing authority. Designated the existing paragraph as (a) and added new paragraphs (b) and (c).

      § 741.221—Suretyship and guaranty requirements. New section added.

   d. **Part 745—Share Insurance and Appendix.**

      § 745.2—General principles applicable in determining insurance of accounts. Added new paragraphs (e) and (f).

      § 745.4—Revocable trust accounts. Revised paragraphs (c) and (e).

      § 745.9–1—Trust accounts. Revised paragraph (c).

      § 745.9–2—IRA/Keogh accounts. Revised paragraph (a).

Appendix to Part 745—Examples of Insurance Coverage Afforded Accounts in Credit Unions Insured by the National Credit Union Share Insurance Fund.

B. How Are Revocable Trust Accounts Insured? Revised the third sentence.

Example 4. Revised Question and Answer paragraphs.

Example 5. New example added.

e. **Part 790—Description of NCUA; Requests for Agency Action.**

§ 790.2—Central and Regional Office Organization. Revised paragraph (a); added new sentence at the end of paragraph (b)(6); and revised paragraph (c)(1).

f. **Part 795—OMB Control Numbers Assigned Pursuant to The Paperwork Reduction Act.**

§ 795.1—OMB Control Numbers. Revised paragraphs (a) and (b).

2. This revision also corrects typing errors.

3. INSTRUCTIONS. Remove from your files the November 2001 NCUA Rules and Regulations, including Changes 1 through 6, and replace with the April 2004 edition.

4. PREAMBLES. Enclosed with this revision are Federal Register published preambles. Although not part of the rules, you may find them useful for explanatory purposes.

NCUA

Rules and Regulations

April 2004

National Credit Union Administration
Washington, D.C. 20456

NCUA 8006 M3500

FOREWORD

This publication of the National Credit Union Administration Rules and Regulations dated April 2004 supersedes the November 2001 edition. All amendments and revisions to the rules and regulations finalized through February 2004 have been incorporated into this edition.

Future changes to this edition will be published on a regular basis. Changes will be furnished as loose leaf pages to replace the original pages and will be numbered beginning with Change 1. These rules and regulations are officially codified in Chapter VII, Title 12 of the Code of Federal Regulations (CFR), Parts 700 through 795.

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*THESE PARTS APPLY TO FEDERALLY INSURED STATE-CHARTERED CREDIT UNIONS AS WELL AS FEDERAL CREDIT UNIONS

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*THESE PARTS APPLY TO FEDERALLY INSURED STATE-CHARTERED CREDIT UNIONS AS WELL AS FEDERAL CREDIT UNIONS

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*THESE PARTS APPLY TO FEDERALLY INSURED STATE-CHARTERED CREDIT UNIONS AS WELL AS FEDERAL CREDIT UNIONS

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Part 700

Definitions

§ 700.1 Scope.

The definitions in § 700.2 apply to terms used in this chapter. Many additional definitions appear in the parts where the terms are used.

§ 700.2 Definitions.

As used in this chapter:

(a) "Act" means the Federal Credit Union Act (73 Stat. 628, 84 Stat. 944, 12 U.S.C. 1751–1795(k)).

(b) "Administration" means the National Credit Union Administration.

(c) "Board" means the National Credit Union Administration Board.

(d) "Credit Union" means a credit union chartered under the Federal Credit Union Act or, as the context permits, under the laws of any State.

(e)(1) Insolvency. A credit union will be determined to be insolvent when the total amount of its shares exceeds the present cash value of its assets after providing for liabilities unless:

(i) It is determined by the Board that the facts that caused the deficient share-asset ratio no longer exist; and

(ii) The likelihood of further depreciation of the share-asset ratio is not probable; and

(iii) The return of the share-asset ratio to its normal limits within a reasonable time for the credit union concerned is probable; and

(iv) The probability of a further potential loss to the insurance fund is negligible.

(2) For purposes of this section, the following definitions are used:

(i) "Cash value of assets." Recorded value will be considered the cash value of any asset account providing accepted accounting principles and practices are followed and the provisions of law, regulation, and bylaws are met.

(ii) "Liabilities." Recorded liabilities which are due and payable, excluding shares of members and nonmembers, are considered liabilities.

(f) *Paid-in and unimpaired capital and surplus* means shares plus post-closing, undivided earnings. This does not include regular reserves or special reserves required by law, regulation or special agreement between the credit union and its regulator or share insurer. "Paid-in and unimpaired capital and surplus" for purposes of the Central Liquidity Facility is defined in § 725.2(o) of this chapter.

(g) "Regional Director" means the representative of the Administration in the designated geographical area in which the office of the Federal credit union is located.

(h) "Regional Office" means the office of the Administration located in the designated geographical area in which the office of the Federal credit union is located.

(i) "State" means a State of the United States, the District of Columbia, any of the several Territories and possessions of the United States and the Commonwealth of Puerto Rico.

(j) *Unimpaired capital and surplus* means the same as "paid-in and unimpaired capital and surplus," as defined in paragraph (f) of this section.

Part 701

Organization and Operations of Federal Credit Unions

§ 701.1 Federal credit union chartering, field of membership modifications, and conversions.

National Credit Union Administration policies concerning chartering, field of membership modifications, and conversions are set forth in Interpretive Ruling and Policy Statement 03–1, Chartering and Field of Membership Policy (IRPS 03–1). Copies may be obtained by contacting NCUA at the addresses found in § 790.2(c) of this chapter.

§ 701.2 [Removed and Reserved]

§§ 701.3–701.5 [Reserved]

§ 701.6 Fees paid by Federal credit unions.

(a) *Basis for assessment.* Each calendar year or as otherwise directed by the Board, each Federal credit union shall pay to the Administration for the current National Credit Union Administration fiscal year (January 1 to December 31) an operating fee in accordance with a schedule as fixed from time to time by the National Credit Union Administration Board based on the total assets of each Federal credit union as of December 31 of the preceding year or as otherwise determined pursuant to paragraph (b) of this section.

(b) *Coverage.* The operating fee shall be paid by each Federal credit union engaged in operations as of January 1 of each calendar year, except as otherwise provided by this paragraph.

(1) *New charters.* A newly chartered Federal credit union will not pay an operating fee until the year following the first full calendar year after the date chartered.

(2) *Conversions.* A state chartered credit union that converts to Federal charter will pay an operating fee in the year following the conversion. Federal credit unions converting to state charter will not receive a refund of the operating fee paid to the Administration in the year in which the conversion takes place.

(3) *Mergers.* A continuing Federal credit union that has merged with another credit union will pay an operating fee in the following year based on the combined total assets of the merged credit union and the continuing Federal credit union as of December 31 of the year in which the merger took place. For purposes of this requirement, a purchase and assumption transaction wherein the continuing Federal credit union purchases all or essentially all of the assets of another credit union shall be deemed a merger. Federal credit unions merging with other Federal or state credit unions will not receive a refund of the operating fee paid to the Administation in the year in which the merger took place.

(4) *Liquidations.* A Federal credit union placed in liquidation will not pay any operating fee after the date of liquidation.

(c) *Notification.* Each Federal credit union shall be notified at least 30 days in advance of the schedule of fees to be paid. A Federal credit union may submit written comments to the Board for consideration regarding the existing fee schedule. Any subsequent revision to the schedule shall be provided to each Federal credit union at least 15 days before payment is due.

(d) *Assessment of Administrative Fee and Interest for Delinquent Payment.* Each Federal credit union shall pay to the Administration an administrative fee, the costs of collection, and interest on any delinquent payment of its operating fee. A payment will be considered delinquent if it is postmarked later than the date stated in the notice to the credit union provided under § 701.6(c). The National Credit Union Administration may waive or abate charges or collection of interest if circumstances warrant.

(1) The administrative fee for a delinquent payment shall be an amount fixed from time to time by the National Credit Union Administration Board and based upon the administrative costs of such delinquent payments to the Administration in the preceding year.

(2) The costs of collection shall be the actual hours expended by Administration personnel multiplied by the average hourly salary and benefits costs of such personnel as determined

by the National Credit Union Administration Board.

(3) The interest rate charged on any delinquent payment shall be the U.S. Department of the Treasury Tax and Loan Rate in effect on the date when the payment is due as provided in 31 U.S.C. § 3717.

(4) If a credit union makes a combined payment of its operating fee and its share insurance deposit as provided in § 741.4 of this chapter and such payment is delinquent, only one administrative fee will be charged and interest will be charged on the total combined payment.

§§ 701.7–701.11 [Reserved]

§ 701.12 [Removed]

§ 701.13 [Removed]

§ 701.14 Change in Official or Senior Executive Officer in Credit Unions that are Newly Chartered or are in Troubled Condition.

(a) *Statement of Scope and Purpose.* Section 212 of the Federal Credit Union Act (12 U.S.C. 1790a) sets forth conditions under which a credit union must notify NCUA in writing of any proposed changes in its board of directors, committee members or senior executive staff. The regulation only applies in cases of newly chartered credit unions and credit unions in troubled condition.

(b) *Definitions.* For the purposes of this section:

(1) "Committee member" means any individual who serves as an official of the credit union in the capacity of a credit committee member or supervisory committee member.

(2) "Senior executive officer" means a credit union's chief executive officer (typically this individual holds the title of president or treasurer/manager), any assistant chief executive officer (e.g., any assistant president, any vice president or any assistant treasurer/manager) and the chief financial officer (controller). The term "senior executive officer" also includes employees of an entity, such as a consulting firm, hired to perform the functions of positions covered by the regulation.

(3) Except as provided in paragraph (b)(4) of this section for corporate credit unions, "troubled condition" means any insured credit union that has one or a combination of the following conditions:

(i) Has been assigned

(A) A 4 or 5 CAMEL composite rating by the NCUA in the case of a federal credit union, or

(B) An equivalent 4 or 5 CAMEL composite rating by the state supervisor in the case of a federally insured, state-chartered credit union, or

(C) A 4 or 5 CAMEL composite rating by NCUA based on core workpapers received from the state supervisor in the case of a federally insured, state-chartered credit union in a state that does not use the CAMEL system. In this case, the state supervisor will be notified in writing by the Regional Director in the Region in which the credit union is located that the credit union has been designated by NCUA as a troubled institution;

(ii) Has been granted assistance as outlined under Sections 208 or 216 of the Federal Credit Union Act.

(4) In the case of a corporate credit union, "troubled condition" means any insured corporate credit union that has one or a combination of the following conditions:

(i) Has been assigned

(A) A 4 or 5 Corporate Risk Information System (CRIS) rating by NCUA in either the Financial Risk or Risk Management composites, in the case of a federal corporate credit union, or

(B) An equivalent 4 or 5 CRIS rating in either the Financial Risk or Risk Management composites by the state supervisor in the case of a federally insured, state-chartered corporate credit union in a state that has adopted the CRIS system, or an equivalent 4 or 5 CAMEL composite rating by the state supervisor in the case of a federally insured, state-chartered corporate credit union in a state that uses the CAMEL system, or

(C) A 4 or 5 CRIS rating in either the Financial Risk or Risk Management composites by NCUA based on core workpapers received from the state supervisor in the case of a federally insured, state-chartered credit union in a state that does not use either the CRIS or CAMEL system. In this case, the state supervisor will be notified in writing by the Director of the Office of Corporate Credit Unions that the corporate credit union has been designated by NCUA as a troubled institution;

(ii) has been granted assistance as outlined under Sections 208 or 216 of the Federal Credit Union Act.

(c) *Procedures for Notice of Proposed Change in Official or Senior Executive Officer*—(1) *Prior Notice Requirement.* An insured credit union must give NCUA written notice at least 30 days before the effective date of any addition or replacement of a member of the board of directors or committee member or the employment or change in responsibilities of any individual to a position of senior executive officer if:

(i) The credit union has been chartered for less than two years; or

(ii) The credit union meets the definition of troubled condition in paragraph (b)(3) or (4) of this section.

(2) *Waiver of Prior Notice*—(i) *Waiver requests.* Parties may petition the appropriate Regional Director for a waiver of the prior notice required under this section. Waiver may be granted if it is found that delay could harm the credit union or the public interest.

(ii) *Automatic waiver.* In the case of the election of a new member of the board of directors or credit committee member at a meeting of the members of a federally insured credit union, the prior 30-day notice is automatically waived and the individual may immediately begin serving, provided that a complete notice is filed with the appropriate Regional Director within 48 hours of the election. If NCUA disapproves a director or credit committee member, the board of directors of the credit union may appoint its own alternate, to serve until the next annual meeting, contingent on NCUA approval.

(iii) *Effect on disapproval authority.* A waiver does not affect the authority of NCUA to issue a Notice of Disapproval within 30 days of the waiver or within 30 days of any subsequent required notice.

(3) *Filing procedures*—(i) *Where to file.* Notices will be filed with the appropriate Regional Director or, in the case of a corporate credit union, with the Director of the Office of Corporate Credit Unions. All references to Regional Director will, for corporate credit unions, mean the Director of Office of Corporate Credit Unions. State-chartered federally insured credit unions will also file a copy of the notice with their state supervisor.

(ii) *Contents.* The notice must contain information about the competence, experience, character, or integrity of the individual on whose behalf the notice is submitted. The Regional Director or his or her designee may require additional information. The information submitted must include the identity, personal history, business background, and experience of the individual, including material business activities and affiliations during the past five years, and a description of any material pending legal or administrative proceedings in which the individual is a party and any criminal indictment or conviction of the individual by a state or federal court. Each individual on whose behalf the notice is filed must attest to the validity of the information filed. At the option of the individual, the information may be forwarded to the Regional Director by the individual; however, in such cases, the credit union must file a notice to that effect.

(iii) *Processing.* Within ten calendar days after receiving the notice, the Regional Director will inform the credit union either that the notice is complete or that additional, specified information is needed and must be submitted within 30 calendar days. If the initial notice is complete, the Regional Director will issue a written decision of approval or disapproval to the individual and the credit union within 30 calendar days of receipt of the notice. If the initial notice is not complete, the Regional Director will issue a written decision within 30 calendar days of receipt of the original notice plus the amount of time the credit union takes to provide the requested additional information. If the additional information is not submitted within 30 calendar days of the Regional Director's request, the Regional Director may either disapprove the proposed individual or review the notice based on the information provided. If the credit union and the individual have submitted all requested information and the Regional Director has not issued a written decision within the applicable time period, the individual is approved.

(d) *Commencement of Service.* A proposed director, committee member, or senior executive officer may begin service after the end of the 30-day period or any other additional period as provided under paragraph (c)(3)(iii) of this section, unless the NCUA disapproves the notice before the end of the period.

(e) *Notice of Disapproval.* NCUA may disapprove the individual's serving as a director, committee member or senior executive officer if it finds that the competence, experience, character, or integrity of the individual with respect to whom a notice under this section is submitted indicates

that it would not be in the best interests of the members of the credit union or of the public to permit the individual to be employed by, or associated with, the credit union. The Notice of Disapproval will advise the parties of their rights of appeal pursuant to 12 CFR Part 747 subpart J of NCUA's Regulations.

§§ 701.15–701.18 [Reserved]

§ 701.19 Benefits for Employees of Federal Credit Unions.

(a) *General authority.* A federal credit union may provide employee benefits, including retirement benefits, to its employees and officers who are compensated in conformance with the Act and the bylaws, individually or collectively with other credit unions. The kind and amount of these benefits must be reasonable given the federal credit union's size, financial condition, and the duties of the employees.

(b) *Plan trustees and custodians.* Where a federal credit union is the benefit plan trustee or custodian, the plan must be authorized and maintained in accordance with the provisions of part 724 of this chapter. Where the benefit plan trustee or custodian is a party other than a federal credit union, the benefit plan must be maintained in accordance with applicable laws governing employee benefit plans, including any applicable rules and regulations issued by the Secretary of Labor, the Secretary of the Treasury, or any other federal or state authority exercising jurisdiction over the plan.

(c) *Investment authority.* A federal credit union investing to fund an employee benefit plan obligation is not subject to the investment limitations of the Act and part 703 or, as applicable, part 704, of this chapter and may purchase an investment that would otherwise be impermissible if the investment is directly related to the federal credit union's obligation or potential obligation under the employee benefit plan and the federal credit union holds the investment only for as long as it has an actual or potential obligation under the employee benefit plan.

(d) *Defined benefit plans.* Under paragraph (c) of this section, a federal credit union may invest to fund a defined benefit plan if the investment meets the conditions provided in that paragraph. If a federal credit union invests to fund a defined benefit plan that is not subject to the fiduciary responsibility provisions of part 4 of the Employee Retirement Income Security Act of 1974, it should diversify its investment portfolio to minimize the risk of large losses unless it is clearly prudent not to do so under the circumstances.

(e) *Liability insurance.* No federal credit union may occupy the position of a fiduciary, as defined in the Employee Retirement Income Security Act of 1974 and the rules and regulations issued by the Secretary of Labor, unless it has obtained appropriate liability insurance as described and permitted by Section 410(b) of the Employee Retirement Income Security Act of 1974.

(f) *Definitions.* For this section, defined benefit plan has the same meaning as in 29 U.S.C. 1002(35) and employee benefit plan has the same meaning as in 29 U.S.C. 1002(3).

§ 701.20 Suretyship and guaranty.

(a) *Scope.* This section authorizes a federal credit union to enter into a suretyship or guaranty agreement as an incidental powers activity. This section does not apply to the guaranty of public deposits or the assumption of liability for member accounts.

(b) *Definitions.* A *suretyship* binds a federal credit union with its principal to pay or perform an obligation to a third person. Under a *guaranty* agreement, a federal credit union agrees to satisfy the obligation of the principal only if the principal fails to pay or perform. The *principal* is the person primarily liable, for whose performance of his obligation the surety or guarantor has become bound.

(c) *Requirements.* The suretyship or guaranty agreement must be for the benefit of a principal that is a member and is subject to the following conditions:

(1) The federal credit union limits its obligations under the agreement to a fixed dollar amount and a specified duration;

(2) The federal credit union's performance under the agreement creates an authorized loan that complies with the applicable lending regulations, including the limitations on loans to one member or associated members or officials for purposes of §§ 701.21(c)(5), (d); 723.2 and 723.8; and

(3) The federal credit union obtains a segregated deposit from the member that is sufficient in amount to cover the federal credit union's total potential liability.

(d) *Collateral.* A segregated deposit under this section includes collateral:

(1) In which the federal credit union has perfected its security interest (for example, if the collateral is a printed security, the federal

credit union must have obtained physical control of the security, and, if the collateral is a book entry security, the federal credit union must have properly recorded its security interest); and

(2) That has a market value, at the close of each business day, equal to 100 percent of the federal credit union's total potential liability and is composed of:

(i) Cash;

(ii) Obligations of the United States or its agencies;

(iii) Obligations fully guaranteed by the United States or its agencies as to principal and interest; or

(iv) Notes, drafts, or bills of exchange or banker's acceptances that are eligible for rediscount or purchase by a Federal Reserve Bank; or

(3) That has a market value equal to 110 percent of the federal credit union's total potential liability and is composed of:

(i) Real estate, the value of which is established by a signed appraisal or evaluation in accordance with part 722 of this chapter. In determining the value of the collateral, the federal credit union must factor in the value of any existing senior mortgages, liens or other encumbrances on the property except those held by the principal to the suretyship or guaranty agreement; or

(ii) Marketable securities that the federal credit union is authorized to invest in. The federal credit union must ensure that the value of the security is 110 percent of the obligation at all times during the term of the agreement.

§ 701.21 Loans to Members and Lines of Credit to Members.

(a) *Statement of Scope and Purpose.* Section 701.21 complements the provisions of Section 107(5) of the Federal Credit Union Act (12 U.S.C. § 1757(5)) authorizing Federal credit unions to make loans to members and issue lines of credit (including credit cards) to members. Section 107(5) of the Act contains limitations on matters such as loan maturity, rate of interest, security, and prepayment penalties. Section 701.21 interprets and implements those provisions. In addition, Section 701.21 states the NCUA Board's intent concerning preemption of state laws, and expands the authority of Federal credit unions to enforce due-on-sale clauses in real property loans. Also, while § 701.21 generally applies to Federal credit unions only, its provisions may be used by state-chartered credit unions with respect to alternative mortgage transactions in accordance with 12 U.S.C. 3801 *et seq.,* and certain provisions apply to loans made by federally insured state-chartered credit unions as specified in § 741.203 of this chapter. Part 722 sets forth requirements for appraisals for certain real estate-secured loans made under Section 701.21 and any other applicable lending authority. Finally, it is noted that Section 701.21 does not apply to loans by Federal credit unions to other credit unions (although certain statutory limitations in Section 107 of the Act apply), nor to loans to credit union organizations (which are governed by Section 107(5)(D) of the Act and Part 712.

(b) *Relation to Other Laws:*

(1) *Preemption of state laws.* Section 701.21 is promulgated pursuant to the NCUA Board's exclusive authority as set forth in Section 107(5) of the Federal Credit Union Act (12 U.S.C. § 1757(5)) to regulate the rates, terms of repayment and other conditions of Federal credit union loans and lines of credit (including credit cards) to members. This exercise of the Board's authority preempts any state law purporting to limit or affect:

(i) (A) rates of interest and amounts of finance charges, including:

(1) the frequency or the increments by which a variable interest rate may be changed;

(2) the index to which a variable interest rate may be tied;

(3) the manner or timing of notifying the borrower of a change in interest rate;

(4) the authority to increase the interest rate on an existing balance;

(B) late charges; and

(C) closing costs, application, origination, or other fees;

(ii) terms of repayment, including:

(A) the maturity of loans and lines of credit;

(B) the amount, uniformity, and frequency of payments, including the accrual of unpaid interest if payments are insufficient to pay all interest due;

(C) balloon payments; and

(D) prepayment limits;

(iii) conditions related to:

(A) the amount of the loan or line of credit;

(B) the purpose of the loan or line of credit;

(C) the type or amount of security and the relation of the value of the security to the amount of the loan or line of credit;

(D) eligible borrowers; and

(E) the imposition and enforcement of liens on the shares of borrowers and accommodation parties.

(2) *Matters not preempted.* Except as provided by paragraph (b)(1) of this section, it is not the Board's intent to preempt state laws that do not affect rates, terms of repayment and other conditions described above concerning loans and lines of credit, for example:

(i) insurance laws;

(ii) laws related to transfer of and security interests in real and personal property (see, however, paragraph (g)(6) of this section concerning the use and exercise of due-on-sale clauses);

(iii) conditions related to:

(A) collection costs and attorneys' fees;

(B) requirements that consumer lending documents be in "plain language"; and

(C) the circumstances in which a borrower may be declared in default and may cure default.

(3) *Other Federal law.* Except as provided by paragraph (b)(1) of this section, it is not the Board's intent to preempt state laws affecting aspects of credit transactions that are primarily regulated by Federal law other than the Federal Credit Union Act, for example, state laws concerning credit cost disclosure requirements, credit discrimination, credit reporting practices, unfair credit practices, and debt collection practices. Applicability of state law in these instances should be determined pursuant to the preemption standards of the relevant Federal law and regulations.

(4) *Examination and Enforcement.* Except as otherwise agreed by the NCUA Board, the Board retains exclusive examination and administrative enforcement jurisdiction over Federal credit unions. Violations of Federal or applicable state laws related to the lending activities of a Federal credit union should be referred to the appropriate NCUA regional office.

(5) *Definition of State Law.* For purposes of paragraph (b) of this section, "state law" means the constitution, laws, regulations and judicial decisions of any state, the District of Columbia, the several territories and possessions of the United States, and the Commonwealth of Puerto Rico.

(c) *General Rules*—

(1) *Scope.* The following general rules apply to all loans to members and, where indicated, all lines of credit (including credit cards) to members, except as otherwise provided in the remaining provisions of Section 701.21.

(2) *Written policies.* The board of directors of each Federal credit union shall establish written policies for loans and lines of credit consistent with the relevant provisions of the Act, NCUA's regulations, and other applicable laws and regulations.

(3) *Credit applications and overdrafts.* Consistent with policies established by the board of directors, the credit committee or loan officer shall ensure that a credit application is kept on file for each borrower supporting the decision to make a loan or establish a line of credit. A credit union may advance money to a member to cover an account deficit without having a credit application from the borrower on file if the credit union has a written overdraft policy. The policy must: set a cap on the total dollar amount of all overdrafts the credit union will honor consistent with the credit union's ability to absorb losses; establish a time limit not to exceed forty-five calendar days for a member either to deposit funds or obtain an approved loan from the credit union to cover each overdraft; limit the dollar amount of overdrafts the credit union will honor per member; and establish the fee and interest rate, if any, the credit union will charge members for honoring overdrafts.

(4) *Maturity.* The maturity of a loan to a member may not exceed 12 years. Lines of credit are not subject to a statutory or regulatory maturity limit. Amortization of line of credit balances and the type and amount of security on any line of credit shall be as determined by contract between the Federal credit union and the member/borrower.

(5) *Ten percent limit.* No loan or line of credit advance may be made to any member if such loan or advance would cause that member to be indebted to the Federal credit union upon loans and advances made to the member in an aggregate amount exceeding 10% of the credit union's total unimpaired capital and surplus. In the case of member business loans as defined in § 723.1 of this chapter, additional limitations apply as set forth in §§ 723.8 and 723.9 of this chapter.

(6) *Early payment.* A member may repay a loan, or outstanding balance on a line of credit, prior to maturity in whole or in part on any business day without penalty.

(7) *Loan interest rates—*

(i) *General.* Except when a higher maximum rate is provided for in paragraph (c)(7)(ii) of this section, a Federal credit union may extend credit to its members at rates not to exceed 15 percent per year on the unpaid balance inclusive of all finance charges. Variable rates are permitted on the condition that the effective rate over the term of the loan (or line of credit) does not exceed the maximum permissible rate.

(ii) *Temporary rates.—(A) 21 percent maximum rate.* Effective from December 3, 1980 through May 14, 1987, a Federal credit union may extend credit to its members at rates not to exceed 21 percent per year on the unpaid balance inclusive of all finance charges. Loans and line of credit balances existing on or before May 14, 1987, may continue to bear rates of interest of up to 21 percent per year after May 14, 1987.

(B) *18 percent maximum rate.* Effective May 15, 1987, a Federal credit union may extend credit to its members at rates not to exceed 18 percent per year on the unpaid balance inclusive of all finance charges.

(C) *Expiration.* After September 8, 2006, or as otherwise ordered by the NCUA Board, the maximum rate on federal credit union extensions of credit to members shall revert to 15 percent per year. Higher rates may, however, be charged, in accordance with paragraph (c)(7)(ii)(A) and (B) of this section, on loans and line of credit balance existing on or before September 8, 2006.

(8)(i) Except as otherwise provided herein, no official or employee of a Federal credit union, or immediate family member of an official or employee of a Federal credit union, may receive, directly or indirectly, any commission, fee, or other compensation in connection with any loan made by the credit union.

(ii) For the purposes of this section:

Compensation includes non monetary items, except those of nominal value.

Immediate family member means a spouse or other family member living in the same household.

Loan includes line of credit.

Official means any member of the board of directors or a volunteer committee.

Person means an individual or an organization.

Senior management employee means the credit union's chief executive officer (typically, this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (e.g., Assistant President, Vice President, or Assistant Treasurer/Manager), and the chief financial officer (Comptroller).

Volunteer official means an official of a credit union who does not receive compensation from the credit union solely for his or her service as an official.

(iii) This section does not prohibit:

(A) Payment, by a Federal credit union, of salary to employees;

(B) Payment, by a Federal credit union, of an incentive or bonus to an employee based on the credit union's overall financial performance;

(C) Payment, by a Federal credit union, of an incentive or bonus to an employee, other than a senior management employee, in connection with a loan or loans made by the credit union, provided that the board of directors of the credit union establishes written policies and internal controls in connection with such incentive or bonus and monitors compliance with such policies and controls at least annually.

(D) Receipt of compensation from a person outside a Federal credit union by a volunteer official or non senior management employee of the credit union, or an immediate family member of a volunteer official or employee of the credit union, for a service or activity performed outside the credit union, provided that no referral has been made by the credit union or the official, employee, or family member.

(d) *Loans and Lines of Credit to Officials—*

(1) *Purpose.* Sections 107(5)(A) (iv) and (v) of the Act require the approval of the board of directors of the Federal credit union in any case where the aggregate of loans to an official and loans on which that official serves as endorser or guarantor exceeds $20,000 plus pledged shares. This paragraph implements the requirement by establishing procedures for determining whether board of directors' approval is required. The section also prohibits preferential treatment of officials.

(2) *Official.* An "official" is any member of the board of directors, credit committee or supervisory committee.

(3) *Initial approval.* All applications for loan or lines of credit on which an official will be

either a direct obligor or an endorser, cosigner or guarantor shall be initially acted upon by either the board of directors, the credit committee or loan officer, as specified in the Federal credit union's bylaws.

(4) *Board of directors' review.* The board of directors shall, in any case, review and approve or deny an application on which an official is a direct obligor, or endorser, cosigner or guarantor if the following computation produces a total in excess of $20,000:

(i) Add:

(A) The amount of the current application.

(B) The outstanding balances of loans including the used portion of an approved line of credit, extended to or endorsed, cosigned or guaranteed by the official.

(C) The total unused portion of approved lines of credit extended to or endorsed, cosigned or guaranteed by the official.

(ii) From the above total subtract:

(A) the amount of shares pledged by the official on loans or lines of credit extended to or endorsed, cosigned or guaranteed by the official.

(B) The amount of shares to be pledged by the official on the loan or line of credit applied for.

(5) *Nonpreferential treatment.* The rates, terms and conditions on any loan or line of credit either made to, or endorsed or guaranteed by

(i) an official

(ii) an immediate family member of an official, or

(iii) any individual having a common ownership, investment or other pecuniary interest in a business enterprise with an official or with an immediate family member of an official shall not be more favorable than the rates, terms and conditions for comparable loans or lines of credit to other credit union members. "Immediate family members" means a spouse or other family member living in the same household.

(e) *Insured, Guaranteed and Advance Commitment Loans.* A loan secured, in full or in part, by the insurance or guarantee of, or with an advance commitment to purchase the loan, in full or in part, by the Federal Government, a State government or any agency of either, may be made for the maturity and under the terms and conditions, including rate of interest, specified in the law, regulations or program under which the insurance, guarantee or commitment is provided.

(f) *20-Year Loans.* (1) Notwithstanding the general 12-year maturity limit on loans to members, a federal credit union may make loans with maturities of up to 20 years in the case of:

(i) a loan to finance the purchase of a mobile home if the mobile home will be used as the member-borrower's residence and the loan is secured by a first lien on the mobile home, and the mobile home meets the requirements for the home mortgage interest deduction under the Internal Revenue Code,

(ii) a second mortgage loan (or a nonpurchase money first mortgage loan in the case of a residence on which there is no existing first mortgage) if the loan is secured by a residential dwelling which is the residence of the member-borrower, and

(iii) a loan to finance the repair, alteration, or improvement of a residential dwelling which is the residence of the member-borrower.

(2) For purposes of this paragraph (f), mobile home may include a recreational vehicle, house trailer or boat.

(g) *Long-Term Mortgage Loans:*

(1) *Authority.* A federal credit union may make residential real estate loans to members, including loans secured by manufactured homes permanently affixed to the land, with maturities of up to 40 years, or such longer period as may be permitted by the NCUA Board on a case-by-case basis, subject to the conditions of this paragraph (g).

(2) *Statutory limits.* The loan shall be made on a one- to four-family dwelling that is or will be the principal residence of the member-borrower and the loan shall be secured by a perfected first lien in favor of the credit union on such dwelling (or a perfected first security interest in the case of either a residential cooperative or a leasehold or ground rent estate).

(3) *Loan application.* The loan application shall be a completed standard Federal Housing Administration, Veterans Administration, Federal Home Loan Mortgage Corporation, Federal National Mortgage Association or Federal Home Loan Mortgage Corporation/Federal National Mortgage Association application form. In lieu of use of a standard application the Federal credit union may have a current attorney's opinion on file stating that the forms in use meet the requirements of applicable Federal, state and local laws.

(4) *Security instrument and note.* The security instrument and note shall be executed on

the most current version of the FHA, VA, FHLMC, FNMA, or FHLMC/FNMA Uniform Instruments for the jurisdiction in which the property is located. No prepayment penalty shall be allowed, although a Federal credit union may require that any partial prepayments be made on the date monthly installments are due and be in the amount of that part of one or more monthly installments that would be applicable to principal. In lieu of use of a standard security instrument and note, the Federal credit union may have a current attorney's opinion on file stating that the security instrument and note in use meet the requirements of applicable Federal, state and local laws.

(5) *First lien, territorial limits.* The loan shall be secured by a perfected first lien or first security interest in favor of the credit union supported by a properly executed and recorded security instrument. No loan shall be secured by a residence located outside the United States of America, its territories and possessions, or the Commonwealth of Puerto Rico.

(6) *Due-on-sale clauses:*

(i) Except as otherwise provided herein, the exercise of a due-on-sale clause by a Federal credit union is governed exclusively by Section 341 of Public Law 97–320 and by any regulations issued by the Federal Home Loan Bank Board implementing Section 341.

(ii) In the case of a contract involving a long-term (greater than twelve years), fixed rate first mortgage loan which was made or assumed, including a transfer of the liened property subject to the loan, during the period beginning on the date a state adopted a constitutional provision or statute prohibiting the exercise of due-on-sale clauses, or the date on which the highest court of such state has rendered a decision (or if the highest court has not so decided, the date on which the next highest court has rendered a decision resulting in a final judgment if such decision applies statewide) prohibiting such exercise, and ending on October 15, 1982, a Federal credit union may exercise a due-on-sale clause in the case of a transfer which occurs on or after November 18, 1982, unless exercise of the due-on-sale clause would be based on any of the following:

(A) the creation of a lien or other encumbrance subordinate to the lender's security instrument which does not relate to a transfer of rights of occupancy in the property;

(B) the creation of a purchase money security interest for household appliances;

(C) a transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety;

(D) the granting of a leasehold interest of 3 years or less not containing an option to purchase;

(E) a transfer to a relative resulting from the death of a borrower;

(F) a transfer where the spouse or children of the borrower become an owner of the property;

(G) a transfer resulting from a decree of a dissolution of marriage, a legal separation agreement, or from an incidental property settlement agreement, by which the spouse of the borrower becomes an owner of the property;

(H) a transfer into an inter vivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property; or

(I) any other transfer or disposition described in regulations promulgated by the Federal Home Loan Bank Board.

(7) *Assumption of real estate loans by nonmembers.* A federal credit union may permit a nonmember to assume a member's mortgage loan in conjunction with the nonmember's purchase of the member's principal residence, provided that the nonmember assumes only the remaining unpaid balance of the loan, the terms of the loan remain unchanged, and there is no extension of the original maturity date specified in the loan agreement with the member. An assumption is impermissible if the original loan was made with the intent of having a nonmember assume the loan.

(h) *Removed and replaced by part 723.*

(i) *Put Option Purchases in Managing Increased Interest-Rate Risk for Real Estate Loans Produced for Sale on the Secondary Market.*

(1) *Definitions.* For purposes of this § 701.21(i):

(i) "Financial options contact" means an agreement to make or take delivery of a standardized financial instrument upon demand by the holder of the contract at any time prior to the expiration date specified in the agreement, under terms and conditions established either by (A) a contract market designated for trading such contracts by the Commodity Futures Trading Commission, or (B) by a Federal credit union and a primary dealer in

Government securities that are counterparties in an over-the-counter transaction.

(ii) "FHLMC security" means obligations or other securities which are or ever have been sold by the Federal Home Loan Mortgage Corporation pursuant to Sections 305 or 306 of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. §§ 1454 and 1455).

(iii) "FNMA security" means an obligation, participation, or any instrument of or issued by, or fully guaranteed as to principal and interest by, the Federal National Mortgage Association.

(iv) "GNMA security" means an obligation, participation, or any instrument of or issued by, or fully guaranteed as to principal and interest by, the Government National Mortgage Association.

(v) "Long position" means the holding of a financial options contract with the option to make or take delivery of a financial instrument.

(vi) "Primary dealer in Government securities" means: (A) a member of the Association of Primary Dealers in United States Government Securities; or (B) any parent, subsidiary, or affiliated entity of such primary dealer where the member guarantees (to the satisfaction of the FCU's board of directors) over-the-counter sales of financial options contracts by the parent, subsidiary, or affiliated entity to a Federal credit union.

(vii) "Put" means a financial options contract which entitles the holder to sell, entirely at the holder's option, a specified quantity of a security at a specified price at any time until the stated expiration date of the contract.

(2) *Permitted Options Transactions.* A Federal credit union may, to manage risk of loss through a decrease in value of its commitments to originate real estate loans at specified interest rates, enter into long put positions on GNMA, FNMA, and FHLMC securities:

(i) if the real estate loans are to be sold on the secondary market within ninety (90) days of closing;

(ii) if the positions are entered into: (A) through a contract market designated by the Commodity Futures Trading Commission for trading such contracts, or (B) with a primary dealer in Government securities;

(iii) if the positions are entered into pursuant to written policies and procedures which are approved by the Federal credit union's board of directors, and include, at a minimum: (A) the Federal credit union's strategy in using financial options contracts and its analysis of how the strategy will reduce sensitivity to changes in price or interest rates in its commitments to originate real estate loans at specified interest rates; (B) a list of brokers or other intermediaries through which positions may be entered into; (C) quantitative limits (e.g., position and stop loss limits) on the use of financial options contracts; (D) identification of the persons involved in financial options contract transactions, including a description of these persons' qualifications, duties, and limits of authority, and description of the procedures for segregating these persons' duties, (E) a requirement for written reports for review by the Federal credit union's board of directors at its monthly meetings, or by a committee appointed by the board on a monthly basis, of: (1) the type, amount, expiration date, correlation, cost of, and current or projected income or loss from each position closed since the last board review, each position currently open and current gains or losses from such positions, and each position planned to be entered into prior to the next board review; (2) compliance with limits established on the policies and procedures; and (3) the extent to which the positions described contributed to reduction of sensitivity to changes in prices or interest rates in the Federal credit union's commitments to originate real estate loans at a specified interest rate; and

(iv) if the Federal credit union has received written permission from the appropriate NCUA Regional Director to engage in financial options contracts transactions in accordance with this § 701.21(i) and its policies and procedures as written.

(3) *Recordkeeping and Reporting.*

(i) The reports described in § 701.21 (i)(2)(iii)(E) for each month must be submitted to the appropriate NCUA Regional Office by the end of the following month. This monthly reporting requirement may be waived by the appropriate NCUA Regional Director on a case-by-case basis for those Federal credit unions with a proven record of responsible use of permitted financial options contracts.

(ii) The records described in § 701.21 (i)(2)(iii)(E) must be retained for two years from the date the financial options contracts are closed.

(4) *Accounting.* A federal credit union must account for financial options contracts transactions in accordance with generally accepted accounting principles.

§ 701.22 Loan Participation.

(a) For purposes of this section:

(1) "Participation loan" means a loan where one or more eligible organizations participates pursuant to a written agreement with the originating lender.

(2) "Eligible organizations" means a credit union, credit union organization, or financial organization.

(3) "Credit union" means any Federal or state chartered credit union.

(4) *Credit union organization* means any credit union service organization meeting the requirements of part 712 of this chapter. This term does not include trade associations or membership organizations principally composed of credit unions.

(5) *Financial organization* means any federally chartered or federally insured financial institution; and any state or federal government agency and their subdivisions.

(6) "Originating lender" means the participant with which the member contracts.

(b) Subject to the provisions of this section any Federal credit union may participate in making loans with eligible organizations within the limitations of the board of directors' written participation loan policies, PROVIDED:

(1) no Federal credit union shall obtain an interest in a participation loan if the sum of that interest and any (other) indebtedness owing to the Federal credit union by the borrower exceeds 10 per centum of the Federal credit union's unimpaired capital and surplus;

(2) a written master participation agreement shall be properly executed, acted upon by the Federal credit union's board of directors, or if the board has so delegated in its policy, the investment committee or senior management official(s) and retained in the Federal credit union's office. The master agreement shall include provisions for identifying, either through a document which is incorporated by reference into the master agreement, or directly in the master agreement, the participation loan or loans prior to their sale; and

(3) a Federal credit union may sell to or purchase from any participant the servicing of any loan in which it owns a participation interest.

(c) An originating lender which is a Federal credit union shall:

(1) originate loans only to its members;

(2) retain an interest of at least 10 per centum of the face amount of each loan;

(3) retain the original or copies of the loan documents; and

(4) Require the credit committee or loan officer to use the same underwriting standards for participation loans used for loans that are not being sold in a participation agreement unless there is a participation agreement in place prior to the disbursement of the loan. Where a participation agreement is in place prior to disbursement, either the credit union's loan policies or the participation agreement shall address any variance from non-participation loan underwriting standards.

(d) A participant Federal credit union that is not an originating lender shall:

(1) participate only in loans it is empowered to grant, having a participation policy in place which sets forth the loan underwriting standards prior to entering into a participation agreement;

(2) participate in participation loans only if made to its own members or members of another participating credit union;

(3) retain the original or a copy of the written participation loan agreement and a schedule of the loans covered by the agreement; and

(4) obtain the approval of the board of directors or investment committee of the disbursement of proceeds to the originating lender.

§ 701.23 Purchase, Sale, and Pledge of Eligible Obligations.

(a) For purposes of this Section:

(1) "Eligible obligation" means a loan or group of loans;

(2) "Student loan" means a loan granted to finance the borrower's attendance at an institution of higher education or at a vocational school, which is secured by and on which payment of the outstanding principal and interest has been deferred in accordance with the insurance or guarantee of the Federal Government, of a State government, or any agency of either.

(b) Purchase.

(1) A Federal credit union may purchase, in whole or in part, within the limitations of the board of directors' written purchase policies:

(i) Eligible obligations of its members, from any source, if either (A) they are loans it is empowered to grant or (B) they are refinanced with the consent of the borrowers,

within 60 days after they are purchased, so that they are loans it is empowered to grant;

(ii) Eligible obligations of a liquidating credit union's individual members, from the liquidating credit union;

(iii) Student loans, from any source, if the purchaser is granting student loans on an ongoing basis and if the purchase will facilitate the purchasing credit union's packaging of a pool of such loans to be sold or pledged on the secondary market; and

(iv) Real estate-secured loans, from any source, if the purchaser is granting real estate secured loans pursuant to Section 701.21 on an ongoing basis and if the purchase will facilitate the purchasing credit union's packaging of a pool of such loans to be sold or pledged on the secondary mortgage market. A pool must include a substantial portion of the credit union's members' loans and must be sold promptly.

(2) A Federal credit union may make purchases in accordance with this paragraph (b), provided:

(i) the board of directors or investment committee approves the purchase;

(ii) a written agreement and a schedule of the eligible obligations covered by the agreement are retained in the purchaser's office; and for purchases under paragraph (b)(1)(ii) of this section, any advance written approval required by § 741.8 of this chapter is obtained before consummation of such purchase.

(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.

(c) Sale.

(1) A Federal credit union may sell, in whole or in part, to any source, eligible obligations of its members, eligible obligations purchased in accordance with subsection (b)(1)(ii), student loans purchased in accordance with subsection (b)(1)(iii), and real estate loans purchased in accordance with subsection (b)(1)(iv), within the limitations of the board of directors' written sale policies, provided:

(i) The board of directors or investment committee approves the sale; and

(ii) A written agreement and a schedule of the eligible obligations covered by the agreement are retained in the seller's office.

(d) Pledge.

(1) A Federal credit union may pledge, in whole or in part, to any source, eligible obligations of its members, eligible obligations purchased in accordance with subsection (b)(1)(ii), student loans purchased in accordance with subsection (b)(1)(iii), and real estate loans purchased in accordance with subsection (b)(1)(iv), within the limitations of the board of directors' written pledge policies, provided:

(i) The board of directors or investment committee approves the pledge;

(ii) Copies of the original loan documents are retained; and

(iii) A written agreement covering the pledging arrangement is retained in the office of the credit union that pledges the eligible obligations.

(2) The pledge agreement shall identify the eligible obligations covered by the agreement.

(e) Servicing.

A Federal credit union may agree to service any eligible obligation it purchases or sells in whole or in part.

(f) 10 Percent Limitation.

The total indebtedness owing to any Federal credit union by any person, inclusive of retained and reacquired interests, shall not exceed 10 percent of its unimpaired capital and surplus.

§ 701.24 Refund of Interest.

(a) The board of directors of a Federal credit union may authorize an interest refund to members who paid interest to the credit union during any dividend period and who are members of record at the close of business on the last day of such dividend period. Interest refunds may be made for a dividend period only if dividends on

share accounts have been declared and paid for that period.

(b) The amount of interest refund to each member shall be determined as a percentage of the interest paid by the member. Such percentage may vary according to the type of extension of credit and the interest rate charged.

(c) The board of directors may exclude from an interest refund: (1) a particular type of extension of credit; (2) any extension of credit made at a particular interest rate; and (3) any extension of credit that is presently delinquent or has been delinquent within the period for which the refund is being made.

§ 701.25 Charitable contributions and donations.

(a) A federal credit union may make charitable contributions and/or donate funds to recipients not organized for profit that are located in or conduct activities in a community in which the federal credit union has a place of business or to organizations that are tax exempt organizations under Section 501(c)(3) of the Internal Revenue Code and operate primarily to promote and develop credit unions.

(b) The board of directors must approve charitable contributions and/or donations, and the approval must be based on a determination by the board of directors that the contributions and/or donations are in the best interests of the federal credit union and are reasonable given the size and financial condition of the federal credit union. The board of directors, if it chooses, may establish a budget for charitable contributions and/or donations and authorize appropriate officials of the federal credit union to select recipients and disburse budgeted funds among those recipients.

§ 701.26 Credit Union Service Contracts.

A Federal credit union may act as a representative of and enter into a contractual agreement with one or more credit unions or other organizations for the purpose of sharing, utilizing, renting, leasing, purchasing, selling, and/or joint ownership of fixed assets or engaging in activities and/or services which relate to the daily operations of credit unions. Agreements must be in writing, and shall advise all parties subject to the agreement that the goods and services provided shall be subject to examination by the NCUA Board to the extent permitted by law.

§ 701.27 [Removed April 1998, replaced by new part 712]

§§ 701.28–701.29 [Reserved]

§ 701.30 [Reserved]

§ 701.31 Nondiscrimination Requirements.

(a) *Definitions:* As used in this part, the term:

(1) "application" carries the meaning of that term as defined in 12 C.F.R. 202.2(f) (Regulation B), which is as follows: "An oral or written request for an extension of credit that is made in accordance with procedures established by a creditor for the type of credit requested";

(2) "dwelling" carries the meaning of that term as defined in 42 U.S.C. 3602(b) (Fair Housing Act), which is as follows: "Any building, structure, or portion thereof which is occupied as, or designed or intended for occupancy as, a residence by one or more families, and any vacant land which is offered for sale or lease for the construction or location thereon of any building, structure, or portion thereof"; and

(3) "real estate-related loan" means any loan for which application is made to finance or refinance the purchase, construction, improvement, repair, or maintenance of a dwelling.

(b) *Nondiscrimination in Lending:*

(1) A Federal credit union may not deny a real estate-related loan, nor may it discriminate in setting or exercising its rights pursuant to the terms or conditions of such a loan, nor may it discourage an application for such a loan, on the basis of the race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18) of:

(i) any applicant or joint applicant;

(ii) any person associated, in connection with a real estate-related loan application, with an applicant or joint applicant;

(iii) the present or prospective owners, lessees, tenants, or occupants of the dwelling for which a real estate-related loan is requested;

(iv) the present or prospective owners, lessees, tenants, or occupants of other dwellings in the vicinity of the dwelling for which a real estate-related loan is requested.

(2) With regard to a real estate-related loan, a Federal credit union may not consider a lending criterion or exercise a lending policy which has the effect of discriminating on the basis of race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18). Guidelines concerning possible exceptions to this provision appear in paragraph (e)(1) of this section.

(3) Consideration of any of the following factors in connection with a real estate-related loan is not necessary to a Federal credit union's business, generally has a discriminatory effect, and is therefore prohibited:

(i) the age or location of the dwelling;

(ii) zip code of the applicant's current residence;

(iii) previous home ownership;

(iv) the age or location of dwellings in the neighborhood of the dwelling;

(v) the income level of residents in the neighborhood of the dwelling;

Guidelines concerning possible exceptions to this provision appear in paragraph (e)(2) of this section.

(c) *Nondiscrimination in Appraisals:*

(1) A Federal credit union may not rely upon an appraisal of a dwelling if it knows or should know that the appraisal is based upon consideration of the race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18) of:

(i) any applicant or joint applicant;

(ii) any person associated, in connection with a real estate-related loan application, with an applicant or joint applicant;

(iii) the present or prospective owners, lessees, tenants, or occupants of the dwelling for which a real estate-related loan is requested;

(iv) the present or prospective owners, lessees, tenants, or occupants of other dwellings in the vicinity of the dwelling for which a real estate-related loan is requested.

(2) With respect to a real estate-related loan, a Federal credit union may not rely upon an appraisal of a dwelling if it knows or should know that the appraisal is based upon consideration of a criterion which has the effect of discriminating on the basis of race, color, national origin, religion, sex, handicap, or familial status (having children under the age of 18). Guidelines concerning possible exceptions to this provision appear in paragraph (e)(1) of this section.

(3) A Federal credit union may not rely upon an appraisal that it knows or should know is based upon consideration of any of the following criteria, for such criteria generally have a discriminatory effect, and are not necessary to a Federal credit union's business:

(i) the age or location of the dwelling;

(ii) the age or location of dwellings in the neighborhood of the dwelling;

(iii) the income level of the residents in the neighborhood of the dwelling.

(4) Notwithstanding paragraph (c)(3) of this section, it is recognized that there may be factors concerning location of the dwelling which can be properly considered in an appraisal. If any such factor(s) is relied upon, it must be specifically documented in the appraisal, accompanied by a brief statement demonstrating the necessity of using such factor(s). Guidelines concerning the consideration of location factors appear in paragraph (e)(3) of this section.

(5) Each Federal credit union shall make available, to any requesting member/applicant, a copy of the appraisal used in connection with that member's real estate-related loan application. The appraisal shall be available for a period of 25 months after the applicant has received notice from the Federal credit union of the action taken by the Federal credit union on the real estate-related loan application.

(d) *Nondiscrimination in advertising.* No federal credit union may engage in any form of advertising of real estate-related loans that indicates the credit union discriminates on the basis of race, color, religion, national origin, sex, handicap, or familial status in violation of the Fair Housing Act. Advertisements must not contain any words, symbols, models or other forms of communication that suggest a discriminatory preference or policy of exclusion in violation of the Fair Housing Act or the Equal Credit Opportunity Act.

(1) *Advertising notice of nondiscrimination compliance.* Any federal credit union that advertises real estate-related loans must prominently indicate in such advertisement, in a manner appropriate to the advertising medium and format used, that the credit union makes such loans without regard to race, color, religion, national origin, sex, handicap, or familial status.

(i) With respect to written and visual advertisements, a credit union may satisfy the notice requirement by including in the advertisement a copy of the logotype, with the legend "Equal Housing Lender," from the poster described in paragraph (d)(3) of this section or a copy of the logotype,

with the legend "Equal Housing Opportunity," from the poster described in § 110.25(a) of the United States Department of Housing and Urban Development's (HUD) regulations (24 CFR 110.25(a)).

(ii) With respect to oral advertisements, a credit union may satisfy the notice requirement by a spoken statement that the credit union is an "Equal Housing Lender" or an "Equal Opportunity Lender."

(iii) When an oral advertisement is used in conjunction with a written or visual advertisement, the use of either of the methods specified in paragraphs (d)(1)(i) or (ii) of this section will satisfy the notice requirement.

(iv) A credit union may use any other method reasonably calculated to satisfy the notice requirement.

(2) *Lobby notice of nondiscrimination.* Every federal credit union that engages in real estate-related lending must display a notice of nondiscrimination. The notice must be placed in the public lobby of the credit union and in the public area of each office where such loans are made and must be clearly visible to the general public. The notice must incorporate either a facsimile of the logotype and language appearing in paragraph (d)(3) of this section or the logotype and language appearing at 24 CFR 110.25(a). Posters containing the logotype and language appearing in paragraph (d)(3) of this section may be obtained from the regional offices of the National Credit Union Administration.

(3) *Logotype and notice of nondiscrimination compliance.* The logotype and text of the notice required in paragraph (d)(2) of this section shall be as follows:

EQUAL HOUSING
LENDER

We Do Business in Accordance With the Federal Fair Lending Laws

UNDER THE FEDERAL FAIR HOUSING ACT, IT IS ILLEGAL, ON THE BASIS OF RACE, COLOR, NATIONAL ORIGIN, RELIGION, SEX, HANDICAP, OR FAMILIAL STATUS (HAVING CHILDREN UNDER THE AGE OF 18), TO:

- Deny a loan for the purpose of purchasing, constructing, improving, repairing or maintaining a dwelling, or deny any loan secured by a dwelling; or
- Discriminate in fixing the amount, interest rate, duration, application procedures or other terms or conditions of such a loan, or in appraising property.

IF YOU BELIEVE YOU HAVE BEEN DISCRIMINATED AGAINST, YOU SHOULD SEND A COMPLAINT TO:

Assistant Secretary for Fair Housing and Equal Opportunity
Department of Housing & Urban Development
Washington, D.C. 20410
For processing under the Federal Fair Housing Act
and to:
National Credit Union Administration
Office of Examination and Insurance
1775 Duke Street
Alexandria, VA 22314–3428
For processing under NCUA Regulations

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UNDER THE EQUAL CREDIT OPPORTUNITY ACT, IT IS ILLEGAL TO DISCRIMINATE IN ANY CREDIT TRANSACTION:

- On the basis of race, color, national origin, religion, sex, marital status, or age
- Because income is from public assistance, or
- Because a right was exercised under the Consumer Credit Protection Act.

IF YOU BELIEVE YOU HAVE BEEN DISCRIMINATED AGAINST, YOU SHOULD SEND A COMPLAINT TO:

National Credit Union Administration
Office of Examination and Insurance
1775 Duke Street
Alexandria, VA 22314–3428

(e) *Guidelines:*

(1) Compliance with the Fair Housing Act is achieved when each loan applicant's creditworthiness is evaluated on an individual basis, without presuming that the applicant has certain characteristics of a group. If certain lending policies or procedures do presume group characteristics, they may violate the Fair Housing Act, even though the characteristics are not based upon race, color, sex, national origin, religion, handicap, or familial status. Such a violation occurs when otherwise facially nondiscriminatory lending procedures (either general lending policies or specific criteria used in reviewing loan applications) have the effect of making real estate-related loans unavailable or less available on the basis of race, color, sex, national origin, religion, handicap, or familial status. Note, however, that a policy or criterion which has a discriminatory effect is not a violation of the Fair Housing Act if its use achieves a legitimate business necessity which cannot be achieved by using less discriminatory standards. It is also important to note that the Equal Credit Opportunity Act and Regulation B prohibit discrimination, either per se or in effect, on the basis of the applicant's age, marital status, receipt of public assistance, or the exer-

cise of any rights under the Consumer Credit Protection Act.

(2) Paragraph (b)(3) of this section prohibits consideration of certain factors because of their likely discriminatory effect and because they are not necessary to make sound real estate-related loans. For purposes of clarification, the prohibited use of location factors in this section is intended to prevent abandonment of areas in which a Federal credit union's members live or want to live. It is not intended to require loans in those areas that are geographically remote from the FCU's main or branch offices or that contravene the parameters of a Federal credit union's charter. Further. this prohibition does not preclude requiring a borrower to obtain flood insurance protection pursuant to the National Flood Insurance Act and Part 760 of NCUA's Rules and Regulations, nor does it preclude involvement with Federal or state housing insurance programs which provide for lower interest rates for the purchase of homes in certain urban or rural areas. Also, the legitimate use of location factors in an appraisal does not constitute a violation of the provision of paragraph (b)(3) of this section, which prohibits consideration of location of the dwelling. Finally, the prohibited use of prior home ownership does not preclude a Federal credit union from considering an applicant's payment history on a loan which was made to obtain a home. Such action entails consideration of the payment record on a previous loan in determining creditworthiness; it does not entail consideration of prior home ownership.

(3)(i) Paragraph (c)(3) of this section prohibits consideration of the age or location of a dwelling in a real estate-related loan appraisal. These restrictions are intended to prohibit the use of unfounded or unsubstantiated assumptions regarding the effect upon loan risk of the age of a dwelling or the physical or economic characteristics of an area. Appraisals should be based on the present market value of the property offered as security (including consideration of specific improvements to be made by the borrower) and the likelihood that the property will retain an adequate value over the term of the loan.

(ii) The term "age of the dwelling" does not encompass structural soundness. In addition, the age of the dwelling may be used by an appraiser as a basis for conducting further inspections of certain structural aspects of the dwelling. Paragraph (c)(3) of this section does, however, prohibit an unsubstantiated determination that a house over X years in age is not structurally sound.

(iii) With respect to location factors, paragraph (c)(4) of this section recognizes that there may be location factors which may be considered in an appraisal, and requires that the use of any such factors be specifically documented in the appraisal. These factors will most often be those location factors which may negatively affect the short range future value (up to 3–5 years) of a property. Factors which in some cases may cause the market value of a property to decline are recent zoning changes or a significant number of abandoned homes in the immediate vicinity of the property. However, not all zoning changes will cause a decline in property values, and proximity to abandoned buildings may not affect the market value of a property because the cause of abandonment is unrelated to high risk. Proper considerations include the condition and utility of the improvement and various physical factors such as street conditions, amenities such as parks and recreation areas, availability of public utilities and municipal services and exposure to flooding and land faults.

§ 701.32 Payment on shares by public units and nonmembers.

(a) *Authority.* A Federal credit union may, to the extent permitted under Section 107(6) of the Act and this section, receive payments on shares, (regular shares, share certificates, and share draft accounts) from public units and political subdivisions thereof (as those terms are defined in § 745.1) and nonmember credit unions, and to the extent permitted under the Act, this section and § 701.34, receive payments on shares (regular shares, share certificates, and share draft accounts) from other nonmembers.

(b) *Limitations.* (1) Unless a greater amount has been approved by the Regional Director, the maximum amount of all public unit and nonmember shares shall not, at any given time, exceed 20% of the total shares of the federal credit union or $1.5 million, whichever is greater.

(2) Before accepting any public unit or nonmember shares in excess of 20% of total shares, the board of directors must adopt a specific written plan concerning the intended use of these shares and forward a copy of the plan to the Regional Director. The plan must include:

(i) A statement of the credit union's needs, sources and intended uses of public unit and nonmember shares;

(ii) Provision for matching maturities of public unit and nonmember shares with corresponding assets, or justification for any mismatch; and

(iii) Provision for adequate income spread between public unit and nonmember shares and corresponding assets.

(3) A federal credit union seeking an exemption from the limits of paragraph (b)(1) of this section must submit to the Regional Director a written request including:

(i) The new maximum level of public unit and nonmember shares requested, either as a dollar amount or a percentage of total shares;

(ii) The current plan adopted by the credit union's board of directors concerning the use of new public unit and nonmember shares;

(iii) A copy of the credit union's latest financial statement; and

(iv) A copy of the credit union's loan and investment policies.

(4) Where the financial condition and management of the credit union are sound and the credit union's plan for the funds is reasonable, there will be a presumption in favor of granting the request. When granted, exemptions will normally be for a two-year period. The Regional Director will provide a written explanation for an exemption that is granted for a lesser time period.

(5) The Regional Director will provide a written determination on an exemption request within 30 calendar days after receipt of the request. The 30-day period will not begin to run until all necessary information has been submitted to the Regional Director. All denials may be appealed to the NCUA Board in a timely manner. Appeals should be submitted through the Regional Director.

(6) Upon expiration of an exemption, nonmember shares currently in the credit union in excess of the limits established pursuant to (b)(1) of this section will continue to be insured by the National Credit Union Insurance Fund within applicable limits. No new shares in excess of the limits established pursuant to (b)(1) of this section shall be accepted. Existing share certificates in excess of the limits established pursuant to (b)(1) of this section may remain in the credit union only until maturity.

(c) The limitations herein do not apply to accounts maintained in accordance with 701.37 (Treasury Tax and Loan Depositaries; Depositaries and Financial Agents of the Government) and matching funds required by 705.7(b) (Community Development Revolving Loan Program for Credit Unions). Once a loan granted pursuant to Part 705 is repaid, nonmember share deposits accepted to meet the matching requirement are subject to this section.

§ 701.33 Reimbursement, Insurance, and Indemnification of Officials and Employees.

(a) *Official.* An "official" is a person who is or was a member of the board of directors, credit committee or supervisory committee, or other volunteer committee established by the board of directors.

(b) *Compensation.*

(1) Only one board officer, if any, may be compensated as an officer of the board. The bylaws must specify the officer to be compensated, if any, as well as the specific duties of each of the board officers. No other official may receive compensation for performing the duties or responsibilities of the board or committee position to which the person has been elected or appointed.

(2) For purposes of this section, the term "compensation" specifically excludes:

(i) payment (by reimbursement to an official or direct credit union payment to a third party) for reasonable and proper costs incurred by an official in carrying out the responsibilities of the position to which that person has been elected or appointed, if the payment is determined by the board of directors to be necessary or appropriate in order to carry out the official business of the credit union, and is in accordance with written policies and procedures, including documentation requirements, established by the board of directors. Such payments may include the payment of travel costs for officials and one guest per official;

(ii) provision of reasonable health, accident and related types of personal insurance protection, supplied for officials at the expense of the credit union: *Provided,* that such insurance protection must exclude life insurance; must be limited to areas of risk, including accidental death and dismemberment, to which the official is exposed by reason of carrying out the duties or responsibilities of the official's credit union position; must cease immediately upon the insured person's leaving office, without pro-

viding residual benefits other than from pending claims, if any; and

(iii) indemnification and related insurance consistent with paragraph (c) of this Section.

(c) *Indemnification.*

(1) A Federal credit union may indemnify its officials and current and former employees for expenses reasonably incurred in connection with judicial or administrative proceedings to which they are or may become parties by reason of the performance of their official duties.

(2) Indemnification shall be consistent either with the standards applicable to credit unions generally in the state in which the principal or home office of the credit union is located, or with the relevant provisions of the Model Business Corporation Act. A Federal credit union that elects to provide indemnification shall specify whether it will follow the relevant state law or the Model Business Corporation Act. Indemnification and the method of indemnification may be provided for by charter or bylaw amendment, contract or board resolution, consistent with the procedural requirements of the applicable state law or the Model Business Corporation Act, as specified. A charter or bylaw amendment must be approved by the National Credit Union Administration.

(3) A Federal credit union may purchase and maintain insurance on behalf of its officials and employees against any liability asserted against them and expenses incurred by them in their official capacities and arising out of the performance of their official duties to the extent such insurance is permitted by the applicable state law or the Model Business Corporation Act.

§ 701.34 Designation of low-income status; receipt of secondary capital accounts by low-income designated credit unions.

(a) *Designation of low-income status.* (1) Section 107(6) of the Federal Credit Union Act (12 U.S.C. 1757(6)) authorizes federal credit unions serving predominantly low-income members to receive shares, share drafts and share certificates from nonmembers. In order to utilize this authority, a federal credit union must receive a low-income designation from its Regional Director. The designation may be removed by the Regional Director upon notice to the federal credit union if the definitions set forth in paragraphs (a) (2) and (3) of this section are no longer met. Removals may be appealed to the NCUA Board within 60 days. Appeals should be submitted through the Regional Director.

(2) The term "low-income members" shall mean those members who make less than 80 percent of the average for all wage earners as established by the Bureau of Labor Statistics or those members whose annual household income falls at or below 80 percent of the median household income for the nation as established by the Census Bureau or those members otherwise defined as low-income members as determined by order of the NCUA Board.

(i) In documenting its low-income membership, a credit union that serves a geographic area where a majority of residents fall at or below the annual income standard is presumed to be serving predominantly low-income members. In applying the standards, Regional Directors shall make allowances for geographical areas with higher costs of living. The following is the exclusive list of geographic areas with the differentials to be used:

	Percent
Hawaii	40
Alaska	36
Washington, DC	19
Boston	17
San Diego	15
Los Angeles	14
New York	13
San Francisco	13
Seattle	10
Chicago	7
Philadelphia	7

(ii) The term "low-income member" also includes those members who are enrolled as full-time or part-time students in a college, university, high school, or vocational school.

(3) The term "predominantly" is defined as a simple majority.

(b) *Receipt of secondary capital accounts by low-income designated credit unions.* A Federal credit union having a designation of low income status pursuant to paragraph (a) of this section may offer secondary capital accounts to nonnatural person members and nonnatural person nonmembers on the following conditions:

(1) Prior to offering secondary capital accounts, the credit union shall adopt, and forward to the appropriate NCUA Regional Director, a written plan for use of the funds in the secondary capital accounts and subsequent liquidity needs to meet repayment requirements upon maturity of the accounts.

(2) The secondary capital account must be established as a uninsured secondary capital account or other form of non-share account.

(3) The maturity of the secondary capital account must be for a minimum of five years.

(4) The secondary capital account must not be redeemable prior to maturity.

(5) The secondary capital account shall not be insured by the National Credit Union Share Insurance Fund or any governmental or private entity.

(6) The secondary capital account holder's claim against the credit union must be subordinate to all other claims including those of shareholders, creditors and the National Credit Union Share Insurance Fund.

(7) Funds deposited into the secondary capital account, including interest accrued and paid into the secondary capital account, must be available to cover operating losses realized by the credit union that exceed its net available reserves and undivided earnings (*i.e.*, reserves and undivided earnings exclusive of allowance accounts for loan losses), and to the extent funds are so used, the credit union shall under no circumstances restore or replenish the account. The credit union may, in lieu of paying interest into the secondary capital account, pay interest accrued on the secondary capital account directly to the investor or into a separate account from which the secondary capital investor may make withdrawals. Losses shall be distributed pro-rata among all secondary capital accounts held by the credit union at the time the losses are realized.

(8) The secondary capital account may not be pledged or provided by the account-holder as security on a loan or other obligation with the credit union or any other party.

(9) In the event of merger or other voluntary dissolution of the credit union, other than merger into another low-income designated credit union, the secondary capital accounts will, to the extent they are not needed to cover losses at the time of merger or dissolution, be closed and paid out to the account-holder.

(10) A secondary capital account contract agreement must be executed between an authorized representative of the account holder and the credit union accurately establishing the terms and conditions of this section and containing no provisions inconsistent therewith.

(11) A disclosure and acknowledgment as set forth in the Appendix to this section must be provided to and executed by an authorized representative of the secondary capital account holder at the time of entering into the account agreement, and original copies of the account agreement and the disclosure and acknowledgment must be retained by the credit union for the term of the agreement.

(12) As provided in § 702.204(b)(11) of this chapter, 60 days after the effective date of a credit union being classified as "critically undercapitalized" under NCUA's prompt corrective action rules, the NCUA Board may prohibit payments of principal, dividends or interest on the credit union's uninsured secondary capital accounts established after August 7, 2000, except that unpaid dividends or interest shall continue to accrue under the terms of the account to the extent permitted by law.

(13) As provided in §§ 702.304(b) and 702.305(b) of this chapter, the NCUA Board may prohibit payments of principal, dividends or interest on the uninsured secondary capital accounts established after August 7, 2000 of a "moderately capitalized", "marginally capitalized", "minimally capitalized" or "uncapitalized" credit union if the credit union's net worth ratio has not increased consistent with its then-present business plan, or the credit union has failed to undertake any mandatory supervisory action prescribed in §§ 702.304(a) or 702.305(a) of this chapter. If NCUA takes this action, unpaid dividends or interest shall continue to accrue under the terms of the account to the extent permitted by law.

(c) *Accounting treatment; weighted value for purposes of recognizing capital value of secondary capital accounts.* (1) A low-income designated credit union that issues secondary capital accounts pursuant to paragraph (b) of this section shall record the funds on its balance sheet in an equity account entitled "uninsured secondary capital account." For such accounts with remaining maturities of less than five years, the credit union shall reflect the capital value of the accounts in its financial statement in accordance with the following scale:

(i) Four to less than five years remaining maturity—80 percent.

(ii) Three to less than four years remaining maturity—60 percent.

(iii) Two to less than three years remaining maturity—40 percent.

(iv) One to less than two years remaining maturity—20 percent.

(v) Less than one year remaining maturity—0 percent.

(2) The credit union will reflect the full amount of the secondary capital on deposit in a footnote to its financial statement.

Appendix to § 701.34

Disclosures and acknowledgment in the following form must be provided to any investor in secondary capital accounts in a low-income designated credit union.

An original, signed copy must be retained by the credit union.

Disclosure and Acknowledgment

I, _____ (name of signatory), hereby acknowledge and agree to the following in my capacity as _____ (official position or title) of _____ (name of institutional investor:

- _____ (name of institutional investor) has committed _____ (amount of funds)- to a secondary capital account with _____ (name of credit union).
- The funds committed to the secondary capital account are committed for a period of ____ years and are not redeemable prior to _____.
- The secondary capital account is not a share account and the funds committed to the secondary capital account are not insured by the National Credit Union Share Insurance Fund or any other governmental or private entity.

The funds committed to the secondary capital account and any interest paid into the account may be used by _____ (name of credit union) to cover any and all operating losses that exceed the credit union's reserves and undivided earnings exclusive of allowance accounts for loan losses, and in the event the funds are so used _____ (name of credit union) will under no circumstances restore or replenish those funds to _____ (name of institutional investor).

By initialing below, _____ (name of credit union) _____ and (name of institutional investor) agree that accrued interest will be:

_____ _____ paid into and become part of the secondary capital account;

_____ _____ paid directly to the investor;

_____ _____ paid into a separate account from which the investor may make withdrawals; or

_____ _____ any combination of the above provided the details are specified and agreed to in writing.

- In the event of liquidation of _____ (name of credit union), the funds committed to the secondary capital account shall be *subordinate to all other claims* on the assets of the credit union, including claims of member shareholders, creditors and the National Credit Union Share Insurance Fund.
- The NCUA may prohibit payments of principal, dividends or interest on _____ (name of credit union) uninsured secondary capital accounts established after August 7, 2000, if _____ (name of credit union) has been in operation less than 10 years and has $10 million or less in assets and the provisions of § 701.34(b)(13) of NCUA's regulations are met, or, if _____ (name of credit union) has been in operation for 10 years or more or has more than $10 million in assets and the provisions of § 701.34(b)(12) of NCUA's regulations are met.

_____

(Signature)

_____

(Official Title)

§ 701.35 Share, Share Draft, and Share Certificate Accounts.

(a) Federal credit unions may offer share, share draft, and share certificate accounts in accordance with Section 107(6) of the Act (12 U.S.C. § 1757(6)) and the board of directors may declare dividends on such accounts as provided in Section 117 of the Act (12 U.S.C. § 1763).

(b) A Federal credit union shall accurately represent the terms and conditions of its share, share draft, and share certificate accounts in all advertising, disclosures, or agreements, whether written or oral.

(c) A federal credit union may, consistent with this section, parts 707 and 740 of this subchapter, other federal law, and its contractual obligations, determine the types of fees or charges and other matters affecting the opening maintaining and closing of a share, share draft or share certificate account. State laws regulating such activities are not applicable to federal credit unions.

(d) For purposes of this Section, "state law" means the constitution, statutes, regulations, and judicial decisions of any state, the District of Columbia, the several territories and possessions of the United States, and the Commonwealth of Puerto Rico.

§ 701.36 FCU Ownership of Fixed Assets.

(a) *Investment in Fixed Assets.* (1) No Federal credit union with $1,000,000 or more in assets may invest in any fixed assets if the investment would cause the aggregate of all such investments to exceed five percent of the credit union's shares and retained earnings.

(2) The NCUA may waive the prohibition in paragraph (a)(1) of this section.

(i) A Federal credit union desiring a waiver must submit a written request to the NCUA regional office having jurisdiction over the geographical area in which the credit union's main office is located. The request must describe in detail the contemplated investment and the need for the investment. The request must also indicate the approximate aggregate amount of fixed assets, as a percentage of shares and retained earnings, that the credit union would hold after the investment.

(ii) The regional director will inform the requesting credit union, in writing, of the date the request was received and of any additional documentation that the regional director might require in support of the waiver request.

(iii) The regional director will approve or disapprove the waiver request in writing within 45 days after receipt of the request and all necessary supporting documentation. If the regional director approves the waiver, the regional director will establish an alternative limit on aggregate investments in fixed assets, either as a dollar limit or as a percentage of the credit union's shares and retained earnings. Unless otherwise specified by the regional director, the credit union may make future acquisition of fixed assets only if the aggregate all of such future investments in fixed assets does not exceed an additional one percent of the shares and retained earnings of the credit union over the amount approved by the regional director.

(iv) If the regional director does not notify the credit union of the action taken on its request within 45 calendar days of the receipt of the waiver request or the receipt of additional requested supporting information, whichever occurs later, the credit union may proceed with its proposed investment in fixed assets. The investment, and any future investments in fixed assets, must not cause the credit union to exceed the aggregate investment limit described in its waiver request.

(b) *Premises Not Currently Used To Transact Credit Union Business.* (1) When a Federal credit union acquires premises for future expansion and does not fully occupy the space within one year, the credit union must have a board resolution in place by the end of that year with definitive plans for full occupation. Premises are fully occupied when the credit union, or a combination of the credit union, CUSOs, or vendors, use the entire space on a full-time basis. CUSOs and vendors must be using the space primarily to support the credit union or to serve the credit union's members. The credit union must make any plans for full occupation available to an NCUA examiner upon request.

(2) When a Federal credit union acquires premises for future expansion, the credit union must partially occupy the premises within a reasonable period, not to exceed three years. Premises are partially occupied when the credit union is using some part of the space on a full-time basis. The NCUA may waive this partial occupation requirement in writing upon written request. The request must be made within 30 months after the property is acquired.

(3) A Federal credit union must make diligent efforts to dispose of abandoned premises and any other real property not intended for use in the conduct of credit union business. The credit union must seek fair market value for the property, and record its efforts to dispose of abandoned premises. After premises have been abandoned for four years, the credit union must publicly advertise the property for sale. Unless otherwise approved in writing by the NCUA, the credit union must complete the sale within five years of abandonment.

(c) *Prohibited Transactions.* (1) Without the prior written approval of the NCUA, no federal credit union may invest in premises through an acquisition or a lease of one year or longer from any of the following:

(i) A director, member of the credit committee or supervisory committee, or senior management employee of the federal credit union, or immediate family member of any such individual.

(ii) A corporation in which any director, member of the credit committee or supervisory committee, official, or senior management employee, or immediate family members of any such individual, is an officer or director, or has a stock interest of 10 percent or more.

(iii) A partnership, limited liability company, or other entity in which any director, member of the credit committee or supervisory committee, or senior management employee, or immediate family members of any such individual, is a general partner, or a limited partner or entity member with an interest of 10 percent or more.

(2) The prohibition contained in paragraph (c)(1) of this section also applies to a lease from any other employee if the employee is directly involved in investments in fixed assets unless the board of directors determines that the employee's involvement does not present a conflict of interest.

(3) All transactions with business associates or family members not specifically prohibited by this paragraph (c) must be conducted at arm's length and in the interest of the credit union.

(d) *Regulatory Flexibility Program.* Federal credit unions that qualify for the Regulatory Flexibility Program provided for in part 742 of this chapter are exempt from the five percent limitation described in paragraph (a) of this section. For Federal credit unions eligible for the Regulatory Flexibility Program that subsequently lose eligibility:

(1) Section 742.8 of this chapter provides that NCUA may require the credit union to divest any existing fixed assets for substantive safety and soundness reasons; and

(2) The credit union may not make any new investments in fixed assets if, after the investment, the credit union's total investments in fixed assets would exceed the five percent limitation described in paragraph (a) of this section. The regional director may waive this prohibition to allow for new investments.

(e) *Definitions*—As used in this section:

(1) *Abandoned premises* means real property previously used to transact credit union business but no longer used for that purpose and real property originally acquired for future expansion for which the credit union no longer contemplates such use.

(2) *Fixed assets* means premises, furniture, fixtures and equipment.

(3) *Furniture, fixtures, and equipment* means all office furnishings, office machines, computer hardware and software, automated terminals, and heating and cooling equipment.

(4) *Investments in fixed assets* means:

(i) Any investment in improved or unimproved real property which is being used or is intended to be used as premises;

(ii) Any leasehold improvement on premises;

(iii) The aggregate of all capital and operating lease payments on fixed assets, without discounting commitments for future payments to present value; and

(iv) Any investment in furniture, fixtures and equipment.

(5) *Immediate family* member means a spouse or other family members living in the same household.

(6) *Premises* means any office, branch office, suboffice, service center, parking lot, other facility, or real estate where the credit union transacts or will transact business.

(7) *Senior management employee* means the credit union's chief executive officer (typically this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (*e.g.*, Assistant President, Vice President or Assistant Treasurer/Manager) and the chief financial officer (Comptroller).

(8) *Shares* means regular shares, share drafts, share certificates, other savings.

(9) *Retained earnings* means undivided earnings, regular reserve, reserve for contingencies, supplemental reserves, reserve for losses, and other appropriations from undivided earnings as designated by management or the Administration.

§ 701.37 Treasury Tax and Loan Depositaries; Depositaries and Financial Agents of the Government.

(a) *Definitions.*

(1) "Treasury Tax and Loan ("TT&L") Remittance Account" means a nondividend-paying account, the balance of which is subject to the right of immediate withdrawal, established for receipt of payments of Federal taxes and certain United States obligations under United States Treasury Department regulations.

(2) "TT&L Note Account" means an account subject to the right of immediate call, evidencing funds held by depositaries electing the note option under United States Treasury Department regulations.

(3) "Treasury General Account" means an account, established under United States Treasury Department regulations, in which a zero balance may be maintained and from which

the entire balance may be withdrawn by the depositor immediately under all circumstances except closure of the credit union;

(4) "U.S. Treasury Time Deposit-Open Account" means a nondividend-bearing account, established under United States Treasury Department regulations, which generally may not be withdrawn until the expiration of 14 days after the date of the United States Treasury Department's written notice of intent to withdraw.

(b) Subject to regulation of the United States Treasury Department, a Federal credit union may serve as a Treasury tax and loan depositary, a depositary of Federal taxes, a depositary of public money, and a financial agent of the United States Government. In serving in these capacities, a Federal credit union may maintain the accounts defined in subsection (a), pledge collateral, and perform the services described under United States Treasury Department regulations for institutions acting in these capacities.

(c) Funds held in a TT&L Remittance Account, a TT&L Note Account, a Treasury General Account, and a U.S. Treasury Time Deposit-Open Account shall be considered deposits of public funds. Funds held in a TT&L Remittance Account and a TT&L Note Account shall be added together and insured up to a maximum of $100,000 in the aggregate. Funds held in a Treasury General Account and a U.S. Treasury Time Deposit-Open Account shall be added together and insured up to a maximum of $100,000 in the aggregate.

(d) Funds held in a TT&L Remittance Account, a TT&L Note Account, a Treasury General Account, and U.S. Treasury Time Deposit-Open Account are not subject to the 60-day notice requirement of Article III, section 5(a) of the Federal Credit Union Bylaws.

§ 701.38 Borrowed Funds From Natural Persons.

(a) Federal credit unions may borrow from a natural person, PROVIDED:

(1) The borrowing is evidenced by a signed promissory note which sets forth the terms and conditions regarding maturity, prepayment, interest rate, method of computation, and method of payment;

(2) The promissory note and any advertisement for such funds contains conspicuous language indicating that:

(i) the note represents money borrowed by the credit union;

(ii) the note does not represent shares and, therefore, is not insured by the National Credit Union Share Insurance Fund.

§ 701.39 Statutory lien.

(a) *Definitions.* Within this section, each of the following terms has the meaning prescribed below:

(1) *Except as otherwise provided by law* or *except as otherwise provided by federal law* is a qualifying phrase referring to a federal and/or state law, as the case may be, which supersedes a requirement of this section. It is the responsibility of the credit union to ascertain whether such statutory or case law exists and is applicable;

(2) *Impress* means to attach to a member's account and is the act which makes the lien enforceable against that account;

(3) *Member* means any member who is primarily, secondarily or otherwise responsible for an outstanding financial obligation to the credit union, including without limitation an obligor, maker, co-maker, guarantor, co-signer, endorser, surety or accommodation party;

(4) *Notice* means written notice to a member disclosing, in plain language, that the credit union has the right to impress and enforce a statutory lien against the member's shares and dividends in the event of failure to satisfy a financial obligation, and may enforce the right without further notice to the member. Such notice must be given at the time, or at any time before, the member incurs the financial obligation;

(5) *Statutory lien* means the right granted by section 107(11) of the Federal Credit Union Act, 12 U.S.C. 1757(11), to a federal credit union to establish a right in or claim to a member's shares and dividends equal to the amount of that member's outstanding financial obligation to the credit union, as that amount varies from time to time.

(b) *Superior claim.* Except as otherwise provided by law, a statutory lien gives the federal credit union priority over other creditors when claims are asserted against a member's account(s).

(c) *Impressing a statutory lien.* Except as otherwise provided by federal law, a credit union can impress a statutory lien on a member's account(s)—

(1) *Account records.* By giving notice thereof in the member's account agreement(s) or other account opening documentation; or

(2) *Loan documents.* In the case of a loan, by giving notice thereof in a loan document signed or otherwise acknowledged by the member(s); or

(3) *By-Law or policy.* Through a duly adopted credit union by-law or policy of the board of directors, of which the member is given notice.

(d) *Enforcing a statutory lien.* (1) *Application of funds.* Except as otherwise provided by federal law, a federal credit union may enforce its statutory lien against a member's account(s) by debiting funds in the account and applying them to the extent of any of the member's outstanding financial obligations to the credit union.

(2) *Default required.* A federal credit union may enforce its statutory lien against a member's account(s) only when the member fails to satisfy an outstanding financial obligation due and payable to the credit union.

(3) *Neither judgment nor set-off required.* A federal credit union need not obtain a court judgment on the member's debt, nor exercise the equitable right of set-off, prior to enforcing its statutory lien against the member's account.

Part 702

Prompt Corrective Action

§ 702.1 Authority, purpose, scope and other supervisory authority.

(a) *Authority.* Subparts A, B and C of this part and subpart L of part 747 of this chapter are issued by the National Credit Union Administration pursuant to section 216 of the Federal Credit Union Act (FCUA), 12 U.S.C. 1790d (section 1790d), as added by section 301 of the Credit Union Membership Access Act, Pub. L. No. 105–219, 112 Stat. 913 (1998). Subpart D of this part is issued pursuant to FCUA section 120, 12 U.S.C. 1766.

(b) *Purpose.* The express purpose of prompt corrective action under section 1790d is to resolve the problems of federally-insured credit unions at the least possible long-term loss to the National Credit Union Share Insurance Fund. This part carries out the purpose of prompt corrective action by establishing a framework of mandatory and discretionary supervisory actions, applicable according to a credit union's net worth ratio, designed primarily to restore and improve the net worth of federally-insured credit unions.

(c) *Scope.* This part implements the provisions of section 1790d as they apply to federally-insured credit unions, whether federally- or state-chartered; to such credit unions defined as "new" pursuant to section 1790d(b)(2); and to such credit unions defined as "complex" pursuant to section 1790d(d). Certain of these provisions also apply to officers and directors of federally-insured credit unions. This part does not apply to corporate credit unions. Procedures for issuing, reviewing and enforcing orders and directives issued under this part are set forth in subpart L of part 747 of this chapter, 12 CFR 747.2001 *et seq.*

(d) *Other supervisory authority.* Neither § 1790d nor this part in any way limits the authority of the NCUA Board or appropriate State official under any other provision of law to take additional supervisory actions to address unsafe or unsound practices or conditions, or violations of applicable law or regulations. Action taken under this part may be taken independently of, in conjunction with, or in addition to any other enforcement action available to the NCUA Board or appropriate State official, including issuance of cease and desist orders, orders of prohibition, suspension and removal, or assessment of civil money penalties, or any other actions authorized by law.

§ 702.2 Definitions

Except as provided below, the terms used in this part have the same meanings as set forth in FCUA sections 101 and 216, 12 U.S.C. 1752, 1790d.

(a) *Appropriate regional director* means the director of the NCUA regional office having jurisdiction over federally-insured credit unions in the state where the affected credit union is principally located.

(b) *Appropriate State official* means the commission, board or other supervisory authority having jurisdiction over credit unions chartered by the State which chartered the affected credit union.

(c) *Credit union* means a federally-insured, natural person credit union, whether federally- or State-chartered, as defined by 12 U.S.C. 1752(6).

(d) *CUSO* means a credit union service organization as described in 12 CFR 712 *et seq.* for federally-chartered credit unions, and as defined under State law for State-chartered credit unions.

(e) *NCUSIF* means the National Credit Union Share Insurance Fund as defined by 12 U.S.C. 1783.

(f) *Net worth* means the retained earnings balance of the credit union at quarter end as determined under generally accepted accounting principles. Retained earnings consists of undivided earnings, regular reserves, and any other appropriations designated by management or regulatory authorities. This means that only undivided earnings and appropriations of undivided earnings are included in net worth. For low income-designated credit unions, net worth also includes secondary capital accounts that are uninsured and subordinate to all other claims, including claims of creditors, shareholders and the NCUSIF. For any credit union, net worth does not include the allowance for loan and lease losses account.

(g) *Net worth ratio* means the ratio of the net worth of the credit union (as defined in paragraph (f) of this section to the total assets of the credit union (as defined by a measure chosen under paragraph (k) of this section.

(h) *New credit union* means a federally-insured credit union which both has been in operation for less than ten (10) years and has $10,000,000 or less in total assets.

(i) *Senior executive officer* means a senior executive officer as defined by 12 CFR 701.14(b)(2).

(j) *Shares* means deposits, shares, share certificates, share drafts, or any other depository account authorized by federal or state law.

(k) *Total assets*

(1) Total assets means a credit union's total assets as measured by either—

(i) *Average quarterly balance.* The average of quarter-end balances of the current and three preceding calendar quarters; or

(ii) *Average monthly balance.* The average of month-end balances over the three calendar months of the calendar quarter; or

(iii) *Average daily balance.* The average daily balance over the calendar quarter; or

(iv) *Quarter-end balance.* The quarter-end balance of the calendar quarter as reported on the credit union's Call Report.

(2) For each quarter, a credit union must elect a measure of total assets from paragraph (k)(1) of this section to apply for all purposes under this part except §§ 702.103 through 702.108 [risk-based net worth requirement].

(l) *Weighted-average life* means the weighted-average time to the return of a dollar of principal, calculated by multiplying each portion of principal received by the time at which it is expected to be received (based on a reasonable and supportable estimate of that time), and then summing and dividing by the total amount of principal.

Subpart A—Net Worth Classification

§ 702.101 Measures and effective date of net worth classification

(a) *Net worth measures.* For purposes of this part, a credit union must determine its net worth category classification at the end of each calendar quarter using two measures:

(1) The net worth ratio as defined in § 702.2(g); and

(2) If determined to be applicable under § 702.103, a risk-based net worth requirement.

(b) *Effective date of net worth classification.* For purposes of this part, the effective date of a federally-insured credit union's net worth category classification shall be the most recent to occur of:

(1) *Quarter-end effective date.* The last day of the calendar month following the end of the calendar quarter; or

(2) *Corrected net worth category.* The date the credit union received subsequent written notice from NCUA or, if State-chartered, from the appropriate State official, of a decline in net worth category due to correction of an error or misstatement in the credit union's most recent Call Report; or

(3) *Reclassification to lower category.* The date the credit union received written notice from NCUA or, if State-chartered, the appropriate State official, of reclassification on safety and soundness grounds as provided under §§ 702.102(b) or 702.302(d).

(c) *Notice to NCUA by filing Call Report.* (1) Other than by filing a Call Report, a federally-insured credit union need not notify the NCUA Board of a change in its net worth ratio that places the credit union in a lower net worth category;

(2) Failure to timely file a Call Report as required under this section in no way alters the effective date of a change in net worth classification under this paragraph (b) of this section, or the affected credit union's corresponding legal obligations under this part.

§ 702.102 Statutory net worth categories.

(a) *Net worth categories.* Except for credit unions defined as "new" under subpart B of this part, a federally-insured credit union shall be classified (Table 1)—

(1) *Well capitalized* if it has a net worth ratio of seven percent (7%) or greater and also meets any applicable risk-based net worth requirement under §§ 702.103 through 702.108; or

(2) *Adequately capitalized* if it has a net worth ratio of six percent (6%) or more but less than seven percent (7%), and also meets any applicable risk-based net worth requirement under §§ 702.103 through 702.108 below; or

(3) *Undercapitalized* if it has a net worth ratio of four percent (4%) or more but less than six percent (6%), or fails to meet any applicable

risk-based net worth requirement under §§ 702.103 through 702.108; or

(4) *Significantly undercapitalized* if it

(i) Has a net worth ratio of two percent (2%) or more but less than four percent (4%); or

(ii) Has a net worth ratio of four percent (4%) or more but less than five percent (5%), and either—

(A) Fails to submit an acceptable net worth restoration plan within the time prescribed in § 702.206; or

(B) Materially fails to implement a net worth restoration plan approved by the NCUA Board; or

(5) *Critically undercapitalized* if it has a net worth ratio of less than two percent (2%).

TABLE 1 – STATUTORY NET WORTH CATEGORY CLASSIFICATION

A credit union's net worth category is . . .	*if its net worth ratio is . . .*	*and subject to the following condition(s) . . .*
"Well Capitalized"	7% or above	Meets applicable risk-based net worth (RBNW) requirement
"Adequately Capitalized"	6% to 6.99%	Meets applicable RBNW requirement
"Undercapitalized"	4% to 5.99%	Or fails applicable RBNW requirement
"Significantly Undercapitalized"	2% to 3.99%	Or if "undercapitalized" at <5% net worth ratio and fails to timely submit or materially implement Net Worth Restoration Plan
"Critically Undercapitalized"	Less than 2%	None

(b) *Reclassification based on supervisory criteria other than net worth.* The NCUA Board may reclassify a "well capitalized" credit union as "adequately capitalized" and may require an "adequately capitalized" or "undercapitalized" credit union to comply with certain mandatory or discretionary supervisory actions as if it were in the next lower net worth category (each of such actions hereinafter referred to generally as "reclassification") in the following circumstances:

(1) *Unsafe or unsound condition.* The NCUA Board has determined, after notice and opportunity for hearing pursuant to § 747.2003 of this chapter, that the credit union is in an unsafe or unsound condition; or

(2) *Unsafe or unsound practice.* The NCUA Board has determined, after notice and opportunity for hearing pursuant to § 747.2003 of this chapter, that the credit union has not corrected a material unsafe or unsound practice of which it was, or should have been, aware.

(c) *Non-delegation.* The NCUA Board may not delegate its authority to reclassify a credit union under paragraph (b) of this section.

(d) *Consultation with State officials.* The NCUA Board shall consult and seek to work cooperatively with the appropriate State official before reclassifying a federally-insured State-chartered credit union under paragraph (b) of this section, and shall promptly notify the appropriate State official of its decision to reclassify.

§ 702.103 Applicability of risk-based net worth requirement.

For purposes of § 702.102, a credit union is defined as "complex" and a risk-based net worth requirement is applicable only if the credit union meets both of the following criteria as reflected its most recent Call Report:

(a) *Minimum asset size.* Its quarter-end total assets exceed ten million dollars ($10,000,000); and

(b) *Minimum RBNW calculation.* Its risk-based net worth requirement as calculated under § 702.106 exceeds six percent (6%).

§ 702.104 Risk portfolios defined.

A risk portfolio is a portfolio of assets, liabilities, or contingent liabilities as specified below, each expressed as a percentage of the credit union's quarter-end total assets reflected in its most re-

cent Call Report, rounded to two decimal places (Table 2):

(a) *Long-term real estate loans.* Total real estate loans and real estate lines of credit outstanding, exclusive of those outstanding that will contractually refinance, reprice or mature within the next five (5) years, and exclusive of all member business loans (as defined in 12 CFR 723.1 or as approved under 12 CFR 723.20);

(b) *Member business loans outstanding.* All member business loans as defined in 12 CFR 723.1 or as approved under 12 CFR 723.20;

(c) *Investments.* Investments as defined by 12 CFR 703.150 or applicable State law, including investments in CUSOs (as defined by § 702.2(d));

(d) *Low-risk assets.* Cash on hand (*e.g.,* coin and currency, including vault, ATM and teller cash) and the NCUSIF deposit;

(e) *Average-risk assets.* One hundred percent (100%) of total assets minus the sum of the risk portfolios in paragraphs (a) through (d) of this section;

(f) *Loans sold with recourse.* Outstanding balance of loans sold or swapped with recourse, excluding loans sold to the secondary mortgage market that have representations and warranties consistent with those customarily required by the U.S. Government and government sponsored enterprises;

(g) *Unused member business loan commitments.* Unused commitments for member business loans as defined in 12 CFR 723.1 or as approved under 12 CFR 723.20; and

(h) *Allowance.* The Allowance for Loan and Lease Losses not to exceed the equivalent of one and one-half percent (1.5%) of total loans outstanding.

TABLE 2 -- §702.104 RISK PORTFOLIOS DEFINED

Risk portfolio	*Assets, liabilities or contingent liabilities*
(a) Long-term real estate loans	Total real estate loans and real estate lines of credit (excluding MBLs) with a maturity (and next rate adjustment period if variable rate) greater than 5 years
(b) MBLs outstanding	Member business loans outstanding
(c) Investments	As defined by federal regulation or applicable State law.
(d) Low-risk assets	Cash on hand and NCUSIF deposit.
(e) Average-risk assets	100% of total assets minus sum of risk portfolios above
(f) Loans sold with recourse	Outstanding balance of loans sold or swapped with recourse, except for loans sold to the secondary mortgage market with a recourse period of 1 year or less.
(g) Unused MBL commitments	Unused commitments for MBLs
(h) Allowance	Allowance for Loan and Lease Losses limited to equivalent of 1.50 percent of total loans

§ 702.105 Weighted-average life of investments.

Except as provided below (Table 3), the weighted-average life of an investment for purposes of §§ 702.106(c) and 702.107(c) is defined pursuant to § 702.2(m):

(a) *Registered investment companies and collective investment funds.*

(1) For investments in registered investment companies (*e.g.,* mutual funds) and collective investment funds, the weighted-average life is defined as the maximum weighted-average life disclosed, directly or indirectly, in the prospectus or trust instrument;

(2) For investments in money market funds, as defined in 17 CFR 270.2a–7, and collective investment funds operated in accordance with short-term investment fund rules set forth in 12 CFR 9.18(b)(4)(ii)(B)(1)–(3), the weighted-average life is defined as one (1) year or less; and

(3) For other investments in registered investment companies or collective investment funds, the weighted-average life is defined as

greater than five (5) years, but less than or equal to seven (7) years;

(b) *Callable fixed-rate debt obligations and deposits.* For fixed-rate debt obligations and deposits that are callable in whole, the weighted-average life is defined as the period remaining to the maturity date;

(c) *Variable-rate debt obligations and deposits.* For variable-rate debt obligations and deposits, the weighted-average life is defined as the period remaining to the next rate adjustment date;

(d) *Capital in mixed-ownership Government corporations and corporate credit unions.* For capital stock in mixed-ownership Government corporations, as defined in 31 U.S.C. 9101(2), and member paid-in capital and membership capital in corporate credit unions, as defined in 12 CFR 704.2, the weighted-average life is defined as greater than one (1) year, but less than or equal to three (3) years;

(e) *Investments in CUSOs.* For investments in CUSOs (as defined in § 702.2(d)), the weighted-average life is defined as greater than one (1) year, but less than or equal to three (3) years; and

(f) *Other equity securities.* For other equity securities, the weighted average life is defined as greater than ten (10) years.

TABLE 3 -- §702.105 WEIGHTED-AVERAGE LIFE OF INVESTMENTS

Investment	*Weighted-average life*
(a) Registered investment companies and collective investment funds	i. *Registered investment companies and collective investment funds*: As disclosed in prospectus or trust instrument, but if not disclosed, greater than five (5) years, but less than or equal to seven (7) years. ii. *Money market funds and STIFs*: One (1) year or less.
(b) Callable fixed-rate debt obligations and deposits	Period remaining to maturity date.
(c) Variable-rate debt obligations and deposits	Period remaining to next rate adjustment date.
(d) Capital in mixed-ownership Government corporations and corporate credit unions	Greater than one (1) year, but less than or equal to three (3) years.
(e) Investments in CUSOs	Greater than one (1) year, but less than or equal to three (3) years.
(f) Other equity securities	Greater than ten (10) years.

§ 702.106 Standard calculation of risk-based net worth requirement.

A credit union's risk-based net worth requirement is the aggregate of the following standard component amounts, each expressed as a percentage of the credit union's quarter-end total assets as reflected in its most recent Call Report, rounded to two decimal places (Table 4):

(a) *Long-term real estate loans.* The sum of:

(1) Six percent (6%) of the amount of long-term real estate loans less than or equal to twenty-five percent (25%) of total assets; and

(2) Fourteen percent (14%) of the amount in excess of twenty-five percent (25%) of total assets;

(b) *Member business loans outstanding.* The sum of:

(1) Six percent (6%) of the amount of member business loans outstanding less than or equal to fifteen percent (15%) of total assets;

(2) Eight percent (8%) of the amount of member business loans outstanding greater than fifteen percent (15%), but less than or equal to twenty-five percent (25%), of total assets; and

(3) Fourteen percent (14%) of the amount in excess of twenty-five percent (25%) of total assets;

(c) *Investments.* The sum of:

(1) Three percent (3%) of the amount of investments with a weighted-average life (as specified in § 702.105 above) of one (1) year or less;

(2) Six percent (6%) of the amount of investments with a weighted-average life greater than one (1) year, but less than or equal to three (3) years;

(3) Twelve percent (12%) of the amount of investments with a weighted-average life greater than three (3) years, but less than or equal to ten (10) years; and

(4) Twenty percent (20%) of the amount of investments with a weighted-average life greater than ten (10) years;

(d) *Low-risk assets.* Zero percent (0%) of the entire portfolio of low-risk assets;

(e) *Average-risk assets.* Six percent (6%) of the entire portfolio of average-risk assets;

(f) *Loans sold with recourse.* Six percent (6%) of the entire portfolio of loans sold with recourse;

(g) *Unused member business loan commitments.* Six percent (6%) of the entire portfolio of unused member business loan commitments; and

(h) *Allowance.* Negative one hundred percent (−100%) of the balance of the Allowance for Loan and Lease Losses account, not to exceed the equivalent of one and one-half percent (1.5%) of total loans outstanding.

TABLE 4 -- §702.106 STANDARD CALCULATION OF RBNW REQUIREMENT

Risk portfolio	*Amount of risk portfolio (as percent of quarter-end total assets) to be multiplied by risk weighting*	*Risk weighting*
(a) Long-term real estate loans	0 to 25.00% over 25.00%	.06 .14
(b) MBLs outstanding	0 to 15.00% >15.00% to 25.00% over 25.00%	.06 .08 .14
(c) Investments	*By weighted-average life*: 0 to 1 year >1year to 3 years >3 years to 10 years >10 years	.03 .06 .12 .20
(d) Low-risk assets	All %	.00
(e) Average-risk assets	All %	.06
(f) Loans sold with recourse	All %	.06
(g) Unused MBL commitments	All %	.06
(h) Allowance	Limited to equivalent of 1.50% of total loans (expressed as a percent of total assets)	(1.00)
A credit union's RBNW requirement is the sum of eight standard components. A standard component is calculated for each of the eight risk portfolios, equal to the sum of each amount of a risk portfolio times its risk weighting. A credit union is classified "undercapitalized" if its net worth ratio is less than its applicable RBNW requirement.		

§ 702.107 Alternative components for standard calculation.

A credit union may substitute one or more alternative components below, in place of the corresponding standard components in § 702.106 above, when any alternative component amount, expressed as a percentage of the credit union's quarter-end total assets as reflected in its most recent Call Report, rounded to two decimal places, is smaller (Table 5):

(a) *Long-term real estate loans.* The sum of:

(1) *Non-callable.* Non-callable long-term real estate loans as follows:

(i) Eight percent (8%) of the amount of such loans with a remaining maturity of greater than 5 years, but less than or equal to 12 years;

(ii) Twelve percent (12%) of the amount of such loans with a remaining maturity of greater than 12 years, but less than or equal to 20 years; and

(iii) Fourteen percent (14%) of the amount of such loans with a remaining maturity greater than 20 years;

(2) *Callable.* Long-term real estate loans callable in 5 years or less as follows:

(i) Six percent (6%) of the amount of such loans with a documented call provision of 5 years or less and with a remaining maturity of greater than 5 years, but less than or equal to 12 years;

(ii) Ten percent (10%) of the amount of such loans with a documented call provision of 5 years or less and with a remaining maturity of greater than 12 years, but less than or equal to 20 years; and

(iii) Twelve percent (12%) of the amount of such loans with a documented call provision of 5 years or less and with a remaining maturity of greater than 20 years;

(b) *Member business loans outstanding.* The sum of:

(1) *Fixed rate.* Fixed-rate member business loans outstanding as follows:

(i) Six percent (6%) of the amount of such loans with a remaining maturity of 3 or fewer years;

(ii) Nine percent (9%) of the amount of such loans with a remaining maturity greater than 3 years, but less than or equal to 5 years;

(iii) Twelve percent (12%) of the amount of such loans with a remaining maturity greater than 5 years, but less than or equal to 7 years;

(iv) Fourteen percent (14%) of the amount of such loans with a remaining maturity greater than 7 years, but less than or equal to 12 years; and

(v) Sixteen percent (16%) of the amount of such loans with a remaining maturity greater than 12 years; and

(2) *Variable-rate.* Variable-rate member business loans outstanding as follows:

(i) Six percent (6%) of the amount of such loans with a remaining maturity of 3 or fewer years;

(ii) Eight percent (8%) of the amount of such loans with a remaining maturity greater than 3 years, but less than or equal to 5 years;

(iii) Ten percent (10%) of the amount of such loans with a remaining maturity greater than 5 years, but less than or equal to 7 years;

(iv) Twelve percent (12%) of the amount of such loans with a remaining maturity greater than 7 years, but less than or equal to 12 years; and

(v) Fourteen percent (14%) of the amount of such loans with a remaining maturity greater than 12 years.

(c) *Investments.* The sum of:

(1) Three percent (3%) of the amount of investments with a weighted-average life (as specified in § 702.105 above) of one (1) year or less;

(2) Six percent (6%) of the amount of investments with a weighted-average life greater than one (1) year, but less than or equal to three (3) years;

(3) Eight percent (8%) of the amount of investments with a weighted-average life greater than three (3) years, but less than or equal to five (5) years;

(4) Twelve percent (12%) of the amount of investments with a weighted-average life greater than five (5) years, but less than or equal to seven (7) years;

(5) Sixteen percent (16%) of the amount of investments with a weighted-average life greater than seven (7) years, but less than or equal to ten (10) years; and

(6) Twenty percent (20%) of the amount of investments with a weighted-average life greater than ten (10) years.

(d) *Loans sold with recourse.* The alternative component is the sum of:

(1) Six percent (6%) of the amount of loans sold with contractual recourse obligations of six percent (6%) or greater; and

(2) The weighted average recourse percent of the amount of loans sold with contractual recourse obligations of less than six percent (6%), as computed by the credit union.

TABLE 5 -- §702.107 ALTERNATIVE COMPONENTS FOR STANDARD CALCULATION

(a) LONG-TERM REAL ESTATE LOANS

Amount of long-term real estate loans by remaining maturity	*Alternative risk weighting*
Non-callable long-term real estate loans	
Remaining maturity:	
> 5 years to 12 years	.08
> 12 years to 20 years	.12
> 20 years	.14
Long-term real estate loans callable in 5 years or less	
Remaining maturity:	
> 5 years to 12 years	.06
> 12 years to 20 years	.10
> 20 years	.12
The "alternative component" is the sum of each amount of the "long-term real estate loans" risk portfolio by non-"callable" and "callable" characteristic and by remaining maturity (as a percent of quarter-end total assets) times its alternative factor. Substitute for corresponding standard component if smaller.	

(b) MEMBER BUSINESS LOANS

Amount of member business loans by remaining maturity	*Alternative risk weighting*
Fixed-rate MBLs	
0 to 3 years	.06
> 3 years to 5 years	.09
> 5 years to 7 years	.12
> 7 years to 12 years	.14
> 12 years	.16
Variable-rate MBLs	
0 to 3 years	.06
> 3 years to 5 years	.08
> 5 years to 7 years	.10
> 7 years to 12 years	.12
> 12 years	.14
The "alternative component" is the sum of each amount of the member business loans risk portfolio by fixed and variable rate and by remaining maturity (as a percent of quarter-end total assets) times its alternative factor. Substitute for corresponding standard component if smaller.	

(c) INVESTMENTS

Amount of investments by weighted-average life	*Alternative risk weighting*
0 to 1 year	.03
>1 year to 3 years	.06
>3 years to 5 years	.08
>5 years to 7 years	.12
>7 years to 10 years	.16
> 10 years	.20
The "alternative component" is the sum of each amount of the Investments risk portfolio by weighted-average life (as a percent of quarter-end total assets) times its alternative factor. Substitute for corresponding standard component if smaller.	

(d) LOANS SOLD WITH RECOURSE

Amount of loans by recourse	*Alternative risk weighting*
Recourse 6% or greater	.06
Recourse <6%	Weighted average recourse percent
The "alternative component" is the sum of each amount of the "loans sold with recourse" risk portfolio by level of recourse (as a percent of quarter-end total assets) times its alternative factor. The alternative factor for loans sold with recourse of less than 6% is equal to the weighted average recourse percent on such loans. A credit union must compute the weighted average recourse percent for its loans sold with recourse of less than six percent (6%). Substitute for corresponding standard component if smaller.	

§ 702.108 Risk mitigation credit.

(a) *Who may apply.* A credit union may apply for a risk mitigation credit if on any of the current or three preceding effective dates of classification it either failed an applicable RBNW requirement or met it by less than 100 basis points.

(b) *Application for credit.* Upon application pursuant to guidelines duly adopted by the NCUA Board, the NCUA Board may in its discretion grant a credit to reduce a risk-based net worth requirement under §§ 702.106 and 702.107 upon proof of mitigation of:

(1) Credit risk; or

(2) Interest rate risk as demonstrated by economic value exposure measures.

(c) *Application by FISCU.* In the case of a FISCU seeking a risk mitigation credit—

(1) Before an application under paragraph (a) above may be submitted to the NCUA Board, it must be submitted in duplicate to the appropriate State official and the appropriate Regional Director; and

(2) The NCUA Board, when evaluating the application of a FISCU, shall consult and seek to work cooperatively with the appropriate State official, and shall provide prompt notice of its decision to the appropriate State official.

APPENDICES A–H TO SUBPART A OF PART 702

APPENDIX A – EXAMPLE STANDARD COMPONENTS FOR RBNW REQUIREMENT, §702.106 (EXAMPLE CALCULATION IN BOLD)

Risk portfolio	***Dollar balance***	***Amount as percent of quarter-end total assets***	*Risk weighting*	***Amount times risk weighting***	***Standard component***
Quarter-end total assets	**200,000,000**	**100.0000 %**			
(a) Long-term real estate loans	**60,000,000**	**30.0000 % =**			**2.20 %**
Threshold amount: 0 to 25%		**25.0000 %**	.06	**1.5000 %**	
Excess amount: over 25%		**5.0000 %**	.14	**0.7000 %**	
(b) MBLs outstanding	**35,000,000**	**17.5000 % =**			**1.10 %**
Threshold amount: 0 to 15%		**15.0000 %**	.06	**0.9000 %**	
Intermediate tier: >15% to 25%		**2.5000 %**	.08	**0.2000 %**	
Excess amount: over 25%		**0.0 %**	.14	**0.0 %**	
(c) Investments	**50,000,000 =**	**25.0000 % =**			**1.51 %**
Weighted-average life:					
0 to 1 year	**24,000,000**	**12.0000 %**	.03	**0.3600 %**	
>1 year to 3 years	**15,000,000**	**7.5000 %**	.06	**0.4500 %**	
>3 years to 10 years	**10,000,000**	**5.0000 %**	.12	**0.6000 %**	
>10 years	**1,000,000**	**0.5000 %**	.20	**0.1000 %**	
(d) Low-risk assets	**4,000,000**	**2.0000 %**	.00		**0 %**
Sum of risk portfolios (a) through (d) above	**149,000,000**	**74.5.000%**			
(e) Average-risk assets	**51,000,000**	**25.5000 %**[a]	.06		**1.53 %**
(f) Loans sold with recourse	**40,000,000**	**20.0000 %**	.06		**1.20 %**
(g) Unused MBL commitments	**5,000,000**	**2.5000 %**	.06		**0.15 %**
(h) Allowance	**2,040,000.00** [b]	**1.0200 %**	(1.00)		**(1.02) %**
Sum of standard components: **RBNW requirement** [c]					**6.67 %**

[a] The Average-risk assets risk portfolio percent of quarter-end total assets equals 100 percent minus the sum of the percentages in the four risk portfolios above (*e.g.,* Long-term real estate loans, MBLs outstanding, Investments, and Low-risk assets).

[b] The Allowance risk portfolio is limited to the equivalent of 1.50 percent of total loans. For an example computation of the permitted dollar balance of Allowance, see worksheet in Appendix B below.

[c] A credit union is classified ''undercapitalized'' if its net worth ratio is less than its applicable RBNW requirement. The dollar equivalent of RBNW requirement may be computed for informational purposes as the RBNW requirement percent of total assets.

APPENDIX B – ALLOWANCE RISK PORTFOLIO DOLLAR BALANCE WORKSHEET
(EXAMPLE CALCULATION IN BOLD)

Balance sheet account	***Dollar balance***	***Percent of total loans***	*Range of ALL permitted*	***Permitted ALL percent of total loans***	***Permitted dollar balance of Allowance***
Allowance for Loan and Lease Losses (ALL)	**2,400,000**	**1.7647%**	0 to 1.50%	**1.50%**	**2,040,000**
Total loans	**136,000,000**				

APPENDIX C – EXAMPLE LONG-TERM REAL ESTATE LOANS ALTERNATIVE COMPONENT, §702.107(a)
(EXAMPLE CALCULATION IN BOLD)

Remaining maturity	**Dollar balance of Long-term real estate loans by remaining maturity**	**Percent of total assets by remaining maturity**	Alternative risk weighting	**Alternative component**
Non-callable long-term real estate loans				
> 5 years to 12 years	**15,000,000**	**7.5000 %**	.08	**0.6000 %**
> 12 years to 20 years	**2,500,000**	**1.2500 %**	.12	**0.1500 %**
> 20 years	**2,500,000**	**1.2500 %**	.14	**0.1750 %**
Long-term real estate loans callable in 5 years or less				
> 5 years to 12 years	**35,000,000**	**17.5000 %**	.06	**1.0500 %**
> 12 years to 20 years	**5,000,000**	**2.5000 %**	.10	**0.2500 %**
> 20 years	**0**	**0.000 %**	.12	**0.000 %**
Sum of above equals Alternative Component*				**2.23 %**

*Substitute for standard component if lower.

APPENDIX D – EXAMPLE OF MEMBER BUSINESS LOANS ALTERNATIVE COMPONENT, §702.107(b)
(EXAMPLE CALCULATION IN BOLD)

Remaining maturity	***Dollar balance of MBLs by remaining maturity***	***Percent of total assets by remaining maturity***	*Alternative risk weighting*	***Alternative component***
Fixed-rate MBLs 0 to 3 years	**6,000,000**	**3.0000 %**	.06	**0.1800 %**
> 3 years to 5 years	**4,000,000**	**2.0000 %**	.09	**0.1800 %**
> 5 years to 7 years	**2,000,000**	**1.0000 %**	.12	**0.1200 %**
> 7 years to 12 years	**0**	**0.0000 %**	.14	**0.0000 %**
> 12 years	**0**	**0.0000 %**	.16	**0.0000 %**
Variable-rate MBLs 0 to 3 years	**17,000,000**	**8.5000 %**	.06	**0.5100 %**
> 3 years to 5 years	**4,000,000**	**2.0000 %**	.08	**0.1600 %**
> 5 years to 7 years	**2,000,000**	**1.0000 %**	.10	**0.1000 %**
> 7 years to 12 years	**0**	**0.0000 %**	.12	**0.0000 %**
>12 years	**0**	**0.0000 %**	.14	**0.0000 %**
Sum of above equals Alternative component*				**1.25 %**

* Substitute for standard component if lower.

APPENDIX E -- EXAMPLE OF INVESTMENTS ALTERNATIVE COMPONENT, §702.107(c)

(EXAMPLE CALCULATION IN BOLD)

Weighted-average life	***Dollar balance of investments by weighted-average life***	***Percent of total assets by weighted-average life***	*Alternative risk weighting*	***Alternative component***
0 to 1 year	**24,000,000**	**12.0000 %**	.03	**0.3600 %**
> 1 year to 3 years	**15,000,000**	**7.5000 %**	.06	**0.4500 %**
> 3 years to 5 years	**8,000,000**	**4.0000 %**	.08	**0.3200 %**
> 5 years to 7 years	**1,000,000**	**0.5000 %**	.12	**0.0600 %**
> 7 years to 10 years	**1,000,000**	**0.5000 %**	.16	**0.0800 %**
> 10 years	**1,000,000**	**0.5000 %**	.20	**0.1000 %**
Sum of above equals Alternative component*				**1.37 %**

* Substitute for standard component if lower.

APPENDIX F – EXAMPLE LOANS SOLD WITH RECOURSE ALTERNATIVE COMPONENT, §702.107(d)

(EXAMPLE CALCULATION IN BOLD)

Percent of contractual recourse obligation	***Dollar balance of Loans sold with recourse***	***Percent of total assets***	***Alternative risk weighting***	***Alternative component***
Recourse 6 % or greater	**5,000,000**	**2.5000 %**	.06	**0.1500 %**
Recourse < 6 %	**35,000,000**	**17.5000 %**	.0500 [a/]	**0.8750 %**
Sum of above equals Alternative component*				**1.03 %**

* Substitute for corresponding standard component if lower.

[a/] The credit union must calculate this alternative risk weighting for loans sold with recourse of less than 6 %. For an example computation, see worksheet in Appendix G below.

APPENDIX G –WORKSHEET FOR ALTERNATIVE RISK WEIGHTING OF LOANS SOLD WITH CONTRACTUAL RECOURSE OBLIGATIONS OF LESS THAN 6 %

(EXAMPLE CALCULATION IN BOLD)

Percent of contractual recourse obligation less than 6%	***Dollar balance of loans sold with recourse***	***Dollars of recourse***	***Alternative risk weighting***
5.50 %	**5,000,000**	**275,000**	
5.00 %	**25,000,000**	**1,250,000**	
4.50 %	**5,000,000**	**225,000**	
Sum of above equals	**35,000,000**	**1,750,000**	
Dollar of recourse divided by dollar balance equals (expressed as %)			**5.00 %**

APPENDIX H -- EXAMPLE RBNW REQUIREMENT USING ALTERNATIVE COMPONENTS
(EXAMPLE CALCULATION IN BOLD)

Risk portfolio	***Standard component***	***Alternative component***	***Lower of standard or alternative component***
(a) Long-term real estate loans	**2.20 %**	**2.85 %**	**2.20 %**
(b) MBLs outstanding	**1.10 %**	**1.25 %**	**1.10 %**
(c) Investments	**1.51 %**	**1.37 %**	**1.37 %**
(f) Loans sold with recourse	**1.20%**	**1.03%**	**1.03%**
			Standard component
(d) Low-risk assets			**0 %**
(e) Average-risk assets			**1.53 %**
(g) Unused MBL commitments			**0.15 %**
(h) Allowance			**(1.02) %**
RBNW requirement* Compare to Net Worth Ratio			**6.53 %**

* A credit union is "undercapitalized" if its net worth ratio is less than its applicable RBNW requirement

Subpart B—Mandatory and Discretionary Supervisory Actions

§ 702.201 Prompt corrective action for "adequately capitalized" credit unions.

(a) *Earnings retention.* Beginning the effective date of classification as "adequately capitalized" or lower, a federally-insured credit union must increase the dollar amount of its net worth quarterly either in the current quarter, or on average over the current and three preceding quarters, by an amount equivalent to at least 1/10th percent (0.1%) of its total assets, and must quarterly transfer that amount (or more by choice) from undivided earnings to its regular reserve account until it is "well capitalized."

(b) *Decrease in retention.* Upon written application received no later than 14 days before the quarter end, the NCUA Board, on a case-by-case basis, may permit a credit union to increase the dollar amount of its net worth and quarterly transfer an amount that is less than the amount required under paragraph (a) of this section, to the extent the NCUA Board determines that such lesser amount—

(1) Is necessary to avoid a significant redemption of shares; and

(2) Would further the purpose of this part.

(c) *Decrease by FISCU.* The NCUA Board shall consult and seek to work cooperatively with the appropriate State official before permitting a federally-insured State-chartered credit union to decrease its earnings retention under paragraph (b) of this section.

(d) *Periodic review.* A decision under paragraph (b) of this section to permit a credit union to decrease its earnings retention is subject to quarterly review and revocation except when the credit union is operating under an approved net worth restoration plan that provides for decreasing its earnings retention as provided under paragraph (b).

§ 702.202 Prompt corrective action for "undercapitalized" credit unions

(a) *Mandatory supervisory actions by credit union.* A federally-insured credit union which is "undercapitalized" must—

(1) *Earnings retention.* Increase net worth and transfer earnings to its regular reserve account in accordance with § 702.201;

(2) *Submit net worth restoration plan.* Submit a net worth restoration plan pursuant to § 702.206, *provided however,* that a credit union in this category having a net worth ratio of less

than five percent (5%) which fails to timely submit such a plan, or which materially fails to implement an approved plan, is classified "significantly undercapitalized" pursuant to § 702.102(a)(4)(ii) above;

(3) *Restrict increase in assets.* Beginning the effective date of classification as "undercapitalized" or lower, not permit the credit union's assets to increase beyond its total assets (per § 702.2(j)) for the preceding quarter unless—

(i) *Plan approved.* The NCUA Board has approved a net worth restoration plan which provides for an increase in total assets and—

(A) The assets of the credit union are increasing consistent with the approved plan; and

(B) The credit union is implementing steps to increase the net worth ratio consistent with the approved plan;

(ii) *Plan not approved.* The NCUA Board has not approved a net worth restoration plan and total assets of the credit union are increasing because of increases since quarter-end in balances of:

(A) Total accounts receivable and accrued income on loans and investments; or

(B) Total cash and cash equivalents; or

(C) Total loans outstanding, not to exceed the sum of total assets (per § 702.2(j)) plus the quarter-end balance of unused commitments to lend and unused lines of credit provided however that a credit union which increases a balance as permitted under paragraphs (A), (B) or (C) cannot offer rates on shares in excess of prevailing rates on shares in its relevant market area, and cannot open new branches;

(4) *Restrict member business loans.* Beginning the effective date of classification as "undercapitalized" or lower, not increase the total dollar amount of member business loans (defined as loans outstanding and unused commitments to lend) as of the preceding quarter-end unless it is granted an exception under 12 U.S.C. 1757a(b).

(b) *"Second tier" discretionary supervisory actions by NCUA.* Subject to the applicable procedures for issuing, reviewing and enforcing directives set forth in subpart L of part 747 of this chapter, the NCUA Board may, by directive, take one or more of the following actions with respect to an "undercapitalized" credit union having a net worth ratio of less than five percent (5%), or a director, officer or employee of such a credit union, if it determines that those actions are necessary to carry out the purpose of this part:

(1) *Requiring prior approval for acquisitions, branching, new lines of business.* Prohibit a credit union from, directly or indirectly, acquiring any interest in any business entity or financial institution, establishing or acquiring any additional branch office, or engaging in any new line of business, unless the NCUA Board has approved the credit union's net worth restoration plan, the credit union is implementing its plan, and the NCUA Board determines that the proposed action is consistent with and will further the objectives of that plan;

(2) *Restricting transactions with and ownership of CUSO.* Restrict the credit union's transactions with a CUSO, or require the credit union to reduce or divest its ownership interest in a CUSO;

(3) *Restricting dividends paid.* Restrict the dividend rates the credit union pays on shares to the prevailing rates paid on comparable accounts and maturities in the relevant market area, as determined by the NCUA Board, except that dividend rates already declared on shares acquired before imposing a restriction under this paragraph may not be retroactively restricted;

(4) *Prohibiting or reducing asset growth.* Prohibit any growth in the credit union's assets or in a category of assets, or require the credit union to reduce its assets or a category of assets;

(5) *Alter, reduce or terminate activity.* Require the credit union or its CUSO to alter, reduce, or terminate any activity which poses excessive risk to the credit union;

(6) *Prohibiting nonmember deposits.* Prohibit the credit union from accepting all or certain nonmember deposits;

(7) *Dismissing director or senior executive officer.* Require the credit union to dismiss from office any director or senior executive officer, *provided however,* that a dismissal under this clause shall not be construed to be a formal administrative action for removal under 12 U.S.C. 1786(g);

(8) *Employing qualified senior executive officer.* Require the credit union to employ qualified senior executive officers (who, if the NCUA Board so specifies, shall be subject to its approval); and

(9) *Other action to carry out prompt corrective action.* Restrict or require such other action by the credit union as the NCUA Board deter-

mines will carry out the purpose of this part better than any of the actions prescribed in paragraphs (b)(1) through (8) of this section.

(c) *"First tier" application of discretionary supervisory actions.* An "undercapitalized" credit union having a net worth ratio of five percent (5%) or more, or which is classified "undercapitalized" by reason of failing to satisfy a risk-based net worth requirement under § 702.105 or 702.106, is subject to the discretionary supervisory actions in paragraph (b) of this section if it fails to comply with any mandatory supervisory action in paragraph (a) of this section or fails to timely implement an approved net worth restoration plan under § 702.206, including meeting its prescribed steps to increase its net worth ratio.

§ 702.203 Prompt corrective action for "significantly undercapitalized" credit unions.

(a) *Mandatory supervisory actions by credit union.* A federally-insured credit union which is "significantly undercapitalized" must—

(1) *Earnings retention.* Increase net worth and transfer earnings to its regular reserve account in accordance with § 702.201;

(2) *Submit net worth restoration plan.* Submit a net worth restoration plan pursuant to § 702.206;

(3) *Restrict increase in assets.* Not permit the credit union's total assets to increase except as provided in § 702.202(a)(3) and

(4) *Restrict member business loans.* Not increase the total dollar amount of member business loans (defined as loans outstanding and unused commitments to lend) as provided in § 702.202(a)(4).

(b) *Discretionary supervisory actions by NCUA.* Subject to the applicable procedures for issuing, reviewing and enforcing directives set forth in subpart L of part 747 of this chapter, the NCUA Board may, by directive, take one or more of the following actions with respect to any "significantly undercapitalized" credit union, or a director, officer or employee of such credit union, if it determines that those actions are necessary to carry out the purpose of this part:

(1) *Requiring prior approval for acquisitions, branching, new lines of business.* Prohibit a credit union from, directly or indirectly, acquiring any interest in any business entity or financial institution, establishing or acquiring any additional branch office, or engaging in any new line of business, except as provided in § 702.202(b)(1);

(2) *Restricting transactions with and ownership of CUSO.* Restrict the credit union's transactions with a CUSO, or require the credit union to divest or reduce its ownership interest in a CUSO;

(3) *Restricting dividends paid.* Restrict the dividend rates that the credit union pays on shares as provided in § 702.202(b)(3);

(4) *Prohibiting or reducing asset growth.* Prohibit any growth in the credit union's assets or in a category of assets, or require the credit union to reduce assets or a category of assets;

(5) *Alter, reduce or terminate activity.* Require the credit union or its CUSO(s) to alter, reduce, or terminate any activity which poses excessive risk to the credit union;

(6) *Prohibiting nonmember deposits.* Prohibit the credit union from accepting all or certain nonmember deposits;

(7) *New election of directors.* Order a new election of the credit union's board of directors;

(8) *Dismissing director or senior executive officer.* Require the credit union to dismiss from office any director or senior executive officer, *provided however,* that a dismissal under this clause shall not be construed to be a formal administrative action for removal under 12 U.S.C. 1786(g);

(9) *Employing qualified senior executive officer.* Require the credit union to employ qualified senior executive officers (who, if the NCUA Board so specifies, shall be subject to its approval);

(10) *Restricting senior executive officers' compensation.* Except with the prior written approval of the NCUA Board, limit compensation to any senior executive officer to that officer's average rate of compensation (excluding bonuses and profit sharing) during the four (4) calendar quarters preceding the effective date of classification of the credit union as "significantly undercapitalized," and prohibit payment of a bonus or profit share to such officer;

(11) *Other actions to carry out prompt corrective action.* Restrict or require such other action by the credit union as the NCUA Board determines will carry out the purpose of this part better than any of the actions prescribed in paragraphs (b)(1) through (10) of this section; and

(12) *Requiring merger.* Require the credit union to merge with another financial institution if one or more grounds exist for placing the

credit union into conservatorship pursuant to 12 U.S.C. 1786(h)(1)(F), or into liquidation pursuant to 12 U.S.C. 1787(a)(3)(A)(i).

(c) *Discretionary conservatorship or liquidation if no prospect of becoming "adequately capitalized."* Notwithstanding any other actions required or permitted to be taken under this section, when a credit union becomes "significantly undercapitalized" (including by reclassification under section 702.102(b) above), the NCUA Board may place the credit union into conservatorship pursuant to 12 U.S.C. 1786(h)(1)(F), or into liquidation pursuant to 12 U.S.C. 1787(a)(3)(A)(i), provided that the credit union has no reasonable prospect of becoming "adequately capitalized."

§ 702.204 Prompt corrective action for "critically undercapitalized" credit unions

(a) *Mandatory supervisory actions by credit union.* A federally-insured credit union which is "critically undercapitalized" must—

(1) *Earnings retention.* Increase net worth and transfer earnings to its regular reserve account in accordance with § 702.201;

(2) *Submit net worth restoration plan.* Submit a net worth restoration plan pursuant to § 702.206;

(3) *Restrict increase in assets.* Not permit the credit union's total assets to increase except as provided in § 702.202(a)(3); and

(4) *Restrict member business loans.* Not increase the total dollar amount of member business loans (defined as loans outstanding and unused commitments to lend) as provided in § 702.202(a)(4).

(b) *Discretionary supervisory actions by NCUA.* Subject to the applicable procedures for issuing, reviewing and enforcing directives set forth in subpart L of part 747 of this chapter, the NCUA Board may, by directive, take one or more of the following actions with respect to any "critically undercapitalized" credit union, or a director, officer or employee of such credit union, if it determines that those actions are necessary to carry out the purpose of this part:

(1) *Requiring prior approval for acquisitions, branching, new lines of business.* Prohibit a credit union from, directly or indirectly, acquiring any interest in any business entity or financial institution, establishing or acquiring any additional branch office, or engaging in any new line of business, except as provided by § 702.202(b)(1);

(2) *Restricting transactions with and ownership of CUSO.* Restrict the credit union's transactions with a CUSO, or require the credit union to divest or reduce its ownership interest in a CUSO;

(3) *Restricting dividends paid.* Restrict the dividend rates that the credit union pays on shares as provided in § 702.202(b)(3);

(4) *Prohibiting or reducing asset growth.* Prohibit any growth in the credit union's assets or in a category of assets, or require the credit union to reduce assets or a category of assets;

(5) *Alter, reduce or terminate activity.* Require the credit union or its CUSO(s) to alter, reduce, or terminate any activity which poses excessive risk to the credit union;

(6) *Prohibiting nonmember deposits.* Prohibit the credit union from accepting all or certain nonmember deposits;

(7) *New election of directors.* Order a new election of the credit union's board of directors;

(8) *Dismissing director or senior executive officer.* Require the credit union to dismiss from office any director or senior executive officer, *provided however,* that a dismissal under this clause shall not be construed to be a formal administrative action for removal under 12 U.S.C. 1786(g);

(9) *Employing qualified senior executive officer.* Require the credit union to employ qualified senior executive officers (who, if the NCUA Board so specifies, shall be subject to its approval);

(10) *Restricting senior executive officers' compensation.* Reduce or, with the prior written approval of the NCUA Board, limit compensation to any senior executive officer to that officer's average rate of compensation (excluding bonuses and profit sharing) during the four (4) calendar quarters preceding the effective date of classification of the credit union as "critically undercapitalized," and prohibit payment of a bonus or profit share to such officer;

(11) *Restrictions on payments on uninsured secondary capital.* Beginning 60 days after the effective date of classification of a credit union as "critically undercapitalized," prohibit payments of principal, dividends or interest on the credit union's uninsured secondary capital accounts established after August 7, 2000, except that unpaid dividends or interest shall continue to accrue under the terms of the account to the extent permitted by law;

(12) *Requiring prior approval.* Require a "critically undercapitalized" credit union to obtain the NCUA Board's prior written approval before doing any of the following:

(i) Entering into any material transaction not within the scope of an approved net worth restoration plan (or approved revised business plan under subpart C of this part);

(ii) Extending credit for transactions deemed highly leveraged by the NCUA Board or, if State-chartered, by the appropriate State official;

(iii) Amending the credit union's charter or bylaws, except to the extent necessary to comply with any law, regulation, or order;

(iv) Making any material change in accounting methods; and

(v) Paying dividends or interest on new share accounts at a rate exceeding the prevailing rates of interest on insured deposits in its relevant market area;

(13) *Other action to carry out prompt corrective action.* Restrict or require such other action by the credit union as the NCUA Board determines will carry out the purpose of this part better than any of the actions prescribed in paragraphs (b)(1) through (12) of this section; and

(14) *Requiring merger.* Require the credit union to merge with another financial institution if one or more grounds exist for placing the credit union into conservatorship pursuant to 12 U.S.C. 1786(h)(1)(F), or into liquidation pursuant to 12 U.S.C. 1787(a)(3)(A)(i).

(c) *Mandatory conservatorship, liquidation or action in lieu thereof*—(1) *Action within 90 days.* Notwithstanding any other actions required or permitted to be taken under this section (and regardless of a credit union's prospect of becoming "adequately capitalized"), the NCUA Board must, within 90 calendar days after the effective date of classification of a credit union as "critically undercapitalized"—

(i) *Conservatorship.* Place the credit union into conservatorship pursuant to 12 U.S.C. 1786(h)(1)(G); or

(ii) *Liquidation.* Liquidate the credit union pursuant to 12 U.S.C. 1787(a)(3)(A)(ii); or

(iii) *Other corrective action.* Take other corrective action, in lieu of conservatorship or liquidation, to better achieve the purpose of this part, provided that the NCUA Board documents why such action in lieu of conservatorship or liquidation would do so, *provided however,* that other corrective action may consist, in whole or in part, of complying with the quarterly timetable of steps and meeting the quarterly net worth targets prescribed in an approved net worth restoration plan.

(2) *Renewal of other corrective action.* A determination by the NCUA Board to take other corrective action in lieu of conservatorship or liquidation under paragraph (c)(1)(iii) of this section shall expire after an effective period ending no later than 180 calendar days after the determination is made, and the credit union shall be immediately placed into conservatorship or liquidation under paragraphs (c)(1)(i) and (ii), unless the NCUA Board makes a new determination under paragraph (c)(1)(iii) of this section before the end of the effective period of the prior determination;

(3) *Mandatory liquidation after 18 months*—(i) *Generally.* Notwithstanding paragraphs (c)(1) and (2) of this section, the NCUA Board must place a credit union into liquidation if it remains "critically undercapitalized" for a full calendar quarter, on a monthly average basis, following a period of 18 months from the effective date the credit union was first classified "critically undercapitalized."

(ii) *Exception.* Notwithstanding paragraph (c)(3)(i) of this section, the NCUA Board may continue to take other corrective action in lieu of liquidation if it certifies that the credit union—

(A) Has been in substantial compliance with an approved net worth restoration plan requiring consistent improvement in net worth since the date the net worth restoration plan was approved;

(B) Has positive net income or has an upward trend in earnings that the NCUA Board projects as sustainable; and

(C) Is viable and not expected to fail.

(iii) *Review of exception.* The NCUA Board shall, at least quarterly, review the certification of an exception to liquidation under paragraph (c)(3)(ii) of this section and shall either—

(A) Recertify the credit union if it continues to satisfy the criteria of paragraph (c)(3)(ii) of this section; or

(B) Promptly place the credit union into liquidation, pursuant to 12 U.S.C. 1787(a)(3)(A)(ii), if it fails to satisfy the criteria of paragraph (c)(3)(ii) of this section.

(4) *Nondelegation.* The NCUA Board may not delegate its authority under paragraph (c) of this section, unless the credit union has less

than $5,000,000 in total assets. A credit union shall have a right of direct appeal to the NCUA Board of any decision made by delegated authority under this section within ten (10) calendar days of the date of that decision.

(d) *Mandatory liquidation of insolvent federal credit union.* In lieu of paragraph (c) of this section, a "critically undercapitalized" federal credit union that has a net worth ratio of less than zero percent (0%) may be placed into liquidation on grounds of insolvency pursuant to 12 U.S.C. 1787(a)(1)(A).

§ 702.205 Consultation with State officials on proposed prompt corrective action.

(a) *Consultation on proposed conservatorship or liquidation.* Before placing a federally-insured State-chartered credit union into conservatorship (pursuant to 12 U.S.C. 1786(h)(1)(F) or (G)) or liquidation (pursuant to 12 U.S.C. 1787(a)(3)) as permitted or required under subparts B or C of this part to facilitate prompt corrective action—

(1) The NCUA Board shall seek the views of the appropriate State official (as defined in § 702.2(b), and give him or her an opportunity to take the proposed action;

(2) The NCUA Board shall, upon timely request of the appropriate State official, promptly provide him or her with a written statement of the reasons for the proposed conservatorship or liquidation, and reasonable time to respond to that statement; and

(3) If the appropriate State official makes a timely written response that disagrees with the proposed conservatorship or liquidation and gives reasons for that disagreement, the NCUA Board shall not place the credit union into conservatorship or liquidation unless it first considers the views of the appropriate State official and determines that—

(i) The NCUSIF faces a significant risk of loss if the credit union is not placed into conservatorship or liquidation; and

(ii) Conservatorship or liquidation is necessary either to reduce the risk of loss, or to reduce the expected loss, to the NCUSIF with respect to the credit union.

(b) *Nondelegation.* The NCUA Board may not delegate any determination under paragraph (a)(3) of this section.

(c) *Consultation on proposed discretionary action.* The NCUA Board shall consult and seek to work cooperatively with the appropriate State official before taking any discretionary supervisory action under §§ 702.202(b), 702.203(b), 702.204(b), 702.304(b) and 702.305(b) with respect to a federally-insured State-chartered credit union; shall provide prompt notice of its decision to the appropriate State official; and shall allow the appropriate State official to take the proposed action independently or jointly with NCUA.

§ 702.206 Net worth restoration plans.

(a) *Schedule for filing*—(1) *Generally.* A federally-insured credit union shall file a written net worth restoration plan (NWRP) with the appropriate Regional Director and, if State-chartered, the appropriate State official, within 45 calendar days of the effective date of classification as either "undercapitalized," "significantly undercapitalized" or "critically undercapitalized," unless the NCUA Board notifies the credit union in writing that its NWRP is to be filed within a different period.

(2) *Exception.* An otherwise "adequately capitalized" credit union that is reclassified "undercapitalized" on safety and soundness grounds under § 702.102(b) is not required to submit a NWRP solely due to the reclassification, unless the NCUA Board notifies the credit union that it must submit an NWRP.

(3) *Filing of additional plan.* Notwithstanding paragraph (a)(1) of this section, a credit union that has already submitted and is operating under a NWRP approved under this section is not required to submit an additional NWRP due to a change in net worth category (including by reclassification under § 702.102(b)), unless the NCUA Board notifies the credit union that it must submit a new NWRP. A credit union that is notified to submit a new or revised NWRP shall file the NWRP in writing with the appropriate Regional Director within 30 calendar days of receiving such notice, unless the NCUA Board notifies the credit union in writing that the NWRP is to be filed within a different period.

(4) *Failure to timely file plan.* When a credit union fails to timely file an NWRP pursuant to this paragraph, the NCUA Board shall promptly notify the credit union that it has failed to file an NWRP and that it has 15 calendar days from receipt of that notice within which to file an NWRP.

(b) *Assistance to small credit unions.* Upon timely request by a credit union having total assets of less than $10 million (regardless how long it has been in operation), the NCUA Board shall provide assistance in preparing an NWRP required to be filed under paragraph (a) of this section.

(c) *Contents of NWRP.* An NWRP must—

(1) Specify—

(i) A quarterly timetable of steps the credit union will take to increase its net worth ratio so that it becomes "adequately capitalized" by the end of the term of the NWRP, and to remain so for four (4) consecutive calendar quarters. If "complex," the credit union is subject to a risk-based net worth requirement that may require a net worth ratio higher than six percent (6%) to become "adequately capitalized";

(ii) The projected amount of earnings to be transferred to the regular reserve account in each quarter of the term of the NWRP as required under § 702.201(a), or as permitted under § 702.201(b);

(iii) How the credit union will comply with the mandatory and any discretionary supervisory actions imposed on it by the NCUA Board under this subpart;

(iv) The types and levels of activities in which the credit union will engage; and

(v) If reclassified to a lower category under § 702.102(b), the steps the credit union will take to correct the unsafe or unsound practice(s) or condition(s);

(2) Include pro forma financial statements, including any off-balance sheet items, covering a minimum of the next two years; and

(3) Contain such other information as the NCUA Board has required.

(d) *Criteria for approval of NWRP.* The NCUA Board shall not accept a NWRP plan unless it—

(1) Complies with paragraph (c) of this section;

(2) Is based on realistic assumptions, and is likely to succeed in restoring the credit union's net worth; and (3) Would not unreasonably increase the credit union's exposure to risk (including credit risk, interest-rate risk, and other types of risk).

(e) *Consideration of regulatory capital.* To minimize possible long-term losses to the NCUSIF while the credit union takes steps to become "adequately capitalized," the NCUA Board shall, in evaluating an NWRP under this section, consider the type and amount of any form of regulatory capital which may become established by NCUA regulation, or authorized by State law and recognized by NCUA, which the credit union holds, but which is not included in its net worth.

(f) *Review of NWRP*—(1) *Notice of decision.* Within 45 calendar days after receiving an NWRP under this part, the NCUA Board shall notify the credit union in writing whether the NWRP has been approved, and shall provide reasons for its decision in the event of disapproval.

(2) *Delayed decision.* If no decision is made within the time prescribed in paragraph (f)(1) of this section, the NWRP is deemed approved.

(3) *Consultation with State officials.* In the case of an NWRP submitted by a federally-insured State-chartered credit union (whether an original, new, additional, revised or amended NWRP), the NCUA Board shall, when evaluating the NWRP, seek and consider the views of the appropriate State official, and provide prompt notice of its decision to the appropriate State official.

(g) *NWRP not approved* (1) *Submission of revised NWRP.* If an NWRP is rejected by the NCUA Board, the credit union shall submit a revised NWRP within 30 calendar days of receiving notice of disapproval, unless it is notified in writing by the NCUA Board that the revised NWRP is to be filed within a different period.

(2) *Notice of decision on revised NWRP.* Within 30 calendar days after receiving a revised NWRP under paragraph (g)(1) of this section, the NCUA Board shall notify the credit union in writing whether the revised NWRP is approved. The Board may extend the time within which notice of its decision shall be provided.

(3) *Disapproval of reclassified credit union's NWRP.* A credit union which has been classified "significantly undercapitalized" under § 702.102(a)(4)(ii) shall remain so classified pending NCUA Board approval of a new or revised NWRP.

(h) *Amendment of NWRP.* A credit union that is operating under an approved NWRP may, after prior written notice to, and approval by the NCUA Board, amend its NWRP to reflect a change in circumstance. Pending approval of an amended NWRP, the credit union shall implement the NWRP as originally approved.

(i) *Publication.* An NWRP need not be published to be enforceable because publication would be contrary to the public interest.

Subpart C—Alternative Prompt Corrective Action for New Credit Unions

§ 702.301 Scope and definition.

(a) *Scope.* This subpart C applies in lieu of subpart B of this part exclusively to credit unions defined in paragraph (b) of this section as "new" pursuant to 12 U.S.C. 1790d(b)(2).

(b) *New credit union defined.* A "new" credit union for purposes of this subpart is a federally-insured credit union that both has been in operation for less than ten (10) years and has total assets of not more than $10 million. A credit union which exceeds $10 million in total assets may become "new" if its total assets subsequently decline below $10 million while it is still in operation for less than 10 years.

(c) *Effect of spin-offs.* A credit union formed as the result of a "spin-off" of a group from the field of membership of an existing credit union is deemed to be in operation since the effective date of the "spin-off." A credit union whose total assets decline below $10 million because a group within its field of membership has been "spun-off" is deemed "new" if it has been in operation less than 10 years.

(d) *Actions to evade prompt corrective action.* If the NCUA Board determines that a credit union was formed, or was reduced in asset size as a result of a "spin-off," or was merged, primarily to qualify as "new" under this subpart, the credit union shall be deemed subject to prompt corrective action under subpart A of this part.

§ 702.302 Net worth categories for new credit unions.

(a) *Net worth measures.* For purposes of this part, a new credit union must determine its net worth category classification quarterly according to its net worth ratio as defined in § 702.2(g).

(b) *Effective date of net worth classification of new credit union.* For purposes of subpart C, the effective date of a new federally-insured credit union's classification within a net worth category in paragraph (c) of this section shall be determined as provided in § 702.101(b); and written notice to the NCUA Board of a decline in net worth category in paragraph (c) of this section shall be given as required by section 702.101(c).

(c) *Net worth categories.* A federally-insured credit union defined as "new" under this section shall be classified (Table 6)—

(1) *Well capitalized* if it has a net worth ratio of seven percent (7%) or greater;

(2) *Adequately capitalized* if it has a net worth ratio of six percent (6%) or more but less than seven percent (7%);

(3) *Moderately capitalized* if it has a net worth ratio of three and one-half percent (3.5%) or more but less than six percent (6%);

(4) *Marginally capitalized* if it has a net worth ratio of two percent (2%) or more but less than three and one-half percent (3.5%);

(5) *Minimally capitalized* if it has a net worth ratio of zero percent (0%) or greater but less than two percent (2%); and

(6) *Uncapitalized* if it has a net worth ratio of less than zero percent (0%) (*e.g.,* a deficit in retained earnings).

TABLE 6 -- NET WORTH CATEGORY CLASSIFICATION FOR "NEW" CREDIT UNIONS

A "new" credit union's net worth category is . . .	*if its net worth ratio is . . .*
"Well Capitalized"	7% or above
"Adequately Capitalized"	6% to 6.99%
"Moderately Capitalized"	3.5% to 5.99%
"Marginally Capitalized"	2% to 3.49%
"Minimally Capitalized"	0% to 1.99%
"Uncapitalized"	Less than 0%

(d) *Reclassification based on supervisory criteria other than net worth.* Subject to § 702.102(b) and (c), the NCUA Board may reclassify a "well capitalized," "adequately capitalized" or "moderately capitalized" new credit union to the next lower net worth category (each of such actions is hereinafter referred to generally as "reclassification") in either of the circumstances prescribed in § 702.102(b).

(e) *Consultation with State officials.* The NCUA Board shall consult and seek to work cooperatively with the appropriate State official before reclassifying a federally-insured State-chartered credit union under paragraph (d) of this section, and shall promptly notify the appropriate State official of its decision to reclassify.

§ 702.303 Prompt corrective action for "adequately capitalized" new credit unions.

Beginning on the effective date of classification, an "adequately capitalized" new credit union must increase the dollar amount of its net worth by the amount reflected in its approved initial or revised business plan in accordance with § 702.304(a)(2), or in the absence of such a plan, in accordance with § 702.201, and quarterly transfer that amount from undivided earnings to its regular reserve account, until it is "well capitalized."

§ 702.304 Prompt corrective action for "moderately capitalized," "marginally capitalized" or "minimally capitalized" new credit unions.

(a) *Mandatory supervisory actions by new credit union.* Beginning on the date of classification as "moderately capitalized," "marginally capitalized" or "minimally capitalized" (including by reclassification under § 702.302(d)), a new credit union must—

(1) *Earnings retention.* Increase the dollar amount of its net worth by the amount reflected in its approved initial or revised business plan and quarterly transfer that amount from undivided earnings to its regular reserve account;

(2) *Submit revised business plan.* Submit a revised business plan within the time provided by § 702.306 if the credit union either:

(i) Has not increased its net worth ratio consistent with its then-present approved business plan;

(ii) Has no then-present approved business plan; or

(iii) Has failed to comply with paragraph (a)(3) of this section; and

(3) *Restrict member business loans.* Not increase the total dollar amount of member business loans (defined as loans outstanding and unused commitments to lend) as of the preceding quarter-end unless it is granted an exception under 12 U.S.C. 1757a(b).

(b) *Discretionary supervisory actions by NCUA.* Subject to the applicable procedures set forth in subpart L of part 747 of this chapter for issuing, reviewing and enforcing directives, the NCUA Board may, by directive, take one or more of the actions prescribed in § 702.204(b) if the credit union's net worth ratio has not increased consistent with its then-present business plan, or the credit union has failed to undertake any mandatory supervisory action prescribed in paragraph (a) of this section.

(c) *Discretionary conservatorship or liquidation.* Notwithstanding any other actions required or permitted to be taken under this section, the NCUA Board may place a new credit union which is "moderately capitalized," "marginally capitalized" or "minimally capitalized" (including by reclassification under § 702.302(d)) into conservatorship pursuant to 12 U.S.C. 1786(h)(1)(F), or into liquidation pursuant to 12 U.S.C. 1787(a)(3)(A)(i), provided that the credit union has no reasonable prospect of becoming "adequately capitalized."

§ 702.305 Prompt corrective action for "uncapitalized" new credit unions.

(a) *Mandatory supervisory actions by new credit union.* Beginning on the effective date of classification as "uncapitalized," a new credit union must—

(1) *Earnings retention.* Increase the dollar amount of its net worth by the amount reflected in the credit union's approved initial or revised business plan;

(2) *Submit revised business plan.* Submit a revised business plan within the time provided by § 702.306, providing for alternative means of funding the credit union's earnings deficit, if the credit union either:

(i) Has not increased its net worth ratio consistent with its then-present approved business plan;

(ii) Has no then-present approved business plan; or

(iii) Has failed to comply with paragraph (a)(3) of this section; and

(3) *Restrict member business loans.* Not increase the total dollar amount of member business loans as provided in § 702.304(a)(3).

(b) *Discretionary supervisory actions by NCUA.* Subject to the procedures set forth in subpart L of part 747 of this chapter for issuing, reviewing and enforcing directives, the NCUA Board may, by directive, take one or more of the actions prescribed in § 702.204(b) if the credit union's net worth ratio has not increased consistent with its then-present business plan, or the credit union has failed to undertake any mandatory supervisory action prescribed in paragraph (a) of this section.

(c) *Mandatory liquidation or conservatorship.* Notwithstanding any other actions required or permitted to be taken under this section, the NCUA Board—

(1) *Plan not submitted.* May place into liquidation pursuant to 12 U.S.C. 1787(a)(3)(A)(ii), or conservatorship pursuant to 12 U.S.C. 1786(h)(1)(F), an "uncapitalized" new credit union which fails to submit a revised business plan within the time provided under paragraph (a)(2) of this section; or

(2) *Plan rejected, approved, implemented.* Except as provided in paragraph (c)(3) of this section, must place into liquidation pursuant to 12 U.S.C. 1787(a)(3)(A)(ii), or conservatorship pursuant to 12 U.S.C. 1786(h)(1)(F), an "uncapitalized" new credit union that remains "uncapitalized" one hundred twenty (120) calendar days after the later of:

(i) The effective date of classification as "uncapitalized"; or

(ii) The last day of the calendar month following expiration of the time period provided in the credit union's initial business plan (approved at the time its charter was granted) to remain "uncapitalized," regardless whether a revised business plan was rejected, approved or implemented.

(3) *Exception.* The NCUA Board may decline to place a new credit union into liquidation or conservatorship as provided in paragraph (c)(2) of this section if the credit union documents to the NCUA Board why it is viable and has a reasonable prospect of becoming "adequately capitalized."

(d) *Mandatory liquidation of "uncapitalized" federal credit union.* In lieu of paragraph (c) of this section, an "uncapitalized" federal credit union may be placed into liquidation on grounds of insolvency pursuant to 12 U.S.C. 1787(a)(1)(A).

§ 702.306 Revised business plans for new credit unions.

(a) *Schedule for filing.* (1) *Generally.* Except as provided in paragraph (a)(2) of this section, a new credit union classified "moderately capitalized" or lower must file a written revised business plan (RBP) with the appropriate Regional Director and, if State-chartered, with the appropriate State official, within 30 calendar days of either:

(i) The last of the calendar month following the end of the calendar quarter that the credit union's net worth ratio has not increased consistent with its the-present approved business plan;

(ii) The effective date of classification as less than "adequately capitalized" if the credit union has no then-present approved business plan; or

(iii) The effective date of classification as less than "adequately capitalized" if the credit union has increased the total amount of member business loans in violation of § 702.304(a)(3).

(2) *Exception.* The NCUA Board may notify the credit union in writing that its RBP is to be filed within a different period or that it is not necessary to file an RBP.

(3) *Failure to timely file plan.* When a new credit union fails to file an RBP as provided under paragraphs (a)(1) or (a)(2) of this section, the NCUA Board shall promptly notify the credit union that it has failed to file an RBP and that it has 15 calendar days from receipt of that notice within which to do so.

(b) *Contents of revised business plan.* A new credit union's RBP must, at a minimum—

(1) Address changes, since the new credit union's current business plan was approved, in any of the business plan elements required for charter approval under Chapter 1, section IV.D. of NCUA's *Chartering and Field of Membership Manual* (IRPS 99–1), 63 FR 71998, 72019 (Dec. 30, 1998), or its successor(s), or for State-chartered credit unions under applicable State law;

(2) Establish a timetable of quarterly targets for net worth during each year in which the RBP is in effect so that the credit union becomes "adequately capitalized" by the time it no longer qualifies as "new" per § 702.301(b);

(3) Specify the projected amount of earnings to be transferred quarterly to its regular reserve as provided under § 702.304(a)(1) or 702.305(a)(1);

(4) Explain how the new credit union will comply with the mandatory and discretionary supervisory actions imposed on it by the NCUA Board under this subpart;

(5) Specify the types and levels of activities in which the new credit union will engage;

(6) In the case of a new credit union reclassified to a lower category under § 702.302(d), specify the steps the credit union will take to correct the unsafe or unsound condition or practice; and

(7) Include such other information as the NCUA Board may require.

(c) *Criteria for approval.* The NCUA Board shall not approve a new credit union's RBP unless it—

(1) Addresses the items enumerated in paragraph (b) of this section;

(2) Is based on realistic assumptions, and is likely to succeed in building the credit union's net worth; and

(3) Would not unreasonably increase the credit union's exposure to risk (including credit risk, interest-rate risk, and other types of risk).

(d) *Consideration of regulatory capital.* To minimize possible long-term losses to the NCUSIF while the credit union takes steps to become "adequately capitalized," the NCUA Board shall, in evaluating an RBP under this section, consider the type and amount of any form of regulatory capital which may become established by NCUA regulation, or authorized by State law and recognized by NCUA, which the credit union holds, but which is not included in its net worth.

(e) *Review of revised business plan*— (1) *Notice of decision.* Within 30 calendar days after receiving an RBP under this section, the NCUA Board shall notify the credit union in writing whether its RBP is approved, and shall provide reasons for its decision in the event of disapproval. The NCUA Board may extend the time within which notice of its decision shall be provided.

(2) *Delayed decision.* If no decision is made within the time prescribed in paragraph (e)(1) of this section, the RBP is deemed approved.

(3) *Consultation with State officials.* When evaluating an RBP submitted by a federally-insured State-chartered new credit union (whether an original, new or additional RBP), the NCUA Board shall seek and consider the views of the appropriate State official, and provide prompt notice of its decision to the appropriate State official.

(f) *Plan not approved*—(1) *Submission of new revised plan.* If an RBP is rejected by the NCUA Board, the new credit union shall submit a new RBP within 30 calendar days of receiving notice of disapproval of its initial RBP, unless it is notified in writing by the NCUA Board that the new RBP is to be filed within a different period.

(2) *Notice of decision on revised plan.* Within 30 calendar days after receiving an RBP under paragraph (f)(1) of this section, the NCUA Board shall notify the credit union in writing whether the new RBP is approved. The Board may extend the time within which notice of its decision shall be provided.

(g) *Amendment of plan.* A credit union that has filed an approved RBP may, after prior written notice to and approval by the NCUA Board, amend it to reflect a change in circumstance. Pending approval of an amended RBP, the new credit union shall implement its existing RBP as originally approved.

(h) *Publication.* An RBP need not be published to be enforceable because publication would be contrary to the public interest.

§ 702.307 Incentives for new credit unions.

(a) *Assistance in revising business plans.* Upon timely request by a credit union having total assets of less than $10 million (regardless how long it has been in operation), the NCUA Board shall provide assistance in preparing a revised business plan required to be filed under § 702.306.

(b) *Assistance.* Management training and other assistance to new credit unions will be provided in accordance with policies approved by the NCUA Board.

(c) *Small credit union program.* A new credit union is eligible to join and receive comprehensive benefits and assistance under NCUA's Small Credit Union Program.

Subpart D—Reserves

§ 702.401 Reserves.

(a) *Special reserve.* Each federally-insured credit union shall establish and maintain such reserves as may be required by the FCUA, by state law, by regulation, or in special cases by the NCUA Board or appropriate State official.

(b) *Regular reserve.* Each federally-insured credit union shall establish and maintain a regular reserve account for the purpose of absorbing losses that exceed undivided earnings and other appropriations of undivided earnings, subject to paragraph (c) of this section. Earnings required to be transferred annually to a credit union's regular reserve under subparts B or C of this part shall be held in this account.

(c) *Charges to regular reserve after depleting undivided earnings.* The board of directors of a federally-insured credit union may authorize losses to be charged to the regular reserve after first depleting the balance of the undivided earnings account and other reserves, provided that the authorization states the amount and provides an explanation of the need for the charge, and either—

(1) The charge will not cause the credit union's net worth classification to fall below "adequately capitalized" under subparts B or C of this part; or

(2) If the charge will cause the net worth classification to fall below "adequately capitalized," the appropriate Regional Director and, if State-chartered, the appropriate State official, have given written approval (in an NWRP or otherwise) for the charge.

(d) *Transfers to regular reserve.* The transfer of earnings to a federally-insured credit union's regular reserve account when required under subparts B or C of this part must occur after charges for loan or other losses are addressed as provided in paragraph (c) of this section and § 702.402(d), but before payment of any dividends to members.

§ 702.402 Full and fair disclosure of financial condition.

(a) *Full and fair disclosure defined.* "Full and fair disclosure" is the level of disclosure which a prudent person would provide to a member of a federally-insured credit union, to NCUA, or, at the discretion of the board of directors, to creditors to fairly inform them of the financial condition and the results of operations of the credit union.

(b) *Full and fair disclosure implemented.* The financial statements of a federally-insured credit union shall provide for full and fair disclosure of all assets, liabilities, and members' equity, including such valuation (allowance) accounts as may be necessary to present fairly the financial condition; and all income and expenses necessary to present fairly the statement of income for the reporting period.

(c) *Declaration of officials.* The Statement of Financial Condition, when presented to members, to creditors or to the NCUA, shall contain a dual declaration by the treasurer and the chief executive officer, or in the latter's absence, by any other officer designated by the board of directors of the reporting credit union to make such declaration, that the report and related financial statements are true and correct to the best of their knowledge and belief and present fairly the financial condition and the statement of income for the period covered.

(d) *Charges for loan losses.* Full and fair disclosure demands that a credit union properly address charges for loan losses as follows:

(1) Charges for loan losses shall be made in accordance with generally accepted accounting principles (GAAP);

(2) The allowance for loan and lease losses (ALL) established for loans must fairly present the probable losses for all categories of loans and the proper valuation of loans. The valuation allowance must encompass specifically identified loans, as well as estimated losses inherent in the loan portfolio, such as loans and pools of loans for which losses have been incurred but are not identifiable on a specific loan-by-loan basis;

(3) Adjustments to the valuation ALL will be recorded in the expense account "Provision for Loan and Lease Losses";

(4) The maintenance of an ALL shall not affect the requirement to transfer earnings to a credit union's regular reserve when required under subparts B or C of this part; and

(5) At a minimum, adjustments to the ALL shall be made prior to the distribution or posting of any dividend to the accounts of members.

§ 702.403 Payment of dividends.

(a) *Restriction on dividends.* Dividends shall be available only from undivided earnings, if any.

(b) *Payment of dividends if undivided earnings depleted.* The board of directors of a "well capitalized" federally-insured credit union that has depleted the balance of its undivided earnings account may authorize a transfer of funds from the credit union's regular reserve account to undivided earnings to pay dividends, provided that either—

(1) The payment of dividends will not cause the credit union's net worth classification to fall below "adequately capitalized" under subpart B or C of this part; or

(2) If the payment of dividends will cause the net worth classification to fall below "adequately capitalized," the appropriate Regional Director and, if State-chartered, the appropriate State official, have given prior written approval (in an NWRP or otherwise) to pay a dividend.

Part 703

Investment and Deposit Activities

§ 703.1 Purpose and scope.

(a) This part interprets several of the provisions of Sections 107(7), 107(8), and 107(15) of the Federal Credit Union Act (Act), 12 U.S.C. 1757(7), 1757(8), 1757(15), which list those securities, deposits, and other obligations in which a Federal credit union may invest. Part 703 identifies certain investments and deposit activities permissible under the Act and prescribes regulations governing those investments and deposit activities on the basis of safety and soundness concerns. Additionally, part 703 identifies and prohibits certain investments and deposit activities. Investments and deposit activities that are permissible under the Act and not prohibited or otherwise regulated by part 703 remain permissible for Federal credit unions.

(b) This part does not apply to:

(1) Investment in loans to members and related activities, which is governed by §§ 701.21, 701.22, 701.23, and part 723 of this chapter;

(2) The purchase of real estate-secured loans pursuant to Section 107(15)(A) of the Act, which is governed by § 701.23 of this chapter;

(3) Investment in credit union service organizations, which is governed by part 712 of this chapter;

(4) Investment in fixed assets, which is governed by § 701.36 of this chapter;

(5) Investment by corporate credit unions, which is governed by part 704 of this chapter; or

(6) Investment activity by State-chartered credit unions, except as provided in § 741.3(a)(2) and § 741.219 of this chapter.

§ 703.2 Definitions.

The following definitions apply to this part:

Adjusted trading means selling an investment to a counterparty at a price above its current fair value and simultaneously purchasing or committing to purchase from the counterparty another investment at a price above its current fair value.

Associated personnel means a person engaged in the investment banking or securities business who is directly or indirectly controlled by a National Association of Securities Dealers (NASD) member, whether or not this person is registered or exempt from registration with NASD. Associated personnel includes every sole proprietor, partner, officer, director, or branch manager of any NASD member.

Banker's acceptance means a time draft that is drawn on and accepted by a bank and that represents an irrevocable obligation of the bank.

Bank note means a direct, unconditional, and unsecured general obligation of a bank that ranks equally with all other senior unsecured indebtedness of the bank, except deposit liabilities and other obligations that are subject to any priorities or preferences.

Borrowing repurchase transaction means a transaction in which the Federal credit union agrees to sell a security to a counterparty and to repurchase the same or an identical security from that counterparty at a specified future date and at a specified price.

Call means an option that gives the holder the right to buy a specified quantity of a security at a specified price during a fixed time period.

Collateralized Mortgage Obligation (CMO) means a multi-class mortgage related security.

Collective investment fund means a fund maintained by a national bank under 12 CFR part 9 (Comptroller of the Currency's regulations).

Commercial mortgage related security means a mortgage related security, as defined below, except that it is collateralized entirely by commercial real estate, such as a warehouse or office building, or a multi-family dwelling consisting of more than four units.

Counterparty means the party on the other side of the transaction.

Custodial Agreement means a contract in which one party agrees to hold securities in safekeeping for others.

Delivery versus payment means payment for an investment must occur simultaneously with its delivery.

Deposit note means an obligation of a bank that is similar to a certificate of deposit but is rated.

Derivatives means any derivative instrument as defined under generally accepted accounting principles (GAAP).

Embedded option means a characteristic of an investment that gives the issuer or holder the right to alter the level and timing of the cash flows of the investment. Embedded options include call and put provisions and interest rate caps and floors. Since a prepayment option in a mortgage is a type of call provision, a mortgage-backed security composed of mortgages that may be prepaid is an example of an investment with an embedded option.

Eurodollar deposit means a U.S. dollar-denominated deposit in a foreign branch of a United States depository institution.

European financial options contract means an option that can be exercised only on its expiration date.

Exchangeable Collateralized Mortgage Obligation means a class of a collateralized mortgage obligation (CMO) that, at the time of purchase, represents beneficial ownership interests in a combination of two or more underlying classes of the same CMO structure. The holder of an exchangeable CMO may pay a fee and take delivery of the underlying classes of the CMO.

Fair value means the amount at which an instrument could be exchanged in a current, arms-length transaction between willing parties, as opposed to a forced or liquidation sale.

Financial options contract means an agreement to make or take delivery of a standardized financial instrument upon demand by the holder of the contract as specified in the agreement.

Immediate family member means a spouse or other family member living in the same household.

Industry-recognized information provider means an organization that obtains compensation by providing information to investors and receives no compensation for the purchase or sale of investments.

Investment means any security, obligation, account, deposit, or other item authorized for purchase by a Federal credit union under Sections 107(7), 107(8), or 107(15) of the Act, or this part, other than loans to members.

Investment repurchase transaction means a transaction in which an investor agrees to purchase a security from a counterparty and to resell the same or an identical security to that counterparty at a specified future date and at a specified price.

Maturity means the date the last principal amount of a security is scheduled to come due and does not mean the call date or the weighted average life of a security.

Mortgage related security means a security as defined in Section 3(a)(41) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(41)), *e.g.*, a privately-issued security backed by first lien mortgages secured by real estate upon which is located a dwelling, mixed residential and commercial structure, residential manufactured home, or commercial structure, that is rated in one of the two highest rating categories by at least one nationally-recognized statistical rating organization.

Mortgage servicing rights means a contractual obligation to perform mortgage servicing and the right to receive compensation for performing those services. Mortgage servicing is the administration of a mortgage loan, including collecting monthly payments and fees, providing recordkeeping and escrow functions, and, if necessary curing defaults and foreclosing.

Negotiable instrument means an instrument that may be freely transferred from the purchaser to another person or entity by delivery, or endorsement and delivery, with full legal title becoming vested in the transferee.

Net worth means the retained earnings balance of the credit union at quarter end as determined under generally accepted accounting principles and as further defined in § 702.2(f) of this chapter.

Official means any member of a Federal credit union's board of directors, credit committee, supervisory committee, or investment-related committee.

Ordinary care means the degree of care, which an ordinarily prudent and competent person engaged in the same line of business or endeavor should exercise under similar circumstances.

Pair-off transaction means an investment purchase transaction that is closed or sold on, or before the settlement date. In a pair-off, an investor commits to purchase an investment, but then pairs-off the purchase with a sale of the same investment before or on the settlement date.

Put means an option that gives the holder the right to sell a specified quantity of a security at a specified price during a fixed time period.

Registered investment company means an investment company that is registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. 80a). Examples of registered investment companies are mutual funds and unit investment trusts.

Regular way settlement means delivery of a security from a seller to a buyer within the time frame that the securities industry has established

for immediate delivery of that type of security. For example, regular way settlement of a Treasury security includes settlement on the trade date (cash), the business day following the trade date (regular way), and the second business day following the trade date (skip day).

Residual interest means the remainder cash flows from collateralized mortgage obligations/real estate mortgage investment conduits (CMOs/REMICs), or other mortgage-backed security transaction, after payments due bondholders and trust administrative expenses have been satisfied.

Securities lending means lending a security to a counterparty, either directly or through an agent, and accepting collateral in return.

Security means a share, participation, or other interest in property or in an enterprise of the issuer or an obligation of the issuer that:

(1) Either is represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer;

(2) Is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment; and

(3) Either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

Senior management employee means a Federal credit union's chief executive officer (typically this individual holds the title of President or Treasurer/Manager), an assistant chief executive officer, and the chief financial officer.

Small business related security means a security as defined in Section 3(a)(53) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(53), *e.g.*, a security that is rated in 1 of the 4 highest rating categories by at least one nationally recognized statistical rating organization, and represents an interest in one or more promissory notes or leases of personal property evidencing the obligation of a small business concern and originated by an insured depository institution, insured credit union, insurance company, or similar institution which is supervised and examined by a Federal or State authority, or a finance company or leasing company. This definition does not include Small Business Administration securities permissible under § 107(7) of the Act.

Weighted average life means the weighted-average time to the return of a dollar of principal, calculated by multiplying each portion of principal received by the time at which it is expected to be received (based on a reasonable and supportable estimate of that time) and then summing and dividing by the total amount of principal.

When-issued trading of securities means the buying and selling of securities in the period between the announcement of an offering and the issuance and payment date of the securities.

Yankee dollar deposit means a deposit in a United States branch of a foreign bank licensed to do business in the State in which it is located, or a deposit in a State-chartered, foreign controlled bank.

Zero coupon investment means an investment that makes no periodic interest payments but instead is sold at a discount from its face value. The holder of a zero coupon investment realizes the rate of return through the gradual appreciation of the investment, which is redeemed at face value on a specified maturity date.

§ 703.3 Investment policies.

A Federal credit union's board of directors must establish written investment policies consistent with the Act, this part, and other applicable laws and regulations and must review the policy at least annually. These policies may be part of a broader, asset-liability management policy. Written investment policies must address the following:

(a) The purposes and objectives of the Federal credit union's investment activities;

(b) The characteristics of the investments the Federal credit union may make including the issuer, maturity, index, cap, floor, coupon rate, coupon formula, call provision, average life, and interest rate risk;

(c) How the Federal credit union will manage interest rate risk;

(d) How the Federal credit union will manage liquidity risk;

(e) How the Federal credit union will manage credit risk including specifically listing institutions, issuers, and counterparties that may be used, or criteria for their selection, and limits on the amounts that may be invested with each;

(f) How the Federal credit union will manage concentration risk, which can result from dealing with a single or related issuers, lack of geographic distribution, holding obligations with similar characteristics like maturities and indexes, holding bonds having the same trustee, and holding

securitized loans having the same originator, packager, or guarantor;

(g) Who has investment authority and the extent of that authority. Those with authority must be qualified by education or experience to assess the risk characteristics of investments and investment transactions. Only officials or employees of the Federal credit union may be voting members of an investment-related committee;

(h) The broker-dealers the Federal credit union may use;

(i) The safekeepers the Federal credit union may use;

(j) How the Federal credit union will handle an investment that, after purchase, is outside of board policy or fails a requirement of this part; and

(k) How the Federal credit union will conduct investment trading activities, if applicable, including addressing:

(1) Who has purchase and sale authority;

(2) Limits on trading account size;

(3) Allocation of cash flow to trading accounts;

(4) Stop loss or sale provisions;

(5) Dollar size limitations of specific types, quantity and maturity to be purchased;

(6) Limits on the length of time an investment may be inventoried in a trading account; and

(7) Internal controls, including segregation of duties.

§ 703.4 Recordkeeping and documentation requirements.

(a) Federal credit unions with assets of $10,000,000 or greater must comply with all generally accepted accounting principles applicable to reports or statements required to be filed with NCUA. Federal credit unions with assets less than $10,000,000 are encouraged to do the same, but are not required to do so.

(b) A Federal credit union must maintain documentation for each investment transaction for as long as it holds the investment and until the documentation has been audited in accordance with § 701.12 of this chapter and examined by NCUA. The documentation should include, where applicable, bids and prices at purchase and sale and for periodic updates, relevant disclosure documents or a description of the security from an industry-recognized information provider, financial data, and tests and reports required by the Federal credit union's investment policy and this part.

(c) A Federal credit union must maintain documentation its board of directors used to approve a broker-dealer or a safekeeper for as long as the broker-dealer or safekeeper is approved and until the documentation has been audited in accordance with § 701.12 of this chapter and examined by NCUA.

(d) A Federal credit union must obtain an individual confirmation statement from each broker-dealer for each investment purchased or sold.

§ 703.5 Discretionary control over investments and investment advisers.

(a) Except as provided in paragraph (b) of this section, a Federal credit union must retain discretionary control over its purchase and sale of investments. A Federal credit union has not delegated discretionary control to an investment adviser when the Federal credit union reviews all recommendations from investment advisers and is required to authorize a recommended purchase or sale transaction before its execution.

(b)(1) A Federal credit union may delegate discretionary control over the purchase and sale of investments to a person other than a Federal credit union official or employee:

(i) Provided the person is an investment adviser registered with the Securities and Exchange Commission under the Investment Advisers Act of 1940 (15 U.S.C. 80b); and

(ii) In an amount up to 100 percent of its net worth in the aggregate at the time of delegation.

(2) At least annually, the Federal credit union must adjust the amount of funds held under discretionary control to comply with the 100 percent of net worth cap. The Federal credit union's board of directors must receive notice as soon as possible, but no later than the next regularly scheduled board meeting, of the amount exceeding the net worth cap and notify in writing the appropriate regional director within 5 days after the board meeting. The credit union must develop a plan to comply with the cap within a reasonable period of time.

(3) Before transacting business with an investment adviser, a Federal credit union must analyze his or her background and information available from State or Federal securities regulators, including any enforcement actions

against the adviser, associated personnel, and the firm for which the adviser works.

(c) A Federal credit union may not compensate an investment adviser with discretionary control over the purchase and sale of investments on a per transaction basis or based on capital gains, capital appreciation, net income, performance relative to an index, or any other incentive basis.

(d) A Federal credit union must obtain a report from its investment adviser at least monthly that details the investments under the adviser's control and their performance.

§ 703.6 Credit analysis.

A Federal credit union must conduct and document a credit analysis on an investment and the issuing entity before purchasing it, except for investments issued or fully guaranteed as to principal and interest by the U.S. government or its agencies, enterprises, or corporations or fully insured (including accumulated interest) by the National Credit Union Administration or the Federal Deposit Insurance Corporation. A Federal credit union must update this analysis at least annually for as long as it holds the investment.

§ 703.7 Notice of non-compliant investments.

A Federal credit union's board of directors must receive notice as soon as possible, but no later than the next regularly scheduled board meeting, of any investment that either is outside of board policy after purchase or has failed a requirement of this part. The board of directors must document its action regarding the investment in the minutes of the board meeting, including a detailed explanation of any decision not to sell it. The Federal credit union must notify in writing the appropriate regional director of an investment that has failed a requirement of this part within 5 days after the board meeting.

§ 703.8 Broker-dealers.

(a) A Federal credit union may purchase and sell investments through a broker-dealer as long as the broker-dealer is registered as a broker-dealer with the Securities and Exchange Commission under the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*) or is a depository institution whose broker-dealer activities are regulated by a Federal or State regulatory agency.

(b) Before purchasing an investment through a broker-dealer, a Federal credit union must analyze and annually update the following:

(1) The background of any sales representative with whom the Federal credit union is doing business;

(2) Information available from State or Federal securities regulators and securities industry self-regulatory organizations, such as the National Association of Securities Dealers and the North American Securities Administrators Association, about any enforcement actions against the broker-dealer, its affiliates, or associated personnel; and

(3) If the broker-dealer is acting as the Federal credit union's counterparty, the ability of the broker-dealer and its subsidiaries or affiliates to fulfill commitments, as evidenced by capital strength, liquidity, and operating results. The Federal credit union should consider current financial data, annual reports, reports of nationally-recognized statistical rating organizations, relevant disclosure documents, and other sources of financial information.

(c) The requirements of paragraph (a) of this section do not apply when the Federal credit union purchases a certificate of deposit or share certificate directly from a bank, credit union, or other depository institution.

§ 703.9 Safekeeping of investments.

(a) A Federal credit union's purchased investments and repurchase collateral must be in the Federal credit union's possession, recorded as owned by the Federal credit union through the Federal Reserve Book-Entry System, or held by a board-approved safekeeper under a written custodial agreement that requires the safekeeper to exercise, at least, ordinary care.

(b) Any safekeeper used by a Federal credit union must be regulated and supervised by either the Securities and Exchange Commission, a Federal or State depository institution regulatory agency, or a State trust company regulatory agency.

(c) A Federal credit union must obtain and reconcile monthly a statement of purchased investments and repurchase collateral held in safekeeping.

(d) Annually, the Federal credit union must analyze the ability of the safekeeper to fulfill its custo-

dial responsibilities, as evidenced by capital strength, liquidity, and operating results. The Federal credit union should consider current financial data, annual reports, reports of nationally-recognized statistical rating organizations, relevant disclosure documents, and other sources of financial information.

§ 703.10 Monitoring non-security investments.

(a) At least quarterly, a Federal credit union must prepare a written report listing all of its shares and deposits in banks, credit unions, and other depository institutions, that have one or more of the following features:

(1) Embedded options;

(2) Remaining maturities greater than 3 years; or

(3) Coupon formulas that are related to more than one index or are inversely related to, or multiples of, an index.

(b) The requirement of paragraph (a) of this section does not apply to shares and deposits that are securities.

(c) If a Federal credit union does not have an investment-related committee, then each member of its board of directors must receive a copy of the report described in paragraph (a) of this section. If a Federal credit union has an investment-related committee, then each member of the committee must receive a copy of the report, and each member of the board must receive a summary of the information in the report.

§ 703.11 Valuing securities.

(a) Before purchasing or selling a security, a Federal credit union must obtain either price quotations on the security from at least two broker-dealers or a price quotation on the security from an industry-recognized information provider. This requirement to obtain price quotations does not apply to new issues purchased at par or at original issue discount.

(b) At least monthly, a Federal credit union must determine the fair value of each security it holds. It may determine fair value by obtaining a price quotation on the security from an industry-recognized information provider, a broker-dealer, or a safekeeper.

(c) At least annually, the Federal credit union's supervisory committee or its external auditor must independently assess the reliability of monthly price quotations received from a broker-dealer or safekeeper. The Federal credit union's supervisory committee or external auditor must follow generally accepted auditing standards, which require either re-computation or reference to market quotations.

(d) If a Federal credit union is unable to obtain a price quotation required by this section for a particular security, then it may obtain a quotation for a security with substantially similar characteristics.

§ 703.12 Monitoring securities.

(a) At least monthly, a Federal credit union must prepare a written report setting forth, for each security held, the fair value and dollar change since the prior month-end, with summary information for the entire portfolio.

(b) At least quarterly, a Federal credit union must prepare a written report setting forth the sum of the fair values of all fixed and variable rate securities held that have one or more of the following features:

(1) Embedded options;

(2) Remaining maturities greater than 3 years; or

(3) Coupon formulas that are related to more than one index or are inversely related to, or multiples of, an index.

(c) Where the amount calculated in paragraph (b) of this section is greater than a Federal credit union's net worth, the report described in that paragraph must provide a reasonable and supportable estimate of the potential impact, in percentage and dollar terms, of an immediate and sustained parallel shift in market interest rates of plus and minus 300 basis points on:

(1) The fair value of each security in the Federal credit union's portfolio;

(2) The fair value of the Federal credit union's portfolio as a whole; and

(3) The Federal credit union's net worth.

(d) If the Federal credit union does not have an investment-related committee, then each member of its board of directors must receive a copy of the reports described in paragraphs (a) through (c) of this section. If the Federal credit union has an investment-related committee, then each member of the committee must receive copies of the reports, and each member of the board of directors

must receive a summary of the information in the reports.

§ 703.13 Permissible investment activities.

(a) *Regular way settlement and delivery versus payment basis.* A Federal credit union may only contract for the purchase or sale of a security as long as the delivery of the security is by regular way settlement and the transaction is accomplished on a delivery versus payment basis.

(b) *Federal funds.* A Federal credit union may sell Federal funds to an institution described in Section 107(8) of the Act and credit unions, as long as the interest or other consideration received from the financial institution is at the market rate for Federal funds transactions.

(c) *Investment repurchase transaction.* A Federal credit union may enter into an investment repurchase transaction so long as:

(1) Any securities the Federal credit union receives are permissible investments for Federal credit unions, the Federal credit union, or its agent, either takes physical possession or control of the repurchase securities or is recorded as owner of them through the Federal Reserve Book Entry Securities Transfer System, the Federal credit union, or its agent, receives a daily assessment of their market value, including accrued interest, and the Federal credit union maintains adequate margins that reflect a risk assessment of the securities and the term of the transaction; and

(2) The Federal credit union has entered into signed contracts with all approved counterparties.

(d) *Borrowing repurchase transaction.* A Federal credit union may enter into a borrowing repurchase transaction so long as:

(1) The transaction meets the requirements of paragraph (c) of this section;

(2) Any cash the Federal credit union receives is subject to the borrowing limit specified in Section 107(9) of the Act, and any investments the Federal credit union purchases with that cash are permissible for Federal credit unions; and

(3) The investments referenced in paragraph (d)(2) of this section mature no later than the maturity of the borrowing repurchase transaction.

(e) *Securities lending transaction.* A Federal credit union may enter into a securities lending transaction so long as:

(1) The Federal credit union receives written confirmation of the loan;

(2) Any collateral the Federal credit union receives is a legal investment for Federal credit unions, the Federal credit union, or its agent, obtains a first priority security interest in the collateral by taking physical possession or control of the collateral, or is recorded as owner of the collateral through the Federal Reserve Book Entry Securities Transfer System; and the Federal credit union, or its agent, receives a daily assessment of the market value of the collateral, including accrued interest, and maintains adequate margin that reflects a risk assessment of the collateral and the term of the loan;

(3) Any cash the Federal credit union receives is subject to the borrowing limit specified in Section 107(9) of the Act, and any investments the Federal credit union purchases with that cash are permissible for Federal credit unions and mature no later than the maturity of the transaction; and

(4) The Federal credit union has executed a written loan and security agreement with the borrower.

(f)(1) *Trading securities.* A Federal credit union may trade securities, including engaging in when-issued trading and pair-off transactions, so long as the Federal credit union can show that it has sufficient resources, knowledge, systems, and procedures to handle the risks.

(2) A Federal credit union must record any security it purchases or sells for trading purposes at fair value on the trade date. The trade date is the date the Federal credit union commits, orally or in writing, to purchase or sell a security.

(3) At least monthly, the Federal credit union must give its board of directors or investment-related committee a written report listing all purchase and sale transactions of trading securities and the resulting gain or loss on an individual basis.

§ 703.14 Permissible investments.

(a) *Variable rate investment.* A Federal credit union may invest in a variable rate investment, as long as the index is tied to domestic interest rates and not, for example, to foreign currencies, foreign interest rates, or domestic or foreign com-

modity prices, equity prices, or inflation rates. For purposes of this part, the U.S. dollar-denominated London Interbank Offered Rate (LIBOR) is a domestic interest rate.

(b) *Corporate credit union shares or deposits.* A Federal credit union may purchase shares or deposits in a corporate credit union, except where the NCUA Board has notified it that the corporate credit union is not operating in compliance with part 704 of this chapter. A Federal credit union's aggregate amount of paid-in capital and membership capital, as defined in part 704 of this chapter, in one corporate credit union is limited to two percent of its assets measured at the time of investment or adjustment. A Federal credit union's aggregate amount of paid-in capital and membership capital in all corporate credit unions is limited to four percent of its assets measured at the time of investment or adjustment.

(c) *Registered investment company.* A Federal credit union may invest in a registered investment company or collective investment fund, as long as the prospectus of the company or fund restricts the investment portfolio to investments and investment transactions that are permissible for Federal credit unions.

(d) *Collateralized mortgage obligation/real estate mortgage investment conduit.* A Federal credit union may invest in a fixed or variable rate collateralized mortgage obligation/real estate mortgage investment conduit.

(e) *Municipal security.* A Federal credit union may purchase and hold a municipal security, as defined in Section 107(7)(K) of the Act, only if a nationally-recognized statistical rating organization has rated it in one of the four highest rating categories.

(f) *Instruments issued by institutions described in Section 107(8) of the Act.* A Federal credit union may invest in the following instruments issued by an institution described in Section 107(8) of the Act:

(1) Yankee dollar deposits;

(2) Eurodollar deposits;

(3) Banker's acceptances;

(4) Deposit notes; and

(5) Bank notes with original weighted average maturities of less than 5 years.

(g) *European financial options contract.* A Federal credit union may purchase a European financial options contract or a series of European financial options contracts only to fund the payment of dividends on member share certificates where the dividend rate is tied to an equity index provided:

(1) The option and dividend rate are based on a domestic equity index;

(2) Proceeds from the options are used only to fund dividends on the equity-linked share certificates;

(3) Dividends on the share certificates are derived solely from the change in the domestic equity index over a specified period;

(4) The options' expiration dates are no later than the maturity date of the share certificate.

(5) The certificate may be redeemed prior to the maturity date only upon the member's death or termination of the corresponding option;

(6) The total costs associated with the purchase of the option is known by the Federal credit union prior to effecting the transaction;

(7) The options are purchased at the same time the certificate is issued to the member.

(8) The counterparty to the transaction is a domestic counterparty and has been approved by the Federal credit union's board of directors;

(9) The counterparty to the transaction:

(i) Has a long-term, senior, unsecured debt rating from a nationally-recognized statistical rating organization of AA- (or equivalent) or better at the time of the transaction, and the contract between the counterparty and the Federal credit union specifies that if the long-term, senior, unsecured debt rating declines below AA- (or equivalent) then the counterparty agrees to post collateral with an independent party in an amount fully securing the value of the option; or

(ii) Posts collateral with an independent party in an amount fully securing the value of the option if the counterparty does not have a long-term, senior unsecured debt rating from a nationally-recognized statistical rating organization.

(10) Any collateral posted by the counterparty is a permissible investment for Federal credit unions and is valued daily by an independent third party along with the value of the option;

(11) The aggregate amount of equity-linked member share certificates does not exceed the credit union's net worth;

(12) The terms of the share certificate include a guarantee that there can be no loss of principal to the member regardless of changes in the value of the option unless the certificate is redeemed prior to maturity; and

(13) The Federal credit union provides its board of directors with a monthly report detailing at a minimum:

(i) The dollar amount of outstanding equity-linked share certificates;

(ii) Their maturities; and

(iii) The fair value of the options as determined by an independent third party.

§ 703.15 Prohibited investment activities.

Adjusted trading or short sales. A Federal credit union may not engage in adjusted trading or short sales.

§ 703.16 Prohibited investments.

(a) *Derivatives.* A Federal credit union may not purchase or sell financial derivatives, such as futures, options, interest rate swaps, or forward rate swaps. This prohibition does not apply to:

(1) Any derivatives permitted under §§ 701.21(i) and 703.14(g) of this chapter;

(2) Embedded options not required under GAAP to be accounted for separately from the host contract; and

(3) Interest rate lock commitments or forward sales commitments made in connection with a loan originated by the Federal credit union.

(b) *Zero coupon investments.* A Federal credit union may not purchase a zero coupon investment with a maturity date that is more than 10 years from the settlement date;

(c) *Mortgage servicing rights.* A Federal credit union may not purchase mortgage servicing rights as an investment but may perform mortgage servicing functions as a financial service for a member as long as the mortgage loan is owned by a member;

(d) A Federal credit union may not purchase a commercial mortgage related security that is not otherwise permitted by Section 107(7)(E) of the Act; and

(e) *Stripped mortgage backed securities (SMBS).* A Federal credit union may not invest in SMBS or securities that represent interests in SMBS except as described in paragraphs (1) and (3) below.

(1) A Federal credit union may invest in and hold exchangeable collateralized mortgage obligations (exchangeable CMOs) representing beneficial ownership interests in one or more interest-only classes of a CMO (IO CMOs) or principal-only classes of a CMO (PO CMOs), but only if:

(i) At the time of purchase, the ratio of the market price to the remaining principal balance is between .8 and 1.2, meaning that the discount or premium of the market price to par must be less than 20 points;

(ii) The offering circular or other official information available at the time of purchase indicates that the notional principal on each underlying IO CMO should decline at the same rate as the principal on one or more of the underlying non-IO CMOs, and that the principal on each underlying PO CMO should decline at the same rate as the principal, or notional principal, on one or more of the underlying non-PO CMOs; and

(iii) The credit union staff has the expertise dealing with exchangeable CMOs to apply the conditions in paragraphs (e)(1)(i) and (e)(1)(ii) of this section.

(2) A Federal credit union that invests in an exchangeable CMO may exercise the exchange option only if all of the underlying CMOs are permissible investments for that credit union.

(3) A Federal credit union may accept an exchangeable CMO representing beneficial ownership interests in one or more IO CMOs or PO CMOs as an asset associated with an investment repurchase transaction or as collateral in a securities lending transaction. When the exchangeable CMO is associated with one of these two transactions, it need not conform to the conditions in paragraphs (e)(1)(i) and (ii) of this section.

(f) *Other prohibited investments*. A Federal credit union may not purchase residual interests in collateralized mortgage obligations, real estate mortgage investment conduits, or small business related securities.

§ 703.17 Conflicts of interest.

(a) A Federal credit union's officials and senior management employees, and their immediate family members, may not receive anything of value in connection with its investment transactions. This prohibition also applies to any other employee, such as an investment officer, if the employee is directly involved in investments, unless the Federal credit union's board of directors determines that the employee's involvement does not present a conflict of interest. This prohibition does not include compensation for employees.

(b) A Federal credit union's officials and employees must conduct all transactions with business associates or family members that are not specifically prohibited by paragraph (a) of this section at arm's length and in the Federal credit union's best interest.

§ 703.18 Grandfathered investments.

(a) Subject to safety and soundness considerations, a Federal credit union may hold a CMO/REMIC residual, stripped mortgage-backed securities, or zero coupon security with a maturity greater than 10 years, if it purchased the investment:

(1) Before December 2, 1991; or

(2) On or after December 2, 1991, but before January 1, 1998, if for the purpose of reducing interest rate risk and if the Federal credit union meets the following:

(i) The Federal credit union has a monitoring and reporting system in place that provides the documentation necessary to evaluate the expected and actual performance of the investment under different interest rate scenarios;

(ii) The Federal credit union uses the monitoring and reporting system to conduct and document an analysis that shows, before purchase, that the proposed investment will reduce its interest rate risk;

(iii) After purchase, the Federal credit union evaluates the investment at least quarterly to determine whether or not it actually has reduced the interest rate risk; and

(iv) The Federal credit union accounts for the investment consistent with generally accepted accounting principles.

(b) All grandfathered investments are subject to the valuation and monitoring requirements of §§ 703.10, 703.11, and 703.12 of this part.

§ 703.19 Investment pilot program.

(a) Under the investment pilot program, NCUA will permit a limited number of Federal credit unions to engage in investment activities prohibited by this part but permitted by the Act.

(b) Except as provided in paragraph (c) of this section, before a Federal credit union may engage in additional activities it must obtain written approval from NCUA. To obtain approval, a Federal credit union must submit a request to its regional director that addresses the following items:

(1) Certification that the Federal credit union is "well-capitalized" under part 702 of this chapter;

(2) Board policies approving the activities and establishing limits on them;

(3) A complete description of the activities, with specific examples of how they will benefit the Federal credit union and how they will be conducted;

(4) A demonstration of how the activities will affect the Federal credit union's financial performance, risk profile, and asset-liability management strategies;

(5) Examples of reports the Federal credit union will generate to monitor the activities;

(6) Projections of the associated costs of the activities, including personnel, computer, audit, and so forth;

(7) Descriptions of the internal systems that will measure, monitor, and report the activities;

(8) Qualifications of the staff and officials responsible for implementing and overseeing the activities; and

(9) Internal control procedures that will be implemented, including audit requirements.

(c) A third-party seeking approval of an investment pilot program must submit a request to the Director of the Office of Strategic Program Support and Planning that addresses the following items:

(1) A complete description of the activities with specific examples of how a credit union will conduct and account for them, and how they will benefit a Federal credit union;

(2) A description of any risks to a Federal credit union from participating in the program; and

(3) Contracts that must be executed by the Federal credit union.

(d) A Federal credit union need not obtain individual written approval to engage in investment activities prohibited by this part but permitted by statute where the activities are part of a third-party investment program that NCUA has approved under this section.

Part 704

Corporate Credit Unions

§ 704.1 Scope.

(a) This part establishes special rules for all federally insured corporate credit unions. Non federally insured corporate credit unions must agree, by written contract, to both adhere to the requirements of this part and submit to examinations, as determined by NCUA, as a condition of receiving shares or deposits from federally insured credit unions. This part grants certain additional authorities to federal corporate credit unions. Except to the extent that they are inconsistent with this part, other provisions of NCUA's Rules and Regulations (12 CFR chapter VII) and the Federal Credit Union Act apply to federally chartered corporate credit unions and federally insured state-chartered corporate credit unions to the same extent that they apply to other federally chartered and federally insured state-chartered credit unions, respectively.

(b) The Board has the authority to issue orders which vary from this part. This authority is provided under Section 120(a) of the Federal Credit Union Act, 12 U.S.C. 1766(a). Requests by state-chartered corporate credit unions for waivers to this part and for expansions of authority under Appendix B of this part must be approved by the state regulator before being submitted to NCUA.

§ 704.2 Definitions.

Adjusted trading means any method or transaction whereby a corporate credit union sells a security to a vendor at a price above its current market price and simultaneously purchases or commits to purchase from the vendor another security at a price above its current market price.

Asset-backed security (ABS) means a security that is primarily serviced by the cashflows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to the securityholders. This definition excludes mortgage related securities.

Capital means the sum of a corporate credit union's retained earnings, paid-in capital, and membership capital.

Capital ratio means the corporate credit union's capital divided by its moving daily average net assets.

Collateralized mortgage obligation (CMO) means a multi-class mortgage-related security.

Core capital means the corporate credit union's retained earnings and paid-in capital.

Core capital ratio means the corporate credit union's core capital divided by its moving daily average net assets.

Corporate credit union means an organization that:

(1) Is chartered under Federal or state law as a credit union;

(2) Receives shares from and provides loan services to credit unions;

(3) Is operated primarily for the purpose of serving other credit unions;

(4) Is designated by NCUA as a corporate credit union;

(5) Limits natural person members to the minimum required by state or federal law to charter and operate the credit union; and

(6) Does not condition the eligibility of any credit union to become a member on that credit union's membership in any other organization.

Daily average net assets means the average of net assets calculated for each day during the period.

Derivatives means any derivative instrument as defined under generally accepted accounting principles (GAAP).

Dollar roll means the purchase or sale of a mortgage backed security to a counterparty with an agreement to resell or repurchase a substantially identical security at a future date and at a specified price.

Embedded option means a characteristic of certain assets and liabilities which gives the issuer of the instrument the ability to change the features such as final maturity, rate, principal amount and average life. Options include, but are not limited to, calls, caps, and prepayment options.

Exchangeable collateralized mortgage obligation means a class of a collateralized mortgage obligation (CMO) that, at the time of purchase,

represents beneficial ownership interests in a combination of two or more underlying classes of the same CMO structure. The holder of an exchangeable CMO may pay a fee and take delivery of the underlying classes of the CMO.

Fair value means the amount at which an instrument could be exchanged in a current, arms-length transaction between willing parties, as opposed to a forced or liquidation sale. Quoted market prices in active markets are the best evidence of fair value. If a quoted market price in an active market is not available, fair value may be estimated using a valuation technique that is reasonable and supportable, a quoted market price in an active market for a similar instrument, or a current appraised value. Examples of valuation techniques include the present value of estimated future cash flows, option-pricing models, and option-adjusted spread models. Valuation techniques should incorporate assumptions that market participants would use in their estimates of values, future revenues, and future expenses, including assumptions about interest rates, default, prepayment, and volatility.

Federal funds transaction means a short-term or open-ended unsecured transfer of immediately available funds by one depository institution to another depository institution or entity.

Foreign bank means an institution which is organized under the laws of a country other than the United States, is engaged in the business of banking, and is recognized as a bank by the banking supervisory authority of the country in which it is organized.

Forward settlement of a transaction means settlement on a date later than regular-way settlement.

Immediate family member means a spouse or other family member living in the same household.

Limited liquidity investment means a private placement or funding agreement.

Member reverse repurchase transaction means an integrated transaction in which a corporate credit union purchases a security from one of its member credit unions under agreement by that member credit union to repurchase the same security at a specified time in the future. The corporate credit union then sells that same security, on the same day, to a third party, under agreement to repurchase it on the same date on which the corporate credit union is obligated to return the security to its member credit union.

Membership capital means funds contributed by members that: are adjustable balance with a minimum withdrawal notice of 3 years or are term certificates with a minimum term of 3 years; are available to cover losses that exceed retained earnings and paid-in capital; are not insured by the NCUSIF or other share or deposit insurers; and cannot be pledged against borrowings.

Mortgage related security means a security as defined in section 3(a)(41) of the Securities Exchange Act of 1934,15 U.S.C. 78c(a)(41), *e.g.*, a privately-issued security backed by mortgages secured by real estate upon which is located a dwelling, mixed residential and commercial structure, residential manufactured home, or commercial structure that is rated in one of the two highest rating categories by at least one nationally recognized statistical rating organization.

Moving daily average net assets means the average of daily average net assets for the month being measured and the previous 11 months.

NCUA means NCUA Board (Board), unless the particular action has been delegated by the Board.

Net assets means total assets less Central Liquidity Facility (CLF) stock subscriptions, CLF loans guaranteed by the NCUSIF, U.S. Central CLF certificates, and member reverse repurchase transactions. For its own account, a corporate credit union's payables under reverse repurchase agreements and receivables under repurchase agreements may be netted out if the Generally Accepted Accounting Principles (GAAP) conditions for offsetting are met.

Net economic value (NEV) means the fair value of assets minus the fair value of liabilities. All fair value calculations must include the value of forward settlements and embedded options. The amortized portion of membership capital and paid-in capital, which do not qualify as capital, are treated as liabilities for purposes of this calculation. The NEV ratio is calculated by dividing NEV by the fair value of assets.

Obligor means the primary party obligated to repay an investment, *e.g.*, the issuer of a security, the taker of a deposit, or the borrower of funds in a federal funds transaction. Obligor does not include an originator of receivables underlying an asset-backed security, the servicer of such receivables, or an insurer of an investment.

Official means any director or committee member.

Paid-in capital means accounts or other interests of a corporate credit union that: are perpetual, non-cumulative dividend accounts; are available to cover losses that exceed retained earnings; are not insured by the NCUSIF or other share or deposit insurers; and cannot be pledged against borrowings.

Pair-off transaction means a security purchase transaction that is closed out or sold at, or prior to, the settlement or expiration date.

Quoted market price means a recent sales price or a price based on current bid and asked quotations.

Regular-way settlement means delivery of a security from a seller to a buyer within the time frame that the securities industry has established for immediate delivery of that type of security. For example, regular-way settlement of a Treasury security includes settlement on the trade date ("cash"), the business day following the trade date ("regular way"), and the second business day following the trade date ("skip day").

Repurchase transaction means a transaction in which a corporate credit union agrees to purchase a security from a counterparty and to resell the same or any identical security to that counterparty at a specified future date and at a specified price.

Residual interest means the remainder cash flows from a CMO or ABS transaction after payments due bondholders and trust administrative expenses have been satisfied.

Retained earnings means the total of the corporate credit union's undivided earnings, reserves, and any other appropriations designated by management or regulatory authorities. For purposes of this regulation, retained earnings does not include the allowance for loan and lease losses account, accumulated unrealized gains and losses on available for sale securities, or other comprehensive income items.

Retained earnings ratio means the corporate credit union's retained earnings divided by its moving daily average net assets.

Section 107(8) institution means an institution described in Section 107(8) of the Federal Credit Union Act (12 U.S.C. 1757(8)).

Securities lending means lending a security to a counterparty, either directly or through an agent, and accepting collateral in return.

Senior management employee means a chief executive officer, any assistant chief executive officer (e.g., any assistant president, any vice president or any assistant treasurer/manager), and the chief financial officer (controller).

Settlement date means the date originally agreed to by a corporate credit union and a counterparty for settlement of the purchase or sale of a security.

Short sale means the sale of a security not owned by the seller.

Small business related security means a security as defined in section 3(a)(53) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(53)), *e.g.*, a security that is rated in 1 of the 4 highest rating categories by at least one nationally recognized statistical rating organization, and represents an interest in 1 or more promissory notes or leases of personal property evidencing the obligation of a small business concern and originated by an insured depository institution, insured credit union, insurance company, or similar institution which is supervised and examined by a Federal or State authority, or a finance company or leasing company. This definition does not include Small Business Administration securities permissible under § 107(7) of the Act.

Stripped mortgage-backed security means a security that represents either the principal or interest only portion of the cash flows of an underlying pool of mortgages.

Trade date means the date a corporate credit union originally agrees, whether orally or in writing, to enter into the purchase or sale of a security.

Weighted average life means the weighted-average time to the return of a dollar of principal, calculated by multiplying each portion of principal received by the time at which it is expected to be received (based on a reasonable and supportable estimate of that time) and then summing and dividing by the total amount of principal.

When-issued trading means the buying and selling of securities in the period between the announcement of an offering and the issuance and payment date of the securities.

Wholesale corporate credit union means a corporate credit union which primarily serves other corporate credit unions.

§ 704.3 Corporate credit union capital.

(a) *Capital plan.* A corporate credit union must develop and ensure implementation of written short- and long-term capital goals, objectives, and strategies which provide for the building of capital consistent with regulatory requirements, the maintenance of sufficient capital to support the risk exposures that may arise from current and projected activities, and the periodic review and reassessment of the capital position of the corporate credit union.

(b) *Requirements for membership capital*—(1) *Form.* Membership capital funds may be in the form of a term certificate or an adjusted balance account.

(2) *Disclosure.* The terms and conditions of a membership capital account must be disclosed to the recorded owner of the account at the time the account is opened and at least annually thereafter.

(i) The initial disclosure must be signed by either all of the directors of the member credit union or, if authorized by board resolution, the chair and secretary of the board; and

(ii) The annual disclosure notice must be signed by the chair of the corporate credit union. The chair must sign a statement that certifies that the notice has been sent to member credit unions with membership capital accounts. The certification must be maintained in the corporate credit union's files and be available for examiner review.

(3) *Three-year remaining maturity.* When a membership capital account has been placed on notice or has a remaining maturity of less than three years, the amount of the account that can be considered membership capital is reduced by a constant monthly amortization that ensures membership capital is fully amortized one year before the date of maturity or one year before the end of the notice period. The full balance of a membership capital account being amortized, not just the remaining non-amortized portion, is available to absorb losses in excess of the sum of retained earnings and paid-in capital until the funds are released by the corporate credit union at the time of maturity or the conclusion of the notice period.

(4) *Release.* Membership capital may not be released due solely to the merger, charter conversion or liquidation of a member credit union. In the event of a merger, the membership capital transfers to the continuing credit union. In the event of a charter conversion, the membership capital transfers to the new institution. In the event of liquidation, the membership capital may be released to facilitate the payout of shares with the prior written approval of the OCCU Director.

(5) *Sale.* A member may sell its membership capital to another member in the corporate credit union's field of membership, subject to the corporate credit union's approval.

(6) *Liquidation.* In the event of liquidation of a corporate credit union, membership capital is payable only after satisfaction of all liabilities of the liquidation estate, including uninsured share obligations to shareholders and the National Credit Union Share Insurance Fund (NCUSIF), but excluding paid-in capital.

(7) *Merger.* In the event of a merger of a corporate credit union, membership capital transfers to the continuing corporate credit union. The minimum three-year notice period for withdrawal of membership capital remains in effect.

(8) *Adjusted balance accounts:*

(i) May be adjusted no more frequently than once every six months; and

(ii) Must be adjusted in relation to a measure, *e.g.*, one percent of a member credit union's assets, established and disclosed at the time the account is opened without regard to any minimum withdrawal period. If the measure is other than assets, the corporate credit union must address the measure's permanency characteristics in its capital plan.

(iii) *Notice of withdrawal.* Upon written notice of intent to withdraw membership capital, the balance of the account will be frozen (no further adjustments) until the conclusion of the notice period.

(9) *Grandfathering.* Membership capital issued before the effective date of this regulation is exempt from the limitation of § 704.3(b)(8)(i).

(c) *Requirements for paid-in capital*—(1) *Disclosure.* The terms and conditions of any paid-in capital instrument must be disclosed to the recorded owner of the instrument at the time the instrument is created and must be signed by either all of the directors of the member credit union or, if authorized by board resolution, the chair and secretary of the board.

(2) *Release.* Paid-in capital may not be released due solely to the merger, charter conversion or liquidation of a member credit union. In the event of a merger, the paid-in capital transfers to the continuing credit union. In the event of a charter conversion, the paid-in capital transfers to the new institution. In the event of liquidation, the paid-in capital may be released to facilitate the payout of shares with the prior written approval of the OCCU Director.

(3) *Callability.* Paid-in capital accounts are callable on a pro-rata basis across an issuance class only at the option of the corporate credit union and only if the corporate credit union meets its minimum level of required capital and NEV ratios after the funds are called.

(4) *Liquidation.* In the event of liquidation of the corporate credit union, paid-in capital is payable only after satisfaction of all liabilities of the liquidation estate, including uninsured

share obligations to shareholders, the NCUSIF, and membership capital holders.

(5) *Merger.* In the event of a merger of a corporate credit union, paid-in capital shall transfer to the continuing corporate credit union.

(6) *Paid-in capital.* Paid-in capital includes both member and nonmember paid-in capital.

(i) Member paid-in capital means paid-in capital that is held by the corporate credit union's members. A corporate credit union may not condition membership, services, or prices for services on a credit union's ownership of paid-in capital.

(ii) Nonmember paid-in capital means paid-in capital that is not held by the corporate credit union's members.

(7) *Grandfathering.* A corporate credit union's authority to include paid-in capital as a component of capital is governed by the regulation in effect at the time the paid-in capital was issued. When a grandfathered paid-in capital instrument has a remaining maturity of less than 3 years, the amount that may be considered paid-in capital is reduced by a constant monthly amortization that ensures the paid-in capital is fully amortized 1 year before the date of maturity. The full balance of grandfathered paid-in capital being amortized, not just the remaining non-amortized portion, is available to absorb losses in excess of retained earnings until the funds are released by the corporate credit union at maturity.

(d) *Capital ratio.* A corporate credit union will maintain a minimum capital ratio of 4 percent, except as otherwise provided in this part. A corporate credit union must calculate its capital ratio at least monthly.

(e) *Individual capital ratio requirement*—(1) When significant circumstances or events warrant, the OCCU Director may require a different minimum capital ratio for an individual corporate credit union based on its circumstances. Factors that may warrant a different minimum capital ratio include, but are not limited to:

(i) An expectation that the corporate credit union has or anticipates losses resulting in capital inadequacy;

(ii) Significant exposure exists, unsupported by adequate capital or risk management processes, due to credit, liquidity, market, fiduciary, operational, and similar types of risks;

(iii) A merger has been approved; or

(iv) An emergency exists because of a natural disaster.

(2) When the OCCU Director determines that a different minimum capital ratio is necessary or appropriate for a particular corporate credit union, he or she will notify the corporate credit union in writing of the proposed capital ratio and the date by which the capital ratio must be reached. The OCCU Director also will provide an explanation of why the proposed capital ratio is considered necessary or appropriate.

(3)(i) The corporate credit union may respond to any or all of the items in the notice. The response must be in writing and delivered to the OCCU Director within 30 calendar days after the date on which the corporate credit union received the notice. The OCCU Director may shorten the time period when, in its opinion, the condition of the corporate credit union so requires, provided that the corporate credit union is informed promptly of the new time period, or with the consent of the corporate credit union. In its discretion, the OCCU Director may extend the time period for good cause.

(ii) Failure to respond within 30 calendar days or such other time period as may be specified by the OCCU Director shall constitute a waiver of any objections to any item in the notice. Failure to address any item in a response shall constitute a waiver of any objection to that item.

(iii) After the close of the corporate credit union's response period, the OCCU Director will decide, based on a review of the corporate credit union's response and other information concerning the corporate credit union, whether a different minimum capital ratio should be established for the corporate credit union and, if so, the capital ratio and the date the requirement must be reached. The corporate credit union will be notified of the decision in writing. The notice will include an explanation of the decision, except for a decision not to establish a different minimum capital ratio for the corporate credit union.

(f) *Failure to maintain minimum capital ratio requirement.* When a corporate credit union's capital ratio falls below the minimum required by paragraphs (d) or (e) of this section, or Appendix B to this part, as applicable, operating management of the corporate credit union must notify its board of directors, supervisory committee, and the OCCU Director within 10 calendar days.

(g) *Capital restoration plan.* (1) A corporate credit union must submit a plan to restore and maintain its capital ratio at the minimum requirement when either of the following conditions exist:

(i) The capital ratio falls below the minimum requirement and is not restored to the minimum requirement by the next month end; or

(ii) Regardless of whether the capital ratio is restored by the next month end, the capital ratio falls below the minimum requirement for three months in any 12-month period.

(2) The capital restoration plan must, at a minimum, include the following:

(i) Reasons why the capital ratio fell below the minimum requirement;

(ii) Descriptions of steps to be taken to restore the capital ratio to the minimum requirement within specific time frames;

(iii) Actions to be taken to maintain the capital ratio at the minimum required level and increase it thereafter;

(iv) Balance sheet and income projections, including assumptions, for the current calendar year and one additional calendar year; and

(v) Certification from the board of directors that it will follow the proposed plan if approved by the OCCU Director.

(3) The capital restoration plan must be submitted to the OCCU Director within 30 calendar days of the occurrence. The OCCU Director will respond to the corporate credit union regarding the adequacy of the plan within 45 calendar days of its receipt.

(h) *Capital directive.* (1) If a corporate credit union fails to submit a capital restoration plan; or the plan submitted is not deemed adequate to either restore capital or restore capital within a reasonable time; or the credit union fails to implement its approved capital restoration plan, NCUA may issue a capital directive.

(2) A capital directive may order a corporate credit union to:

(i) Achieve adequate capitalization within a specified time frame by taking any action deemed necessary, including but not limited to the following:

(A) Increase the amount of capital to specific levels;

(B) Reduce dividends;

(C) Limit receipt of deposits to those made to existing accounts;

(D) Cease or limit issuance of new accounts or any or all classes of accounts;

(E) Cease or limit lending or making a particular type or category of loans;

(F) Cease or limit the purchase of specified investments;

(G) Limit operational expenditures to specified levels;

(H) Increase and maintain liquid assets at specified levels; and

(I) Restrict or suspend expanded authorities issued under Appendix B of this part.

(ii) Adhere to a previously submitted plan to achieve adequate capitalization.

(iii) Submit and adhere to a capital plan acceptable to NCUA describing the means and a time schedule by which the corporate credit union shall achieve adequate capitalization.

(iv) Meet with NCUA.

(v) Take a combination of these actions.

(3) Prior to issuing a capital directive, NCUA will notify a corporate credit union in writing of its intention to issue a capital directive.

(i) The notice will state:

(A) The reasons for the issuance of the directive; and

(B) The proposed content of the directive.

(ii) A corporate credit union must respond in writing within 30 calendar days of receipt of the notice stating that it either concurs or disagrees with the notice. If it disagrees with the notice, it must state the reasons why the directive should not be issued and/or propose alternative contents for the directive. The response should include all matters that the corporate credit union wishes to be considered. For good cause, including the following conditions, the response time may be shortened or lengthened:

(A) When the condition of the corporate requires, and the corporate credit union is notified of the shortened response period in the notice;

(B) With the consent of the corporate credit union; or

(C) When the corporate credit union already has advised NCUA that it cannot or will not achieve adequate capitalization.

(iii) Failure to respond within 30 calendar days, or another time period specified in the notice, shall constitute a waiver of any objections to the proposed directive.

(4) After the closing date of the corporate credit union's response period, or the receipt of the response, if earlier, NCUA shall consider the response and may seek additional information or clarification. Based on the information provided during the response period, NCUA will

determine whether or not to issue a capital directive and, if issued, the form it should take.

(5) Upon issuance, a capital directive and a statement of the reasons for its issuance will be delivered to the corporate credit union. A directive is effective immediately upon receipt by the corporate credit union, or upon such later date as may be specified therein, and shall remain effective and enforceable until it is stayed, modified, or terminated by NCUA.

(6) A capital directive may be issued in addition to, or in lieu of, any other action authorized by law in response to a corporate credit union's failure to achieve or maintain the applicable minimum capital ratios.

(7) Upon a change in circumstances, a corporate credit union may request reconsideration of the terms of the directive. Requests that are not based on a significant change in circumstances or are repetitive or frivolous will not be considered. Pending a decision on reconsideration, the directive shall continue in full force and effect.

(i) *Earnings retention requirement.* A corporate credit union must increase retained earnings if the prior month-end retained earnings ratio is less than 2 percent.

(1) Its retained earnings must increase:

(i) During the current month, by an amount equal to or greater than the monthly earnings retention amount; or

(ii) During the current and prior two months, by an amount equal to or greater than the quarterly earnings retention amount.

(2) Earnings retention amounts are calculated as follows:

(i) The monthly earnings retention amount is determined by multiplying the earnings retention factor by the prior month-end moving daily average net assets; and

(ii) The quarterly earnings retention amount is determined by multiplying the earnings retention factor by moving daily average net assets for each of the prior three month-ends.

(3) The earnings retention factor is determined as follows:

(i) If the prior month-end retained earnings ratio is less than 2 percent and the core capital ratio is less than 3 percent, the earnings retention factor is .15 percent per annum; or

(ii) If the prior month-end retained earnings ratio is less than 2 percent and the core capital ratio is equal to or greater than 3 percent, the earnings retention factor is .10 percent per annum.

(4) The OCCU Director may approve a decrease to the earnings retention amount if it is determined a lesser amount is necessary to avoid a significant adverse impact upon a corporate credit union.

(5) Operating management of the corporate credit union must notify its board of directors, supervisory committee, the OCCU Director and, if applicable, the state regulator within 10 calendar days of determining that the retained earnings ratio has declined below 2 percent. If the decline in the retained earnings ratio is due, in full or in part, to a decline in the dollar amount of retained earnings and the retained earnings ratio is not restored to at least 2 percent by the next month end, a retained earnings action plan is required to be submitted within 30 calendar days.

(6) The retained earnings action plan must be submitted to the OCCU Director and, if applicable, the state regulator and, at a minimum, include the following:

(i) Reasons why the dollar amount of retained earnings has decreased;

(ii) Description of actions to be taken to increase the dollar amount of retained earnings within specific time frames; and

(iii) Monthly balance sheet and income projections, including assumptions, for the next 12-month period.

§ 704.4 Board responsibilities.

(a) *General.* A corporate credit union's board of directors must approve comprehensive written strategic plans and policies, review them annually, and provide them upon request to the auditors, supervisory committee, and NCUA.

(b) *Policies.* A corporate credit union's policies must be commensurate with the scope and complexity of the corporate credit union.

(c) *Other requirements.* The board of directors of a corporate credit union must ensure:

(1) Senior managers have an in-depth, working knowledge of their direct areas of responsibility and are capable of identifying, hiring, and retaining qualified staff;

(2) Qualified personnel are employed or under contract for all line support and audit areas, and designated back-up personnel or resources with adequate cross-training are in place;

(3) GAAP is followed, except where law or regulation has provided for a departure from GAAP;

(4) Accurate balance sheets, income statements, and internal risk assessments (*e.g.*, risk management measures of liquidity, market, and credit risk associated with current activities) are produced timely in accordance with §§ 704.6, 704.8, and 704.9;

(5) Systems are audited periodically in accordance with industry-established standards;

(6) Financial performance is evaluated to ensure that the objectives of the corporate credit union and the responsibilities of management are met; and

(7) Planning addresses the retention of external consultants, as appropriate, to review the adequacy of technical, human, and financial resources dedicated to support major risk areas.

§ 704.5 Investments.

(a) *Policies.* A corporate credit union must operate according to an investment policy that is consistent with its other risk management policies, including, but not limited to, those related to credit risk management, asset and liability management, and liquidity management. The policy must address, at a minimum:

(1) Appropriate tests and criteria for evaluating investments and investment transactions before purchase; and

(2) Reasonable and supportable concentration limits for limited liquidity investments in relation to capital.

(b) *General.* All investments must be U.S. dollar-denominated and subject to the credit policy restrictions set forth in § 704.6.

(c) *Authorized activities.* A corporate credit union may invest in:

(1) Securities, deposits, and obligations set forth in Sections 107(7), 107(8), and 107(15) of the Federal Credit Union Act, 12 U.S.C. 1757(7), 1757(8), and 1757(15), except as provided in this section;

(2) Deposits in, the sale of federal funds to, and debt obligations of corporate credit unions, Section 107(8) institutions, and state banks, trust companies, and mutual savings banks not domiciled in the state in which the corporate credit union does business;

(3) Corporate CUSOs, as defined in and subject to the limitations of § 704.11;

(4) Marketable debt obligations of corporations chartered in the United States. This authority does not apply to debt obligations that are convertible into the stock of the corporation; and

(5) Domestically-issued asset-backed securities.

(d) *Repurchase agreements.* A corporate credit union may enter into a repurchase agreement provided that:

(1) The corporate credit union, directly or through its agent, receives written confirmation of the transaction, and either takes physical possession or control of the repurchase securities or is recorded as owner of the repurchase securities through the Federal Reserve Book-Entry Securities Transfer System;

(2) The repurchase securities are legal investments for that corporate credit union;

(3) The corporate credit union, directly or through its agent, receives daily assessment of the market value of the repurchase securities and maintains adequate margin that reflects a risk assessment of the repurchase securities and the term of the transaction; and

(4) The corporate credit union has entered into signed contracts with all approved counterparties and agents, and ensures compliance with the contracts. Such contracts must address any supplemental terms and conditions necessary to meet the specific requirements of this part. Third party arrangements must be supported by tri-party contracts in which the repurchase securities are priced and reported daily and the tri-party agent ensures compliance; and

(e) *Securities Lending.* A corporate credit union may enter into a securities lending transaction provided that:

(1) The corporate credit union, directly or through its agent, receives written confirmation of the loan, obtains a first priority security interest in the collateral by taking physical possession or control of the collateral, or is recorded as owner of the collateral through the Federal Reserve Book-Entry Securities Transfer System;

(2) The collateral is a legal investment for that corporate credit union;

(3) The corporate credit union, directly or through its agent, receives daily assessment of the market value of collateral and maintains adequate margin that reflects a risk assessment of the collateral and terms of the loan; and

(4) The corporate credit union has entered into signed contracts with all agents and, directly or through its agent, has executed a written loan and security agreement with the borrower. The corporate or its agent ensures compliance with the agreements.

(f) *Investment companies.* A corporate credit union may invest in an investment company registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. 80a), provided that the prospectus of the company restricts the investment portfolio to investments and investment transactions that are permissible for that corporate credit union.

(g) *Forward settlement of transactions later than regular way.* A corporate credit union may enter into an agreement to purchase or sell an instrument, with settlement later than regular way, provided that:

(1) Delivery and acceptance are mandatory;

(2) The transaction is clearly disclosed in the appropriate risk reporting required under § 704.8(b);

(3) If the corporate credit union is the purchaser, it has adequate cash flow projections evidencing its ability to purchase the instrument;

(4) If the corporate credit union is the seller, it owns the instrument on the trade date; and

(5) The transaction is settled on a cash basis at the settlement date.

(h) *Prohibitions.* A corporate credit union is prohibited from:

(1) Purchasing or selling derivatives, except for embedded options not required under GAAP to be accounted for separately from the host contract or forward sales commitments on loans to be purchased by the corporate credit union;

(2) Engaging in trading securities unless accounted for on a trade date basis;

(3) Engaging in adjusted trading or short sales; and

(4) Purchasing mortgage servicing rights, small business related securities, residual interests in collateralized mortgage obligations, residual interests in real estate mortgage investment conduits, or residual interests in asset-backed securities; and

(5) Purchasing stripped mortgage backed securities (SMBS), or securities that represent interests in SMBS, except as described in subparagraphs (i) and (iii) below.

(i) A corporate credit union may invest in exchangeable collateralized mortgage obligations (exchangeable CMOs) representing beneficial ownership interests in one or more interest-only classes of a CMO (IO CMOs) or principal-only classes of a CMO (PO CMOs), but only if:

(A) At the time of purchase, the ratio of the market price to the remaining principal balance is between .8 and 1.2, meaning that the discount or premium of the market price to par must be less than 20 points;

(B) The offering circular or other official information available at the time of purchase indicates that the notional principal on each underlying IO CMO should decline at the same rate as the principal on one or more of the underlying non-IO CMOs, and that the principal on each underlying PO CMO should decline at the same rate as the principal, or notional principal, on one or more of the underlying non-PO CMOs; and

(C) The credit union investment staff has the expertise dealing with exchangeable CMOs to apply the conditions in paragraphs (h)(5)(i)(A) and (B) of this section.

(ii) A corporate credit union that invests in an exchangeable CMO may exercise the exchange option only if all of the underlying CMOs are permissible investments for that credit union.

(iii) A corporate credit union may accept an exchangeable CMO representing beneficial ownership interests in one or more IO CMOs or PO CMOs as an asset associated with an investment repurchase transaction or as collateral in a securities lending transaction. When the exchangeable CMO is associated with one of these two transactions, it need not conform to the conditions in paragraphs (h)(5)(i)(A) or (B) of this section.

(i) *Conflicts of interest.* A corporate credit union's officials, employees, and immediate family members of such individuals, may not receive pecuniary consideration in connection with the making of an investment or deposit by the corporate credit union. Employee compensation is exempt from this prohibition. All transactions not specifically prohibited by this paragraph must be conducted at arm's length and in the interest of the corporate credit union.

(j) *Grandfathering.* A corporate credit union's authority to hold an investment is governed by the regulation in effect at the time of purchase. However, all grandfathered investments are subject to the requirements of §§ 704.8 and 704.9.

§ 704.6 Credit risk management.

(a) *Policies.* A corporate credit union must operate according to a credit risk management policy that is commensurate with the investment risks and activities it undertakes. The policy must address at a minimum:

(1) The approval process associated with credit limits;

(2) Due diligence analysis requirements;

(3) Maximum credit limits with each obligor and transaction counterparty, set as a percentage of capital. In addition to addressing deposits and securities, limits with transaction counterparties must address aggregate exposures of all transactions including, but not limited to, repurchase agreements, securities lending, and forward settlement of purchases or sales of investments; and

(4) Concentrations of credit risk (*e.g.*, originator of receivables, insurer, industry type, sector type, and geographic).

(b) *Exemption.* The requirements of this section do not apply to investments that are issued or fully guaranteed as to principal and interest by the U.S. government or its agencies or enterprises (excluding subordinated debt) or are fully insured (including accumulated interest) by the NCUSIF or Federal Deposit Insurance Corporation.

(c) *Concentration limits*—(1) *General rule.* The aggregate of all investments in any single obligor is limited to 50 percent of capital or $5 million, whichever is greater.

(2) *Exceptions.* Exceptions to the general rule are:

(i) Aggregate investments in repurchase and securities lending agreements with any one counterparty are limited to 200 percent of capital;

(ii) Investments in corporate CUSOs are subject to the limitations of § 704.11; and

(iii) Aggregate investments in corporate credit unions are not subject to the limitations of paragraph (c)(1) of this section.

(3) For purposes of measurement, each new credit transaction must be evaluated in terms of the corporate credit union's capital at the time of the transaction. An investment that fails a requirement of this section because of a subsequent reduction in capital will be deemed nonconforming. A corporate credit union is required to exercise reasonable efforts to bring nonconforming investments into conformity within 90 calendar days. Investments that remain nonconforming for 90 calendar days will be deemed to fail a requirement of this section and the corporate credit union will have to comply with § 704.10.

(d) *Credit ratings.*—(1) All investments, other than in a corporate credit union or CUSO, must have an applicable credit rating from at least one nationally recognized statistical rating organization (NRSRO).

(2) At the time of purchase, investments with long-term ratings must be rated no lower than AA– (or equivalent) and investments with short-term ratings must be rated no lower than A–1 (or equivalent).

(3) Any rating(s) relied upon to meet the requirements of this part must be identified at the time of purchase and must be monitored for as long as the corporate owns the investment.

(4) When two or more ratings are relied upon to meet the requirements of this part at the time of purchase, the board or an appropriate committee must place on the § 704.6(e)(1) investment watch list any investment for which a rating is downgraded below the minimum rating requirements of this part.

(5) Investments are subject to the requirements of § 704.10 if:

(i) One rating was relied upon to meet the requirements of this part and that rating is downgraded below the minimum rating requirements of this part; or

(ii) Two or more ratings were relied upon to meet the requirements of this part and at least two of those ratings are downgraded below the minimum rating requirements of this part.

(e) *Reporting and documentation.* (1) At least annually, a written evaluation of each credit limit with each obligor or transaction counterparty must be prepared and formally approved by the board or an appropriate committee. At least monthly, the board or an appropriate committee must receive an investment watch list of existing and/or potential credit problems and summary credit exposure reports, which demonstrate compliance with the corporate credit union's risk management policies.

(2) At a minimum, the corporate credit union must maintain:

(i) A justification for each approved credit limit;

(ii) Disclosure documents, if any, for all instruments held in portfolio. Documents for an instrument that has been sold must be retained until completion of the next NCUA examination; and

(iii) The latest available financial reports, industry analyses, internal and external analyst evaluations, and rating agency information sufficient to support each approved credit limit.

§ 704.7 Lending.

(a) *Policies.* A corporate credit union must operate according to a lending policy which addresses, at a minimum:

(1) Loan types and limits;

(2) Required documentation and collateral; and

(3) Analysis and monitoring standards.

(b) *General.* Each loan or line of credit limit will be determined after analyzing the financial and operational soundness of the borrower and the ability of the borrower to repay the loan.

(c) *Loans to members*—(1) *Credit unions.* (i) The maximum aggregate amount in unsecured loans and lines of credit to any one member credit union, excluding pass-through and guaranteed loans from the CLF and the NCUSIF, must not exceed 50 percent of capital.

(ii) The maximum aggregate amount in secured loans and lines of credit to any one member credit union, excluding those secured by shares or marketable securities and member reverse repurchase transactions, must not exceed 100 percent of capital.

(2) *Corporate CUSOs.* Any loan or line of credit must comply with § 704.11.

(3) *Other members.* The maximum aggregate amount of loans and lines of credit to any other one member must not exceed 15 percent of the corporate credit union's capital plus pledged shares.

(d) *Loans to nonmembers*—(1) *Credit unions.* A loan to a nonmember credit union, other than through a loan participation with another corporate credit union, is only permissible if the loan is for an overdraft related to the providing of correspondent services pursuant to § 704.12. Generally, such a loan will have a maturity of one business day.

(2) *Corporate CUSOs.* Any loan or line of credit must comply with § 704.11.

(e) *Member business loan rule.* Loans, lines of credit and letters of credit to:

(1) Member credit unions are exempt from part 723 of this chapter;

(2) Corporate CUSOs are not subject to part 723 of this chapter.

(3) Other members not excluded under § 723.1(b) of this chapter must comply with part 723 of this chapter unless the loan or line of credit is fully guaranteed by a credit union or fully secured by U.S. Treasury or agency securities. Those guaranteed and secured loans must comply with the aggregate limits of § 723.16 but are exempt from the other requirements of part 723.

(f) *Participation loans with other corporate credit unions.* A corporate credit union is permitted to participate in a loan with another corporate credit union provided the corporate retains an interest of at least 5 percent of the face amount of the loan and a master participation loan agreement is in place before the purchase or the sale of a participation. A participating corporate credit union must exercise the same due diligence as if it were the originating corporate credit union.

(g) *Prepayment penalties.* If provided for in the loan contract, a corporate credit union is authorized to assess prepayment penalties on loans.

§ 704.8 Asset and liability management.

(a) *Policies.* A corporate credit union must operate according to a written asset and liability management policy which addresses, at a minimum:

(1) The purpose and objectives of the corporate credit union's asset and liability activities;

(2) The maximum allowable percentage decline in net economic value (NEV), compared to base case NEV;

(3) The minimum allowable NEV ratio;

(4) Policy limits and specific test parameters for the interest rate sensitivity analysis requirements set forth in paragraph (d) of this section; and

(5) The modeling of indexes that serve as references in financial instrument coupon formulas; and

(6) The tests that will be used, prior to purchase, to estimate the impact of investments on the percentage decline in NEV, compared to base case NEV. The most recent NEV analysis, as determined under paragraph (d)(1)(i) of this section may be used as a basis of estimation.

(b) *Asset and liability management committee (ALCO).* A corporate credit union's ALCO must have at least one member who is also a member of the board of directors. The ALCO must review asset and liability management reports on at least

a monthly basis. These reports must address compliance with Federal Credit Union Act, NCUA Rules and Regulations (12 CFR chapter VII), and all related risk management policies.

(c) *Penalty for early withdrawals.* A corporate credit union that permits early certificate/share withdrawals must assess market-based penalties sufficient to cover the estimated replacement cost of the certificate/share redeemed. This means the minimum penalty must be reasonably related to the rate that the corporate credit union would be required to offer to attract funds for a similar term with similar characteristics.

(d) *Interest rate sensitivity analysis.* (1) A corporate credit union must:

(i) Evaluate the risk in its balance sheet by measuring, at least quarterly, the impact of an instantaneous, permanent, and parallel shock in the yield curve of plus and minus 100, 200, and 300 basis points on its NEV and NEV ratio. If the base case NEV ratio falls below 3 percent at the last testing date, these tests must be calculated at least monthly until the base case NEV ratio again exceeds 3 percent;

(ii) Limit its risk exposure to levels that do not result in a base case NEV ratio or any NEV ratio resulting from the tests set forth in paragraph (d)(1)(i) of this section below 2 percent; and

(iii) Limit its risk exposures to levels that do not result in a decline in NEV of more than 15 percent.

(2) A corporate credit union must assess annually if it should conduct periodic additional tests to address market factors that may materially impact that corporate credit union's NEV. These factors should include, but are not limited to, the following:

(i) Changes in the shape of the Treasury yield curve;

(ii) Adjustments to prepayment projections used for amortizing securities to consider the impact of significantly faster/slower prepayment speeds;

(iii) Adjustments to the market spread assumptions for non Treasury instruments to consider the impact of widening spreads; and

(iv) Adjustments to volatility assumptions to consider the impact that changing volatilities have on embedded option values.

(e) *Regulatory violations.* If a corporate credit union's decline in NEV, base case NEV ratio or any NEV ratio resulting from the tests set forth in paragraph (d)(1)(i) of this section violates the limits established by this rule and is not brought into compliance within 10 calendar days, operating management of the corporate credit union must immediately report the information to the board of directors, supervisory committee, and the OCCU Director. If any violation persists for 30 calendar days, the corporate credit union must submit a detailed, written action plan to the OCCU Director that sets forth the time needed and means by which it intends to correct the violation. If the OCCU Director determines that the plan is unacceptable, the corporate credit union must immediately restructure the balance sheet to bring the exposure back within compliance or adhere to an alternative course of action determined by the OCCU Director.

(f) *Policy violations.* If a corporate credit union's decline in NEV, base case NEV ratio, or any NEV ratio resulting from the tests set forth in paragraph (d)(1)(i) of this section violates the limits established by its board, it must determine how it will bring the exposure within policy limits. The disclosure to the board of the violation must occur no later than its next regularly scheduled board meeting.

§ 704.9 Liquidity management.

(a) *General.* In the management of liquidity, a corporate credit union must:

(1) Evaluate the potential liquidity needs of its membership in a variety of economic scenarios;

(2) Regularly monitor sources of internal and external liquidity;

(3) Demonstrate that the accounting classification of investment securities is consistent with its ability to meet potential liquidity demands; and

(4) Develop a contingency funding plan that addresses alternative funding strategies in successively deteriorating liquidity scenarios. The plan must:

(i) List all sources of liquidity, by category and amount, that are available to service an immediate outflow of funds in various liquidity scenarios;

(ii) Analyze the impact that potential changes in fair value will have on the disposition of assets in a variety of interest rate scenarios; and

(iii) Be reviewed by the board or an appropriate committee no less frequently than annually or as market or business conditions dictate.

(b) *Borrowing.* A corporate credit union may borrow up to 10 times capital or 50 percent of shares (excluding shares created by the use of member reverse repurchase agreements) and capital, whichever is greater. CLF borrowings and borrowed funds created by the use of member reverse repurchase agreements are excluded from this limit. The corporate credit union must demonstrate that sufficient contingent sources of liquidity remain available.

§ 704.10 Investment action plan.

(a) Any corporate credit union in possession of an investment, including a derivative, that fails to meet a requirement of this part must, within 30 calendar days of the failure, report the failed investment to its board of directors, supervisory committee and the OCCU Director. If the corporate credit union does not sell the failed investment, and the investment continues to fail to meet a requirement of this part, the corporate credit union must, within 30 calendar days of the failure, provide to the OCCU Director a written action plan that addresses:

(1) The investment's characteristics and risks;

(2) The process to obtain and adequately evaluate the investment's market pricing, cash flows, and risk;

(3) How the investment fits into the credit union's asset and liability management strategy;

(4) The impact that either holding or selling the investment will have on the corporate credit union's earnings, liquidity, and capital in different interest rate environments; and

(5) The likelihood that the investment may again pass the requirements of this part.

(b) The OCCU Director may require, for safety and soundness reasons, a shorter time period for plan development than that set forth in paragraph (a) of this section.

(c) If the plan described in paragraph (a) of this section is not approved by the OCCU Director, the credit union must adhere to the OCCU Director's directed course of action.

§ 704.11 Corporate Credit Union Service Organizations (Corporate CUSOs).

(a) A corporate CUSO is an entity that:

(1) Is at least partly owned by a corporate credit union;

(2) Primarily serves credit unions;

(3) Restricts its services to those related to the normal course of business of credit unions; and

(4) Is structured as a corporation, limited liability company, or limited partnership under state law.

(b) *Investment and loan limitations.* (1) The aggregate of all investments in member and nonmember corporate CUSOs must not exceed 15 percent of a corporate credit union's capital.

(2) The aggregate of all investments in and loans to member and nonmember corporate CUSOs must not exceed 30 percent of a corporate credit union's capital. A corporate credit union may lend to member and nonmember corporate CUSOs an additional 15 percent of capital if the loan is collateralized by assets in which the corporate has a perfected security interest under state law.

(3) If the limitations in paragraphs (b)(1) and (b)(2) of this section are reached or exceeded because of the profitability of the CUSO and the related GAAP valuation of the investment under the equity method without an additional cash outlay by the corporate, divestiture is not required. A corporate credit union may continue to invest up to the regulatory limit without regard to the increase in the GAAP valuation resulting from the corporate CUSO's profitability.

(c) *Due diligence.* A corporate credit union must comply with the due diligence requirements of §§ 723.5 and 723.6(f) through (j) of this chapter for all loans to corporate CUSOs. This requirement does not apply to loans excluded under § 723.1(b).

(d) *Separate entity.* (1) A corporate CUSO must be operated as an entity separate from a corporate credit union.

(2) A corporate credit union investing in or lending to a corporate CUSO must obtain a written legal opinion that concludes the corporate CUSO is organized and operated in a manner that the corporate credit union will not reasonably be held liable for the obligations of the corporate CUSO. This opinion must address factors that have led courts to "pierce the corporate veil," such as inadequate capitalization, lack of corporate identity, common boards of directors and employees, control of one entity over another, and lack of separate books and records.

(e) *Prohibited activities.* A corporate credit union may not use this authority to acquire control, directly or indirectly, of another depository financial institution or to invest in shares, stocks, or obligations of an insurance company, trade association, liquidity facility, or similar organization.

(f) An official of a corporate credit union which has invested in or loaned to a corporate CUSO may not receive, either directly or indirectly, any salary, commission, investment income, or other income, compensation, or consideration from the corporate CUSO. This prohibition also extends to immediate family members of officials.

(g) Prior to making an investment in or loan to a corporate CUSO, a corporate credit union must obtain a written agreement that the corporate CUSO will:

(1) Follow GAAP;

(2) Provide financial statements to the corporate credit union at least quarterly;

(3) Obtain an annual CPA opinion audit and provide a copy to the corporate credit union. A wholly owned or majority owned CUSO is not required to obtain a separate annual audit if it is included in the corporate credit union's annual consolidated audit; and

(4) Allow the auditor, board of directors, and NCUA complete access to its books, records, and any other pertinent documentation.

(h) Corporate credit union authority to invest in or loan to a CUSO is limited to that provided in this section. A corporate credit union is not authorized to invest in or loan to a CUSO under part 712 of this chapter.

§ 704.12 Permissible services.

(a) *Preapproved services.* A corporate credit union may provide to members the preapproved services set out in this section. NCUA may at any time, based upon supervisory, legal, or safety and soundness reasons, limit or prohibit any preapproved service. The specific activities listed within each preapproved category are provided as illustrations of activities permissible under the particular category, not as an exclusive or exhaustive list.

(1) *Correspondent services agreement.* A corporate credit union may only provide financial services to nonmembers through a correspondent services agreement. A correspondent services agreement is an agreement between two corporate credit unions, whereby one of the corporate credit unions agrees to provide services to the other corporate credit union or its members.

(2) *Credit and investment services.* Credit and investment services are advisory and consulting activities that assist the member in lending or investment management. These services may include loan reviews, investment portfolio reviews and investment advisory services.

(3) *Electronic financial services.* Electronic financial services are any services, products, functions, or activities that a corporate credit union is otherwise authorized to perform, provide or deliver to its members but performed through electronic means. Electronic services may include automated teller machines, online transaction processing through a website, website hosting services, account aggregation services, and internet access services to perform or deliver products or services to members.

(4) *Excess capacity.* Excess capacity is the excess use or capacity remaining in facilities, equipment or services that: a corporate credit union properly invested in or established, in good faith, with the intent of serving its members; and it reasonably anticipates will be taken up by the future expansion of services to its members. A corporate credit union may sell or lease the excess capacity in facilities, equipment or services, such as office space, employees and data processing.

(5) *Liquidity and asset and liability management.* Liquidity and asset and liability management services are any services, functions or activities that assist the member in liquidity and balance sheet management. These services may include liquidity planning and balance sheet modeling and analysis.

(6) *Operational services.* Operational services are services established to deliver financial products and services that enhance member service and promote safe and sound operations. Operational services may include tax payment, electronic fund transfers and providing coin and currency service.

(7) *Payment systems.* Payment systems are any methods used to facilitate the movement of funds for transactional purposes. Payment systems may include Automated Clearing House, wire transfer, item processing and settlement services.

(8) *Trustee or custodial services.* Trustee services are services in which the corporate credit union is authorized to act under a written trust agreement to the extent permitted under part 724 of this chapter. Custodial and safe-

keeping services are services a corporate credit union performs on behalf of its member to act as custodian or safekeeper of investments.

(b) *Procedure for adding services that are not preapproved.* To provide a service to its members that is not preapproved by NCUA:

(1) A federal corporate credit union must request approval from NCUA. The request must include a full explanation and complete documentation of the service and how the service relates to a corporate credit union's authority to provide services to its members. The request must be submitted jointly to the OCCU Director and the Secretary of the Board. The request will be treated as a petition to amend § 704.12 and NCUA will request public comment or otherwise act on the petition within a reasonable period of time. Before engaging in the formal approval process, a corporate credit union should seek an advisory opinion from NCUA's Office of General Counsel as to whether a proposed service is already covered by one of the authorized categories without filing a petition to amend the regulation; and

(2) A state-chartered corporate credit union must submit a request for a waiver that complies with § 704.1(b) to the OCCU Director.

(c) *Prohibition.* A corporate credit union is prohibited from purchasing loan servicing rights.

§ 704.13 [Removed and Reserved].

§ 704.14 Representation.

(a) *Board representation.* The board will be determined as stipulated in its bylaws governing election procedures, provided that:

(1) At least a majority of directors, including the chair of the board, must serve on the board as representatives of member credit unions;

(2) The chair of the board may not serve simultaneously as an officer, director, or employee of a credit union trade association;

(3) A majority of directors may not serve simultaneously as officers, directors, or employees of the same credit union trade association or its affiliates (not including chapters or other subunits of a state trade association);

(4) For purposes of meeting the requirements of paragraphs (a)(2) and (a)(3) of this section, an individual may not serve as a director or chair of the board if that individual holds a subordinate employment relationship to another employee who serves as an officer, director, or employee of a credit union trade association; and

(5) In the case of a corporate credit union whose membership is composed of more than 25 percent non credit unions, the majority of directors serving as representatives of member credit unions, including the chair, must be elected only by member credit unions.

(b) *Credit union trade association.* As used in this section, a credit union trade association includes but is not limited to, state credit union leagues and league service corporations and national credit union trade associations.

(c) *Representatives of organizational members.* (1) An organizational member of a corporate credit union is a member that is not a natural person. An organizational member may appoint one of its members or officials as a representative to the corporate credit union. The representative shall be empowered to attend membership meetings, to vote, and to stand for election on behalf of the member. No individual may serve as the representative of more than one organizational member in the same corporate credit union.

(2) Any vacancy on the board of a corporate credit union caused by a representative being unable to complete his or her term shall be filled by the board of the corporate credit union according to its bylaws governing the filling of board vacancies.

(d) *Recusal provision.* (1) No director, committee member, officer, or employee of a corporate credit union shall in any manner, directly or indirectly, participate in the deliberation upon or the determination of any question affecting his or her pecuniary interest or the pecuniary interest of any entity (other than the corporate credit union) in which he or she is interested, except if the matter involves general policy applicable to all members, such as setting dividend or loan rates or fees for services.

(2) An individual is "interested" in an entity if he or she:

(i) Serves as a director, officer, or employee of the entity;

(ii) Has a business, ownership, or deposit relationship with the entity; or

(iii) Has a business, financial, or familial relationship with an individual whom he or she knows has a pecuniary interest in the entity.

(3) In the event of the disqualification of any directors, by operation of paragraph (c)(1) of this section, the remaining qualified directors

present at the meeting, if constituting a quorum with the disqualified directors, may exercise, by majority vote, all the powers of the board with respect to the matter under consideration. Where all of the directors are disqualified, the matter must be decided by the members of the corporate credit union.

(4) In the event of the disqualification of any committee member by operation of paragraph (c)(1) of this section, the remaining qualified committee members, if constituting a quorum with the disqualified committee members, may exercise, by majority vote, all the powers of the committee with respect to the matter under consideration. Where all of the committee members are disqualified, the matter shall be decided by the board of directors.

(e) *Administration.* (1) A corporate credit union shall be under the direction and control of its board of directors. While the board may delegate the performance of administrative duties, the board is not relieved of its responsibility for their performance. The board may employ a chief executive officer who shall have such authority and such powers as delegated by the board to conduct business from day to day. Such chief executive officer must answer solely to the board of the corporate credit union, and may not be an employee of a credit union trade association.

(2) The provisions of § 701.14 of this chapter apply to corporate credit unions, except that where "Regional Director" is used, read "NCUA Board."

§ 704.15 Audit requirements.

(a) *External audit.* The corporate credit union supervisory committee shall cause an annual opinion audit of the financial statements to be made. The audit must be performed in accordance with generally accepted auditing standards and the audited financial statements must be prepared consistent with GAAP, except where law or regulation has provided for a departure from GAAP. The supervisory committee shall submit the audit report to the board of directors. A copy of the audit report, and copies of all communications that are provided to the corporate credit union by the external auditor, shall be submitted to the OCCU Director within 30 calendar days after receipt by the board of directors. If requested by the OCCU Director, the external auditor's workpapers shall be made available, at the auditor's office or elsewhere, for the OCCU Director's review. The corporate credit union shall submit a summary of the audit report to the membership at the next annual meeting.

(b) *Internal audit.* A corporate credit union with average daily assets in excess of $400 million for the preceding calendar year, or as ordered by the OCCU Director, must employ or contract, on a full- or part-time basis, the services of an internal auditor. The internal auditor's responsibilities will, at a minimum, comply with the Standards and Professional Practices of Internal Auditing, as established by the Institute of Internal Auditors. The internal auditor will report directly to the chair of the corporate credit union's supervisory committee, who may delegate supervision of the internal auditor's daily activities to the chief executive officer of the corporate credit union. The internal auditor's reports, findings, and recommendations will be in writing and presented to the supervisory committee no less than quarterly, and will be provided upon request to the external auditor and the OCCU Director.

§ 704.16 Contracts/written agreements.

Services, facilities, personnel, or equipment shared with any party shall be supported by a written contract, with the duties and responsibilities of each party specified and the allocation of service fee/expenses fully supported and documented.

§ 704.17 State-chartered corporate credit unions.

(a) This part does not expand the powers and authorities of any state-chartered corporate credit union, beyond those powers and authorities provided under the laws of the state in which it was chartered.

(b) A state-chartered corporate credit union that is not insured by the NCUSIF, but that receives funds from federally insured credit unions, is considered an "institution-affiliated party" within the meaning of Section 206(r) of the Federal Credit Union Act, 12 U.S.C. 1786(r).

(c) NCUA will notify, consult with, and provide explanation to the appropriate state supervisory authority before taking administrative action against a state-chartered corporate credit union.

§ 704.18 Fidelity bond coverage.

(a) *Scope.* This section provides the fidelity bond requirements for employees and officials in corporate credit unions.

(b) *Review of coverage.* The board of directors of each corporate credit union shall, at least annually, carefully review the bond coverage in force to determine its adequacy in relation to risk exposure and to the minimum requirements in this section.

(c) *Minimum coverage; approved forms.* Every corporate credit union will maintain bond coverage with a company holding a certificate of authority from the Secretary of the Treasury. All bond forms, and any riders and endorsements which limit the coverage provided by approved bond forms, must receive the prior written approval of NCUA. Fidelity bonds must provide coverage for the fraud and dishonesty of all employees, directors, officers, and supervisory and credit committee members. Notwithstanding the foregoing, all bonds must include a provision, in a form approved by NCUA, requiring written notification by surety to NCUA:

(1) When the bond of a credit union is terminated in its entirety;

(2) When bond coverage is terminated, by issuance of a written notice, on an employee, director, officer, supervisory or credit committee member; or

(3) When a deductible is increased above permissible limits. Said notification shall be sent to NCUA and shall include a brief statement of cause for termination or increase.

(d) *Minimum coverage amounts.* (1) The minimum amount of bond coverage will be computed based on the corporate credit union's daily average net assets for the preceding calendar year. The following table lists the minimum requirements:

Daily average net assets	Minimum bond (million)
Less than $50 million	$1.0
$50–$99 million	2.0
$100–$499 million	4.0
$500–$999 million	6.0
$1.0–$1.999 billion	8.0
$2.0–$4.999 billion	10.0
$5.0–$9.999 billion	15.0
$10.0–$24.999 billion	20.0
$25.0 billion plus	25.0

(2) It is the duty of the board of directors of each corporate credit union to provide adequate protection to meet its unique circumstances by obtaining, when necessary, bond coverage in excess of the minimums in the table in paragraph (d)(1) of this section.

(e) *Deductibles.* (1) The maximum amount of deductibles allowed are based on the corporate credit union's core capital ratio. The following table sets out the maximum deductibles, except that in each category the maximum deductible shall be $5 million:

Core Capital ratio	Maximum deductible
Less than 1.0 percent	7.5 percent of the sum of retained earnings and paid-in capital.
1.0–1.74 percent	10.0 percent of the sum of retained earnings and paid-in capital.
1.75–2.24 percent	12.0 percent of the sum of retained earnings and paid-in capital.
Greater than 2.25 percent	15.0 percent of the sum of retained earnings and paid-in capital.

(2) A deductible may be applied separately to one or more insuring clauses in a blanket bond. Deductibles in excess of those showing in this section must have the written approval of NCUA at least 30 calendar days prior to the effective date of the deductibles.

(f) *Additional coverage.* NCUA may require additional coverage for any corporate credit union when, in the opinion of NCUA, current coverage is insufficient. The board of directors of the corporate credit union must obtain additional coverage within 30 calendar days after the date of written notice from NCUA.

§ 704.19 Wholesale corporate credit unions.

(a) *General.* Wholesale corporate credit unions are subject to the preceding requirements of this part, except as set forth in this section.

(b) *Earnings retention requirement.* A wholesale corporate credit union must increase retained earnings if the prior month-end retained earnings ratio is less than 1 percent.

(1) Its retained earnings must increase:

(i) During the current month, by an amount equal to or greater than the monthly earnings retention amount; or

(ii) During the current and prior two months, by an amount equal to or greater than the quarterly earnings retention amount.

(2) Earnings retention amounts are calculated as follows:

(i) The monthly earnings retention amount is determined by multiplying the earnings retention factor by the prior month-end moving daily average net assets; and

(ii) The quarterly earnings retention amount is determined by multiplying the earnings retention factor by moving daily average net assets for each of the prior three month-ends.

(3) The earnings retention factor is determined as follows:

(i) If the prior month-end retained earnings ratio is less than 1 percent and the core capital ratio is less than 3 percent, the earnings retention factor is .15 percent per annum; or

(ii) If the prior month-end retained earnings ratio is less than 1 percent and the core capital ratio is equal to or greater than 3 percent, the earnings retention factor is .075 percent per annum.

(4) The OCCU Director may approve a decrease to the earnings retention amount set forth in this section if it is determined a lesser amount is necessary to avoid a significant adverse impact upon a wholesale corporate credit union.

(5) Operating management of the wholesale corporate credit union must notify its board of directors, supervisory committee, OCCU Director and, if applicable, the state regulator within 10 calendar days of determining the retained earnings ratio has declined below 1 percent. If the decline in the retained earnings ratio is due in full or in part, to a decline in the dollar amount of retained earnings and the retained earnings ratio is not restored to at least 1 percent by the next month end, a retained earnings action plan is required to be submitted within 30 calendar days.

(6) The retained earnings action plan must be submitted to the OCCU Director and, if applicable, the state regulator and, at a minimum, include the following:

(i) Reasons why the dollar amount of retained earnings has decreased;

(ii) Description of actions to be taken to increase the dollar amount of retained earnings within specific time frames; and

(iii) Monthly balance sheet and income projections, including assumptions for the ensuing 12-month period.

Appendix A to Part 704—Model Forms

This appendix contains sample forms intended for use by corporate credit unions to aid in compliance with the membership capital account and paid-in capital disclosure requirements of § 704.3.

SAMPLE FORM 1

Terms and Conditions of Membership Capital Account

(1) A membership capital account is not subject to share insurance coverage by the NCUSIF or other deposit insurer.

(2) A membership capital account is not releasable due solely to the merger, charter conversion or liquidation of the member credit union. In the event of a merger, the membership capital account transfers to the continuing credit union. In the event of a charter conversion, the membership capital account transfers to the new institution. In the event of liquidation, the membership capital account may be released to facilitate the payout of shares with the prior written approval of NCUA.

(3) A member credit union may withdraw membership capital with three years' notice.

(4) Membership capital cannot be used to pledge borrowings.

(5) Membership capital is available to cover losses that exceed retained earnings and paid-in capital.

(6) Where the corporate credit union is liquidated, membership capital accounts are payable only after satisfaction of all liabilities of the liquidation estate including uninsured obligations to shareholders and the NCUSIF.

(7) Where the corporate credit union is merged into another corporate credit union, the membership capital account will transfer to the continuing corporate credit union. The three-year notice period for withdrawal of the membership capital account will remain in effect.

(8) {If an adjusted balance account}: The membership capital balance will be adjusted ____(1 or 2)_____ time(s) annually in relation to the member credit union's _____ (assets or other measure)

_____ as of _____(date(s))_____. {If a term certificate}: The membership capital account is a term certificate that will mature on _____(date)_____.

I have read the above terms and conditions and I understand them.

I further agree to maintain in the credit union's files the annual notice of terms and conditions of the membership capital account.

The notice form must be signed by either all of the directors of the member credit union or, if authorized by board resolution, the chair and secretary of the board of the credit union.

The annual disclosure notice form must be signed by the chair of the corporate credit union. The chair must then sign a statement that certifies that the notice has been sent to member credit unions with membership capital accounts. The certification must be maintained in the corporate credit union's files and be available for examiner review.

SAMPLE FORM 2

Terms and Conditions of Paid-In Capital

(1) A paid-in capital account is not subject to share insurance coverage by the NCUSIF or other deposit insurer.

(2) A paid-in capital account is not releasable due solely to the merger, charter conversion or liquidation of the member credit union. In the event of a merger, the paid-in capital account transfers to the continuing credit union. In the event of a charter conversion, the paid-in capital account transfers to the new institution. In the event of liquidation, the paid-in capital account may be released to facilitate the payout of shares with the prior written approval of NCUA.

(3) The funds are callable only at the option of the corporate credit union and only if the corporate credit union meets its minimum required capital and NEV ratios after the funds are called.

(4) Paid-in capital cannot be used to pledge borrowings.

(5) Paid-in capital is available to cover losses that exceed retained earnings.

(6) Where the corporate credit union is liquidated, paid-in capital accounts are payable only after satisfaction of all liabilities of the liquidation estate including uninsured obligations to shareholders and the NCUSIF, and membership capital holders.

(7) Where the corporate credit union is merged into another corporate credit union, the paid-in capital account will transfer to the continuing corporate credit union.

(8) Paid-in capital is perpetual maturity and noncumulative dividend.

I have read the above terms and conditions and I understand them. I further agree to maintain in the credit union's files the annual notice of terms and conditions of the paid-in capital instrument.

The notice form must be signed by either all of the directors of the credit union or, if authorized by board resolution, the chair and secretary of the board of the credit union.

Appendix B to Part 704—Expanded Authorities and Requirements

A corporate credit union may obtain all or part of the expanded authorities contained in this Appendix if it meets the applicable requirements of Part 704 and Appendix B, fulfills additional management, infrastructure, and asset and liability requirements, and receives NCUA's written approval. Additional guidance is set forth in the NCUA publication Guidelines for Submission of Requests for Expanded Authority.

A corporate credit union seeking expanded authorities must submit to NCUA a self-assessment plan supporting its request. A corporate credit union may adopt expanded authorities when NCUA has provided final approval. If NCUA denies a request for expanded authorities, it will advise the corporate credit union of the reason(s) for the denial and what it must do to resubmit its request. NCUA may revoke these expanded authorities at any time if an analysis indicates a significant deficiency. NCUA will notify the corporate credit union in writing of the identified deficiency. A corporate credit union may request, in writing, reinstatement of the revoked authorities by providing a self-assessment plan detailing how it has corrected the deficiency.

Minimum Requirement

In order to participate in any of the authorities set forth in Base-Plus, Part I, Part II, Part III, Part IV, and Part V of this Appendix, a corporate credit union must evaluate monthly the changes in NEV and the NEV ratio for the tests set forth in § 704.8(d)(1)(i).

Base-Plus

A corporate that has met the requirements for this Base-plus authority may, in performing the rate stress tests set forth in § 704.8(d)(1)(i), allow its NEV to decline as much as 20 percent.

Part I

(a) A corporate credit union that has met the requirements for this Part I may:

(1) Purchase investments with long-term ratings no lower than A– (or equivalent);

(2) Purchase investments with short-term ratings no lower than A–2 (or equivalent), provided that the issuer has a long-term rating no lower than A– (or equivalent) or the investment is a domestically-issued asset-backed security;

(3) Engage in short sales of permissible investments to reduce interest rate risk;

(4) Purchase principal only (PO) stripped mortgage-backed securities to reduce interest rate risk; and

(5) Enter into a dollar roll transaction.

(b) Aggregate investments in repurchase and securities lending agreements with any one counterparty are limited to 300 percent of capital.

(c) In performing the rate stress tests set forth in § 704.8(d)(1)(i), the NEV of a corporate credit union that has met the requirements of this Part I may decline as much as:

(1) 20 percent;

(2) 28 percent if the corporate credit union has a 5 percent minimum capital ratio and is specifically approved by NCUA; or

(3) 35 percent if the corporate credit union has a 6 percent minimum capital ratio and is specifically approved by NCUA.

(d) The maximum aggregate amount in unsecured loans and lines of credit to any one member credit union, excluding pass-through and guaranteed loans from the CLF and the NCUSIF, must not exceed 100 percent of the corporate credit union's capital. The board of directors must establish the limit, as a percent of the corporate credit union's capital plus pledged shares, for secured loans and lines of credit.

Part II

(a) A corporate credit union that has met the requirements for this Part II may:

(1) Purchase investments with long-term ratings no lower than BBB (flat) (or equivalent). The aggregate of all investments rated BBB+ (or equivalent) or lower in any single obligor is not to exceed 25 percent of capital;

(2) Purchase investments with short-term ratings no lower than A–2 (or equivalent), provided that the issuer has a long-term rating no lower than BBB (flat) (or equivalent) or the investment is a domestically issued asset-backed security;

(3) Engage in short sales of permissible investments to reduce interest rate risk;

(4) Purchase principal only (PO) stripped mortgage-backed securities to reduce interest rate risk; and

(5) Enter into a dollar roll transaction.

(b) Aggregate investments in repurchase and securities lending agreements with any one counterparty are limited to 400 percent of capital.

(c) In performing the rate stress tests set forth in § 704.8(d)(1)(i), the NEV of a corporate credit union which has met the requirements of this Part II may decline as much as:

(1) 20 percent;

(2) 28 percent if the corporate credit union has a 5 percent minimum capital ratio and is specifically approved by NCUA; or

(3) 35 percent if the corporate credit union has a 6 percent minimum capital ratio and is specifically approved by NCUA.

(d) The maximum aggregate amount in unsecured loans and lines of credit to any one member credit union, excluding pass-through and guaranteed loans from the CLF and the NCUSIF, must not exceed 100 percent of the corporate credit union's capital. The board of directors must establish the limit, as a percent of the corporate credit union's capital plus pledged shares, for secured loans and lines of credit.

Part III

(a) A corporate credit union that has met the requirements of either Part I or Part II of this Appendix and the additional requirements for Part III may invest in:

(1) Debt obligations of a foreign country;

(2) Deposits and debt obligations of foreign banks or obligations guaranteed by these banks;

(3) Marketable debt obligations of foreign corporations. This authority does not apply to debt obligations that are convertible into the stock of the corporation; and

(4) Foreign issued asset-backed securities.

(b) All foreign investments are subject to the following requirements:

(1) Investments must be rated no lower than the minimum permissible domestic rating under the corporate credit union's Part I or Part II authority;

(2) A sovereign issuer, and/or the country in which an obligor is organized, must have a long-term foreign currency (non-local currency) debt rating no lower than AA– (or equivalent);

(3) For each approved foreign bank line, the corporate credit union must identify the specific banking centers and branches to which it will lend funds;

(4) Obligations of any single foreign obligor may not exceed 50 percent of capital; and

(5) Obligations in any single foreign country may not exceed 250 percent of capital.

Part IV

(a) A corporate credit union that has met the requirements for this Part IV may enter into derivative transactions specifically approved by NCUA to:

(1) Create structured products;

(2) Manage its own balance sheet; and

(3) Hedge the balance sheets of its members.

(b) Credit Ratings:

(1) All derivative transactions are subject to the following requirements:

(i) If the counterparty is domestic, the counterparty rating must be no lower than the minimum permissible rating for comparable term permissible investments; and

(ii) If the counterparty is foreign, the corporate must have Part III expanded authority and the counterparty rating must be no lower that the minimum permissible rating for a comparable term investment under Part III Authority.

(iii) Any rating(s) relied upon to meet the requirements of this part must be identified at the time the transaction is entered into and must be monitored for as long as the contract remains open.

(iv) Section 704.10 of this part if:

(A) one rating was relied upon to meet the requirements of this part and that rating is downgraded below the minimum rating requirements of this part; or

(B) two or more ratings were relied upon to meet the requirements of this part and at least two of those ratings are downgraded below the minimum rating requirements of this part.

(2) Exceptions. Credit ratings are not required for derivative transactions with:

(i) Domestically chartered credit unions;

(ii) U.S. government sponsored enterprises; or

(iii) Counterparties if the transaction is fully guaranteed by an entity with a minimum permissible rating for comparable term investments.

Part V

A corporate credit union that has met the requirements for this Part V may participate in loans with member natural person credit unions as approved by the OCCU Director and subject to the following:

(a) The maximum aggregate amount of participation loans with any one member credit union must not exceed 25 percent of capital; and

(b) The maximum aggregate amount of participation loans with all member credit unions will be determined on a case-by-case basis by the OCCU Director.

Part 705

Community Development Revolving Loan Program For Credit Unions

§ 705.0 Applicability.

Monies from the Community Development Revolving Loan Fund for Credit Unions are governed by this Part.

§ 705.1 Scope.

(a) This Part implements the Community Development Revolving Loan Program for Credit Unions (Program) under the sole administration of the National Credit Union Administration.

(b) This Part establishes the following:

(1) Definitions;

(2) The application process and requirements for qualifying for a loan under the program;

(3) How loan funds are to be made available and their repayment; and

(4) Technical assistance to be provided to participating credit unions.

§ 705.2 Purpose of the Program.

(a) The Community Development Revolving Loan Program for Credit Unions is intended to support the efforts of participating credit unions through loans to those credit unions in:

(1) Providing basic financial and related services to residents in their communities; and

(2) Stimulating economic activities in the communities they service which will result in increased income, ownership and employment opportunities for low-income residents, and other community growth efforts.

(b) The policy of NCUA is to revolve loan funds to qualifying credit unions as often as practical in order to gain maximum economic impact on as many participating credit unions as possible.

§ 705.3 Definitions.

(a)(1) The term "low-income members" shall mean those members who make less than 80 percent of the average for all wage earners as established by the Bureau of Labor Statistics or those members whose annual household income falls at or below 80 percent of the median household income for the nation as established by the Census Bureau or those members otherwise defined as low-income members as determined by order of the NCUA Board.

(2) In documenting its low-income membership, a credit union that serves a geographic area where a majority of residents fall at or below the annual income standard is presumed to be serving predominantly low-income members. In applying the standards, Regional Directors shall make allowances for geographical areas with higher costs of living. The following is the exclusive list of geographic areas and the differentials to be used:

	Percent
Hawaii	40
Alaska	36
Washington, DC	19
Boston	17
San Diego	15
Los Angeles	14
New York	13
San Francisco	13
Seattle	10
Chicago	7
Philadelphia	7

(b) For purposes of this part, a *participating credit union* means a state- or federally-chartered credit union that is specifically involved in the stimulation of economic development activities and community revitalization efforts aimed at benefiting the community it serves; whose membership consists of predominantly low-income members as defined in paragraph (a) of this section or applicable state standards as reflected by a current low-income designation pursuant to § 701.34(a)(1) or § 741.204 of this chapter or, in the case of a state-chartered nonfederally insured credit union, under applicable state standards; and has submitted an application for a loan and/or technical assistance and has been selected for participation in the Program in accordance with this part.

§ 705.4 Program Activities.

In order to meet the objectives of the Program, a credit union applicant should provide a variety of financial and related services designed to meet the particular needs of the low-income community served. These activities shall include basic member share accounts and member loan services.

§ 705.5 Application for Participation.

(a) Applications to participate and qualify for a loan or technical assistance under the Program may be obtained from the National Credit Union Administration, Community Development Revolving Loan Program for Credit Unions.

(b) The application for a loan shall contain the following information:

(1) Information demonstrating a sound financial position and the credit union's ability to manage its day-to-day business affairs, including the credit union's latest financial statement. Nonfederally insured credit unions must include the following:

(i) A copy of its most recent outside audit report;

(ii) Proof of deposit and surety bond insurance which states the maximum insurance levels permitted by the policies;

(iii) A balance sheet, an income and expense statement, and a schedule of delinquent loans, for the most recent month-end and each of the twelve months preceding that month-end.

(2) Evidence that the credit union has a need for increased funds in order to improve financial services to its members.

(3) The following information concerning a state-chartered credit union's field of membership:

(i) Current field of membership as set forth in the credit union's charter;

(ii) Changes, if any, to be made to the field of membership for participation in the Program, including:

(A) Evidence of approval of change by credit union board of directors;

(B) Evidence of submission and approval of change by the state supervisor;

(iii) Current designation as a low-income credit union if the credit union is not federally insured.

(4) Along with a community needs plan, specifics of how the credit union proposes to serve the needs of its members and the community with Program funds. The applicant credit union will also construct and submit a plan for its growth and development. The plan will set forth objectives for financial growth, credit union development and capitalization, and the means for achieving these objectives.

(5) Indication of any other involvement in existing community development programs of state and federal agencies.

(c) NCUA will notify applicant credit unions as to whether or not they have qualified for a loan or technical assistance under this Part. Reasons for nonqualification will be stated. Any applicant whose qualification is denied may appeal that decision to the NCUA Board.

§ 705.6 Community Needs Plan.

(a) The credit union's board of directors will prepare a Community Needs Plan and submit it with its loan application. The Plan will contain a list of needed community services that the credit union will provide.

(b) The credit union's board of directors will report on the progress of providing needed community services to the credit union members once a year, either at the annual meeting or in a written report sent to all members. The credit union will also submit the written report or a summary of the report given at the annual meeting to NCUA.

§ 705.7 Loans to Participating Credit Unions.

(a) *Amount and Recording of Loans.* A participating credit union will be eligible to receive up to $300,000, in the aggregate as determined by the NCUA Board, in the form of a loan from the Community Development Revolving Loan Fund for Credit Unions. The amount of the loan will be based on funds availability, the creditworthiness of the participating credit union, financial need, and a demonstrated capability of a participating credit union to provide financial and related services to its members. At the discretion of NCUA, a loan will be recorded by a participating credit union as either a note payable or a nonmember deposit.

(b) *Matching Requirements.* Participating credit unions will be encouraged to develop, as rapidly as possible, a permanent source of member shares.

(1) Generally loan monies made available must be matched by the participating credit

union by increasing its share deposits in an amount equal to the loan amount. However, any loan monies matched by member share deposits will be credited as two-for-one match. Nonmember share deposits accepted to meet the matching requirement are not subject to the 20 percent limitation on nonmember deposits under § 701.32. Participating credit unions must meet this matching requirement within one year of the approval of the loan application and must maintain the increase in the total amount of share deposits for the duration of the loan. Once the loan is repaid, nonmember share deposits accepted to meet the matching requirement are subject to § 701.32.

(2) Upon approval of its loan application, and before it meets its matching requirement, a participating credit union may receive the entire loan commitment in a single payment. If any funds are withheld, the remainder of the funds committed will be available to the participating credit union only after it has documented that it has met the match requirement for the total amount of the loan committed.

(3) Failure of a participating credit union to generate the required match within one year of the approval of the loan will result in the reduction of the loan proportionate to the amount of match actually generated. Payment of any additional funds initially approved will be limited as appropriate to reflect the revised amount of the loan approved. Any funds already advanced to the participating credit union in excess of the revised amount of loan approval must be repaid immediately to NCUA. Failure to repay such funds to NCUA upon demand shall result in the default of the entire loan.

(c) *Terms and Repayment.* (1) Assistance made available through Program loans, whether recorded by the credit union as a note payable or nonmember deposit at NCUA's direction, is in the form of a loan and must be repaid to NCUA. All loans will be scheduled for repayment within the shortest time compatible with sound business practices and with objectives of the Program, but in no case will the term exceed five years.

(2) Semiannual interest payments (beginning six months after the initial distribution of a loan) and semiannual principal payments (beginning one year after the initial distribution of a loan) will be required.

(d) *Interest Rates.* Loans made under this Part shall bear interest at a fixed annual percentage rate of not more than 3 percent and not less than 1 percent as determined by the NCUA Board.

(e) *Default, Collections and Adjustments.* The terms of each loan agreement shall provide for the immediate acceleration of the unpaid balance for breach or default in the performance by the participating credit union of the terms or conditions of the loan. This will include misrepresentations, default in making interest/principal payments, failure to report, insolvency, failure to maintain adequate match for the duration of the loan period, etc. The unpaid balance will also be accelerated and immediately due if any part of the loan funds are improperly used, or if uninvested loan proceeds remain unused for an unreasonable or unjustified period of time.

§ 705.8 State-Chartered Credit Unions.

State-chartered credit union loan applicants approved for participation by NCUA must obtain written concurrence from their respective state regulatory authority. Such applicants shall make copies of their state examination reports available to NCUA and shall agree to examination by NCUA for the limited purpose of compliance with this Part.

§ 705.9 Application Period.

NCUA will announce annually and publish in the Federal Register when applications for participation in the Program may be submitted. Such notice will be dependent upon the availability of funds.

§ 705.10 Technical Assistance.

NCUA may provide technical assistance to participating credit unions directly or through outside providers selected by the credit unions or NCUA. NCUA will base technical assistance on funds availability, the needs of the participating credit union, and a demonstrated capability of the participating credit union to provide financial and related services to its members. NCUA will consider applications for technical assistance and determine whether to grant them in accordance with established procedures and standards that are publicly available. Participating credit unions can be provided with technical assistance without obtaining a Program loan. NCUA technical assistance will aid participating credit unions in providing services to their members and in the efficient operation of such credit unions.

Part 706

Credit Practices

§ 706.1 Definitions.

(a) *Person.* An individual, corporation, or other business organization.

(b) *Consumer.* A natural person member who seeks or acquires goods, services, or money for personal, family, or household use.

(c) *Obligation.* An agreement between a consumer and a Federal credit union.

(d) *Debt.* Money that is due or alleged to be due from one to another.

(e) *Earnings.* Compensation paid or payable to an individual or for his or her account for personal services rendered or to be rendered by him or her, whether denominated as wages, salary, commission, bonus, or otherwise, including periodic payments pursuant to a pension, retirement, or disability program.

(f) *Household goods.* Clothing, furniture, appliances, one radio and one television, linens, china, crockery, kitchenware, and personal effects (including wedding rings) of the consumer and his or her dependents, provided that the following are not included within the scope of the term "household goods":

(1) Works of art;

(2) Electronic entertainment equipment (except one television and one radio);

(3) Items acquired as antiques; and

(4) Jewelry (except wedding rings).

(g) *Antique.* Any item over one hundred years of age, including such items that have been repaired or renovated without changing their original form or character.

(h) *Cosigner.* A natural person who renders himself or herself liable for the obligation of another person without receiving goods, services, or money in return for the credit obligation, or, in the case of an open-end credit obligation, without receiving the contractual right to obtain extensions of credit under the obligation. The term includes any person whose signature is requested as a condition to granting credit to a consumer, or as a condition for forbearance on collection of a consumer's obligation that is in default. The term does not include a spouse whose signature is required on a credit obligation to perfect a security interest pursuant to state law. A person is a cosigner within the meaning of this definition whether or not he or she is designated as such on a credit obligation.

§ 706.2 Unfair Credit Practices.

(a) In connection with the extension of credit to consumers, it is an unfair act or practice for a Federal credit union, directly or indirectly, to take or receive from a consumer an obligation that:

(1) Constitutes or contains a cognovit or confession of judgment (for purposes other than executory process in the State of Louisiana), warrant of attorney, or other waiver of the right to notice and the opportunity to be heard in the event of suit or process thereon.

(2) Constitutes or contains an executory waiver or a limitation of exemption from attachment, execution, or other process on real or personal property held, owned by, or due to the consumer, unless the waiver applies solely to property subject to a security interest executed in connection with the obligation.

(3) Constitutes or contains an assignment of wages or other earnings unless:

(i) The assignment by its terms is revocable at the will of the debtor, or

(ii) The assignment is a payroll deduction plan or preauthorized payment plan, commencing at the time of the transaction, in which the consumer authorizes a series of wage deductions as a method of making each payment, or

(iii) The assignment applies only to wages or other earnings already earned at the time of the assignment.

(4) Constitutes or contains a nonpossessory security interest in household goods other than a purchase money security interest.

§ 706.3 Unfair or Deceptive Cosigner Practices.

(a) *Prohibited practices.* In connection with the extension of credit to consumers, it is:

(1) A deceptive act or practice for a Federal credit union, directly or indirectly, to misrepresent the nature or extent of cosigner liability to any person.

(2) An unfair act or practice for a Federal credit union, directly or indirectly, to obligate a cosigner unless the cosigner is informed prior to becoming obligated, which in the case of open-end credit means prior to the time that the agreement creating the cosigner's liability for future charges is executed, of the nature of his or her liability as cosigner.

(b) Disclosure requirement.

(1) To comply with the cosigner information requirement of paragraph (a)(2), a clear and conspicuous disclosure statement shall be given in writing to the cosigner prior to becoming obligated. The disclosure statement will contain only the following statement, or one which is substantially equivalent, and shall either be a separate document or included in the documents evidencing the consumer credit obligation.

NOTICE TO COSIGNER

> You are being asked to guarantee this debt. Think carefully before you do. If the borrower doesn't pay the debt, you will have to. Be sure you can afford to pay if you have to, and that you want to accept this responsibility.
>
> You may have to pay up to the full amount of the debt if the borrower does not pay. You may also have to pay late fees or collection costs, which increase this amount.
>
> The creditor can collect this debt from you without first trying to collect from the borrower. The creditor can use the same collection methods against you that can be used against the borrower, such as suing you, garnishing your wages, etc. If this debt is ever in default, that fact may become a part of your credit record.
>
> This notice is not the contract that makes you liable for the debt.

(2) If the notice to cosigner is a separate document, nothing other than the following items may appear with the notice. Items (i) through (v) may not be part of the narrative portion of the notice to cosigner.

(i) The name and address of the Federal credit union;

(ii) An identification of the debt to be cosigned (e.g., a loan identification number);

(iii) The amount of the loan;

(iv) The date of the loan;

(v) A signature line for a cosigner to acknowledge receipt of the notice; and

(vi) To the extent permitted by state law, a cosigner notice required by state law may be included in the paragraph (b)(1) notice.

(3) To the extent the notice to cosigner specified in paragraph (b)(1) refers to an action against a cosigner that is not permitted by state law, the notice to cosigner may be modified.

§ 706.4 Late Charges.

(a) In connection with collecting a debt arising out of an extension of credit to a consumer, it is an unfair act or practice for a Federal credit union, directly or indirectly, to levy or collect any delinquency charge on a payment, which payment is otherwise a full payment for the applicable period and is paid on its due date or within an applicable grace period, when the only delinquency is attributable to late fee(s) or delinquency charge(s) assessed on earlier installment(s).

(b) For purposes of this section, "collecting a debt" means any activity other than the use of judicial process that is intended to bring about or does bring about repayment of all or part of a consumer debt.

§ 706.5 State Exemptions.

(a) If, upon application to the NCUA by an appropriate state agency, the NCUA determines that:

(1) there is a state requirement or prohibition in effect that applies to any transaction to which a provision of this rule applies; and

(2) the state requirement or prohibition affords a level of protection to consumers that is substantially equivalent to, or greater than, the protection afforded by this rule; then that provision of this rule will not be in effect in the state to the extent specified by the NCUA in its determination, for as long as the state administers and enforces the state requirement or prohibition effectively.

(b) States that received an exemption from the Federal Trade Commission's Credit Practices Rule prior to September 17, 1987, are not required to reapply to NCUA for an exemption under subparagraph (a) of this section provided that the state forwards a copy of its exemption determination to the appropriate Regional Office. NCUA will honor the exemption for as long as the state administers and enforces the state requirement or

prohibition effectively. Any state seeking a greater exemption than that granted to it by the Federal Trade Commission must apply to NCUA for the exemption.

Part 707

Truth in Savings

§ 707.1 Authority, purpose, coverage and effect on state laws.

(a) *Authority.* This part is issued by the National Credit Union Administration Board to implement the Truth in Savings Act of 1991 (TISA), contained in the Federal Deposit Insurance Corporation Improvement Act of 1991 (12 U.S.C. § 4301 *et seq.,* Pub. L. No. 102–242, 105 Stat. 2236).

(b) *Purpose.* The purpose of this part is to enable credit union members and potential members to make informed decisions about accounts at credit unions. This part requires credit unions to provide disclosures so that members and potential members can make meaningful comparisons among credit unions and depository institutions.

(c) *Coverage.* This part applies to all credit unions whose accounts are either insured by, or eligible to be insured by, the National Credit Union Share Insurance Fund, except for any credit union that has been designated as a corporate credit union by the National Credit Union Administration and any credit union that has $2 million or less in assets, after subtracting any nonmember deposits, and is determined to be nonautomated by the National Credit Union Administration. In addition, the advertising rules in § 707.8 apply to any person who advertises an account offered by a credit union, including any person who solicits any amount from any other person for placement in a credit union.

(d) *Effect on state laws.* State law requirements that are inconsistent with the requirements of the TISA and this part are preempted to the extent of the inconsistency.

§ 707.2 Definitions.

For purposes of this part, the following definitions apply:

(a) *Account* means a share or deposit account at a credit union held by or offered to a member or potential member. It includes, but is not limited to, accounts such as share, share draft, checking and term share accounts. For purposes of the advertising regulations in § 707.8, the term also includes an account at a credit union that is held by or offered by a share or deposit broker.

(b) *Advertisement* means a commercial message, appearing in any medium, that promotes directly or indirectly the availability of, or a deposit in, an account.

(c) *Annual percentage yield* means a percentage rate reflecting the total amount of dividends paid on an account, based on the dividend rate and the frequency of compounding for a 365-day period and calculated according to the rules in Appendix A of this part.

(d) *Average daily balance method* means the application of a periodic rate to the average daily balance in the account for the period. The average daily balance is determined by adding the full amount of principal in the account for each day of the period and dividing that figure by the number of days in the period.

(e) *Board* means the National Credit Union Administration Board.

(f) *Bonus* means a premium, gift, award, or other consideration worth more than $10 (whether in the form of cash, credit, merchandise, or any equivalent) given or offered to a member during a year in exchange for opening, maintaining, or renewing an account, or increasing an account balance. The term does not include dividends, other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, or extraordinary dividends.

(g) *Credit union* means a federal or state-chartered credit union that is either insured by, or is eligible to apply for insurance from, the National Credit Union Share Insurance Fund.

(h) *Daily balance method* means the application of a daily periodic rate to the full amount of principal in the account each day.

(i) *Dividend and dividends* mean any declared or prospective earnings on a member's shares in a credit union to be paid to a member or to the member's account. For purposes of this part, the term does not include the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, or extraordinary dividends.

(j) *Dividend declaration date* means the date that the board of directors of a credit union de-

clares a dividend for the preceding dividend period.

(k) *Dividend period* means the span of time established by the board of directors of a credit union by the end of which shares in a member account earn dividend credit. The dividend period may be different for each type of account.

(l) *Dividend rate* means the declared or prospective annual dividend rate paid on an account, which does not reflect compounding. For purposes of the account disclosures in § 707.4(b)(1)(i), the rate may, but need not, be referred to as the "annual percentage rate" in addition to being referred to as the "dividend rate."

(m) *Extraordinary dividends* means a nonrepetitive dividend paid at an irregular time from funds legally available for such distribution.

(n) *Fixed-rate account* means an account that is not a variable rate account as defined in paragraph (z) of this section.

(o) *Grace period* means a period following the maturity of an automatically renewing term share account during which the member may withdraw funds without being assessed a penalty.

(p) *Interest* means any payment to a member or to a member's account for the use of funds in a nondividend-bearing account at a state-chartered credit union offered pursuant to state law, calculated by application of a periodic rate to the balance. For purposes of this regulation, the term does not include the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, or extraordinary dividends. Except as is specifically otherwise provided in this part, in the case of an interest-bearing account held in or offered by a state-chartered credit union pursuant to state law, the word "interest" shall be substituted for all references to "dividend" or "dividends" in this part.

(q) *Member* means:

(1) A natural person member of the credit union who holds an account primarily for personal, family, or household purposes;

(2) A natural person nonmember who holds an account primarily for personal, family, or household purposes, either jointly with a natural person member or in a credit union designated as a low-income credit union, or to whom such an account is offered; and

(3) A natural person nonmember who holds a deposit account in a state-chartered credit union pursuant to state law, or to whom such deposit account is offered.

The term does not include a natural person who holds an account for another in a professional capacity or an unincorporated nonbusiness association of natural person members.

(r) *Non-dividend membership benefits* means any property or service provided by a credit union to its members, the nature of which makes its valuation unreasonable and administratively impracticable.

(s) *Passbook account* means an account in which the member retains a book or other document in which the credit union records transactions on the account.

(t) *Periodic statement* means a statement setting forth information about an account (other than a term share account or passbook account) that is provided to a member on a regular basis four or more times a year.

(u) *Potential member* means a natural person within the credit union's field of membership (or an unincorporated nonbusiness association of such persons) or otherwise eligible to become a member as defined in paragraph (q) of this section.

(v) *State* means a state, the District of Columbia, the Commonwealth of Puerto Rico, and any territory or possession of the United States.

(w) *Stepped-rate account* means an account that has two or more dividend rates that take effect in succeeding periods and are known when the account is opened.

(x) *Term share account* means any share certificate, interest-bearing certificate of deposit account, or other account with a maturity of at least seven days in which the member generally does not have a right to make withdrawals for six days after the account is opened, unless the account is subject to an early withdrawal penalty of at least seven days' dividends on amounts withdrawn, offered by a credit union to a member or potential member.

(y) *Tiered-rate account* means an account that has two or more dividend rates that are applicable to specified balance levels.

(z) *Variable-rate account* means a share, share draft, checking, or term share account in which the simple dividend rate may change after the account is opened, unless the credit union contracts to give at least thirty days advance written notice of rate decreases.

§ 707.3 General disclosure requirements.

(a) *Form.* Credit unions must make the disclosures required by §§ 707.4 through 707.6 and § 707.10 of this part, as applicable, clearly and

conspicuously in writing and in a form the member or potential member may keep. Disclosures for each account offered by a credit union may be presented separately or combined with disclosures for the credit union's other accounts, as long as it is clear which disclosures are applicable to the member's account.

(b) *General.* The disclosures shall reflect the terms of the legal obligation between the member and the credit union. Disclosures may be made in languages other than English, provided the disclosures are available in English upon request.

(c) *Relation to Regulation E (12 CFR part 205).* Disclosures required by and provided in accordance with the Electronic Fund Transfer Act (15 U.S.C. 1601) and its implementing Regulation E (12 CFR part 205) that are also required by this part may be substituted for the disclosures required by this part.

(d) *Multiple members.* If an account is held by more than one member, disclosures may be made to any one of the members.

(e) *Oral responses to inquiries.* In an oral response to a member or potential member's inquiry about dividend rates payable on its accounts, the credit union shall state the annual percentage yield. The dividend rate may be stated in addition to the annual percentage yield. No other rate may be stated. In stating a dividend rate and annual percentage yield, a credit union shall:

(1) For dividend-bearing accounts other than term share accounts, specify a dividend rate and annual percentage yield as of the last dividend declaration date. In the event that disclosures of a dividend rate and annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective dividend rate and prospective annual percentage yield. Such prospective dividend rate and prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(2) For interest-bearing accounts and for dividend-bearing term share accounts, specify an interest (dividend) rate and annual percentage yield that were offered within the most recent seven calendar days; state that the rate and yield are accurate as of an identified date; and provide a telephone number members may call to obtain current rate information.

(f) *Rounding and accuracy rules for rates and yields.*

(1) *Rounding.* The annual percentage yield, the annual percentage yield earned, and the dividend rate shall be rounded to the nearest one-hundredth of one percentage point (.01%) and expressed to two decimal places. For account disclosures, the dividend rate may be expressed to more than two decimal places.

(2) *Accuracy.* The annual percentage yield (and the annual percentage yield earned) will be considered accurate if not more than one-twentieth of one percentage point (.05%) above or below the annual percentage yield (and the annual percentage yield earned) determined in accordance with the rules in Appendix A of this part.

(g) Electronic communication. For rules governing the electronic delivery of disclosures, including the definition of electronic communication, see § 707.10.

§ 707.4 Account disclosures.

(a) Delivery of account disclosures.—(1) *Account opening.*—(i) *General.* A credit union must provide account disclosures to a member or potential member before an account is opened or a service is provided, whichever is earlier. A credit union is deemed to have provided a service when a fee required to be disclosed is assessed. Except as provided in paragraph (a)(1)(ii) of this section, if the member is not present at the credit union when the account is opened or the service is provided and has not already received the disclosures, the credit union must mail or deliver the disclosures no later than 10 business days after the account is opened or the service is provided, whichever is earlier.

(ii) *Electronic communication.* If a member or potential member who is not present at the credit union uses electronic communication (as defined in § 707.10) to open an account or request a service, the disclosures required under paragraph (a)(1) of this section must be provided before an account is opened or a service is provided.

(2) *Requests.* (i) A credit union must provide account disclosures to a member or potential member upon request. If a member who is not present at the credit union makes a request, the credit union must mail or deliver the disclosures within a reasonable time after it receives the request and may provide the disclosures in paper form, or electronically if the member provides an electronic mail address.

(ii) In providing disclosures upon request, the credit union may:

(A) Specify rates as follows:

(*1*) For dividend-bearing accounts other than term share accounts, specify a dividend rate and annual percentage yield as of the last dividend declaration date. In the event that disclosures of a dividend rate and annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective dividend rate and prospective annual percentage yield. Such prospective dividend rate and prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(*2*) For interest-bearing accounts and for dividend-bearing term share accounts, specify an interest rate and annual percentage yield that were offered within the most recent seven calendar days; state that the rate and yield are accurate as of an identified date; and provide a telephone number members may call to obtain current rate information; and

(B) State the maturity of a term share account as either a term or a date.

(b) Content of account disclosures. Account disclosures shall include the following, as applicable:

(1) *Rate information.*

(i) *Annual percentage yield and dividend rate.*

(A) For interest-bearing accounts and for dividend-bearing term share accounts, the "annual percentage yield" and the "interest rate" ("dividend rate"), using those terms, and for fixed-rate accounts the period of time the interest (dividend) rate will be in effect.

(B) For dividend-bearing accounts other than term share accounts, a credit union shall specify a dividend rate and annual percentage yield (using those terms) as of the last dividend declaration date. In the event that disclosures of a dividend rate and annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective dividend rate and prospective annual percentage yield. Such prospective dividend rate and prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(ii) *Variable rates.* For variable-rate accounts:

(A) The fact that the dividend rate and annual percentage yield may change;

(B) How the dividend rate is determined;

(C) The frequency with which the dividend rate may change; and

(D) Any limitation on the amount the dividend rate may change.

(2) *Compounding and crediting.*

(i) *Frequency.* The frequency with which dividends are compounded and credited, and the dividend period for dividend-bearing accounts.

(ii) *Effect of closing an account.* If members will forfeit dividends if they close an account before accrued dividends are credited, a statement that the dividends will not be paid in such cases.

(3) *Balance information.*

(i) *Minimum balance requirements.* Any minimum balance required to:

(A) Open the account;

(B) Avoid the imposition of a fee; or

(C) Obtain the annual percentage yield disclosed.

Except for the balance to open the account, the disclosure shall state how the balance is determined for these purposes.

(ii) *Balance computation method.* An explanation of the balance computation method specified in § 707.7, used to calculate dividends on the account.

(iii) *When dividends begin to accrue.* A statement of when dividends begin to accrue on noncash deposits.

(4) *Fees.* The amount of any fee that may be imposed in connection with the account (or an explanation of how the fee will be determined) and the conditions under which the fee may be imposed.

(5) *Transaction limitations.* Any limitations on the number or dollar amount of withdrawals or deposits.

(6) *Features of Term Share Accounts.* For term share accounts:

(i) *Time requirements.* The maturity date.

(ii) *Early withdrawal penalties.* A statement that a penalty will be imposed for early withdrawal, how it is calculated, and the conditions for its assessment.

(iii) *Withdrawal of dividends prior to maturity.* If compounding occurs and dividends may be withdrawn prior to maturity, a statement that the annual percentage yield assumes

dividends remain in the account until maturity and that a withdrawal will reduce earnings. For accounts with a stated maturity greater than one year that do not compound dividends on an annual or more frequent basis, that require dividend payouts at least annually, and that disclose an APY determined in accordance with section E of appendix A of this part, a statement that dividends cannot remain on account and that payout of dividends is mandatory.

(iv) *Renewal policies.* A statement of whether or not the account will renew automatically at maturity. If it will, a statement of whether or not a grace period will be provided and, if so, the length of that period must be stated. If the account will not renew automatically, a statement of whether dividends will be paid after maturity if the member does not renew the account must be stated.

(7) *Bonuses.* The amount or type of any bonus, when the bonus will be provided, and any minimum balance and time requirements to obtain the bonus.

(8) *Nature of dividends.* For accounts earning dividends, other than term share accounts, a statement that dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

(c) *Notice to existing account holders.*

(1) *Notice of availability of disclosures.* Credit unions shall provide a notice to members who receive periodic statements and who hold existing accounts of the type offered by the credit union on January 1, 1995. The notice shall be included on or with the first periodic statement sent after January 1, 1995 (or on or with the first periodic statement for a statement cycle beginning on or after that date). The notice shall state that the members may request account disclosures containing terms, fees, and rate information for the account. In responding to such a request, credit unions shall provide disclosures in accordance with paragraph (a)(2) of this section.

(2) *Alternative to notice.* As an alternative to the notice described in paragraph (c)(1) of this section, credit unions may provide account disclosures to members. The disclosures may be provided either with a periodic statement or separately, but must be sent no later than when the periodic statement described in paragraph (c)(1) of this section is sent.

§ 707.5 Subsequent disclosures.

(a) *Change in terms.*

(1) *Advance notice required.* A credit union shall give advance notice to affected members of any change in a term required to be disclosed under § 707.4(b), if the change may reduce the annual percentage yield or adversely affect the member. The notice shall include the effective date of the change. The notice shall be mailed or delivered at least 30 calendar days before the effective date of the change.

(2) *No notice required.* No notice under this section is required for:

(i) *Variable-rate changes.* Changes in the dividend rate and corresponding changes in the annual percentage yield in variable-rate accounts.

(ii) *Share draft and check printing fees.* Changes in fees for check printing.

(iii) *Short-term term share accounts.* Changes in any term for term share accounts with maturities of one month or less.

(b) *Notice before maturity for term share accounts longer than one month that renew automatically.* For term share accounts with a maturity longer than one month that renew automatically at maturity, credit unions shall provide the disclosures described below before maturity. The disclosures shall be mailed or delivered at least 30 calendar days before maturity of the existing account. Alternatively, the disclosures may be mailed or delivered at least 20 calendar days before the end of the grace period on the existing account, provided a grace period of at least five calendar days is allowed.

(1) *Maturities of longer than one year.* If the maturity is longer than one year, the credit union shall provide account disclosures set forth in § 707.4(b) for the new account, along with the date the existing account matures. If the dividend rate and annual percentage yield that will be paid for the new account are unknown when disclosures are provided, the credit union shall state that those rates have not yet been determined, the date when they will be determined, and a telephone number members may call to obtain the dividend rate and the annual percentage yield that will be paid for the new account.

(2) *Maturities of one year or less but longer than one month.* If the maturity is one year or less but longer than one month, the credit union shall either:

(i) Provide disclosures as set forth in paragraph (b)(1) of this section; or

(ii) Disclose to the member:

(A) The date the existing account matures and the new maturity date if the account is renewed;

(B) The dividend rate and the annual percentage yield for the new account if they are known (or that those rates have not yet been determined, the date when they will be determined, and a telephone number the member may call to obtain the dividend rate and the annual percentage yield that will be paid for the new account); and

(C) Any difference in the terms of the new account as compared to the terms required to be disclosed under § 707.4(b) for the existing account.

(c) *Notice before maturity for term share accounts longer than one year that do not renew automatically.* For term share accounts with a maturity longer than one year that do not renew automatically at maturity, credit unions shall disclose to members the maturity date and whether dividends will be paid after maturity. The disclosures shall be mailed or delivered at least 10 calendar days before maturity of the existing account.

§ 707.6 Periodic statement disclosures.

(a) *Rule when statement and crediting periods vary.* In making the disclosures described in paragraph (b) of this section, credit unions that calculate and credit dividends for a period other than the statement period, such as the dividend period, may calculate and disclose the annual percentage yield earned and amount of dividends earned based on that period rather than the statement period. The information in paragraph (b)(4) shall be stated for that period as well as for the statement period.

(b) *Statement disclosures.* If a credit union mails or delivers a periodic statement, the statement shall include the following disclosures:

(1) *Annual percentage yield earned.* The "annual percentage yield earned," using that term as calculated according to the rules in Appendix A of this part.

(2) *Amount of dividends.* The dollar amount of dividends earned (accrued or paid and credited) on the account. The dollar amount of any extraordinary dividends earned during the statement period shall be shown as a separate figure.

(3) *Fees imposed.* Fees required to be disclosed under § 707.4(b)(4) of this part and imposed on the account during the statement period. The fees shall be itemized by type and dollar amounts.

(4) *Length of period.* The total number of days in the statement period, or the beginning and ending dates of the period.

§ 707.7 Payment of dividends.

(a) *Permissible methods.*

(1) *Balance on which dividends are calculated.* Credit unions shall calculate dividends on the full amount of principal in an account for each day by use of either the daily balance method or the average daily balance method. Credit unions shall calculate dividends by use of a daily rate of at least 1/365 of the dividend rate. In a leap year a daily rate of 1/366 of the dividend rate may be used.

(2) *Determination of minimum balance to earn dividends.* A credit union shall use the same method to determine any minimum balance required to earn dividends as it uses to determine the balance on which dividends are calculated. A credit union may use an additional method that is unequivocally beneficial to the member.

(b) *Compounding and crediting policies.* This section does not require credit unions to compound or credit dividends at any particular frequency.

(c) *Date dividends begin to accrue.* Dividends shall begin to accrue not later than the day specified in § 606 of the Expedited Funds Availability Act (12 U.S.C. 4005) and implementing Regulation CC (12 CFR part 229). Dividends shall accrue on funds until the day funds are withdrawn.

§ 707.8 Advertising.

(a) *Misleading or inaccurate advertisements.* An advertisement shall not be misleading or inaccurate and shall not misrepresent a credit union's account contract. An advertisement shall not refer to or describe an account as "free" or "no cost" (or contain a similar term) if any maintenance or activity fee may be imposed on the account. The word "profit" shall not be used in referring to interest paid on an account.

(b) *Permissible rates.* If an advertisement states a rate of return, it shall state the rate as an "an-

nual percentage yield," using that term. (The abbreviation "APY" may be used provided the term "annual percentage yield" is stated at least once in the advertisement.) The advertisement shall not state any other rate, except that the "dividend rate," using that term, may be stated in conjunction with, but not more conspicuously than, the annual percentage yield to which it relates.

(c) *When additional disclosures are required.* Except as provided in paragraph (e) of this section, if the annual percentage yield is stated in an advertisement, the advertisement shall state the following information, to the extent applicable, clearly and conspicuously:

(1) *Variable rates.* For variable-rate accounts, a statement that the rate may change after the account is opened.

(2) *Time annual percentage yield is offered.* For interest-bearing accounts and dividend-bearing term share accounts, the period of time the annual percentage yield will be offered, or a statement that the annual percentage yield is accurate as of a specified date. For dividend-bearing accounts other than term share accounts, a statement that the annual percentage yield is accurate as of the last dividend declaration date. In the event that disclosure of an annual percentage yield as of the last dividend declaration date might be inaccurate because of known or contemplated dividend rate changes, the credit union may disclose the prospective annual percentage yield. Such prospective annual percentage yield may be disclosed either in lieu of, or in addition to, the dividend rate and annual percentage yield as of the last dividend declaration date.

(3) *Minimum balance.* The minimum balance required to earn the advertised annual percentage yield. For tiered-rate accounts, the minimum balance required for each tier shall be stated in close proximity and with equal prominence to the applicable annual percentage yield.

(4) *Minimum opening deposit.* The minimum deposit required to open the account, if it is greater than the minimum balance necessary to earn the advertised annual percentage yield.

(5) *Effect of fees.* A statement that fees could reduce the earnings on the account.

(6) *Features of term share accounts.* For term share accounts:

(i) *Time requirements.* The term of the account.

(ii) *Early withdrawal penalties.* A statement that a penalty will or may be imposed for early withdrawal.

(iii) *Required dividend payouts.* For noncompounding term share accounts with a stated maturity greater than one year that do not compound dividends on an annual or more frequent basis, that require dividend payouts at least annually, and that disclose an APY determined in accordance with section E of appendix A of this part, a statement that dividends cannot remain on account and that payout of dividends is mandatory.

(d) *Bonuses.* Except as provided in paragraph (e) of this section, if a bonus is stated in an advertisement, the advertisement shall state the following information, to the extent applicable, clearly and conspicuously:

(1) The "annual percentage yield," using that term;

(2) The time requirements to obtain the bonus;

(3) The minimum balance required to obtain the bonus;

(4) The minimum balance required to open the account, if it is greater than the minimum balance necessary to obtain the bonus; and

(5) When the bonus will be provided.

(e) *Exemption for certain advertisements.*

(1) *Certain media.* If an advertisement is made through one of the following media, it need not contain the information in paragraphs (c)(1), (c)(2), (c)(4), (c)(5), (c)(6)(ii), (d)(4) and (d)(5) of this section:

(i) Broadcast or electronic media, such as television or radio;

(ii) Outdoor media, such as billboards; or

(iii) Telephone response machines.

(2) *Indoor signs.*

(i) Signs inside the premises of a credit union (or the premises of a share or deposit broker) are not subject to paragraphs (b), (c), (d) or (e)(1) of this section.

(ii) If a sign exempted by paragraph (e)(2) of this section states a rate of return, it shall:

(A) State the rate as an "annual percentage yield," using that term or the term "APY." The sign shall not state any other rate, except that the dividend rate may be stated in conjunction with the annual percentage yield to which it relates.

(B) Contain a statement advising members to contact an employee for further information about applicable fees and terms.

(3) *Newsletters.*

(i) Newsletters sent by a credit union to existing members only are not subject to paragraphs (b), (c), (d) or (e)(1) of this section.

(ii) If a newsletter exempted by paragraph (e)(3) of this section states a rate of return, it shall:

(A) State the rate as an "annual percentage yield," using that term or the term "APY." The newsletter shall not state any other rate, except that the dividend rate may be stated in conjunction with the annual percentage yield to which it relates.

(B) Contain a statement advising members to contact an employee for further information about applicable fees and terms.

§ 707.9 Enforcement and record retention.

(a) *Administrative enforcement.* Section 270 of TISA (12 U.S.C. 4309) contains the provisions relating to administrative sanctions for failure to comply with the requirements of TISA and this part.

(b) *Civil liability.* Section 271 of TISA (12 U.S.C. 4310) contains the provisions relating to civil liability for failure to comply with the requirements of TISA and this part; Section 271 is repealed effective September 30, 2001.

(c) *Record retention.* A credit union shall retain evidence of compliance with this regulation for a minimum of two years after the date disclosures are required to be made or action is required to be taken.

§ 707.10 Electronic communication.

(a) Definition. Electronic communication means a message transmitted electronically between a credit union and a member in a format that allows visual text to be displayed on equipment, for example, a personal computer monitor.

(b) General rule. In accordance with the Electronic Signatures in Global and National Commerce Act (the E-Sign Act) (15 U.S.C. 7001 *et seq.*) and the rules of this part, a credit union may provide by electronic communication any disclosure required by this part to be in writing.

(c) When consent is required. Under the E-Sign Act, a credit union must obtain a member's affirmative consent when providing disclosures related to a transaction. For purposes of this requirement, the disclosures required under §§ 707.4(a)(2) and 707.8 are deemed not to be related to a transaction.

(d) Address or location to receive electronic communication. A credit union that uses electronic communication to provide disclosures required by this part must:

(1) Send the disclosure to the member's electronic address; or

(2) Make the disclosure available at another location such as an Internet web site; and

(i) Alert the member of the disclosure's availability by sending a notice to the member's electronic address (or to a postal address, at the credit union's option). The notice must identify the account involved (if applicable) and the address of the Internet web site or other location where the disclosure is available; and

(ii) Make the disclosure available for at least 90 days from the date the disclosure first becomes available or from the date of the notice alerting the member of the disclosure, whichever comes later.

(3) Exceptions. A credit union need not comply with paragraph (d)(2)(ii) of this section for disclosures required under § 707.4(a)(2), and need not comply with paragraphs (d)(2)(i) and (ii) of this section for disclosures required under § 707.8.

(e) Redelivery. When a disclosure provided by electronic communication is returned to a credit union undelivered, the credit union must take reasonable steps to attempt redelivery using information in its files.

(f) Entities other than a credit union. A person other than a credit union that is required to comply with this part may use electronic communication in accordance with the requirements of this section, as applicable.*

*Credit unions choosing to make disclosures and advertisements electronically may either follow the requirements as outlined in 707.4, 707.10 and Appendix C of this part or the requirements of the Electronics Signatures in Global and National Commerce Act, (15 U. S. C. 7001 et seq., E-Sign Act). *See* Supplementary Information published in 66 Fed. Reg. 33159 (6/21/01) and 66 Fed. Reg. 48206 (9/19/01) for a discussion of electronic disclosure requirements. This supplementary information was distributed with the November 2001 publication of the NCUA Rules and Regulations.

Appendix A to Part 707—Annual Percentage Yield Calculation

The annual percentage yield (APY) measures the total amount of dividends a credit union pays on an account based on the dividend rate and the frequency of compounding. The annual percentage yield is expressed as an annualized rate, based on a 365-day year. (Credit unions may calculate the annual percentage yield based on a 365-day or a 366-day year in a leap year.) Part I of this appendix discusses the annual percentage yield calculations for account disclosures and advertisements, while Part II discusses annual percentage yield earned calculations for statements. The annual percentage yield reflects only dividends and does not include the value of any bonus, as that term is defined in part 707, that may be provided to the member to open, maintain, increase or renew an account. Dividends, interest or other earnings are not to be included in the annual percentage yield if such amounts are determined by circumstances that may or may not occur in the future. These formulas apply to both dividend-bearing and interest-bearing accounts held by credit unions.

Part I. Annual Percentage Yield for Account Disclosures and Advertising Purposes

In general, the annual percentage yield for account disclosures under §§ 707.4 and 707.5 and for advertising under § 707.8 is an annualized rate that reflects the relationship between the amount of dividends that would be earned by the member for the term of the account and the amount of principal used to calculate those dividends. The amount of dividends that would be earned may be projected based on the most recent past declared rate or an anticipated future rate, whichever the credit union judges to most reasonably approximate the dividends to be earned. Special rules apply to accounts with tiered and stepped dividend rates, and to certain term share accounts with a stated maturity greater than one year.

A. General rules

Except as provided in Part I. E. of this appendix, the annual percentage yield shall be calculated by the formula shown below. Credit unions may calculate the annual percentage yield using projected dividends based on either the rate at the last dividend declaration date or the rate anticipated at a future date. The credit union must disclose whichever option it uses to members. Credit unions shall calculate the annual percentage yield based on the actual number of days for the term of the account. For accounts without a stated maturity date (such as a typical share or share draft account), the calculation shall be based on an assumed term of 365 days. In determining the total dividends figure to be used in the formula, credit unions shall assume that all principal and dividends remain on deposit for the entire term, and that no other transactions (deposits or withdrawals) occur during the term. (This assumption shall not be used if a credit union requires, as a condition of the account, that members withdraw dividends during the term. In such a case, the dividends (and annual percentage yield calculation) shall reflect that requirement.) For term share accounts that are offered in multiples of months, credit unions may base the number of days on either the actual number of days during the applicable period, or the number of days that would occur for any actual sequence of that many calendar months. If credit unions choose to use this permissive rule, they must use the same number of days to calculate the dollar amount of dividends that will be earned on the account in the annual percentage yield formula (where "Dividends" are divided by "Principal".)

The annual percentage yield is to be calculated by use of the following general formula (("APY") is used for convenience in the formulas):

$$APY = 100[(1 + \text{Dividends/Principal})^{(365\ /\text{Days in term})} - 1]$$

"Principal" is the amount of funds assumed to have been deposited at the beginning of the account.

"Dividends" is the total dollar amount of dividends earned on the Principal for the term of the account.

"Days in term" is the actual number of days in the term of the account.

When the "days in term" is 365 (that is, where the stated maturity is 365 days or where the account does not have a stated maturity), the APY can be calculated by use of the following simple formula:

$$APY = 100\ (\text{Dividends/Principal}).$$

EXAMPLES:

(1) If a credit union would pay $61.68 in dividends for a 365-day year on $1,000 deposited into a share draft account, the APY is 6.17%:

$$APY = 100\ [(1 + 61.68/1{,}000)^{(365/365)} - 1]$$

APY = 6.17%

Or, using the simple formula above (since the term is deemed to be 365 days):

APY = 100 (61.68/1,000)

APY = 6.17%

(2) If a credit union pays $30.37 in dividends on a $1,000 six-month term share certificate account (where the six-month period used by the credit union contains 182 days), using the general formula above, the APY is 6.18%:

$$APY = 100\ [(1 + 30.37/1{,}000)^{(365/182)} - 1]$$

APY = 6.18%

The APY is affected by the frequency of compounding, i.e., the amount of dividends will be greater the more frequently dividends are compounded for a given nominal rate. When two credit unions are offering the same dividend rate on, for example, a share account, the APY disclosed may be different if the credit unions use a different frequency of compounding.

EXAMPLES:

(1) If a credit union pays $1,268.25 in dividends for a 365-day year on $10,000 deposited into a regular share account earning 12%, and the dividends are compounded monthly, the APY will be 12.68%:

APY = 100 ($1,268.25/10,000)

APY = 12.68%

(2) However, if a credit union is compounding dividends on a quarterly basis on an account which otherwise has the same terms, the dividends will be $1,255.09 and the APY will be 12.55%:

APY = 100 ($1,255.09/10,000)

APY = 12.55%

B. Stepped-Rate Accounts (Different Rates Apply in Succeeding Periods)

For accounts with two or more dividend rates applied in succeeding periods (where the rates are known at the time the account is opened), a credit union shall assume each dividend rate is in effect for the length of time provided for in any share agreement.

EXAMPLES:

(1) If a credit union offers a $1,000 6-month term share (certificate) account on which it pays a 5% dividend rate, compounded daily, for the first three months (which contain 91 days), and a 5.5% dividend rate, compounded daily, for the next three months (which contain 92 days), the total dividends for six months is $26.68, and, using the general formula above, the APY is 5.39%:

$$APY = 100\ [(1 + 26.68/1{,}000)^{(365/183)} - 1]$$

APY = 5.39%

(2) If a credit union offers a $1,000 2-year share certificate on which it pays a 6% dividend rate, compounded daily, for the first year, and a 6.5% dividend rate, compounded daily, for the next year, the total dividends for two years is $133.13, and, using the general formula above, the APY is 6.45%:

$$APY = 100[(1 + 133.13/1{,}000)^{(365/730)} - 1]$$

APY = 6.45%

C. Variable-Rate Accounts

For variable-rate accounts without an introductory premium or discounted rate, a credit union must base the calculation only on the initial dividend rate in effect when the account is opened (or advertised), and assume that this rate will not change during the year.

Variable-rate accounts with an introductory premium or discount rate must be treated like stepped-rate accounts. Thus, a credit union shall assume that: (1) the introductory simple dividend rate is in effect for the length of time provided for in the account contract; and (2) the variable dividend rate that would have been in effect when the account is opened or advertised (but for the introductory rate) is in effect for the remainder of the year. If the variable rate is tied to an index, the index-based rate in effect at the time of disclosure must be used for the remainder of the year. If the rate is not tied to an index, the rate in effect for existing members holding the same account (who are not receiving the introductory dividend rate) must be used for the remainder of the year.

For example, if a credit union offers an account on which it pays a 7% dividend rate, com-

pounded daily, for the first three months (which, for example, contains 91 days), while the variable dividend rate that would have been in effect when the account was opened was 5%, the total dividends for a 365-day year for a $1,000 account balance is $56.52, (based on 91 days at 7% followed by 274 days at 5%). Using the simple formula, the APY is 5.65%:

APY = 100 (56.52/1,000)

APY = 5.65%

D. Accounts With Tiered Rates (Different Rates Apply To Specified Balance Level)

For accounts in which two or more dividend rates paid on the account are applicable to specified balance levels, the credit union must calculate the annual percentage yield in accordance with the method described below that it uses to calculate dividends. In all cases, an annual percentage yield (or a range of annual percentage yields, if appropriate) must be disclosed for each balance tier.

For purposes of the examples discussed below, assume the following:

Simple dividend rate	*Share balance required to earn rate*
5.25%	up to but not exceeding $2,500
5.50%	above $2,500, but not exceeding $15,000
5.75%	above $15,000.

Tiering Method A

Under this method, a credit union pays on the full balance in the account the stated dividend rate that corresponds to the applicable share balance tier. For example, if a member deposits $8,000, the credit union pays the 5.50% dividend rate on the entire $8,000. This is also known as a "hybrid" or "plateau" tiered rate account.

When this method is used to determine dividends, only one annual percentage yield will apply to each tier. Within each tier, the annual percentage yield will not vary with the amount of principal assumed to have been deposited. For the dividend rates and account balances assumed above, the credit union will state three annual percentage yields—one corresponding to each balance tier. Calculation of each annual percentage yield is similar for this type of account as for accounts with a single fixed dividend rate. Thus, the calculation is based on the total amount of dividends that would be received by the member for each tier of the account for a year and the principal assumed to have been deposited to earn that amount of dividends.

First tier. Assuming daily compounding, the credit union will pay $53.90 in dividends on a $1,000 account balance. Using the general formula for the first tier, the APY is 5.39%:

$$APY = 100\ [(1 + 53.90/1{,}000)^{(365/365)} - 1]$$

APY = 5.39%

Using the simple formula:

APY = 100 (53.90/1,000)

APY = 5.39%

Second tier. The credit union will pay $452.29 in dividends on a $8,000 deposit. Thus, using the simple formula, the annual percentage yield for the second tier is 5.65%:

APY = 100 (452.29/8,000)

APY = 5.65%

Third tier. The credit union will pay $1,183.61 in dividends on a $20,000 account balance. Thus, using the simple formula, the annual percentage yield for the third tier is 5.92%:

APY = 100 (1,183.61/20,000)

APY = 5.92%

Tiering Method B

Under this method, a credit union pays the stated dividend rate only on that portion of the balance within the specified tier. For example, if a member deposits $8,000, the credit union pays 5.25% on only $2,500 and 5.50% on $5,500 (the difference between $8,000 and the first tier cutoff of $2,500). This is also known as a "pure" tiered rate account.

The credit union that computes dividends in this manner must provide a range that shows the lowest and the highest annual percentage yields for each tier (other than for the first tier, which, like the tiers in Method A, has the same annual percentage yield throughout). The low figure for an annual percentage yield is calculated based on the total amount of dividends earned for a year assuming the minimum principal required to earn the dividend rate for that tier. The high figure for an annual percentage yield is based on the amount of dividends the credit union would pay on the highest principal

that could be deposited to earn that same dividend rate. If the account does not have a limit on the amount that can be deposited, the credit union may assume any amount.

For the tiering structure assumed above, the credit union would state a total of five annual percentage yields—one figure for the first tier and two figures stated as a range for the other two tiers.

First tier. Assuming daily compounding, the credit union could pay $53.90 in dividends on a $1,000 account balance. For this first tier, using the simple formula, the annual percentage yield is 5.39%:

APY = 100 (53.90/1,000)

APY = 5.39%

Second tier. For the second tier the credit union would pay between $134.75 and $841.45 in dividends, based on assumed balances of $2,500.01 and $15,000, respectively. For $2,500.01, dividends would be figured on $2,500 at 5.25% dividend rate plus dividends on $.01 at 5.50%. For the low end of the second tier, therefore, the annual percentage yield is 5.39%. Using the simple formula:

APY = 100 (134.75/2,500)

APY = 5.39%

For $15,000, dividends are figured on $2,500 at 5.25% dividend rate plus dividends on $12,500 at 5.50% dividend rate. For the high end of the second tier, the annual percentage yield, using the simple formula, is 5.61%:

APY = 100 (841.45/15,000)

APY = 5.61%

Thus, the annual percentage yield range that would be stated for the second tier is 5.39% to 5.61%.

Third tier. For the third tier, the credit union would pay $841.45 and $5,871.78 in dividends on the low end of the third tier (a balance of $15,000.01). For $15,000.01, dividends would be figured on $2,500 at 5.25% dividend rate, plus dividends on $12,500 at 5.50% dividend rate, plus dividends on $.01 at 5.75% dividend rate. For the low end of the third tier, therefore, the annual percentage yield, using the simple formula, is 5.61%:

APY = 100 (841.45/15,000)

APY = 5.61%

Assuming the credit union does not limit the account balance, it may assume any maximum amount for the purposes of computing the annual percentage yield for the high end of the third tier. For an assumed maximum balance amount of $100,000, dividends would be figured on $2,500 at 5.25% dividend rate, plus dividends on $12,500 at 5.50% dividend rate, plus dividends on $85,000 at 5.75% dividend rate. For the high end of the third tier, therefore, the annual percentage yield, using the simple formula, is 5.87%:

APY = 100 (5,871.78/100,000)

APY = 5.87%

Thus, the annual percentage yield that would be stated for the third tier is 5.61% to 5.87%. If the assumed maximum balance amount is $1,000,000, credit unions would use $985,000 rather than $85,000 in the last calculation. In that case for the high end of the third tier, the annual percentage yield, using the simple formula, is 5.91%:

APY = 100 (59,134.22/1,000,000)

APY = 5.91%

Thus, the annual percentage yield range that would be stated for the third tier is 5.61% to 5.91%.

E. Term Share Accounts with a Stated Maturity Greater than One Year that Pay Dividends At Least Annually

1. For term share accounts with a stated maturity greater than one year, that do not compound dividends on an annual or more frequent basis, and that require the member to withdraw dividends at least annually, the annual percentage yield may be disclosed as equal to the dividend rate.

EXAMPLE

If a credit union offers a $1,000 two-year term share account that does not compound and that pays out dividends semi-annually by check or transfer at a 6.00% dividend rate, the annual percentage yield may be disclosed as 6.00%.

2. For term share accounts covered by this paragraph that are also stepped-rate accounts, the annual percentage yield may be disclosed as equal to the composite dividend rate.

EXAMPLE

(1) If a credit union offers a $1,000 three-year term share account that does not compound and

that pays out dividends annually by check or transfer at a 5.00% dividend rate for the first year, 6.00% dividend rate for the second year, and 7.00% dividend rate for the third year, the credit union may compute the composite dividend rate and APY as follows:

(a) Multiply each dividend rate by the number of days it will be in effect;

(b) Add these figures together; and

(c) Divide by the total number of days in the term.

(2) Applied to the example, the products of the dividend rates and days the rates are in effect are (5.00%×365 days) 1825, (6.00%×365 days) 2190, and (7.00%×365) 2555, respectively. The sum of these products, 6570, is divided by 1095, the total number of days in the term. The composite dividend rate and APY are both 6.00%.

Part II. Annual Percentage Yield Earned for Statements

The annual percentage yield earned for statements under § 707.6 is an annualized rate that reflects the relationship between the amount of dividends actually earned (accrued or paid and credited) to the member's account during the period and the average daily balance in the account for the period over which the dividends were earned.

Pursuant to § 707.6(a), when dividends are paid less frequently than statements are sent, the APY Earned may reflect the number of days over which dividends were earned rather than the number of days in the statement period, e.g., if a credit union uses the average daily balance method and calculates dividends for a period other than the statement period, the annual percentage yield earned shall reflect the relationship between the amount of dividends earned and the average daily balance in the account for the other period, such as a crediting or dividend period.

The annual percentage yield shall be calculated by using the following formulas ("APY Earned" is used for convenience in the formulas):

A. General formula

$$\text{APY Earned} = 100[(1 + \text{Dividends earned/Balance})^{(365/\text{Days in period})} - 1]$$

"Balance" is the average daily balance in the account for the period.

"Dividends earned" is the actual amount of dividends accrued or paid and credited to the account for the period.

"Days in period" is the actual number of days over which the dividends disclosed on the statement were earned.

EXAMPLES:

(1) If a credit union calculates dividends for the statement period (and uses either the daily balance or the average daily balance method), and the account had a balance of $1,500 for 15 days and a balance of $500 for the remaining 15 days of a 30-day statement period, the average daily balance for the period is $1,000. Assume that $5.25 in dividends was earned during the period. The annual percentage yield earned (using the formula above) is 6.58%:

$$\text{APY Earned} = 100\ [(1 + 5.25/1{,}000)^{(365/30)} - 1]$$

APY Earned = 6.58%

(2) Assume a credit union calculates dividends on the average daily balance for the calendar month and provides periodic statements that cover the period from the 16th of one month to the 15th of the next month. The account has a balance of $2,000 September 1 through September 15 and a balance of $1,000 for the remaining 15 days of September. The average daily balance for the month of September is $1,500, which results in $6.50 in dividends earned for the month. The annual percentage yield earned for the month of September would be shown on the periodic statement covering September 16 through October 15. The annual percentage yield earned (using the formula above) is 5.40%:

$$\text{APY Earned} = 100\ [(1 + 6.50/1{,}500)^{(365/30)} - 1]$$

APY Earned = 5.40%

(3) Assume a credit union calculates dividends on the average daily balance for a quarter (for example, the calendar months of September through November), and provides monthly periodic statements covering calendar months. The account has a balance of $1,000 throughout the 30 days of September, a balance of $2,000 throughout the 31 days of October, and a balance of $3,000 throughout the 30 days of November. The average daily balance for the quarter is $2,000, which results in $21 in dividends earned for the quarter. The annual percentage yield earned would be shown on the periodic statement for November. The annual

percentage yield earned (using the formula above) is 4.28%:

$$\text{APY Earned} = 100\ [(1 + 21/2{,}000)^{(365/91)} - 1]$$

APY Earned = 4.28%

B. Special formula for use where periodic statement is sent more often than the period for which dividends are compounded.

Credit unions that use the daily balance method to accrue dividends and that issue periodic statements more often than the period for which dividends are compounded shall use the following special formula:

$$\text{APY Earned} = 100\left[\left\{1+\frac{(\text{Dividends earned/Balance})}{\text{Days in period (Compounding)}}\right\}^{(365/\text{Compounding})} - 1\right]$$

The following definition applies for use in this formula (all other terms are defined under Part II):

"Compounding" is the number of days in each compounding period.

Assume a credit union calculates dividends for the statement period using the daily balance method, pays a 5.00% dividend rate, compounded annually, and provides periodic statements for each monthly cycle. The account has a daily balance of $1,000.00 for a 30-day statement period. The dividend earned of $4.11 for the period, and the annual percentage yield earned (using the special formula above) is 5.00%:

$$\text{APY Earned} = 100\left[\left\{1+\frac{(\$4.11/1{,}000)}{30}(365)\right\}^{(365/365)} - 1\right]$$

Appendix B to Part 707—Model Clauses and Sample Forms

General Note: Appendix B contains model clauses and sample forms intended for optional use by credit unions to aid in compliance with the disclosure requirements of §§ 707.4 (account disclosures), 707.5 (subsequent disclosures), 707.6 (statement disclosures), and 707.8 (advertisements). Section 269(b) of TISA provides that credit unions that use these clauses and forms will be in compliance with TISA's disclosure provisions.

As discussed in the supplementary information to § 707.3(a), this final rule provides for flexibility in designing the format of the disclosures. Credit unions can choose to prepare a single document or brochure that incorporates disclosures for all accounts offered, or to prepare different documents for each type of account. Credit unions may also use inserts to a document, or fill in blanks to show current rates, fees and other terms.

In the model clauses, words in parentheses indicate the type of disclosure a credit union should insert in the space provided (for example, a credit union might insert "July 23, 1995" in the blank for a "(date)" disclosure). Brackets and "/" indicate that a credit union must choose the alternative that best describes its practice (for example, "[daily balance/ average daily balance]"). It should be noted that only in sections B–6 through B–10 of this appendix have specific examples of disclosures been given, with dates and figures. Sections B–1 through B–5, and section B–11 provide only unspecific model clauses or blank forms. The Board felt, as did the FRB in the Appendix A to Regulation DD, that a mix of blank clauses and forms and application of the model clauses to real specific situations would benefit those who must comply with TISA.

Any references to NCUA Rules and Regulations, the *NCUA Standard FCU Bylaws,* or the *NCUA Accounting Manual for FCUs,* are provided for guidance and as a point of reference for credit unions. Citations to these sources does not indicate that their application is required for those credit unions who need not follow them.

B–1 MODEL CLAUSES FOR ACCOUNT DISCLOSURES (§ 707.4(b))

(a) Rate Information (Sec.707.4(b)(1))

(i) *Fixed-Rate Accounts (§ 707.4(b)(1)(i)(A–B))*

1. Interest-bearing Accounts

The interest rate on your deposit account is _____% with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

Note: This provision reflects an accurate statement for an interest-bearing account authorized by state law for state-chartered credit unions. While the definition of the term "interest" permits its substitution for the term "dividends," separate disclosures should be made for interest-bearing accounts. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Given the definition of fixed-rate account in § 707.2(n), credit unions offering fixed-rate accounts must contract to hold rates steady for at least a 30-day period. Thus, if the 30-day option of the last sentence is not chosen, the period chosen must be longer than 30 days.

2. Dividend-bearing Term Share Accounts

The dividend rate on your term share account is _____% with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

Note: This provision reflects an accurate statement for a fixed-rate, dividend-bearing

term share account. Interest-bearing term share accounts would use the disclosure in § 1, above. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Given the definition of fixed-rate account in § 707.2(n), credit unions offering fixed-rate accounts must contract to hold rates steady for at least a 30-day period. Thus, if the 30-day option of the last sentence is not chosen, the period chosen must be longer than 30 days.

3. Other Dividend-bearing Accounts

[As of [the last dividend declaration date/(date)], the dividend rate was _____% with an annual percentage yield (APY) of _____% on your account./or The prospective dividend rate on your account is _____% with a prospective APY of _____% for the current dividend period.] You will be paid this rate for [(time period)/at least 30 calendar days].

or

[As of [the last dividend declaration date/(date)], the dividend rate was _____% with an annual percentage yield (APY) of _____% on your account./or The prospective dividend rate on your account is _____% with an annual percentage yield (APY) of _____% for this dividend period.] This rate will not change unless the credit union notifies you at least 30 calendar days prior to any change.

Note: Credit unions may disclose the dividend rate and annual percentage yield on accounts as of the last dividend declaration date. This necessitates inclusion of a disclosure of the actual calendar date of the last dividend declaration date. Additionally or alternatively (if the last dividend rate could be inaccurate), credit unions may disclose a prospective dividend rate and a prospective annual percentage yield. Such prospective rates and yields must be estimated in good faith, and must be declared at the proper time if it is at all possible to do so. As for the last sentence in these disclosures, this provision reflects a credit union policy to set prospective dividend rates for the next month (or at least 30 days), quarter or other period. Many credit unions, at their mid-monthly board meeting, set prospective dividend rates for the next month beginning on the 1st day of the month and continuing to the last day of the month. These rates must be formalized or ratified at the end of a dividend period. Given the timing of the board meetings, the time to prepare and mail notices and the 30 day period, it will often take credit unions 45 to 60 days to effectively change rates. For these reasons, the Board strongly suggests that credit unions do not offer fixed-rate, dividend-bearing accounts.

(ii) Variable-Rate Accounts (§ 707.4(b)(1)(ii))

1. Interest-bearing Accounts

The interest rate on your deposit account is _____%, with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] The interest rate and annual percentage yield may change every (time period) based on [(name of index)/the determination of the credit union board of directors]. The interest rate for your account will [never change by more than _____% each (time period)/never be less/more than _____%/never exceed _____% above or fall more than _____% below the initial interest rate].

Note: This disclosure combines the requirements of § 707.4(b)(1)(i) with § 707.4(b)(1)(ii) for interest-bearing accounts. The variable nature of a deposit account usually is based on an external index or is set at the discretion of the board. If another means of rate setting is used, that, instead of the proposed language, must be disclosed. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Rarely would there be limitations on rate changes, but language is provided for this situation in the last sentence. Of

course, it is only to be used if it applies to an account.

2. Dividend-bearing Term Share Accounts

The dividend rate on your term share account is _____%, with an annual percentage yield (APY) of _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] The dividend rate and annual percentage yield may change every (time period) based on [(name of index)/the determination of the credit union board of directors]. The dividend rate for your account will [never change by more than _____% each (time period)/never be less/more than _____%/never exceed _____% above or fall more than _____% below the initial dividend rate].

Note: This disclosure combines the requirements of § 707.4(b)(1)(i) with § 707.4(b)(1)(ii) for dividend-bearing, variable-rate term share accounts. The variable nature of a deposit account usually is based on an external index or is set at the discretion of the board. If another means of rate setting is used, that, instead of the model language, must be disclosed. Since account opening disclosures may be provided to potential members requesting account information before opening an account, and members opening new accounts, information is provided indicating that the rate may not be current, but that the potential member or member may call the credit union to obtain up-to-date information. When opening a new account, of course, a credit union could provide the contractual rate alone, and delete the sentences in brackets. Rarely would there be limitations on rate changes, but language is provided for this situation in the last sentence. Of course, it is only to be used if it applies to an account.

3. Other Dividend-bearing Accounts

[As of [the last dividend declaration date/(date)], the dividend rate was _____% with an annual percentage yield (APY) of _____% on your account./or The prospective dividend rate on your account is _____% with an anticipated annual percentage yield (APY) of _____% for the current dividend period.] The dividend rate and annual percentage yield may change every (dividend period) as determined by the credit union board of directors.

Note: This language combines the requirements of § 707.4(b)(1)(i) with § 707.4(b)(1)(ii). Credit unions may disclose the dividend rate and annual percentage yield on accounts as of the last dividend declaration date. This necessitates inclusion of a disclosure of the actual calendar date of the last dividend declaration date or use of the phrase "last dividend declaration date". Additionally or alternatively, credit unions may disclose a prospective dividend rate and a prospective annual percentage yield. Such prospective rates and yields must be estimated in good faith, and must be declared at the proper time if it is at all possible to do so. As for the last sentence in these disclosures, this provision reflects the variable nature of the account. Generally, there is only one variable-rate feature for share accounts: the frequency of dividend period rate changes (e.g., daily, weekly, monthly, quarterly, semi-annually, annually). Normally, there are no contractual limitations on share account earnings (unless imposed by a regulator), nor are earnings based on any internal or external index. If contractual limitations or an index are involved, however, those factors would need to be disclosed (unless a regulator orders otherwise).

(iii) Stepped-Rate Accounts (§ 707.4(b)(1)(i))

1. Interest-bearing Accounts

The initial interest rate on your deposit account is _____%. You will be paid that rate [for (time period)/until (date)]. After that time, the interest rate for your deposit account will be _____% and you will be paid that rate [for (time period)/until (date)]. The annual percentage yield (APY) for your account is _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

2. Dividend-bearing Term Share Accounts

The initial dividend rate on your term share account is _____%. You will be paid that rate [for (time period)/until (date)]. After that time, the dividend rate for your term share account will be _____% and you

will be paid that rate [for (time period)/until (date)]. The annual percentage yield (APY) for your account is _____%. [For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.] You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days].

3. Other Dividend-bearing Accounts

[As of [the last dividend declaration date/(date)], the initial dividend rate on your account was _____%./or The prospective dividend rate on your account is _____%.] You will be paid that rate [for (time period)/until (date)]. After that time, the prospective dividend rate for your share account will be _____% and you will be paid such rate [for (time period)/until (date)]. The annual percentage yield (APY) for your account is _____%. You will be paid this rate for [(time period)/at least 30 calendar days].

Note: Stepped-rate accounts are accounts with two or more rates that take effect in succeeding periods. The applicable rates and time periods are known when the account is opened. By nature these are fixed-rate accounts and are usually associated with term share (certificate) accounts. Accordingly, a contract provision (for share accounts) to change rates should be included.

(iv) Tiered-Rate Accounts (§ 707.4(b)(1)(i))

1. Interest-bearing Accounts

Tiering Method A

1* If your [daily balance/average daily balance] is $ _____ or more, the interest rate paid on the entire balance in your account will be _____%, with an annual percentage yield (APY) of _____%.

2* If your [daily balance/average daily balance] is more than $ _____, but less than $ _____, the interest rate paid on the entire balance in your account will be _____%, with an APY of _____%.

3* If your [daily balance/average daily balance] is $ _____ or less, the interest rate paid on the entire balance will be _____% with an APY of _____%.

[For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.]

[*Fixed-rate*—You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days]./*Variable-rate*—The interest rate and APY may change every (time period) based on [(name of index)/the determination of the credit union board of directors.]

Note: Tiering Method A pays the stated dividend rate that corresponds to the applicable account balance tier on the full balance in the account. This example contemplates a two-tier system. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the currency of the rate, as is provided in the first set of brackets. A disclosure regarding the fixed-rate or variable-rate nature of the account must be added, as is provided in the last set of brackets.

Tiering Method B

1* A dividend rate of _____% will be paid only on the portion of your [daily balance/average daily balance] that is greater than $_____. The annual percentage yield (APY) for this tier will range from _____% to _____%, depending on the balance in the account.

2* A dividend rate of _____% will be paid only on the portion of your [daily balance/average daily balance] that is greater than $_____, but less than $_____. The annual percentage yield (APY) for this tier will range from _____% to _____%, depending on the balance in the account.

3* If your [daily balance/average daily balance] is $_____ or less, the dividend rate paid on the entire balance will be _____%, with an annual percentage yield (APY) of _____%.

[For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.]

[*Fixed-rate*—You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days]./*Variable-rate*—The interest

rate and APY may change every (time period) based on [(name of index)/the determination of the credit union board of directors.]

Note: Tiering Method B pays different stated dividend rates corresponding to applicable deposit tiers, on the applicable balance in each tier of the account. For example, a credit union might pay 3% dividend on account funds of $500 or below, and pay 4% dividend on the portion of the same account that exceeds $500. The example contemplates an account with two tiers, but additional tiers are possible. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the currentness of the rate, as is provided in the first set of brackets.

Tiered-rate accounts can be either fixed-rate or variable-rate accounts. The last sentence offers an option of either fixed-rate or variable-rate disclosure. Thus, the disclosures outlined above will be made in addition to either: (i) disclosure of the period the fixed-rates are in effect or (ii) the variable-rate disclosures. Tiered-rate accounts are also subject to the requirement for disclosure of the balance computation method, *see* paragraph (e) to this appendix.

2. Dividend-bearing Term Share Accounts

Tiering Method A

1* If your [daily balance/average daily balance] is $_____ or more, the dividend rate paid on the entire balance in your account will be _____%, with an annual percentage yield (APY) of _____%.

2* If your [daily balance/average daily balance] is more than $_____, but less than $_____, the dividend rate paid on the entire balance in your account will be _____%, with an APY of _____%.

3* If your [daily balance/average daily balance] is $_____ or less, the dividend rate paid on the entire balance will be _____% with an APY of _____%.

[For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.]

[*Fixed-rate*—You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days]./ *Variable-rate*—The interest rate and APY may change every (time period) based on [(name of index)/ the determination of the credit union board of directors.]

Note: Tiering Method A pays the stated dividend rate that corresponds to the applicable account balance tier on the full balance in the account. This example contemplates a two-tier system. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the currency of the rate, as is provided in the first set of brackets. A disclosure regarding the fixed-rate or variable-rate nature of the account must be added, as is provided in the last set of brackets.

Tiering Method B

1* A dividend rate of _____% will be paid only on the portion of your [daily balance/ average daily balance] that is greater than $_____. The annual percentage yield (APY) for this tier will range from _____% to _____%, depending on the balance in the account.

2* A dividend rate of _____% will be paid only on the portion of your [daily balance/ average daily balance] that is greater than $_____, but less than $_____. The annual percentage yield (APY) for this tier will range from _____% to _____%, depending on the balance in the account.

3* If your [daily balance/average daily balance] is $_____ or less, the dividend rate paid on the entire balance will be _____%, with an annual percentage yield (APY) of _____%.

[For purposes of this disclosure, this is a rate and APY that were offered within the most recent seven calendar days and were accurate as of (date). Please call (credit union telephone number) to obtain current rate information.]

[*Fixed-rate*—You will be paid this rate [for (time period)/until (date)/for at least 30 calendar days]./ *Variable-rate*—The interest rate and APY may change every (time period) based on [(name of index)/ the determination of the credit union board of directors.]

Note: Tiering Method B pays different stated dividend rates corresponding to applicable account balance tiers, on the applicable balance in each tier of the account. For example, a credit union might pay 3% dividend on account funds

of $500 or below, and pay 4% dividend on the portion of the same account that exceeds $500. The example contemplates an account with two tiers, but additional tiers are possible. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the currentness of the rate, as is provided in the first set of brackets.

Tiered-rate accounts can be either fixed-rate or variable-rate accounts. The last sentence offers an option of either fixed-rate or variable-rate disclosure. Thus, the disclosures outlined above will be made in addition to either: (i) Disclosure of the period the fixed-rates are in effect or (ii) the variable-rate disclosures. Tiered-rate accounts are also subject to the requirement for disclosure of the balance computation method, *see* paragraph (e) to this appendix.

3. Other Dividend-bearing Accounts

Tiering Method A

1* [As of [the last dividend declaration date/(date)], if your [daily balance/average daily balance] was $_____ or more, the dividend rate paid on the entire balance in your account was _____%, with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] is $_____ or more, a prospective dividend rate of _____% will be paid on the entire balance in your account with a prospective annual percentage yield (APY) of _____% for this dividend period.]

2* [As of [the last dividend declaration date/(date)], if your [daily balance/average daily balance] was more than $_____, but was less than $_____, the dividend rate paid on the entire balance in your account was _____%, with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] is more than $_____, but is less than $_____, a prospective dividend rate of _____% will be paid on the entire balance in your account with a prospective annual percentage yield (APY) of _____% for this dividend period.]

3* [As of the last dividend declaration date/(date)], if your [daily balance/average daily balance] was $_____ or less, the dividend rate paid on the entire balance in your account will be _____% with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] is $_____ or less, the prospective dividend rate of_____% will be paid on the entire balance in your account with an annual percentage yield (APY) of _____% for this dividend period.]

[*Fixed-rate*—You will be paid this rate for [(time period)/at least 30 calendar days]./ *Variable-rate*—The dividend rate and APY may change every (dividend period) as determined by the credit union board of directors.]

Note: Tiering Method A pays the stated dividend rate that corresponds to the applicable deposit tier on the full balance in the account. This example contemplates a two-tier system. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. For tiered-rate accounts, a disclosure may be added about the prospective rate. Note that the prospective rate disclosure options match the required tiered-rate disclosures based on the previous dividend declaration date. A disclosure regarding the fixed-rate or variable-rate nature of the account must be added, as is provided in the last set of brackets.

Tiering Method B

1* [As of [the last dividend declaration date/(date)], a dividend rate of _____% was paid only on the portion of your [daily balance/average daily balance] that was greater than $_____. The annual percentage yield (APY) for this tier ranged from _____% to _____%, depending on the balance in the account./or A prospective dividend rate of _____% will be paid only on the portion of your [daily balance/average daily balance] that is greater than $_____ with a prospective annual percentage yield (APY) ranging from _____% to _____%, depending on the balance in the account, for this dividend period.]

2* [As of [the last dividend declaration date/(date)], a dividend rate of _____% was paid only on the portion of your [daily balance/average daily balance] that was greater than $_____ but less than $_____. The annual percentage yield (APY) for this tier ranged from _____% to _____%, depending on the balance in the account./or A prospective dividend rate of _____% will be paid only on the portion of your [daily balance/average daily

balance] that is greater than $_____, but less than $_____] with a prospective annual percentage yield (APY) ranging from _____% to _____%, depending on the balance in the account, for this dividend period.]

3* [As of [the last dividend declaration date/(date)], if your [daily balance/average daily balance] was $_____ or less, the dividend rate paid on the entire balance was _____%, with an annual percentage yield (APY) of _____%./or If your [daily balance/average daily balance] was $_____ or less, the prospective dividend rate paid on the entire balance in your account will be _____% with a prospective annual percentage yield (APY) of _____% for this dividend period.]

Note: Tiering Method B pays different stated dividend rates corresponding to applicable account tiers, on the applicable balance in each tier of the account. For example, a credit union might pay a 3% dividend on account funds of $500 or below, and pay a 4% dividend on the portion of the same account that exceeds $500. The example contemplates an account with two tiers, but additional tiers are possible. The option (1, 2 or 3) most closely matching the terms of the account should be chosen as the appropriate disclosure. Note that the prospective rate disclosure options match the required tiered-rate disclosures based on the previous dividend declaration date.

Tiered-rate accounts can be either fixed-rate or variable-rate accounts. The last sentence offers an option of either fixed-rate or variable-rate disclosures. Thus, the disclosures outlined above must be made in addition to either: (i) disclosure of the period the fixed-rates are in effect or (ii) the variable-rate disclosures. Tiered-rate accounts are also subject to the requirement for disclosure of the balance computation method, *see* paragraph (e) to this appendix.

(b) Nature of Dividends (§ 707.4(b)(8))

Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

Note: The Board of Directors declares dividends based on current income and available earnings of the credit union after providing for the required reserves at the end of the month. The dividend rate and annual percentage yield shown may reflect either the last dividend declaration date on the account or the earnings the credit union anticipates having available for distribution. This disclosure only applies to share and share draft (as opposed to deposit) accounts and should be grouped with the Rate Information to make the disclosures more meaningful. This disclosure also does not apply to term share accounts for reasons discussed in the supplementary information regarding §§ 707.3(e) and 707.4(b)(8).

(c) Compounding and Crediting (§ 707.4(b)(2))

[Dividends/Interest] will be compounded (frequency) and will be credited (frequency).

and, if applicable:

If you close your [share/deposit] account before [dividends/interest] [are/is] paid, you will not receive the accrued [dividends/interest].

and, if applicable (for dividend-bearing accounts):

For this account type, the dividend period is (frequency), for example, the beginning date of the first dividend period of the calendar year is (date) and the ending date of such dividend period is (date). All other dividend periods follow this same pattern of dates. The dividend declaration date follows the ending date of a dividend period, and for the example is (date).

Note: Where the word "(frequency)" appears, time periods must be inserted to coincide with those specified in board resolutions of each credit union's board of directors. A disclosure of dividend period was added to § 707.4(b)(2)(i) in the final rule to assist members in knowing when dividend rate and APY disclosures would be given by a credit union using the optional statement rule of § 707.6(a). The dividend declaration date is important for purposes of § 707.4(a)(2)(ii), request disclosures, § 707.4(b)(2), account opening disclosures, and § 707.8(c)(2), advertising disclosures. The Board believes that this is critical information for dividend-bearing accounts, but that provision by an example (whether of the first dividend period of the year, or of any randomly chosen dividend period) is favorable to providing a list of such dates for the entire year or for a period of years (although these methods would also be permissible). As noted in the supplementary information to § 707.2(j), dividend declaration date, the dividend period and actual dividend distribution date may vary. Thus, it is possible for crediting

periods and dividend periods not to coincide, though the Board believes that credit unions should make every effort to attempt to coordinate the two periods.

(d) Minimum Balance Requirements (§ 707.4 (b)(3)(i))

(i) *To open the account*

The minimum balance required to open this account is $_____.

or, for first share account at a credit union

The minimum required to open this account is the purchase of a (par value of a share) share in the credit union.

(ii) *To avoid imposition of fees*

You must maintain a minimum daily balance of $_____ in your account to avoid a service fee. If, during any (time period), your account balance falls below the required minimum daily balance, your account will be subject to a service fee of $_____ for that (time period).

or

You must maintain a minimum average daily balance of $_____ in your account to avoid a service fee. If, during any (time period), your average daily balance is below the required minimum, your account will be subject to a service fee of $_____ for that (time period).

(iii) *To obtain the annual percentage yield disclosed*

You must maintain a minimum daily balance of $_____ in your account each day to obtain the disclosed annual percentage yield.

or

You must maintain a minimum average daily balance of $_____ in your account to obtain the disclosed annual percentage yield.

(iv) *Absence of minimum balance requirements*

No minimum balance requirements apply to this account.

(v) *Par value*

The par value of a share in this credit union is $_____.

Note: Where the words "(time period)" appear, time periods should be inserted to coincide with those specified in board resolutions of each credit union's board of directors. As the supplementary information to § 707.4(b)(3)(i) explains, the par value of a share to establish membership is a critical disclosure to be made to potential members of credit unions. The par value disclosure is required by § 707.4(b)(3)(i) as being analogous to a minimum balance account opening requirement.

(e) Balance Computation Method (§ 707.4(b)(3)(ii))

(i) *Daily Balance Method*

[Dividends/Interest] [are/is] calculated by the daily balance method which applies a daily periodic rate to the balance in the account each day.

(ii) *Average Daily Balance Method*

[Dividends/Interest] [are/is] calculated by the average daily balance method which applies a periodic rate to the average daily balance in the account for the period. The average daily balance is calculated by adding the balance in the account for each day of the period and dividing that figure by the number of days in the period.

Note: Any explanation of balance computation method must contain enough information for members to grasp the means by which dividends or interest will be calculated on their accounts. Using a shorthand form, such as "day in/day out" for the daily balance method or "average balance" for the average daily balance method, without more information, is insufficient. In addition, any disclosure based on the equivalency of the two allowable methods, such as stating that the average daily balance method was the same as the daily balance method, is impermissible and misleading.

(f) Accrual of Dividends/Interest on Noncash Deposits (§ 704.4(b)(3)(iii))

[Dividends/Interest] will begin to accrue on the business day you [place/deposit] noncash items (e.g. checks) to your account.

or

[Dividends/Interest] will begin to accrue no later than the business day we receive provisional credit for the [placement/deposit] of noncash items (e.g. checks) to your account.

Note: Accrual information is not included in the explanation of balance computation method required by § 707.4(b)(4)(ii). In addition, the disclosures required by TISA do not affect the substantive requirements of the EFAA and Regulation CC. The EFAA and Regulation CC control,

and any modifications to them should occasion credit unions to revisit this disclosure with a view to revising it to reflect current law.

(g) Fees and Charges (§ 707.4(b)(4))

The following fees and charges may be assessed against your account:
(service/explanation) $_____
(service/explanation) $_____

Note: Fees and charges may be disclosed in an account disclosure, or separately in a Rate and Fee Schedule (see section B–11 of this appendix). In either event, the disclosure should also specify when the fee will be assessed by using phrases such as "per item," "per month," or "per inquiry."

(h) Transaction Limitations (§ 707.4(b)(5))

The minimum amount you may [withdraw/write a draft for] is $_____.

During any statement period, you may not make more than six withdrawals or transfers to another credit union account of yours or to a third party by means of a preauthorized or automatic transfer or telephonic order or instruction. No more than three of the six transfers may be made by check, draft, debit card, if applicable, or similar order to a third party. If you exceed the transfer limitations set forth above in any statement period, your account will be subject to [closure by the credit union/a fee of $_____].

Note: This paragraph satisfies the requirements of § 707.4(b)(6) with respect to Regulation D limitations on share accounts and money market accounts. These are some of the more common limitations applicable.

The credit union reserves the right to require a member intending to make a withdrawal from any account (except a share draft account) to give written notice of such intent not less than seven days and up to 60 days before such withdrawal.

Note: This disclosure is limted to federal credit unions with Bylaws containing this limitation. See Standard Federal Credit Union Bylaws, Art. III, § 5(a). Similar disclosures are required of any state-chartered credit unions having similar limitations in their bylaws, or under state law. This limitation does not directly relate to the "number" or "amount" of transactions, and accordingly, may not be necessary under § 707.4(b)(5), but would, if applicable, be required by § 707.3(b).

(i) Disclosures related to term share accounts (§ 707.4(b)(6))

(i) *Time requirements*

Your account will mature on (date).

or

Your account will mature after (time period).

(ii) *Early withdrawal penalties*

We [will/may] impose a penalty if you withdraw [any/all] of the [funds/principal] in your account before the maturity date. The penalty will equal [_____ days'/weeks'/months'] [dividends/interest] on your account.

or

We [will/may] impose a penalty of $_____ if you withdraw [any/all] of the [funds/principal] before the maturity date.

If you withdraw some of your funds before maturity, the [dividend/interest] rate for the remaining funds in your account will be _____%, with an annual percentage yield of _____%.

Note: In most cases, the dividend rate and annual percentage yield on the funds remaining in the account after early withdrawal are the same as before the withdrawal. Accordingly, the disclosure of dividend rate and annual percentage yield after withdrawal is required only if the dividend rate and APY will change.

(iii) *Withdrawal of dividends/interest prior to maturity*

The annual percentage yield is based on an assumption that [dividends/interest] will remain in the account until maturity. A withdrawal will reduce earnings.

Note: This disclosure may be used if the credit union compounds dividends/interest and allows withdrawal of accrued dividends/interest before maturity. This disclosure alerts members that the annual percentage yield is based on an assumption that the dividends/interest remain on deposit until maturity.

(iv) *Renewal policies*

1. *Automatically renewable term share accounts*

Your term share account will automatically renew at maturity. You will have a grace period of _____ [calendar/business] days after the maturity date to withdraw the funds in the account without being charged an early withdrawal penalty.

or

Your term share account will automatically renew at maturity. There is no grace period following the maturity of this account.

2. *Non-automatically renewable term share accounts*

This account will not renew automatically at maturity. If you do not renew the account, your account will [continue to earn/ no longer earn] [dividends/interest] after the maturity date.

Note: These disclosures should agree with the necessary prematurity notices for term share accounts in B–3 of this appendix.

(v) *Required dividend distribution.*

This account requires the distribution of dividends and does not allow dividends to remain in the account.

(j) Bonuses (§ 704.4(b)(7))

You will [be paid/receive] [$_____/ (description of item)] as a bonus [when you open the account/on (date)].

You must maintain a minimum [daily balance/ average daily balance] of $_____ to obtain the bonus.

To earn the bonus, [$_____/your entire principal] must remain on deposit [for (time period)/until (date)].

Note: These disclosures follow the requirements of § 707.4(b)(7) and should be used as applicable. Further information may also be added, especially if it clarifies the conditions and timing of receiving the bonus, or better informs the member about the bonus.

B–2 MODEL CLAUSES FOR CHANGES IN TERMS (§ 707.5(a))

On (date), the (type of fee) will increase to $_____. On (date), the [dividend/interest] rate on your account will decrease to _____%, with an annual percentage yield (APY) of _____%.

On (date), the [minimum daily balance/ average daily balance] required to avoid imposition of a fee will increase to $_____.

Note: These examples apply to the more common changes necessitating a changes in terms notice. However, any change, amendment or modification reducing the APY or adversely affecting the members holding such accounts must be disclosed. For such changes not contemplated by the model clauses, the Board recommends the use of as simple language as possible to convey the change, along with cross-referencing to the particular sections or paragraph numbers of the account opening disclosures, when to do so will assist members in reviewing and understanding the change.

B–3 MODEL CLAUSES FOR PRE-MATURITY NOTICES FOR TERM SHARE ACCOUNTS (§ 707.5(b–d))

(a) *Maturity date*

Your term share account will mature on _____.

(b) *Nonrenewal*

Unless your term share account is renewed, it will not accrue further [dividends/ interest] after the maturity date.

(c) *Rate information*

The [dividend/interest] rate and annual percentage yield that will apply to your term share account if it is renewed have not yet been determined. That information will be available on _____. After that date, you may call the credit union during regular business hours at (telephone number) to find out the [dividend/interest] rate and annual percentage yield (APY) that will apply to your term share account if it is renewed.

Note: Pre-maturity notices should follow the requirements of § 707.5(b–d) as closely as possible. Care should be taken to explain any grace periods used. See discussion of use of alternative timing in supplementary information to § 707.2(o) and § 707.5(b–d).

B–4 SAMPLE FORM (SIGNATURE CARD/ APPLICATION FOR MEMBERSHIP)

SIGNATURE CARD/APPLICATION FOR MEMBERSHIP

ACCOUNT NUMBER _____

_____ _____ _____
(last name) (first name) (middle name)

_____ _____
(street address) (apartment no.)

_____ _____ _____
(city) (state) (zip code)

_____ _____
(home telephone no.) (business telephone no.)

_____ _____
(Social Security # or TIN) (date of birth)

_____ _____
(mother's maiden name) (employer, occupation)

I hereby make application for membership in and agree to conform to the Bylaws, as amended, of _____ Credit Union (the "Credit Union"). I certify that: I am within the field of membership of this Credit Union; the information provided on this application is true and correct; and my signature on this card applies to all accounts under my name at this Credit Union. I also agree to be bound to the terms and conditions of any account that I have in the Credit Union now or in the future.

_____
(signature of applicant)

This application approved _____ (date) by the (Check one)
( ) Board ( ) Exec. Committee ( ) Membership Officer
Signed: _____
(Secretary; Exec. Cmte. Member, or Membership Officer)

Note: This form is modeled on NCUA Form FCU 150, Application for Membership, as discussed in the Accounting Manual for FCUs, §§ 5030.1, 5150.3. It is noted that other information can also be requested on the signature card, as long as it is in accordance with federal and state laws. For example, information identifying the member, such as a state driver's license number, could be added. The types of accounts that the signature applies to could be specified. Furthermore, the Board notes that this card contains much identification information that may not be necessary for all credit unions; common sense should guide credit union boards of directors in designing their applications for membership/signature cards. However, the Board believes that the information solicited on this form is reasonable and prudent for many credit unions. Payable on death designations, joint account language required under state law, life savings beneficiary designations, and other like variations and designations may be added to the card if so desired. The proposed signature card/ application for membership form contained taxpayer certification language. One commenter noted that the IRS may always change its requirements in this area, which are beyond the authority of the Board. Therefore, the Board has deleted reference to the IRS taxpayer certification required by 26 USC 3406, but notes that such certification must be made in accordance with applicable law and IRS rules. The information may be included on the front and back of a standard size signature card, or on the front of a large size signature card. However, no account terms may be included on a signature card unless a copy of the signature card is provided to the member at the time of account opening. The Board recommends that credit unions refrain from this practice, and instead use standard account disclosures. One reason for this is that if laws, regulations or credit union policies change, discrepancies may result between them and the earlier signature card terms. Given the longevity of credit union membership, signature cards may well be in use for up to or over a century. In addition, as signature cards are relatively small, they probably will not contain enough space to make all desired and required disclosures. Fragmentation of terms, some on signature cards, some on separate disclosures, could easily lead to member confusion. As terms are usually construed against the drafter, credit unions should be very careful in their use of account terms and conditions varying from those provided as model clauses and sample forms in this appendix.

B–5 SAMPLE FORM (TERM SHARE [CERTIFICATE] ACCOUNT)

TERM SHARE (CERTIFICATE) ACCOUNT

_____ _____
Date Issued Account Number

_____ _____
Certificate Number Social Security Number

This is to certify that (name(s)) _____ [is/are] the owner(s) of a term share certificate account in the _____ Credit Union (the "Credit Union") in the amount of _____ Dollars ($_____). This term share certificate account may be redeemed on (maturity date) _____ only upon presentation of the certificate to the Credit Union. The dividend rate of this certificate account is _____% with an annual percentage yield of _____%. The annual percentage yield and dividend rate assume that dividends are to be [check one] ( ) added to principal/ ( ) paid to regular share account number _____/( ) mailed to owner(s). This account is subject to all terms and conditions stated in the Term Share Certificate Account Disclosures, as they may be amended from time to time, and incorporates the same by reference into this agreement.

_____
Authorized signature

_____
Authorized signature

Note: This form is modeled on NCUA Form FCU 107SCP, Credit Union Share Certificate, as discussed in the Accounting Manual for FCUs, §§ 5030.1, 5150.6. It is simplified to reflect the term share (certificate) account agreement, the parties involved, the maturity term and the annual percentage yield and dividend rate. All other terms are incorporated by reference. This should allow the credit union maximum flexibility in fashioning certificate, and other term share account, products. If a credit union so desired, other terms and conditions could be incorporated into the term share certificate itself, as long as a copy is presented to the member at the account opening. Care should also be taken to ensure that the term share certificate format addresses any necessary state law concerns. As the FRB's Regulation D on reserve requirements permits all term share accounts to be represented by a transferable or nontransferable, or a negotiable or nonnegotiable, certificate, instrument, passbook, statement or otherwise, and still be considered a "time deposit", the Board has made no entry on this sample form regarding such terms, leaving the decision instead to each credit union's board of directors. 12 CFR 202.4(c)(2).

B–6 SAMPLE FORM (REGULAR SHARE ACCOUNT DISCLOSURES)

REGULAR SHARE ACCOUNT DISCLOSURES

1. *Rate information.* As of April 1, 1995, the dividend rate was 5.00% and the annual percentage yield (APY) was 5.13% on your regular share account. In addition, the credit union estimates a prospective dividend rate of 5.25% and a prospective APY of 5.39% on your share account for this dividend period. The divident rate and annual percentage yield may change every quarter as determined by the credit union board of directors.

2. *Compounding and crediting.* Dividends will be compounded daily and will be credited quarterly. For this account type, the dividend period is quarterly, for example, the beginning date of the first dividend period of the calendar year is January 1 and the ending date of such dividend period is March 31. All other dividend periods follow this same pattern of dates. The dividend declaration date follows the ending date of a dividend period, and for the example is April 1. If you close your regular share account before dividends are credited, you will not receive accrued dividends.

3. *Minimum balance requirements.* The minimum balance to open this account is the purchase of a $5 share in the Credit Union. You must maintain a minimum daily balance of $500 in your account to avoid a service fee. If, during any day during a quarter, your account balance falls below the required minimum daily balance, your account will be subject to a service fee of $5 for that quarter.

4. *Balance computation method.* Dividends are calculated by the daily balance method which applies a daily periodic rate to the principal in your account each day.

5. *Accrual of dividends.* Dividends will begin to accrue on the business day you deposit noncash items (e.g., checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies	$5.00 per statement
b. Account inquiries	$3.00 per inquiry
c. Dormant account fee	$10.00 per month
d. Wire transfers	$8.00 per transfer
e. Minimum balance service fee.	$5.00 per quarter
f. Share transfer	$1.00 per transfer
g. Excessive share	$1.00 per item withdrawals

7. *Transaction limitations.* During any statement period, you may not make more than six withdrawals or transfers to another credit union account of yours or to a third party by means of a preauthorized or automatic transfer or telephonic order or instruction. No more than three of the six transfers may be made by check, draft, debit card, if applicable, or similar order to a third party. If you exceed the transfer limitations set forth above in any statement period, your account will be subject to closure by the credit union or to a fee of $1.00 per item.

8. *Nature of dividends.* Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

9. *Bylaw Requirements.* A member who fails to complete payment of one share within

_____ of his admission to membership, or within _____ from the increase in the par value in shares, or a member who reduces his share balance below the par value of one share and does not increase the balance to at least the par value of one share within _____ of the reduction may be terminated from membership at the end of a dividend period. [All blanks should be filled with time chosen by credit union board of directors, but must be at least 6 months.] Shares may be transferred only from one member to another, by written instrument in such form as the Credit Union may prescribe. The Credit Union reserves the right, at any time, to require members to give, in writing, not more than 60 days notice of intention to withdraw the whole or any part of the amounts so paid in by them. No member may withdraw shareholdings that are pledged as required on security on loans without the written approval of the credit committee or a loan officer, except to the extent that such shares exceed the member's total primary and contingent liability to the Credit Union. No member may withdraw any shareholdings below the amount of his/her primary or contingent liability to the Credit Union if he/she is delinquent as a borrower, or if borrowers for whom he/she is comaker, endorser, or guarantor are delinquent, without the written approval of the credit committee or loan officer.

10. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $5. The dividend period of the Credit Union is quarterly.

11. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.

12. *Other Terms and Conditions.* [In this item, which may be titled or subdivided in any manner by each credit union, NCUA suggests that the following issues be covered or handled: statutory lien or setoff; expenses (garnishments and bankruptcy orders and holds on account); joint ownership accounts; trust accounts; payable-on-death accounts; retirement accounts; Uniform Transfer to Minor Act accounts; sole proprietorship accounts; escrow and custodial accounts; corporation accounts; not-for-profit corporation accounts; voluntary association accounts; partnership accounts; public unit accounts; powers of attorney (guardianship orders); tax disclosures and certifications; Uniform Commercial Code variances; amendments; reliance on signature card; change of address; incorporations of other documents by reference, such as expedited funds availability policies, service charges schedules or electronic banking disclosures; ability to suspend services; and operational matters (stop payment orders—verbal and written, satisfactory identification, refusal of deposits not in proper form, wire transfers, stale check deposits, availability of periodic statements or passbook feature.)]

Note: This form is modeled on the share account disclosures in the Accounting Manual for FCUs, § 5150.7. The disclosures are for a variable-rate, daily balance method dividend calculation regular share account in an FCU with a $500 minimum balance to avoid service fees. For the example, the account was opened on May 1, 1995. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures will reflect the prospective dividend rate for a given dividend period. Item nos. 1–8 reflect standard TISA and part 707 disclosures discussed in sections B–1 through B–3 of this Appendix. Note that if the credit union limits the maximum amount of shares which may be held by one member under NCUA Standard FCU Bylaws, Art. III, § 2, that this should be stated in item no. 7, transaction limitations. Item no. 9 reflects various terms provided in Art. III, §§ 3–6 of the NCUA Standard FCU Bylaws. If this were a passbook account, then the requirements of Art. IV, Receipting for Money—Passbooks, in the NCUA Standard FCU Bylaws would also be included in item no. 9. Item no. 10 reflects the par value amount of regular shares in a federal credit union, pursuant to section 117 of the FCU Act, 12 USC 117, and Art. XIV, § 3 of the NCUA Standard FCU Bylaws. It also states the dividend period of the credit union, which is set by the board of directors. Item no. 11 addresses the requirements of 12 CFR part 740. Nonfederally insured credit unions (NICUs) would be expected to disclose information required by section 151 of the Federal Deposit Insurance Corporation Improvement Act of 1991. 12 USC 1831t. By December 19, 1992, all NICUs were required to include conspicuously on all periodic

statements of account, signature cards, passbooks, share certificates and other similar instruments of deposit and in all advertising a notice that the credit union is not federally insured. Additional disclosures will be required of NICUs by June 19, 1994. Item no. 12 is inserted to ensure that credit unions add other account terms and conditions not covered by the proposed regulation. These sorts of terms are contemplated by proposed § 707.3(b), requiring that the disclosures reflect the terms of the legal obligation between the member and the credit union. This list is not meant to be exhaustive, but to give a general idea of other topics often covered in share account contracts. Item no. 12 is not expressly required by either TISA or part 707, but any of these terms that are disclosed must be accurate and not misleading. Also the Board strongly recommends that such terms are included in account opening disclosures to inform the membership and to clearly set forth the legal relationship between the members and their credit union.

B–7 SAMPLE FORM (SHARE DRAFT ACCOUNT DISCLOSURES)

SHARE DRAFT ACCOUNT DISCLOSURES

1. *Rate information.* As of January 1, 1995, the dividend rate was 3.00% and the annual percentage yield (APY) was 3.04% on your share account. In addition, the prospective dividend rate on your account is 3.15% with a prospective annual percentage yield (APY) of 3.20% for the current dividend period. The dividend rate and APY may change every dividend period as determined by the credit union board of directors.

2. *Compounding and crediting.* Dividends will be compounded monthly and will be credited monthly. For this account type, the dividend period is monthly, for example, the beginning date of the first dividend period of the calendar year is January 1 and the ending date of such dividend period is January 31. All other dividend periods follow this same pattern of dates. The dividend declaration date follows the ending date of a dividend period, and for the example above is February 1. If you close your share draft account before dividends are credited, you will not receive accrued dividends.

3. *No minimum balance requirements apply to this account.*

4. *Balance computation method.* Dividends are calculated by the average daily balance method which applies a periodic rate to the average daily balance in the account for the period. The average daily balance is calculated by adding the balance in the account for each day of the period and dividing that figure by the number of days in the period.

5. *Accrual of dividends.* Dividends will begin to accrue no later than the business day we receive provisional credit for the placement of noncash items (e.g. checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies	$5.00 per statement
b. Account inquiries	$3.00 per inquiry
c. Dormant account fee	$10.00 per month
d. Wire transfers	$8.00 per transfer
e. Overdrafts/Returned Items.	$5.00 per draft
f. Share transfer	$1.00 per transfer
g. Excessive share withdrawal.	$1.00 per item
h. Certified checks	$5.00 per check
i. Stop Payment Order ..	$5.00 per order
j. Check Printing Fee	$12.00 per 200 checks (varies depending on style of check ordered)

7. *No transaction limitations apply to this account.*

8. *Nature of dividends.* Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

9. *Bylaw Requirements.* A member who fails to complete payment of one share within _____ of his admission to membership, or within _____ from the increase in the par value in shares, or a member who reduces his share balance below the par value of one share and does not increase the balance to at least the par value of one share within _____ of the reduction may be terminated from membership at the end of a dividend period. [All blanks should be filled with time chosen by credit union board of directors, but must be at least 6 months.] Shares may be transferred only from one member to another, by written instrument in such form as the Credit Union may prescribe. The Credit Union reserves the right, at any time, to require members to give, in writing, not more than 60 days notice of intention to withdraw the

whole or any part of the amounts so paid in by them. Shares paid in under an accumulated payroll deduction plan may not be withdrawn until credited to a member's account. No member may withdraw shareholdings that are pledged as required on security on loans without the written approval of the credit committee or a loan officer, except to the extent that such shares exceed the member's total primary and contingent liability to the Credit Union. No member may withdraw any shareholdings below the amount of his/her primary or contingent liability to the Credit Union if he/she is delinquent as a borrower, or if borrowers for whom he/she is comaker, endorser, or guarantor are delinquent, without the written approval of the credit committee or loan officer.

10. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $5. The dividend period of the Credit Union is monthly, beginning on the first of a month and ending on the last day of the month.

11. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.

12. *Other Terms and Conditions.* [See section B–6, item 12, of this appendix].

Note: This form is modeled on the share account disclosures in the Accounting Manual for FCUs, § 5150.7. The disclosures are for a variable-rate, average daily balance method dividend calculation share draft account in an FCU with no minimum balance requirement. For purposes of this example, the account was opened on January 15, 1995. The Credit Union has monthly dividend periods. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures will reflect the prospective dividend rate for a given dividend period. The disclosures are very similar to the ones in section B–6 of Appendix B, except for the rollback and par value disclosures, which have been removed from the final rule and appendices.

B–8 SAMPLE FORM (MONEY MARKET SHARE ACCOUNT DISCLOSURES)

MONEY MARKET SHARE ACCOUNT DISCLOSURES

1. *Rate information.* As of January 1, 1995, if your average daily balance was $500 or more, the dividend rate paid on the entire balance in your account was 4.75%, with an annual percentage yield (APY) of 4.85%. If your average daily balance is $500 or more, a prospective dividend rate of 4.95% will be paid on the entire balance in your account with a prospective APY of 5.00% for this dividend period on your account. The dividend rate and APY may change every dividend period as determined by the credit union board of directors.

2. *Compounding and crediting.* Dividends will be compounded monthly and will be credited quarterly. If you close your share money market account before dividends are credited, you will not receive accrued dividends.

3. *Minimum balance requirements.* The minimum balance required to open this account is $500. You must maintain a minimum daily balance of $500 in your account to avoid a service fee. If, during any (time period), your account falls below the required minimum daily balance, your account will be subject to a service fee of $5 for that (time period).

4. *Balance computation method.* Dividends are calculated by the average daily balance method which applies a periodic rate to the average daily balance in your account for the period. The average daily balance is calculated by adding the principal in the account for each day of the period and dividing that figure by the number of days in the period.

5. *Accrual of dividends.* Dividends will begin to accrue on the business day you deposit noncash items (e.g., checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies	$5.00 per statement
b. Account inquiries	$3.00 per inquiry
c. Dormant accountee ...	$10.00 per month
d. Wire transfers	$8.00 per transfer
e. Minimum balance service fee.	$5.00 per time period
f. Share transfer	$1.00 per transfer
g. Excessive share withdrawals.	$1.00 per item
h. Certified checks	$5.00 per check
i. Stop Payment Order ..	$5.00 per order
j. Check Printing Fee	$12.00 per 200 checks (varies depending on style of check ordered)

7. *Transaction limitations.* During any statement period, you may not make more than six withdrawals or transfers to another credit union account of yours or to a third party by means of a preauthorized or automatic transfer or telephonic order or instruction. No more than three of the six transfers may be made by check, draft, debit card, if applicable, or similar order to a third party. If you exceed the transfer limitations set forth above in any statement period, your account will be subject to closure by the credit union or to a fee of $1.00 per item.

8. *Nature of dividends.* Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.

9. *Bylaw Requirements.* [This section should reflect any requirements concerning share accounts in the FISCU's bylaws or charter.]

10. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $50. The dividend period of the Credit Union is monthly, beginning on the first of a month and ending on the last day of the month.

11. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.

12. *Other Terms and Conditions.* [See section B–6, item 12, of this appendix.]

Note: This form is modeled on the share account disclosures in the Accounting Manual for FCUs, § 5150.7 and on the share draft account disclosures in section B–7 of this appendix. The disclosures are for a variable-rate, tiered-rate (method A, option 1), average daily balance method dividend calculation, money market share account in a FISCU with a $500 minimum balance to open the account and to avoid service fees. For purposes of this example, the account was opened on January 29, 1995. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures will reflect the prospective dividend rate for a given dividend period. Note that the contents of Item 9, Bylaw requirements, must be tailored to the specific bylaws of a FISCU or NICU. Also note the high par value amount in Item 10.

B–9 SAMPLE FORM (TERM SHARE [CERTIFICATE] ACCOUNT DISCLOSURES)

TERM SHARE (CERTIFICATE) ACCOUNT DISCLOSURES

1. *Rate information.* [Repeat rates disclosed on face of term share certificate, see B–5, Sample Form (Term Share (Certificate) Account).]

2. *Compounding and crediting.* Dividends will be compounded monthly and will be credited annually. If you close your certificate account before dividends are credited, you will not receive accrued dividends.

3. *Minimum balance requirements.* The minimum balance required to open this account is $500.

4. *Balance computation method.* Dividends are calculated by the daily balance method, which applies a daily periodic rate to the principal in your account each day.

5. *Accrual of dividends.* Dividends will begin to accrue on the business day you deposit noncash items (e.g., checks) to your account.

6. *Fees and charges.* The following fees and charges may be assessed against your account.

a. Statement copies ..... $5.00 per statement
b. Account inquiries ..... $3.00 per inquiry
c. Share transfer ..... $1.00 per transfer

7. *Transaction limitations.* After the account is opened, you may not make deposits into the account until the maturity date stated on the certificate.

8. *Maturity date.* Your account will mature on January 1, 1996.

9. *Early withdrawal penalties.* We may impose a penalty if you withdraw any of the funds before the maturity date. The penalty will equal three months' dividends on your deposit.

10. *Renewal policies.* Your certificate account will automatically renew at maturity. You will have a grace period of 10 business days after the maturity date to withdraw the funds in the account without being charged an early withdrawal penalty.

11. *Bonus.* You will receive a new (insert brand name) toaster-oven as a bonus when you open the account after December 31, 1994, and before June 30, 1995. You must maintain your entire principal on deposit until the maturity date of your certificate account to obtain the bonus.

12. **[RESERVED]**

13. *Bylaw Requirements.* [This section should reflect any requirements concerning share accounts in the FISCU's bylaws or charter.]

14. *Par value of shares; Dividend period.* The par value of a regular share in this Credit Union is $25. The dividend period of the Credit Union on this type of account is annual, beginning on the date the account is opened, and ending on the stated maturity date, unless renewed.

15. *National Credit Union Share Insurance Fund.* Member accounts in this Credit Union are federally insured by the National Credit Union Share Insurance Fund.

16. *Other Terms and Conditions.* [See section B–6, item 12, of this appendix.]

Note: Even though this disclosure is for an account at a FISCU, this form is modeled on the share account disclosures in the Accounting Manual for FCUs, § 5150.7 and upon the regular share account disclosures in section B–6 of this appendix. The disclosures are for a fixed-rate, daily balance method dividend calculation, automatically renewing term share certificate account in a FISCU with a $500 minimum balance to open the account and a ten day grace period. For the example, the account is opened on January 1, 1995 and matures on January 1, 1996. Other terms are self-explanatory. The dividend rate paid and annual percentage yield disclosures reflect the contracted, prospective dividend rate for a given dividend period. Note the special disclosures for term share certificate accounts, items nos. 8–10. Note also the bonus disclosure, item no. 11.

B–10 SAMPLE FORM (PERIODIC STATEMENT)

PERIODIC STATEMENT

_____ _____
Member Name Account Number

[Transaction account activity by date]

[Average daily balance of $1,500 for the month, daily compounding]

Your account earned $6.72, with an annual percentage yield earned of 5.40%, for the statement period from May 1 through and including May 31. In addition, your account earned $15 in extraordinary dividends for this period. Any fees assessed against your account are shown in the body of the periodic statement and are identified by the code at the bottom margin of this statement.

Service charge codes

SC-1 Stop Payment Order Fee
SC-2 Statement Copy Fee
SC-3 Draft Return Fee
SC-4 Transfer from Shares
SC-5 Microfilm Copy
SC-6 Share Draft Printing Fee
SC-7 Dormant Account Fee
SC-8 Wire Transfer Fee
SC-9 Excessive Share Withdrawal Fee
SC-10 _____

Other transactions

D=Dividends
EC=Error Correction
OR=Overdraft Returned
OL=Overdraft Loan
OS=Overdraft Share Transfer

Note: This form is modeled on the share draft statement of account, Form FCU 107G-SD, in the Accounting Manual for FCUs, § 5150.4. All information is self-explanatory. Codes of transactions are not required, but are a common credit union practice. The information regarding fees could also be included on the line of the periodic statement showing when the fees were debited from the account. Alternatively, a credit union could show all fees debited against the account for the statement period in a special area of the periodic statement. Clarity to the member of the required information—annual percentage yield earned; amount of dividends; fees imposed and length of period—is the important goal. An additional disclosure regarding the dollar value of any extraordinary dividends earned must be added to those statements showing the payment of such extraordinary dividends to the member.

B–11 SAMPLE FORM (RATE AND FEE SCHEDULE)

RATE AND FEE SCHEDULE

This Rate and Fee Schedule for all Accounts sets forth certain conditions, rates, fees and charges applicable to your regular share, share draft, and money market accounts at the _____ Federal Credit Union as of _____ [insert date of delivery to member]. This schedule is incorporated as part of your account agreement with the _____ Federal Credit Union.

REGULAR SHARE

Dividend Rate as of Last Dividend Declaration Date _____%

Annual Percentage Yield as of Last Dividend Declaration Date _____%

Prospective Dividend Rate _____%

Prospective Annual Percentage Yield _____%

Dividends Compounded [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Dividends Credited—At close of a dividend period

Dividend Period [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Minimum Opening Deposit $5.00 par value share

Minimum Monthly Balance [None, $ amount]

SHARE DRAFT

Dividend Rate as of Last Dividend Declaration Date _____%

Annual Percentage Yield as of Last Dividend Declaration Date _____%

Prospective Dividend Rate _____%

Prospective Annual Percentage Yield _____%

Dividends Compounded [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Dividends Credited—At close of a dividend period

Dividend Period [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Minimum Opening Deposit [None, $ amount]

Minimum Monthly Balance [None, $ amount]

MONEY MARKET

Dividend Rate as of Last Dividend Declaration Date _____%

Annual Percentage Yield as of Last Dividend Declaration Date _____%

Prospective Dividend Rate _____%

Prospective Annual Percentage Yield _____%

Dividends Compounded [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Dividends Credited— At close of a dividend period

Dividend Period [Annually, Semiannually, Quarterly, Monthly, Weekly, Daily]

Minimum Opening Deposit [None, $ amount]

Minimum Monthly Balance [None, $ amount]

The following fees may be assessed in connection with your accounts:

Fees Applicable to All Accounts:	
Returned item fee	$____.00 per item
Account reconciliation fee.	$____.00 per hour
Statement copies fee	$____.00 per statement
Certified draft fee	$____.00 per draft
Wire	$____.00 per transfer
Account inquiry fee	$____.00 per inquiry
Dormant account fee	$____.00 per month
Minimum balance service fee.	$____.00 per day
Share transfer fee	$____.00 per Transfer
Excessive share withdrawal transfer fee.	$____.00 per item
Share Draft Account Fees:	
Monthly service fee	$____.00 per month
Overdraft transfers fee	$____.00 per overdraft
Drafts returned insufficient funds fee.	$____.00 per draft
Stop payment order fee	$____.00 per order
Draft copy fee	$____.00 per copy
Check printing fee	$____.00 per 200 drafts
Money Market Share Account Fees:	
Monthly service fee	$____.00 per month
Check printing fee	$____.00 per 200 drafts

Note: This illustration is for use of an FCU. The information provided on a Rate and Fee Schedule can be presented in any format. To ensure that it is a part of the account agreement, if used, it should be incorporated by reference into the appropriate share account disclosures. The figures used are illustrative only, except for the overdraft transfer fee of $1.00 per overdraft and the excessive share transfer fee of $1.00 per item, which are set in the NCUA Standard FCU Bylaws, Art. III, § 4 and § 5(f), respectively.

Appendix C—Official Staff Interpretations

Introduction

1. *Official status.* This commentary is the means by which the staff of the Office of General Counsel of the National Credit Union Administration issues official staff interpretations of Part 707 of the NCUA Rules and Regulations. Good faith compliance with this commentary affords protection from liability under section 271(f) of the Truth in Savings Act (TISA), 12 U.S.C. § 4311.

§ 707.1—Authority, purpose, coverage, and effect on state laws.

(c) Coverage

1. *Foreign applicability.* Part 707 applies to all credit unions that offer share and deposit accounts to residents (including resident aliens) of any state as defined in 707.2(v) and that offer accounts insurable by the National Credit Union Share Insurance Fund (NCUSIF) whether or not such accounts are insured by the NCUSIF. Corporate credit unions designated as such by NCUA under 12 CFR § 704.2 (definition of "corporate credit union") are exempt from part 707.

2. *Persons who advertise accounts.* Persons who advertise accounts are subject to the advertising rules. This includes agent and agented accounts, such as a member who subdivides interests in a jumbo term share certificate account for sale to other parties or among members who form a certificate account investment club. For example, if an agent places an advertisement that offers members an interest inan account at a credit union, the advertising rules apply to the advertisement, whether the account is held by the agent or directly by the member.

3. *Nonautomated credit unions.* Nonautomated credit unions with an asset size of $2 million or less, after subtracting any nonmember deposits, are exempt from TISA and part 707. NCUA defines a "nonautomated credit union" as a credit union without sufficient data processing capability and capacity to establish, operate and maintain a share and loan software system to timely and accurately process all account transactions of all members. The nonautomated credit union exemption is available to all credit unions meeting the asset size and automation standards of this comment, including newly chartered credit unions. If any of the credit unions eligible for this exemption grow to have more than $2 million in assets as of December 31 of any year, the NCUA Board will require such credit unions to comply with TISA and part 707 on January 1 of one year after such credit union loses its exemption eligibility. Similarly, if a credit union becomes sufficiently automated to operate a complete share and loan system, such credit union will be entitled to the same compliance phase-in period.

(d) Effect on state laws

1. *Preemption of state laws/Inconsistent requirements.* State law requirements that are inconsistent with the requirements of TISA and part 707 are preempted to the extent of the inconsistency. A state law is inconsistent if it requires a credit union to make disclosures or take actions that contradict the requirements of the federal law. A state law is also contradictory if it requires the use of the same term to represent a different amount or a different meaning than the federal law, requires the use of a term different from that required in the federal law to describe the same item, or permits a method of calculating dividends or interest on an account different from that required in the federal law.

2. *Preemption determinations.* A credit union, state, or other interested party may request the Board to determine whether a state law requirement is inconsistent with the federal requirements. A request for a determination should be addressed to NCUA's Office of General Counsel, 1775 Duke Street, Alexandria, VA 22314. Written preemption requests should cite (or include a copy of) the allegedly inconsistent state law, demonstrate the inconsistency with TISA and part 707 and the burden on credit unions, and formally request a preemption determination. The Office of General Counsel may provide other interested parties, particularly affected states, an informal opportunity to comment on any request for a preemption determination, unless it finds that such notice and opportunity for comment would be impracticable, unnecessary, or contrary to the public interest. NCUA will publicize any preemption determinations using any means readily at its disposal.

3. *Effect of preemption determinations.* After the Board, through its Office of General Counsel, determines that a state law is incon-

sistent, a credit union may not make disclosures using the inconsistent term or take actions relying on the inconsistent law.

4. *Reversal of determination.* The Board reserves the right to reverse a determination for any reason bearing on the coverage or effect of state or federal law.

§ 707.2—Definitions.

(a) Account

1. *Covered accounts.* Examples of accounts subject to the regulation are:

i. Dividend-bearing and interest-bearing accounts.

ii. Non-dividend-bearing and non-interest-bearing accounts.

iii. Accounts opened as a condition of obtaining a credit card.

iv. Escrow accounts with a consumer purpose, such as an account established by a member to escrow rental payments, pending resolution of a dispute with the member's landlord.

v. Accounts held by a parent or custodian for a minor under a state's Uniform Gift to Minors Act (or Uniform Transfers to Minors Act).

vi. Individual retirement accounts (IRAs) and simplified employee pension (SEP) accounts.

vii. Payable-on-Death (POD) or "Totten trust" accounts.

2. *Other accounts.* Examples of accounts not subject to the regulation are:

i. Mortgage escrow accounts for collecting taxes and property insurance premiums.

ii. Accounts established to make periodic disbursements on construction loans.

iii. Trust accounts opened by a trustee pursuant to a formal written trust agreement (not merely declarations of trust on a signature card such as a "Totten trust," or an IRA or SEP account).

iv. Accounts opened by an executor in the name of a decedent's estate.

v. Accounts of individuals operating businesses as sole proprietors.

vi. Certificates of indebtedness. Some credit unions borrow funds from their members through a certificate of indebtedness that sets forth the terms and conditions of the repayment of the borrowing, such as federal credit unions do through 12 CFR § 701.38. Such an account does not represent an account in a credit union and is not covered by part 707.

vii. Unincorporated nonbusiness association accounts.

3. *Other investments.* The term "account" does not apply to these products. Examples of products not covered are:

i. Government securities.

ii. Mutual funds.

iii. Annuities.

iv. Securities or obligations of a credit union.

v. Contractual arrangements such as repurchase agreements, interest rate swaps, and bankers acceptances.

vi. Purchases of U.S. Savings Bonds through a credit union.

vii. Services offered through a group purchasing plan or a credit union service organization (CUSO).

4. *Options.* All dividend-bearing and interest-bearing accounts are either fixed-rate or variable-rate accounts.

5. *Use of synonyms.* Generally, it is not the purpose of part 707 to prohibit specific descriptive terms for accounts. For example, credit unions can use adjectives and trade names to describe accounts such as "Best Share Draft Account," or "Ultra Money Market Share Account." Synonyms for share, share draft, money market share, and term share accounts may be used to describe various types of credit union share and deposit accounts as long as the synonym is accurate and not misleading and, for account disclosures, is used in conjunction with the correct legal term. For example, the following synonyms may be used:

i. The term "checking account" may be used to describe sharedraft accounts.

ii. The term "money market account" may be used to describe money market share accounts.

iii. The term "savings account" may be used to describe regular share and share accounts.

iv. The terms "share certificate," "certificate account," or "certificate" may be used to describe share certificates and other dividend-bearing term share accounts.

v. However, under no circumstances may a credit union describe a share account as a deposit account, or vice versa. For example, the term "certificate of deposit" or "CD" may not be used to describe share certificates and other dividend-bearing term share accounts. Similarly, the terms "time account" (used in Regulation DD, 12 CFR § 230.2(u)) and "time deposit"

(used in Regulation D, 12 CFR § 204.2(c)) may not be used to describe term share accounts.

(b) *Advertisement*

1. *Covered messages.* Advertisements include commercial messages in visual, oral, or print media that invite, offer, or otherwise announce generally to members and potential members the availability of member accounts such as:

i. Telephone solicitations.

ii. Messages on automated teller machine (ATM) screens (including any printout).

iii. Messages on a computer screen in a credit union's lobby (including any printout) other than a screen viewed solely by the credit union's employee.

iv. Messages in a newspaper, magazine, or promotional flyer or on radio or television.

v. Messages promoting an account that are provided along with information about the member's existing account at a credit union and that promote another account at the credit union (such as account promotional messages on the periodic statement).

2. *Other messages.* Examples of messages that are not advertisements are:

i. Rate sheets published in newspapers, periodicals, or trade journals (unless the credit union or share and deposit broker that offers accounts at the credit union pays a fee to have the information included or otherwise controls publication).

ii. Telephone conversations initiated by a member or potential member about an account.

iii. An in-person discussion with a member about the terms for a specific account.

iv. Information provided to members about their existing accounts, such as on IRA disbursements, notices for automatically renewable term share accounts sent before renewal, or current rates recorded on a voice response machine.

(c) Annual Percentage Yield.

1. *General.* The annual percentage yield (APY) is required for disclosures for new accounts, oral responses to inquiries about rates; disclosures provided upon request; initial disclosures (if the credit union chooses to provide full disclosures instead of the abbreviated notice); notices prior to the renewal of a term share account, if known at the time the notice is sent, and in advertising. The annual percentage yield shows the total amount of dividends for a 365 day period (or a 366 day period for a leap year) on an assumed principal amount based on the dividend rate and frequency of compounding as a percentage of the assumed principal (for accounts such as share or share draft accounts) or for the total amount of dividends over the term of the account for term share accounts. The annual percentage yield assumes the principal amount remains in the account for 365 days (366 days for leap year) or for the term of the account.

2. *How Annual Percentage Yield Differs from Annual Percentage Yield Earned.* The annual percentage yield (APY) differs from the annual percentage yield earned (APYE). The annual percentage yield earned is required for periodic statements only. The annual percentage yield earned shows the total amount of dividends earned for the dividend or statement period as a percent of the actual average daily balance in the member's account. Unlike the annual percentage yield, the annual percentage yield earned is affected by additions and withdrawals during the period. The annual percentage yield and the annual percentage yield earned must be calculated according to the formulas provided in Appendix A to this rule.

(d) Average Daily Balance Method.

1. *General.* One of the two required methods (the daily balance is the other) of determining the balance upon which dividends must be accrued and paid. The average daily balance method requires the application of a periodic rate to the average daily balance in the account for the average daily balance calculation period. The average daily balance is determined by adding the full amount of principal in the account for each day of the period and dividing that figure by the number of days in the period.

(e) Board.

1. *General.* The NCUA Board.

(f) Bonus

1. *General.* Bonuses include items of value offered as incentives to members, such as an offer to pay the final installment deposit for a holiday club account if the final installment is over $10. Bonuses do not include the payment of dividends (including extraordinary dividends), the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, or other consideration aggregating $10 or less per year.

2. *Examples.* The following are examples of bonuses.

i. A credit union offers $25 to potential members for becoming a member and opening

an account. The $25 could be provided by check, cash, or direct deposit.

ii. A credit union offers $25 to a member with only a regular share account to open a share draft account. The $25 could be provided by check, cash, or direct deposit.

iii. A credit union offers a portable radio with a value of $20 to members and potential members for opening a share draft account.

iv. A credit union pays the final installment deposit for a holiday club account if over $10.

3. *Examples not comprising bonuses.* The following are examples of items that are not bonuses:

i. Discount coupons distributed by credit unions for use at restaurants or stores.

ii. A credit union offers $20 to any member if the member is responsible for encouraging a potential member to open an account. The $20 is not a bonus because the $20 is not paid to the individual opening the account. Any item, including cash, given or offered to a third party (that is not a joint member or joint owner in an account being opened) in exchange for a member or potential member opening (ora member renewing or adding to) an account is not a bonus.

iii. A credit union offers $25 to a member if the member can locate his name in the body of a newsletter.

iv. Life savings benefits. Many credit unions offer life savings benefits to beneficiaries of deceased members. Because the benefit accrues to a third party, such life savings plans offered are not bonuses.

v. A credit union offers to pay annual membership dues in a benevolent organization for a class of members.

4. *De minimis rule.* Items with a de minimis value of $10 or less are not bonuses. Credit unions may rely on the valuation standard used by the Internal Revenue Service (IRS) to determine if the value of the item is de minimis. Items required to be reported by the credit union under IRS rules are bonuses under this regulation. Examples of items of de minimis value are:

i. Disability insurance premiums on a share account valued at an amount of $10 or less per year.

ii. Coffee mugs, T-shirts or other merchandise with a market value of $10 or less per year.

5. *Aggregation.* In determining if an item valued at $10 or less is a bonus, credit unions must aggregate per account per calendar year items that may be given to members. In making this determination, credit unions aggregate per account only the market value of items that may be given for a specific promotion. To illustrate, assume a credit union offers in January to give members an item valued at $7 for each calendar quarter during the year that the average account balance in a share draft account exceeds $10,000. The bonus rules are triggered, since members are eligible under the promotion to receive up to $28 during the year. However, the bonus rules are not triggered if an item valued at $7 is offered to members opening a share draft account during the month of January, even though in November the credit union introduces a new promotion that includes, for example, an offer to existing share draft accountholders for an item valued at $8 for maintaining an average balance of $5,000 for the month.

6. *Waiver or reduction of a fee or absorption of expenses.* Bonuses do not include value received by members through the waiver or reduction of fees for credit union-related services (even if the fees waived exceed $10), such as the following:

i. Waiving a safe deposit box rental fee for one year for members who open a new account.

ii. Waiving fees for travelers checks for members, and waiving check and share draft printing fees.

iii. Nondiscriminatorily waiving all fees for a particular class of members, such as seniors or minors.

iv. Discounts on interest rates charged for loans at the credit union.

v. Rebates of loan interest already paid by a member.

vi. Discounts on application fees charged for loans at the credit union.

vii. Packaged, linked, or tied-account services.

7. *Non-dividend membership benefits.* Such benefits are not bonuses because they are sporadic in nature, often difficult to value, and providing non-dividend membership benefits is a long-standing unique credit union practice. (See commentary to § 707.2(r) for examples of such benefits.)

(g) Credit union.

1. *General.* Includes credit unions in the United States, Puerto Rico, Guam, U.S. Virgin Islands, and U.S. territories. Applies to credit unions whether or not the accounts in the credit union are federally, state, privately insured, or uninsured.

(h) Daily balance method.

1. *General.* One of the two required methods (the average daily balance is the other) of determining the balance upon which dividends must be accrued and paid. The daily balance method requires the application of a daily periodic rate to the full amount of principal in the account each day.

(i) Dividend and dividends.

1. *General.* Member savings placed in share accounts are equity investments, and the returns earned on these accounts are dividends. Federal credit unions may only offer dividend-bearing and non-dividend-bearing share accounts. State-chartered credit unions may offer both share and deposit accounts if permitted by state law. State law, including without limitation regulations and official interpretations, will determine if returns earned in accounts in state-chartered credit unions are dividends. Dividends exclude the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, and extraordinary dividends. Dividend-bearing accounts must be either fixed-rate or variable-rate accounts.

2. *Procedure.* Credit unions must follow appropriate law (state law for state-chartered credit unions and federal law for federal credit unions) in determining dividend policies and declaring dividends. Generally, dividends may be viewed as a portion of the available current and undivided earnings of the credit union which is set apart, after required transfers to reserves, by valid act of the board of directors, for distribution among the members. As a matter of legal procedure, members are usually not entitled to dividends until the following steps are completed: (1) the board of the credit union develops a nondiscriminatory dividend policy, by establishing dividend periods, dividend credit determination dates, dividend distribution dates, any associated penalties (if applicable), and the method of dividend computation for each type of share account; (2) the provision for required transfers to reserves are made; (3) sufficient and available prior and/or current earnings are available at the end of the dividend period; (4) the board formally makes a dividend declaration in accordance with the credit union's dividend policy; and (5) dividends must be paid to members by a credit to the appropriate share account, payment by check or share draft, or by a combination of the two methods.

3. *When available.* Credit unions must follow the law of their primary chartering authority to determine when dividends are available. Generally, it is the declaration of the dividend itself which creates the dividend and the member has no right to receive a dividend until it is so declared. The decision of when to declare dividends lies within the official discretion of each credit union's board of directors and cannot be abrogated by contract. An agreement to pay dividends on a share account is generally interpreted not as an obligation to pay the stipulated dividends absolutely and unconditionally, but as an undertaking to pay them out of the earnings when sufficiently accumulated from which dividends in general are properly payable. Generally, "prospective rates" are rates set in good faith in advance of the close of a dividend period, that may be altered if sufficient funds are not available, or in the event of a superseding event, such as a strike, plant closure, significant fluctuation in market rates and/or a significant change in financial structure, natural disaster or emergency that alters the assumptions under which the "prospective rates" were made. It is the intent of TISA that all disclosures be accurate when made, and credit unions are urged to make every effort to ratify disclosed "prospective rates." "Prospective rates" may also be referred to as "projected rates" or similar wording, but not as "estimated rates." (See comment 3(b)-2, prohibiting use of estimates).

4. *Sample dividend resolutions.*

(i) The following resolution may be used where the dividend rates are set after the close of a dividend period.

RESOLUTION OF BOARD OF DIRECTORS FOR THE DECLARATION OF DIVIDENDS

A. I, _____, certify that I am Secretary of_____ Credit Union Board of Directors, and that the following is a correct copy of the resolution for declaring dividends adopted by the _____ Credit Union at a meeting of the Board of Directors

duly and properly held on _____,19____. This resolution appears in the minutes of this meeting and has not been rescinded or modified.

B. RESOLVED, that

(1) The Board of Directors has developed a nondiscriminatory dividend policy, by establishing dividend periods, dividend credit determination dates, dividend distribution dates, any associated penalties (if applicable), and the method of dividend computation for each type of share account;

(2) The required transfers to reserves have been made; and

(3) Sufficient and available prior and/or current earnings are available at the end of this dividend period.

C. RESOLVED, further, that the Board of Directors now formally makes a dividend declaration in accordance with the Credit Union's dividend policy and authorizes that on _____,19____, dividends must be paid to members by a credit to the appropriate share account, payment by share draft or by a combination of the two methods.

D. I further certify that the Board of Directors of this Credit Union has, and the time of adoption of this resolution had, full power and lawful authority to adopt the foregoing resolutions and that this resolution revokes any prior resolution.

IN WITNESS WHEREOF, this is my signature and the date on which I signed this Resolution.

_____

Signature

_____

Date

[Attach list of accounts with dividend rates for each type of account.]

(ii) The following resolution may be used where the dividend rates are set before the close of a dividend period.

RESOLUTION OF BOARD OF DIRECTORS FOR THE DECLARATION OF DIVIDENDS

A. I, _____, certify that I am the Secretary of_____ Credit Union, and that the following is a correct copy of the resolution for declaring dividends adopted by the_____ Credit Union at a meeting of the Board of Directors duly and properly held on _____, 19____.This resolution appears in the minutes of that meeting and has not been rescinded or modified.

B. RESOLVED, that the Board of Directors has adopted a nondiscriminatory dividend policy, by establishing dividend periods, dividend credit determination dates, dividend distribution dates, any associated penalties (if applicable) and the method of dividend computation for each type of share account.

C. RESOLVED, that it is the policy and practice of the Board of Directors to meet periodically to establish prospective dividend rates for each type of dividend-bearing share account.

D. RESOLVED, that if the required transfers to reserves have been made and there are sufficient and available prior and/or current earnings available at the end of a dividend period, the officers of the Credit Union are authorized to pay dividends at the rate prospectively established by the Board of Directors for each account for the dividend period. The officers may pay the dividends without any further action of the Board of Directors. The act of paying the dividends shall constitute the declaration of the dividends and shall be a ratification of the prospective dividend rate.

IN WITNESS WHEREOF, this is my signature and the date on which I signed this Resolution.

_____

Signature

_____

Date

[Attach list of accounts with prospective dividend rates for each type of account.]

5. *Referencing.* Except where specifically stated otherwise, use of the term "share" in part 707, as in "share account," also refers to "deposit," as in "deposit account," where appropriate (for interest-bearing or non-interest-bearing deposit accounts at some state-chartered credit unions).

(j) Dividend declaration date.

1. *General.* The importance of the dividend declaration date is to tie the last paid dividend to a certain period of time to place members and potential members on notice that the last paid dividend is different from the next dividend to be paid. In order to achieve this purpose, a credit union may use any of the following methods:

i. "As of 3/15/95" (the date the board of directors last met and declared the last paid dividend).

ii. "As of 3/31/95" (the last day of the last dividend period upon which a dividend has been paid).

iii. "For the period 1/1/95 to 3/31/95" (the last dividend period upon which a dividend has been paid).

iv. "For the first quarter of 1995" (the last dividend period upon which a dividend has been paid).

v. "For April 1995" (the last dividend period upon which a dividend has been paid).

vi. "As of the last dividend declaration date" (the last dividend period upon which a dividend has been paid).

(k) Dividend period.

1. *General.* The dividend period is to be set by a credit union's board of directors for each account type, e.g., regular share, share draft, money market share, and term share. The most common dividend periods are weekly, monthly, quarterly, semi-annually, and annually. Dividend periods need not agree with calendar months, e.g., a monthly dividend period could begin March 15 and end April 14.

(l) Dividend rate.

1. *General.* The dividend rate does not reflect compounding. Compounding is reflected in the "annual percentage yield" definition.

2. *Referencing.* Except where specifically stated otherwise, use of the term "dividend rate" in part 707 also refers to "interest rate," where appropriate (for interest-bearing and non-interest-bearing deposit accounts at some state-chartered credit unions).

(m) Extraordinary dividends.

1. *General.* The definition encompasses all irregularly scheduled and declared dividends, and as dividends, extraordinary dividends are exempt from the "bonus" disclosure requirements. Extraordinary dividends do not have to be disclosed on account disclosures, but the dollar amount of an extraordinary dividend credited to the account during the statement period does have to be separately disclosed on the periodic statement for the dividend period during which the extraordinary dividends are earned. Extra ordinary dividends, like ordinary dividends, do not include the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses or non-dividend membership benefits. See comments 2(f) 1 through 7 and 2(i) 1 through 4. Extraordinary dividends may be calculated by any means determined by the board of directors of a credit union and may not be used in the annual percentage yield earned calculation.

2. *Use of synonym.* Extraordinary dividends may be described as "bonus dividends."

(n) Fixed-rate account.

1. *General.* Includes all accounts in which the credit union, by contract, agrees to give at least 30 days advance written notice of decreases in the dividend rate. Thus, credit unions can decrease rates only after providing advance written notice of rate decreases, e.g., a "change-in-terms notice."

(o) Grace period.

1. *General.* A period after maturity of an automatically renewing term share account during which the member may withdraw funds without being assessed a penalty. Use of a "grace period" is discretionary, not mandatory. This definition does not refer to the "grace period" account, which is a synonym for "federal rollback method" or "in by the 10th" accounts, which are prohibited by TISA and part 707.

(p) Interest.

1. *General.* Member savings placed in deposit accounts are debt investments, and the return earned on these accounts is interest. Federal credit unions are not authorized to offer any interest-bearing deposit accounts. State-chartered credit unions may offer both share and deposit accounts if permitted by state law. State law, including without limitation regulations and official interpretations, will determine if returns earned in accounts in state-chartered credit unions are interest. Interest excludes the payment of a bonus or other consideration worth $10 or less given during a year, the waiver or reduction of a fee, the absorption of expenses, non-dividend membership benefits, and extraordinary dividends.

2. *Differences between Dividends and Interest.* Generally, dividends are returns on an equity investment (shares); interest is return on a debt investment (deposits). Dividends, in general, are not properly payable until declared at the close of a dividend period; interest, in general, is properly payable daily according to the deposit contract. Dividend rates are prospective until actually declared; interest rates are set according to contract in advance and are earned on that basis. Share accounts establish a member (owner)/credit union (cooperative) relationship; deposit accounts establish a depositor (creditor)/depositary (debtor) relationship.

3. *Referencing.* Except where specifically stated otherwise, use of the terms "dividend" or

"dividends" in part 707 also refers to "interest" where appropriate (for interest-bearing and non-interest-bearing deposit accounts at some state-chartered credit unions).

(q) Member

1. *Professional capacity.* Examples of accounts held by a natural person in a professional capacity for another are:

i. Attorney-client trust accounts.

ii. Trust, estate and court-ordered accounts.

iii. Landlord-tenant security accounts.

2. *Other accounts.* Examples of accounts not held in a professional capacity include accounts held by parents for a child under the Uniform Gifts to Minors Act (or Uniform Transfers to Minors Act.

3. *Retirement plans.* IRAs and SEP accounts are member accounts to the extent that funds are invested in accounts subject to the regulation. Keogh accounts, like sole proprietor accounts, are not subject to the regulation.

(r) Non-dividend membership benefits.

1. *General.* Term reflects unique credit union practices that are difficult to value, encourage community spirit, and are not granted in such quantity as to be includable as calculable dividends.

2. *Examples.* Examples include:

i. Food, refreshments, and drawings and raffles at annual meetings, member functions, and branch openings.

ii. Travel club benefits.

iii. Prizes offered at annual meetings, such as U.S. Savings Bonds, a deposit of funds into the winner's account, trips, and other gifts. Such prizes are not bonuses because they are offered as an incentive to increase attendance at the annual meeting, and not to entice members to open, maintain, or renew accounts or increase an account balance.

iv. Life savings benefits.

(s) Passbook Account

1. *Relation to Regulation E.* Passbook accounts include accounts accessed by preauthorized electronic fund transfers to the account (as defined in 12 CFR § 205.2(j)), such as an account credited by direct share and deposit of social security payments. Accounts that permit access by other electronic means are not "passbook accounts," and any statements that are sent four or more times a year must comply with the requirements of 707.6.

(t) Periodic Statement

1. *General.* Periodic statements are not required by part 707. Passbook and term share accounts are exempt from periodic statement requirements.

2. *Examples.* Periodic statements do not include:

i. Additional statements provided solely upon request.

ii. General service information such as a quarterly newsletter or other correspondence that describes available services and products.

(u) Potential Member.

1. *General.* A potential member is a natural person eligible for membership in a credit union, who has not yet taken the steps necessary to become a member. The term also includes natural person nonmembers eligible to hold accounts in a credit union pursuant to relevant federal or state law.

2. *Verification of eligibility.* It is recommended that credit unions have sound written procedures in place to identify those eligible for membership. If these procedures include verification measures, such as an application process, verification telephone call or letter to an employer or association within the field of membership, witnessing by an existing member, or similar procedure, then the credit union may first verify the membership eligibility of a potential member before providing account disclosures or other information to the potential member. This process of verifying a member's eligibility status, making a recommendation for membership, and providing account disclosures should be completed within 20 calendar days. This period also applies when potential members not on credit union premises request disclosures.

3. *Nonmembers.* Within its sole discretion, the board of directors of a credit union may provide TISA disclosures to nonmembers who are ineligible for membership or to hold an account at the credit union. If disclosures are made to such nonmembers, it is the position of the Board that no civil liability can accrue to the credit union for any errors in such disclosures. (See commentary to 707.3(d)).

(v) State

General. Territories and possessions include American Samoa, Guam, the Mariana Islands, and the Marshall Islands.

(w) Stepped-rate account

1. *General.* Stepped-rate accounts are those accounts in which two or more dividend rates

(known at the time the account is opened) will take effect in succeeding periods.

2. *Example.* An example of a stepped-rate account is a one-year term share certificate account in which a 5.00 percent dividend rate is paid for the first six months, and 5.50 percent for the second six months.

(x) Term share account

1. *Relation to Regulation D.* Regulation D permits, in limited circumstances, the withdrawal of funds without penalty during the first six days after a "time deposit" is opened. (See 12 CFR § 204.2(c)(1)(i).) But the fact that a member makes a withdrawal as permitted by Regulation D does not disqualify the account from being aterm share account for purposes of this regulation (such as withdrawals upon the death of the member, or within a "grace period" for automatically renewable term share accounts).

2. *Club accounts.* Club accounts, including Christmas club, holiday club, and vacation club accounts may be either term share or regular share accounts, depending on the terms of the account. Although club accounts typically have a maturity date, they are not term share accounts unless they also require a penalty of at least seven days' dividends for withdrawals during the first six days after the account is opened.

(y) Tiered-rate Account

1. *General.* Tiered-rate accounts are those accounts in which two or more dividend rates are paid on the account and are determined by reference to a specified balance level. Tiered-rate accounts are of two types: Tiering Method A and Tiering Method B. In Tiering Method Aaccounts, the credit union pays the applicable tiered dividends rate on the entire amount in the account. This method is also known as the "hybrid" or "plateau" tiered-rate account. In Tiering Method B accounts, the credit union does not pay the applicable tiered dividends rate on the entire amount in the account, but only on the portion of the share account balance that falls within each specified tier. This method is also known as the "pure" or "split-rate" tiered-rate account. (See Appendix A, Section I, D.)

2. *Example.* An example of a tiered-rate account is one in which a credit union pays a 5.00 percent dividend rate on balances below $1,000, and 5.50 percent on balances $1,000 and above.

3. *Term share accounts.* Term share accounts that pay different rates based solely on the amount of the initial share and deposit are not tiered-rate accounts.

4. *Minimum balance accounts.* A requirement to maintain a minimum balance to earn dividends does not make an account a tiered-rate account. If dividends are not paid on amounts below a specified balance level, then the account has a minimum balance requirement (required to be disclosed under § 707.4(b)(3)(i)), but the account does not constitute a tiered-rate account. A zero rate (0%) cannot constitute a tier. Minimum balance accounts are single rate accounts with a minimum balance requirement.

(z) Variable-rate account

1. *General.* Includes accounts in which the credit union does not contract to give at least 30 days advance written notice of decreases in the dividend rate. An account meets this definition whether the rate change is determined by reference to an index, by use of a formula, or merely at the discretion of the credit union's board of directors. An account that permits one or more rate adjustments prior to maturity at the member's option, such as a rate relock option, is a variable-rate account.

2. *Differences between fixed-rate and variable-rate accounts.* All accounts must either be fixed-rate or variable-rate accounts. Classifying an account as variable-rate affects credit unions three ways:

i. Additional account disclosures are required (§ 707.4(b)(1)(ii));

ii. Rate decreases are exempted from change-in-terms requirements (§ 707.5(a)(2)(i)); and

iii. Advertising notice required (§ 707.8(c)(1)). Fixed-rate accounts require a contract term obligating the credit union to a 30-day advance, written notice to members before decreasing the dividend rate on the account. Term changes adversely affecting the member and rate decreases cannot take effect until 30 days after such fixed-rate change-in-terms notices are mailed or delivered to members (§ 707.5(a)).

§ 707.3—General disclosure requirements.

(a) Form

1. *General.* All required disclosures (e.g., account disclosures, change-in-terms notices, term share renewal/maturity notices, statement disclosures and advertising disclosures) must be made clearly and conspicuously, in a form the member may retain. Disclosures need be made

only as applicable (e.g., disclosures for a non-dividend-bearing account would not include disclosure of annual percentage yield, dividend rate, or other disclosures pertaining to dividend calculations).

2. *Design requirements.* Disclosures must be presented in a format that allows members and potential members to readily understand the terms of their account. Credit unions are not required to use a particular type size or typeface, nor are credit unions required to state any term more conspicuously than any other term. Disclosures maybe made:

i. In any order.

ii. In combination with other disclosures or account terms.

iii. In combination with disclosures for other types of accounts, as long as it is clear to members and potential members which disclosures apply to their account.

iv. On more than one page and on the front and reverse sides.

v. By using inserts to a document or filling in blanks.

vi. On more than one document, as long as the documents are provided at the same time.

3. *Consistent terminology.* A credit union must use the same terminology to describe terms or features that are required to be disclosed. For example, if a credit union describes a monthly fee (regardless of account activity), as a "monthly service fee" in account opening disclosures, the periodic statements and change-in-terms notices must use the same terminology so that members and potential members can readily identify the fee.

(b) General

1. *Terms and conditions.* Credit unions are required to have disclosures reflect the terms of the legal obligation between the credit union and a member at the time the member opens the account. This provision does not impose any contract terms or supersede state or other laws that define how the legal obligations between a credit union and its membership are determined.

2. *Specificity of legal obligation.* Credit unions may refer to the calendar month or to roughly equivalent intervals during a calendar year as a "month." Use of estimates is prohibited in TISA disclosures.

3. *Foreign language.* Disclosures may be made in any foreign language, if desired by the board of directors of a credit union. However, disclosures must also be provided in English, upon request.

(c) Relation to Regulation E

1. *General rule.* Compliance with Regulation E (12 CFR part 205) is deemed to satisfy the disclosure requirements of this regulation, such as when:

i. A credit union changes a term that triggers a notice under Regulation E, and the timing and disclosure rules of Regulation E for sending change-in-terms notices.

ii. A member adds an ATM access feature to an account, and the credit union provides disclosures pursuant to Regulation E, including disclosure of fees before the member receives ATM access. (See 12 CFR § 205.7.)

iii. A credit union complying with the timing rules of Regulation E discloses at the same time fees for electronic services (such as balance inquiry fees imposed if the inquiry is made at an ATM) that are required to be disclosed by this regulation, but not by Regulation E.

iv. A credit union relies on Regulation E's rules regarding disclosures of limitations on the frequency and amount of electronic fund transfers, including security-related exceptions. But any limitation on the number of "intra-institutional transfers" to or from the member's other accounts at the credit union during a given time period must be disclosed, even though intra-institutional transfers are exempt from Regulation E.

(d) Multiple members

1. *General.* When an account has multiple natural person member accountholders, delivery of disclosures to any member account holder or agent authorized by the account holder satisfies the disclosure requirements of part 707.

(e) Oral response to inquiries

1. *Application of rule.* Credit unions need not provide rate information orally. Disclosures need be made only as appropriate. For example, the requirement to give a telephone number for a member to call about rates for interest-bearing accounts and dividend-bearing term share accounts, would not be necessary for members calling the credit union for information. Also, the disclosure requirements are applicable only to credit union employees and volunteers acting in the ordinary course of credit union business.

2. *Relation to advertising.* The advertising rules do not cover an oral response to a question about rates.

3. *Existing accounts.* This paragraph does not apply to oral responses about rate information for existing term share accounts or accounts not currently offered. For example, if a member holding a one-year term share account requests dividend rate information about the account during the term, the credit union need not disclose the annual percentage yield, unless the member is calling for rate information under a maturity notice.

(f) Rounding and accuracy rules for rates and yields

(f)(1) Rounding

1. *Permissible rounding.* The annual percentage yield, annual percentage yield earned and dividend rate must be rounded to the nearest one-hundredth of one percentage point (.01%) when disclosed. Examples of permissible rounding are an annual percentage yield calculated to be 5.644%, rounded down and shown as 5.64%; 5.645% would be rounded up and disclosed as 5.65%. For account disclosures, the dividend rate may be expressed to more than two decimal places.

(f)(2) Accuracy

1. *Annual percentage yield and annual percentage yield earned.* The tolerance for annual percentage yield and annual percentage yield earned calculations is designed to accommodate in advertent errors. Credit unions may not purposely incorporate the one- twentieth of one percentage point (.05%) tolerance into their calculation of yields.

2. *Dividend rate.* There is no tolerance for an inaccuracy in the dividend rate.

§ 707.4—Account disclosures.

(a) Delivery of account disclosures

(a)(1) Account opening

1. *New accounts.* New account disclosures must be provided when:

i. A term share account that does not automatically rollover is renewed by a member.

ii. A member changes the term for a renewable term share account (from a one-year term share account to a six-month term share account, for instance) (see comment 5(b)-5 regarding disclosure alternatives).

iii. A credit union transfers funds from an account to open a new account not at the member's request, unless the credit union previously gave account disclosures and any change-in-terms notices for the new account (e.g., funds in a money market share account are transferred by a credit union to open a new account for the member, such as a share draft account, because the member exceeded transaction limitations on the money market share account).

iv. A credit union accepts a deposit from a member to an account that the credit union had previously deemed to be "closed," under applicable federal or state law, for the purpose of treating accrued, but uncredited, dividends as forfeited dividends. New account numbers are not required by this requirement.

2. *Acquired accounts.* New account disclosures need not be given when a credit union acquires an account through an acquisition of, or merger with, another credit union (but see 707.5(a) regarding advance notice requirements if terms are changed).

3.*Combination disclosures.* New account disclosures need not be given when a member has already received disclosures covering several accounts, and opens a new account properly disclosed by the already received combination disclosures, if the new account is opened within a reasonable amount of time after receipt of the combination disclosures and if the received disclosures and terms are accurate at the time the new account is opened.

(a)(2) Requests

(a)(2)(i)

1. *Inquiries versus requests.* A response to an oral inquiry (by telephone or in person) about rates and yields or fees does not trigger the duty to provide account disclosures. But, when a member asks for written information about an account (whether by telephone, in person, or by other means), the credit union must provide disclosures unless the account is no longer offered to the public.

2. *General requests.* When members or potential members request disclosures about a type of account (a share draft account, for example), a credit union that offers several variations may provide disclosures for any one of them. No disclosures need be made to nonmembers, though a credit union may provide disclosures to nonmembers within its sole discretion.

3. *Timing for response.* Ten business days is a reasonable time for responding to requests for account information that members do not make in person, including requests made by electronic communication.

4. *Requests by electronic communication.* Posting disclosures on a credit union's website generally does not relieve the credit union's duty to provide disclosures upon request. If the member provides an e-mail address, the credit

union may provide the disclosures electronically, but the credit union must either send the disclosures by e-mail or send a notice to the member's e-mail address pursuant to § 707.10(d)(2)(i) to inform the member where the disclosures are posted.

(a)(2)(ii)(A)(2)

1. *Recent rates.* Credit unions comply with this paragraph if they disclose an interest rate (or dividend rate on a dividend- bearing term share account) and annual percentage yield accurate within the seven calendar days preceding the date they send the disclosures.

(a)(2)(ii)(B)

1. *Term.* Describing the maturity of a term share account as "1 year" or "6 months," for example, illustrates a response stating the maturity of a term share account as a term rather than a date (e.g., "June 1, 1995").

(b) Content of account disclosures

(b)(1) Rate information

(b)(1)(i) Annual percentage yield and dividend rate

1. *Rate disclosures.* In addition to the dividend rate and annual percentage yield, credit unions may disclose a periodic rate corresponding to the dividend rate. No other rate or yield (such as "tax effective yield") is permitted. If the annual percentage yield is the same as the dividend rate, credit unions may disclose a single figure but must use both terms.

2. *Fixed-rate accounts.* For fixed-rate term share accounts paying the opening rate until maturity, credit unions may disclose the period of time the dividend rate will be in effect by stating, or cross-referencing, the maturity date. For other fixed-rate accounts, credit unions may use a date (such as "This rate will be in effect through June 30, 1995") or a period (such as "This rate will be in effect for at least 30 days").

3. *Tiered-rate accounts.* Each dividend rate, along with the corresponding annual percentage yield for each specified balance level (or range of annual percentage yields, if appropriate), must be disclosed for tiered-rate accounts. (See Appendix A, Part I, Paragraph D.)

4. *Stepped-rate accounts.* A single composite annual percentage yield must be disclosed for stepped-rate accounts. (See Appendix A, Part I, Paragraph B.) The dividend rates and the period of time each will be in effect also must be provided. When the initial rate offered for a specified time on a variable-rate account is higher or lower than the rate that would otherwise be paid on the account, the calculation of the annual percentage yield must be made as if for a stepped-rate account. (See Appendix A, Part I, Paragraph C.)

5. *Minimum balance accounts.* If a credit union sets a minimum balance to earn dividends, the credit union may, but need not, state that the annual percentage yield is 0% for those days the balance in the account drops below the minimum balance level when using the daily balance method. Nor is a disclosure of 0% required for credit unions using the average daily balance method, if the member fails to meet the minimum balance required for the average daily balance period.

(b)(1)(ii) Variable rates

(b)(1)(ii)(B)

1. *Determining dividend rates.* To disclose how the dividend rate is determined, credit unions must:

i. Identify the index and specific margin, if the dividend rate is tied to an index.

ii. State that rate changes are within the credit union's discretion, if the credit union does not tie changes to an index.

(b)(1)(ii)(C).

1. *Frequency of rate changes.* A credit union reserving the right to change rates at its discretion must state the fact that rates may change at any time.

(b)(1)(ii)(D)

1. *Limitations.* A floor or ceiling on rates or on the amount the rate may decrease or increase during any time period must be disclosed. Credit unions need not disclose the absence of limitations on rate changes.

(b)(2) Compounding and crediting

(b)(2)(i) Frequency

1. *General.* Descriptions such as "quarterly" or "monthly" are sufficient. Irregular crediting and compounding periods, such as if a cycle is cut short at year end for tax reporting purposes, need not be disclosed.

2. *Dividend period.* For dividend-bearing accounts, the dividend period must be disclosed. (A specific example must also begiven, see Appendix B, B-1(c).) The dividend period for term share accounts generally may be disclosed as the account's term (e.g., two years).

(b)(2)(ii) Effect of closing an account

1. *Deeming an account closed.* A credit union may, subject to state or other law, provide in account contracts the actions by members that will be treated as closing the account and that will result in the forfeiture of accrued but uncredited dividends. An example is the with-

drawal of all funds from the account prior to the date dividends are credited. Credit unions are cautioned that bylaw requirements may prevent a credit union from deeming a member's account closed until certain time periods are extinguished if funds remain in a member's account. *NCUA Standard FCU Bylaws,* Art. III, section 3 (members have at least six months to replenish membership share before membership terminates and account is deemed closed). Such bylaw requirements may not be overridden without proper agency approval.

(b)(3) Balance information

(b)(3)(i) Minimum balance requirements

1. *Par value.* Credit unions must disclose any minimum balance required to open the account, to avoid the imposition of a fee, or to obtain the annual percentage yield. Since members cannot generally maintain any accounts until the par value of the membership share is paid in full, this section requires that credit unions disclose the par value of a share necessary to become a member and maintain accounts at the credit union. The par value of a share and the minimum balance requirement do not have to be the same amount (e.g., a credit union may have a $5 par value for a membership share, in order for accounts to be opened and maintained, and a $100 minimum balance requirement, in order for the account to earn dividends).

2. *Disclosures.* The explanation of minimum balance computation methods may be combined with the balance computation method disclosures (§ 707.4(b)(3)(ii)) if they are the same. If a credit union uses different cycles for determining minimum balance requirements for purposes of assessing fees and for paying dividends, the credit union must disclose the specific cycle or time period used for each purpose (e.g., use of a midmonth statement cycle for determining dividends, and use of a calendar month cycle for determining fees). Credit unions may assess fees by using any method. If fees on one account are tied to the balance in another account, such provision must be explained (e.g., if share draft fees are tied to a minimum balance in the regular share account (or a combination of the share draft and regular share accounts), the share draft account must explain that fact and how the balance in the regular share account (or both accounts) is determined). The fee need not be disclosed in the account disclosures if the fee is not imposed on that account.

(b)(3)(ii) Balance computation method

1. *Methods and periods.* Credit unions may use different methods or periods to calculate minimum balances for purposes of imposing a fee (the daily balance for a calendar month, for example) and accruing dividends (the average daily balance for a statement period, for example). Each method and corresponding period must be disclosed.

(b)(3)(iii) When dividends begin to accrue

1. *Additional information.* Credit unions must include a statement as to when dividends begin to accrue for non cash deposits. Credit unions may disclose additional information such as the time of day after which deposits are treated as having been received the following business day, and may use additional descriptive terms such as "ledger" or "collected" balances to disclose when dividends begin to accrue. Under the ledger balance method, dividends begin to accrue on the day of deposit. Under the collected balance method, dividends begin to accrue when provisional credit is received for the item deposited.

(b)(4) Fees

1. *Types of fees.* Fees related to the routine use of an account must be disclosed. The following are types of fees that must be disclosed in connection with an account:

i. Maintenance fees, such as monthly service fees.

ii. Fees related to share deposits or withdrawals.

iii. Fees for special services, such as stop payment fees, fees for balance inquiries or verification of shares and deposits, fees associated with checks returned unpaid, fees for regularly sending to members share drafts that otherwise would be held by the credit union, and overdraft line of credit access fees (if charged against the share account).

iv. Fees to open or to close an account.

v. Fees imposed upon dormant or inactive accounts.

2. *Other fees.* Credit unions need not disclose fees such as the following:

i. Fees for services offered to members and nonmembers alike, such as fees for certain travelers checks, for wire transfers and automated clearinghouse (ACH) transfers, to process credit card cash advances, or to handle U.S. Savings Bond redemption (even if different amounts are charged to members and nonmembers).

ii. Incidental fees, such as fees associated with state escheat laws, garnishment or attor-

neys fees, to change names on an account, to generate a midcycle periodic statement, to wrap loose coins, for photocopying for statements returned to the credit union because of a wrong address, and locator fees.

3. *Amount of fees.* Credit unions are cautioned that merely providing fee information in an account disclosure may not be sufficient to gain the legal right to impose the fee involved under applicable law. Credit unions must state the amount and conditions under which a fee may be imposed. Naming and describing the fee typically satisfies this requirement. Some examples are:

i. "$4.00 monthly service fee".

ii. "$7.00 and up" or "fee depends on style of checks ordered" for check printing fees.

4. *Tied-accounts.* Credit unions must state if fees that maybe assessed against an account are tied to other accounts at the credit union. For example, if a credit union ties the fees payable on a share draft account to balances held in the share draft account and in a regular share account, the share draft account disclosures must state that fact and explain how the fee is determined.

5. *Regulation E statements.* Some fees are required to be disclosed under both Regulation E (12 CFR § 205.7) and part 707. If such fees, such as ATM transaction fees, are disclosed on a Regulation E statement, they need not be disclosed again on a periodic statement required under part 707.

(b)(5) Transaction limitations

1. *General rule.* Examples of limitations on the number or dollar amount of share deposits or withdrawals that credit unions must disclose are:

i. Limits on the number of share drafts or checks that may be written on an account for a given time period.

ii. Limits on withdrawals or share deposits during the term of a term share account.

iii. Limitations required by Regulation D, such as the number of withdrawals permitted from money market share accounts by check to third parties each month (credit unions need not disclose reservation of right to require a notice for withdrawals from accounts required by federal or state law).

(b)(6) Features of term share accounts

(b)(6)(i) Time requirements

1. *"Callable"* term share accounts. In addition to the maturity date, credit unions must state the date or the circumstances under which the credit union may redeem a term share account at the credit union's option (a "callable" term share account).

(b)(6)(ii) Early withdrawal penalties

1. *General.* The term "penalty" may, but need not, be used to describe the loss that may be incurred by members for early withdrawal of funds from term share accounts.

2. *Examples.* Examples of early withdrawal penalties are:

i. Monetary penalties, such as a specific dollar amount (e.g., "$10.00") or a specific days' worth of dividends (e.g., "seven days' dividends plus accrued but uncredited dividends, but only if the account is closed").

ii. Adverse changes to terms such as the lowering of the dividend rate, annual percentage yield, or reducing the compounding or crediting frequency for funds remaining in shares or on deposit.

iii. Reclamation of bonuses

3. *Relation to rules for IRAs or similar plans.* Penalties imposed by the Internal Revenue Code for certain withdrawals from IRAs or similar pension or savings plans are not early withdrawal penalties for purposes of this regulation.

4. *Disclosing penalties.* Penalties may be stated in months, whether credit unions assess the penalty using the actual number of days during the period or using another method such as a number of days that occurs in any actual sequence of the total calendar months involved. For example, stating "one month's dividends" is permissible, whether the credit union assesses 30 days' dividends during the month of April, or selects a time period between 28 and 31 days for calculating the dividends for all early withdrawals regardless of when the penalty is assessed.

(b)(6)(iv) Renewal policies

1. *Rollover term share accounts.* Credit unions are not required to provide a grace period, to pay dividends during the grace period, or to disclose whether or not dividends will be paid during the grace period. Credit unions offering a grace period on term share accounts must give the length of the grace period. Commentary, Appendix B, Model Clauses, B-1(i)(iv).

2. *Non rollover term share accounts.* Credit unions that pay dividends on funds following the maturity of term share accounts that do not renew automatically need not state the rate (or annual percentage yield) that may be paid.

(b)(7) Bonuses

1. *General.* Credit unions are required to state the amount and type of bonus, and disclose any minimum balance or time requirement to obtain the bonus and when the bonus will be provided. If the minimum balance or time requirement is otherwise required to be disclosed, credit unions need not duplicate the disclosure for purposes of this paragraph.

(b)(8) Nature of dividends

1. *General.* Dividends are not payable until declared and unless sufficient current and undivided earnings are available after required transfers to reserves at the close of a dividend period. A disclosure explaining dividends educates members and protects credit unions in the event that a prospective dividend cannot be paid, or is not properly payable. This disclosure is required for all dividend-bearing share accounts. Term share accounts need not include a statement regarding the nature of dividends.

2. *State-chartered credit unions with interest-bearing deposit accounts.* State law controls the nature of accounts (i.e., whether an account is a share account or a deposit account). If a member of a state-chartered credit union is opening only an interest-bearing deposit account, or is requesting account disclosures only for an interest-bearing deposit account (if state law requires the deposit or to hold a share account), the disclosures must generally include the following information on any dividend-bearing share portion of the account (e.g., membership share): the par value of a share; a statement that the portion of the deposit that represents the par value of the membership share will earn dividends; and that dividends are paid from current income and available earnings after required transfers to reserves. Further additional disclosures, such as a separate dividend rate and annual percentage yield for the membership share, are not required (if the additional disclosures would agree with the remainder of the account which is invested in an interest-bearing deposit).

(c) Notice to existing accountholders

1. *General.* Only members who receive periodic statements (provided regularly at least four times per year) and who hold accounts of the type offered by the credit union as of the compliance date of part 707 (generally January 1, 1995) must receive the notice. If following receipt of the notice members request disclosures, credit unions have twenty calendar days from receipt of the request to provide the disclosures. Rate and annual percentage yield information in such disclosures must conform to that required for disclosures upon request. As an alternative to including the notice in or on the periodic statement, the final rule permits credit unions to send the account disclosures themselves, as long as they are sent at the same time as the periodic statement (the disclosures may be mailed either with the periodic statement or separately).

2. *Form of the notice.* The notice may be included on the periodic statement, in a member newsletter, or on a statement stuffer or other insert, if it is clear and conspicuous. The notice cannot be sent in a separate mailing from the periodic statement.

3. *Timing.* The notice may accompany the first periodic statement after the compliance date for part 707, or the periodic statement for the first cycle beginning after that date. For example, a credit union's statement cycle is December 15, 1994—January 14, 1995. The statement is mailed on January 15. The next cycle is January 15, 1995 through February 14, 1995, and the statement for that cycle is mailed on February 15. The credit union may provide the notice either on or with the January 15 statement or on or with the February 15 statement, as it covers the first cycle after January 1, 1995.

4. *Early compliance.* Credit unions that provide the notice to existing members prior to the compliance date of part 707, must be prepared to provide accurate and timely disclosures when, following receipt of the notice, members ask for account disclosures. Such disclosures must be provided even if they are requested before the compliance date of part 707. Credit unions who provide early notice to existing members need to comply with other aspects of part 707, but need not provide disclosures already provided in compliance with part 707.

§ 707.5—Subsequent disclosures.

(a) Change in terms

(a)(1) Advance notice required

1. *Form of notice.* Credit unions may provide a change-in-term notice on or with a regular periodic statement or in another mailing (such as a highlighted portion of a newsletter or statement stuffer insert). If a credit union provides notice through revised account disclosures, the changed term must be highlighted in some manner. For example, credit unions may state that a particular fee has been changed (also

specifying the new amount) or use an accompanying letter that refers to the changed term. Credit unions are cautioned that unless credit unions have reserved the right to change terms in the account agreement or disclosures, a change-in-terms notice may not be sufficient to amend the terms under applicable law.

2. *Effective date.* An example of language for disclosing the effective date of a change is: "As of May 11, 1995."

3. *Terms that change upon the occurrence of an event.* A credit union offering terms that will automatically change upon the occurrence of a stated event need not send an advance notice of the change provided the credit union fully describes the conditions of the change in the account opening disclosures (and sends any change-in-term notices regardless of whether the changed term affects that member's account at that time).

4. *Examples.* Examples of changes not requiring an advance change-in-terms notice are:

i. The termination of employment for employee-members for whom account maintenance or activity fees were waived during their employment by the credit union.

ii. The expiration of one year in a promotion described in the account opening disclosures to "waive $4.00 monthly service charges for one year".

(a)(2) No notice required

(a)(2)(ii) Check printing fees

1. *Increase in fees.* A notice is not required for an increase in fees for printing share drafts (or deposit and withdrawal slips) even if the credit union adds some amount to the price charged by the vendor.

(b) Notice before maturity for term share accounts longer than one month that renew automatically

1. *Maturity dates on non business days.* In determining the term of a term share account, credit unions may disregard the fact that the term will be extended beyond the disclosed number of days if the maturity date falls on a nonbusiness day. For example, a holiday or weekend may cause a "one-year" term share account to extend beyond 365 days (or 366, in a leap year), or a "one-month" term share account to extend beyond 31 days.

2. *Disclosing when rates will be determined.* Ways to disclose when the annual percentage yield will be available include the use of:

i. A specific date, such as "October 28".

ii. A date that is easily discernible, such as "the Tuesday prior to the maturity date stated on the notice" or "as of the maturity date stated on this notice".

3. *Alternative timing rule.* Under the alternative timing rule, a credit union that offers a 10-day grace period would have to provide the disclosures at least 10 calendar days prior to the scheduled maturity date.

4. *Club accounts.* If members have agreed to the transfer of payments from another account to a club term share account for the next club period, the credit union must comply with the requirements for automatically renewable term share accounts—even though members may withdraw funds from the club account at the end of the current club period.

5. *Renewal of a term share account.* In the case of a change-in- terms that becomes effective if a rollover term share account is subsequently renewed:

i. If the change is initiated by the credit union, the disclosure requirements of this paragraph apply. (Paragraph 707.5(a) applies if the change becomes effective prior to the maturity of the existing term share account.)

ii. If the change is initiated by the member, the account opening disclosure requirements of § 707.4(b) apply. (If the notice required by this paragraph has been provided, credit unions may give new account disclosures or disclosures that reflect the new term.)

6. *Example.* If a member receives a notice prior to maturity on a one-year term share account and requests a rollover to a six-month account, the credit union must provide either account opening disclosures including the new maturity date or, if all other terms previously disclosed in the prematurity notice remain the same, only the new maturity date.

(b)(1) Maturities of longer than one year

1. *Highlighting changed terms.* Credit unions need not highlight terms that have changed since the last account disclosures were provided.

(c) Notice before maturity for term share accounts longer than one year that do not renew automatically

1. *Subsequent account.* When funds are transferred following maturity of a non rollover term share account, credit unions need not provide account disclosures unless a new account is established.

§ 707.6—Periodic statement disclosures.

(a) Rule When Statement and Crediting Periods Vary

1. *General.* Credit unions are not required to provide periodic statements. If they provide periodic statements, disclosures need only be furnished to the extent applicable. For example, if no dividends are earned for a statement period, credit unions need not state that fact. Or, credit unions may disclose "$0" dividends earned and "0%" annual percentage yield earned.

2. *Regulation E interim statements.* When a credit union provides regular quarterly statements, and in addition provides a monthly interim statement to comply with Regulation E, the interim statement need not comply with this section unless it states dividend or rate information. (See 12 CFR § 205.9.) For credit unions that choose not to treat Regulation E activity statements as part 707 periodic statements, the quarterly periodic statement must reflect the annual percentage yield earned and dividends earned for the full quarter. However, credit unions choosing this option need not redisclose fees already disclosed on an interim Regulation E activity statement on the quarterly periodic statement. For credit unions that choose to treat Regulation E activity statements as part 707 periodic statements, the Regulation E statement must meet all part 707 requirements.

3. *Combined statements.* Credit unions may provide certain information about an account (such as a money market share account or regular share account) on the periodic statement for another account (such as a share draft account) without triggering the disclosures required by this section, as long as:

i. The information is limited to information such as the account number, the type of account, balance information, accountholders' names, and social security or tax identification number; and.

ii. The credit union also provides members a periodic statement complying with this section for the account (the money market share account or regular share account, in the example).

4. *Other information.* Additional information that may be given on or with a periodic statement, includes:

i. Dividend rates and corresponding periodic rates to the dividend rate applied to balances during the statement period.

ii. The dollar amount of dividends earned year-to-date.

iii. Bonuses paid (or any de minim is consideration of $10 or less).

iv. Fees for other products, such as safe deposit boxes.

v. Accounts not covered by the periodic statement disclosure requirements (passbook and term share accounts) may disclose any information on the statement related to such accounts, so long as such information is accurate and not misleading.

5. *When statement and crediting periods vary.* This rule permits credit unions, on dividend-bearing share accounts, to report the annual percentage yield earned and the amount of dividends earned on a statement other than on each periodic statement when the dividend period does not agree with, varies from, or is different than, the statement period. For dividend- bearing share accounts, credit unions may disclose the required information either upon each periodic statement, or on the statement on which dividends are actually earned (credited or posted) to the member's account. In addition, for accounts using the average daily balance method of calculating dividends, when the average daily balance period and the statement periods do not agree, vary or are different, credit unions may also report annual percentage yield earned and the dollar amount of dividends earned on the periodic statement on which the dividends or interest is earned. For example, if a credit union has quarterly dividend periods, or uses a quarterly average daily balance on an account, the first two monthly statements may not state annual percentage yield earned and dividends earned figures; the third "monthly" statement will reflect the dividends earned and the annual percentage yield earned for the entire quarter. The fees imposed disclosure must be given on the periodic statement on which they are imposed.

6. *Length of the period.* Credit unions must disclose the length of both the dividend period (or average daily balance calculation period) and the statement period. For example, a statement could disclose a statement period of April 16 through May 15 and further state that "the dividends earned and the annual percentage yield earned are based on your dividend period (or average daily balance) for the period April 1 through April 30."

7. *Dividend period more frequent than statement period.* Credit unions that calculate dividends on a monthly basis, but send statements on a quarterly basis, may disclose a single divi-

dend (and annual percentage yield earned) figure. Alternatively, a credit union may disclose three dividends earned and three annual percentage yield earned figures, one for each month in the quarter, as long as the credit union states the number of days (or beginning and ending date) in each dividend period if it varies from the statement period.

8. *Additional voluntary disclosures.* For credit unions not disclosing the annual percentage yield earned and dividends earned on all periodic statements, credit unions may place a notice on statements without dividends and annual percentage yield earned figures, that the annual percentage yield earned and dollar amount of dividends earned will appear on the first statement at the close of the dividend (or average daily balance) period, or similar wording. Credit unions may also choose to include a telephone number to call for interim information, if desired by a member.

(b) Statement Disclosures

(b)(1) Annual percentage yield earned

1. *Ledger and collected balances.* Credit unions that accrue interest using the collected balance method may use either the ledger or collected balance methods to determine the balance used to determine the annual percentage yield earned. Ledger balance means the record of the balance in a member's account, as per the credit union's records. (The ledger balance may reflect additions and deposits for which the credit union has not yet received final payment). Collected balance means the record of balance in a member's account reflecting collected funds, that is, cash or checks deposited in the credit union which have been presented for payment and for which payment has actually been received. (See Regulation CC, 12 CFR § 229.14).

(b)(2) Amount of dividends or interest

1. *Definition of earned.* The term "earned" is defined to include dividends and interest either "accrued" or "paid and credited." Credit unions may use either the "ledger" or the "collected" balance for either option. (See 707.6(b)(1)1 and 707.7(c)(2) of the Appendix.)

2. *Accrued interest.* Credit unions must state the amount of interest that accrued during the statement period, even if it was not credited.

3. *Terminology.* In disclosing dividends earned for the period, credit unions must use the term "dividends" or terminology such as:

"Dividends paid," to describe dividends that have been credited;

"Dividends accrued," to indicate that dividends are not yet credited.

4. *Closed accounts.* If a member closes an account between crediting periods and forfeits accrued dividends, the credit union may not show any figures for "dividends earned" or annual percentage yield earned for the period (other than zero, at the credit union's option).

5. *Extraordinary dividends.* Extraordinary dividends are not a component of the annual percentage yield earned or the dividend rate, but are an addition to the member's account. The dollar amount of the extraordinary dividends paid, denoted as a separate, identified figure, must be disclosed on the periodic statement on which the extraordinary dividends are earned. A credit union may also disclose information regarding the calculation of the extraordinary dividends, and additional annual percentage yield earned and dividend rate figures taking into account the extraordinary dividend, so long as such information is accurate and not misleading.

(b)(3) Fees imposed

1. *General.* Periodic statements must state fees disclosed under 707.4(b) that were debited to the account during the statement period, even if assessed for an earlier period.

2. *Itemizing fees by type.* In itemizing fees imposed more than once in the period, credit unions may group fees if they are the same type. But, the description must make clear that the dollar figure represents more than a single fee, for example, "total fees for checks written this period." Examples of fees that may not be grouped together are:

i. Monthly maintenance with excess activity fees.

ii. "Transfer" fees, if different dollar amounts are imposed—such as $.50 for share deposits and $1.00 for withdrawals.

iii. Fees for electronic fund transfers with fees for other services, such as balance inquiry or maintenance fees.

3. *Identifying fees.* Statement details must enable the member to identify the specific fee. For example:

i. Credit unions may use a code to identify a particular fee if the code is explained on the periodic statement or in documents accompanying the statement.

ii. Credit unions using debit slips may disclose the date the fee was debited on the periodic statement and show the amount and type of fee on the dated debit slip.

4. *Relation to Regulation E.* Disclosure of fees in compliance with Regulation E complies with this section for fees related to electronic fund transfers (for example, totaling all electronic funds transfer fees in a single figure).

(b)(4) Length of period

1. *General.* Credit unions providing the beginning and ending dates of the period must make clear whether both dates are included in the period. For example, stating "April 1 through April 30" would clearly indicate that both April 1 and April 30 are included in the period.

2. *Opening or closing an account mid-cycle.* If an account is opened or closed during the period for which a statement is sent, credit unions must calculate the annual percentage yield earned based on account balances for each day the account was open.

§ 707.7—Payment of dividends.

(a) Permissible methods

1. *Prohibited calculation methods.* Calculation methods thatdo not comply with the requirement to pay dividends on the full amount of principal in the account each day include:

i. The "rollback" method, also known as the "grace period" or "in by the 10th" method, where credit unions pay dividends on the lowest balance in the account for the period.

ii. The "increments of par value" method, where credit unions only pay dividends on full shares in an account, e.g., a credit union with $5 par value shares pays dividends on $20 of a $24 account balance.

iii. The "ending balance" method, where credit unions pay dividends on the balance in the account at the end of the period.

iv. The "investable balance" method, where credit unions pay dividends on a percentage of the balance, excluding an amount credit unions set aside for reserve requirements.

v. The "low balance" method, where credit unions pay dividends on the lowest balance in the account for any day in that period.

2. *Use of 365-day basis.* Credit unions may apply a daily periodic rate that is greater than 1/365 of the dividend rate—such as 1/360 of the dividend rate—as long as it is applied 365 days a year.

3. *Periodic dividend payments.* A credit union can pay dividends each day on the account and still make uniform dividend payments. For example, for a one-year term share account, a credit union could make monthly dividend payments that are equal to 1/12 of the amount of dividends that will be earned for a 365-day period (or 11 uniform monthly payments—each equal to roughly 1/12 of the total amount of dividends—and one payment that accounts for the remainder of the total amount of dividends earned for the period).

4. *Leap year.* Credit unions may apply a daily rate of 1/366 or 1/365 of the dividend rate for 366 days in a leap year, if the account will earn dividends for February 29.

5. *Maturity of term share accounts.* Credit unions are not required to pay dividends after term share accounts mature. Examples include:

i. During any grace period offered by a credit union for an automatically renewable term share account, if the member decides during that period not to renew the account.

ii. Following the maturity of non rollover term share accounts.

iii. When the maturity date falls on a holiday, and the member must wait until the next business day to obtain the funds.

6. *Dormant accounts.* Credit unions must pay dividends on funds in an account, even if inactivity or the infrequency of transactions would permit the credit union to consider the account to be "inactive" or "dormant" (or similar status) as defined by state or other law or the account contract.

7. *Insufficient funds.* Credit unions are not required to pay dividends on checks or share drafts deposited to a member's account that are returned for insufficient funds. If a credit union accrues dividends on a check that it later determines is not good, it may deduct from the accrued dividends any dividends attributed to the proceeds of the returned check. If dividends have already been credited before the credit union determines the item has insufficient funds, the credit union may deduct the amount of the check and associated dividends from the account balance. The amount deducted will not be reflected in the dividend amount and annual percentage yield earned reported for the next period.

8. *Account drawn below par value of a share.* If a member draws his or her account below the par value of a share, dividends would continue to accrue on the account so long as any minimum balance requirement is met. However, under the NCUA Standard FCU Bylaws, if a member who reduces his or her share balance below the value of a par value share and does

not increase the balance within at least six months, the credit union may terminate the member's membership. State-chartered credit unions may have similar termination provisions.

(a)(2) Determination of minimum balance to earn dividends

1. *General.* Credit unions may set minimum balance requirements that must be met in order to earn dividends. However, credit unions must use the same method to determine a minimum balance required to earn dividends as they use to determine the balance upon which dividends will accrue and pay. For example, a credit union that calculates dividends on the daily balance method must use the daily balance method to determine if the minimum balance to earn dividends has been met. Similarly, a credit union that calculates dividends on the average daily balance method must use the average daily balance method to determine if the minimum to earn dividends has been met. Credit unions may have a par value of a share that is different from the minimum balance requirement to earn dividends. (See commentary to § 707.4(b)(3)(i)).

2. *Daily balance accounts.* Credit unions that require a minimum balance to earn dividends may choose not to pay dividends for days when the balance drops below the required minimum balance if they use the daily balance method to calculate dividends. For example, a credit union could set a minimum daily balance level of $200 and pay dividends only those days the $200 daily balance is maintained.

3. *Average daily balance accounts.* Credit unions that require a minimum balance to earn dividends may choose not to pay dividends for the average daily balance calculation period in which the average daily balance drops below the required minimum, if they use the average daily balance method to calculate dividends. For example, a credit union could set a minimum average daily balance level of $200 and pay dividends only if the $200 average daily balance is met for the calculation period.

4. *Beneficial method.* Credit unions may not require members to maintain both a minimum daily balance and a minimum average daily balance to earn dividends, such as by requiring the member to maintain a $500 daily balance and a prescribed average daily balance (whether higher or lower). But a credit union could offer a minimum balance to earn dividends that includes an additional method that is "unequivocally beneficial" to the member such as the following:

i. A credit union using the daily balance method to calculate dividends and requiring a $500 minimum daily balance could choose to pay dividends on the account (for those days the minimum balance is not met) as long as the member maintained an average daily balance throughout the month of $400.

ii. A credit union using the average daily balance method to calculate dividends and requiring a $400 minimum average daily balance could choose to pay dividends on the account as long as the member maintained a daily balance of $500 for at least half of the days in the period.

iii. A credit union using either the daily balance method or average daily balance method to calculate dividends that requires: (A) a $500 daily balance; or (B) a $400 average daily balance to pay dividends on the account.

5. *Paying on full balance.* Credit unions must pay dividends on the full balance in the account that meets the required minimum balance. For example, if $300 is the minimum daily balance required to earn dividends, and a member deposits $500, the credit union must pay the stated dividend rate on the full $500 and not just on $200.

6. *Negative balances prohibited.* Credit unions must treat a negative account balance as zero to determine:

i. The daily or average daily balance on which dividends will be paid.

ii. Whether any minimum balance to earn dividends is met (See commentary to Appendix A, Part II, which prohibits credit unions from using negative balances in calculating the dividends figure for the annual percentage yield earned.)

7. *Club accounts.* Credit unions offering club accounts (such as a "holiday" or "vacation" club accounts) cannot impose a minimum balance requirement for dividends based on the total number or dollar amount of payments required under the club plan. For example, if a plan calls for $10 weekly payments for 50 weeks, the credit union cannot set a $500 minimum balance and then pay only if the member makes all 50 payments.

8. *Minimum balances not affecting dividends.* Credit unions may use the daily balance, average daily balance, or other computation method to calculate minimum balance requirements not involving the payment of dividends—such as to compute minimum balances for assessing fees.

(b) Compounding and crediting policies

1. *General.* Credit unions choosing to compound dividends may compound or credit dividends annually, semi-annually, quarterly, monthly, daily, continuously, or on any other basis.

2. *Withdrawals prior to crediting date.* If members withdraw funds (without closing the account), prior to a scheduled crediting date, credit unions may delay paying the accrued dividends on the withdrawn amount until the scheduled crediting date, but may not avoid paying dividends.

3. *Closed accounts.* Subject to state or other law, a credit union may choose not to pay accrued dividends if members close an account prior to the date accrued dividends are credited, as long as the credit union has disclosed that fact. If accrued dividends are paid, accrued dividends must be paid on funds up until the account is closed or the account is deemed closed. For example, if an account is closed on a Tuesday, accrued dividends on the funds through Monday would be paid. Whether (and the conditions under which) credit unions are permitted to deem an account closed by a member is determined by state or other law, if any. Credit unions are cautioned that bylaw requirements may prevent a credit union from deeming a member's account closed until certain time periods are extinguished. (See NCUA Standard FCU Bylaws, Art. III, 3 (members have at least 6 months to replenish membership share before membership can terminate and the account is deemed closed). Such bylaw requirements may not be overridden without proper agency approval.)

(c) Date dividends begin to accrue

1. *Relation to Regulation CC.* Credit unions may rely on the Expedited Funds Availability Act (EFAA) and Regulation CC (12 CFR part 229) to determine, for example, when a deposit is considered made for purposes of dividend accrual, or when dividends need not be paid on funds because a deposited check is later returned unpaid.

2. *Ledger and collected balances.* Credit unions may calculate dividends by using a "ledger" balance or "collected" balance method, as long as the crediting requirements of the EFAA are met (12 CFR § 229.14).

3. *Withdrawal of principal.* Credit unions must accrue dividends on funds until the funds are withdrawn from the account. For example, if a check is debited to an account on a Tuesday, the credit union must accrue dividends on those funds through Monday.

§ 707.8—Advertising.

(a) Misleading or inaccurate advertisements

1. *General.* All advertisements are subject to the rule against misleading or inaccurate advertisements, even though the disclosures applicable to various media differ. The word "profit" may be used when referring to dividend-bearing share accounts, as it reflects the nature of dividends. The word "profit" may not be used when referring to interest-bearing deposit accounts.

2. *Indoor signs.* An indoor sign advertising an annual percentage yield is not misleading or inaccurate if:

i. For a tiered-rate account, it also provides the upper and lower dollar amounts of the tier corresponding to the advertised annual percentage yield.

ii. For a term share account, it also provides the term required to obtain the advertised annual percentage yield.

3. *"Free" or "no cost" accounts.* For purposes of determining whether an account can be advertised as "free" or "no cost," maintenance and activity fees include:

i. Any fee imposed if a minimum balance requirement is not met, or if the member exceeds a specified number of transactions.

ii. Transaction and service fees that members reasonably expect to be imposed on an account on a regular basis (See comments 4(b)(4)-1 and2.)

iii. A flat fee, such as a monthly service fee.

iv. Fees imposed to deposit, withdraw or transfer funds, including per-check or per-transaction charges (for example, $.25 for each withdrawal, whether by check, or in person).

4. *Other fees.* Examples of fees that are not maintenance or activity fees include:

i. Fees that are not required to be disclosed under § 707.4(b)(4).

ii. Check printing fees of any type.

iii. Fees for obtaining copies of checks, whether or not the original checks have been truncated or returned to the member periodically.

iv. Balance inquiry fees.

v. Fees assessed against a dormant account.

vi. Fees for using an ATM.

vii. Fees for electronic transfer services that are not required to obtain an account, such as preauthorized transfers or home electronic credit union services.

viii. Stop payment fees and fees for share drafts or checks returned unpaid.

5. *Similar terms.* An advertisement may not use a term such as "fees waived" if a maintenance or activity fee may be imposed because it is similar to the terms "free" or "no cost."

6. *Specific account services.* Credit unions may advertise a specific account service or feature as free as long as no fee is imposed for that service or feature. For example, credit unions offering an account that is free of deposit or withdrawal fees could advertise that fact, as long as the advertisement does not mislead members by implying that the account is free and that no other fee (a monthly service fee, for example) may be charged.

7. *Free for limited time.* If an account (or a specific account service) is free only for a limited period of time—for example, for one year following the account opening—the account (or service) may be advertised as free as long as the time period is stated.

8. *Conditions not related to share accounts.* Credit unions may advertise accounts as "free" for members that meet conditions not related to share accounts, such as the member's age. For example, credit unions may advertise a share draft account as "free for persons over 65 years old," even though a maintenance or activity fee may be assessed on accounts held by members that are 65 or younger.

9. *Electronic advertising*. If an advertisement using electronic communication displays a triggering term (such as a bonus or annual percentage yield) the advertisement must clearly refer the member to the location where the additional required information begins. For example, an advertisement that includes a bonus or annual percentage yield may be accompanied by a link that directly takes the member to the additional information.

(b) Permissible rates

1. *Tiered-rate accounts.* An advertisement for a tiered-rate account that states an annual percentage yield must also state the annual percentage yield for each tier, along with corresponding minimum balance requirements. Any dividend rates stated must appear in conjunction with the annual percentage yields for each tier.

2. *Stepped-rate accounts.* An advertisement that states a dividend rate for a stepped-rate account must state all the dividend rates and the time period that each rate is in effect.

3. *Representative examples.* An advertisement that states an annual percentage yield for a type of account (such as a term share account for a specified term) need not state the annual percentage yield applicable to every variation offered by the credit union or indicate that other maturity terms are available. In an advertisement stating that rates for an account may vary depending on the amount of the initial deposit or the term of a term share account, credit unions need not list each balance level and term offered. Instead, the advertisement may:

i. Provide a representative example of the annual percentage yields offered, clearly described as such. For example, if a credit union offers a $25 bonus on all term share accounts and the annual percentage yield will vary depending on the term selected, the credit union may provide a disclosure of the annual percentage yield as follows: "For example, our 6-month share certificate currently pays a 3.15% annual percentage yield."

ii. Indicate that various rates are available, such as by stating short-term and longer-term maturities along with the applicable annual percentage yields. "We offer share certificates with annual percentage yields that depend on the maturity you choose. For example, our one-month share certificate earns a 2.75% APY. Or, earn a 5.25% APY for a three-year share certificate."

4. *Electronic communication*. A dividend rate may be stated only if it is provided in conjunction with, but not more conspicuously than, the annual percentage yield to which it relates. In an advertisement using electronic communication, the member must be able to view both rates simultaneously. This requirement is not satisfied if the member can view the annual percentage yield only by use of a link that connects the member to information appearing at another location.

(c) When additional disclosures are required

1. *Trigger terms.* The following are examples of information stated in advertisements that are not "trigger" terms:

i. "One, three, and five year share certificates available".

ii. "Bonus rates available".

iii. "1% over our current rate," so long as the rates are not determinable from the advertisement.

(c)(2) Time annual percentage yield is offered

1. *Specified recent date.* If an advertisement discloses an annual percentage yield as of a specified date, that date must be recent in relation to the publication or broadcast frequency of the media used. For example, the printing date of a brochure printed once for an account promotion that will be in effect for six months would be considered "recent," even though rates change during the six-month period. Dividend rates published in a daily newspaper or on television must be a rate offered shortly before (or on) the date the rates are published or broadcast. Similarly, dividend rates published in a daily newspaper or on television must be a rate reflecting either the preceding dividend period, or a prospective rate, and the option chosen should be noted.

2. *Reference to date of publication.* An advertisement may refer to the annual percentage yield as being accurate as of the date of publication, if the date is on the publication itself. For instance, an advertisement in a periodical may state that a rate is "current through the date of this issue," if the periodical shows the date.

(c)(5) Effect of fees

1. *Scope.* This requirement applies only to maintenance or activity fees as described in paragraph 8(a).

(c)(6) Features of term share accounts

(c)(6)(i) Time requirements

1. *Club accounts.* If a club account has a maturity date, but the term may vary depending on when the account is opened, credit unions may use a phrase such as: "The maturity date of this club account is November 15; its term varies depending on when the account is opened."

(c)(6)(ii) Early withdrawal penalties

1. *Discretionary penalties.* Credit unions imposing early withdrawal penalties on a case-by-case basis may disclose that they "may" (rather than "will") impose a penalty if that accurately describes the account terms.

(d) Bonuses

1. *General reference to "bonus."* General statements such as "bonus checking" or "get a bonus when you open a checking account" do not trigger the bonus disclosures.

(e) Exemption for certain advertisements

(e)(1) Certain media

(e)(1)(i)

1. *ATM messages.* Messages provided on ATM or computer screens are eligible for this exemption.

2. *Internet advertisements*. The exemption for advertisements made through broadcast or electronic media does not extend to advertisements made by electronic communication, such as advertisements posted on the Internet or sent by e-mail.

(e)(1)(iii)

1. *Tiered-rate accounts.* Solicitations for tiered-rate accounts made through telephone response machines must provide all annual percentage yields and the balance requirements applicable to each tier.

(e)(2) Indoor signs

(e)(2)(i)

1. *General.* Indoor signs include advertisements displayed on computer screens, banners, preprinted posters, and chalk or peg boards. Any advertisement inside the premises that can be retained by a member (such as a brochure or a printout from a computer) is not an in door sign.

(e)(3) Newsletters

1. *General.* The partial exemption applies to all credit union news letters, whether instituted before or after the compliance date of part 707. Nor must a newsletter be of any particular circulation frequency (e.g., weekly, monthly, quarterly, biannually, annually, or irregularly) or of any certain format (e.g. magazine, bulletin, broadside, circular, mimeograph, letter, or pamphlet) in order to be eligible for the partial advertising exemption.

2. *Permissible Distribution.* In order for news letters to retain the partial advertising exemption, news letters can be sent to existing credit union members only. Any distribution reasonably calculated to reach only members is also acceptable, such as:

i. Mailing newsletters to existing members.

ii. Distributing newsletters at a function reasonably limited to members, such as an annual meeting or member picnic.

iii. Displaying or offering newsletters at a credit union lobby, branch, or office.

3. *Impermissible Distribution.* Distributing a news letter in a place open to nonmembers, such as a sponsor's lunch room, is not reasonably calculated to reach only members, and such newsletter would be subject to all applicable advertising rules.

§ 707.9—Enforcement and record retention.

(c) Record retention

1. *Evidence of required actions.* Credit unions comply with the regulation by demonstrating they have done the following:

i. Established and maintained procedures for paying dividends and providing timely disclosures as required by the regulation, and.

ii. Retained sample disclosures for each type account offered to members, such as account-opening disclosures, copies of advertisements, and change-in-term notices; and information regarding the dividend rates and annual percentage yields offered.

2. *Methods of retaining evidence.* Credit unions must be able to reconstruct the required disclosures or other actions. They need not keep disclosures or other business records in hard copy. Records evidencing compliance may be retained on microfilm, microfiche, or by other methods that reproduce records accurately (including computer files). Credit unions must retain copies of all printed advertisements and the text of all advertisements conveyed by electronic or broadcast media, and newsletters.

3. *Payment of dividends.* Credit unions must retain sufficient rate and balance information to permit the verification of dividends paid on an account, including the payment of dividends on the full principal balance.

§ 707.10—Electronic Communication

(b) General Rule

1. *Relationship to the E-Sign Act*. The E-Sign Act authorizes the use of electronic disclosures. It does not affect any requirement imposed under this part other than a provision that requires disclosures to be in paper form, and it does not affect the content or timing of disclosures. Electronic disclosures are subject to the regulation's format, timing, and retainability rules and the clear and conspicuous standard. For example, to satisfy the clear and conspicuous standard for disclosures, electronic disclosures must use visual text.

2. *Clear and conspicuous standard.* A credit union must provide electronic disclosures using a clear and conspicuous format. Also, in accordance with the E-Sign Act:

i. The credit union must disclose the requirements for accessing and retaining disclosures in that format;

ii. The member must demonstrate the ability to access the information electronically and affirmatively consent to electronic delivery; and

iii. The credit union must provide the disclosures in accordance with the specified requirements.

3. *Timing and effective delivery*.

i. *When a member opens an account on-line*. When a member opens an account on-line, the member must be required to access the disclosures required under § 707.4 before the account is opened or a service is provided, whichever is earlier. A link to the disclosures satisfies the timing rule if the member cannot bypass the disclosures before opening the account. Or the disclosures in this example must automatically appear on the screen, even if multiple screens are required to view the entire disclosure. The credit union is not required to confirm that the member has read the disclosure.

ii. *For disclosures provided periodically*. Disclosures provided by mail are timely based on when the disclosures are sent. Disclosures posted at an Internet web site, such as periodic statements or change-in-terms and other notices, are timely when the credit union has both made the disclosures available and sent a notice alerting the member that the disclosures have been posted. For example, under § 707.5, credit unions must give advance notice to affected members at least 30 calendar days in advance of certain changes. For a change in terms notice posted on the Internet, a credit union must both post the notice and notify members of its availability at least 30 days in advance of the change.

4. *Retainability of disclosures*. Credit unions satisfy the requirement that disclosures be in a form that the member may keep if electronic disclosures are delivered in a format that is capable of being retained (such as by printing or storing electronically). The format must also be consistent with the information required to be provided under Section 101(c)(1)(C)(i) of the E-Sign Act, 15 U.S.C.7001(c)(1)(C)(i)), about the hardware and software requirements for accessing and retaining electronic disclosures.

5. *Disclosures provided on credit union's equipment*. A credit union that controls the equipment providing electronic disclosures to members (for example, a computer terminal located in a credit union's lobby or at a public kiosk) must ensure that the equipment satisfies the regulation's requirements to provide timely disclosures in a clear and conspicuous format and in a form that the member may keep. For

example, if disclosures are required at the time of an on-line transaction, the disclosures must be sent to the member's e-mail address or must be posted at another location such as the credit union's Internet web site, unless the credit union provides a printer that automatically prints the disclosures.

(d) Address Or Location To Receive Electronic Communication

(d)(1)

1. *Electronic address*. A member's electronic address is an e-mail address that is not limited to receiving communications transmitted solely by the credit union.

(d)(2)

1. *Identifying account involved*. A credit union may identify a specific account in a variety of ways and is not required to identify an account by reference to the account number. For example, where the member has only one share account, and no confusion would result, the credit union may refer to "your share account." If the member has two accounts, the credit union may, for example, differentiate accounts by using terms such as "primary account" and "secondary account" or by using a truncated account number.

2. *90-day rule*. The actual disclosures provided to a member must be available for at least 90 days, but the credit union has discretion to determine whether they should be available at the same location for the entire period.

(e) Redelivery

1. *E-mail returned as undeliverable*. If an e-mail to the member (containing an alert notice or other disclosure) is returned as undeliverable, the redelivery requirement is satisfied if, for example, the credit union sends the disclosure to a different e-mail address or postal address that the credit union has on file for the member. Sending the disclosures a second time to the same electronic address is not sufficient if the credit union has a different address for the member on file.

Appendix A to Appendix C of Part 707—Annual Percentage Yield Calculation

Part I. Annual percentage yield for account disclosures and advertising purposes.

1. *Rounding for calculations.* The following are examples of permissible rounding rules for calculating dividends and the annual percentage yield:

i. The daily rate applied to a balance carried to five or more decimals. For example: .008219178%, 3.00% for a 365 day year, would be rounded to no less than .00822%.

ii. The daily dividends or interest earned carried to five or more decimals. For example; $.08219178082, daily dividends on $1,000 at 3%for a 365 day year, would be rounded to no less than $.08219.

2. *Exponents in a leap year.* The annual percentage yield formula's exponent numerator will remain 365 in leap years. The "days in term" figure used in the denominator should be consistent with the length of term used in the dividends calculation.

3. *First tier of a tiered-rate account.* When credit unions use a rate table, the first tier of a tiered rate account is to be disclosed and advertised: "Up to but not exceeding . . .", "$.01 to. . .", or similar language.

4. *Term share accounts opened in midterm.* For club accounts that meet the definition of a term share account, the annual percentage yield is based on the maximum number of days in the term not to exceed 365 days (or 366 days in a leap year).

Part II. Annual percentage yield earned for periodic statements.

1. *Balance method.* The dividend or interest figure used in the calculation of the annual percentage yield earned may be derived from the daily balance method or the average daily balance method. Regardless of the dividend calculation method, the balance used in the annual percentage yield earned formula is the average daily balance. The average daily balance calculation is the sum of the balances for each day in the period divided by the number of days in the period. The balance for each day is based on a point in time; i.e. beginning of day balance, end of day balance, closing of day balance, etc. Each day's balance, for dividend accrual and payment purposes, must be based on the same point in time and cannot be based on the day's low balance.

2. *Negative balances prohibited.* Credit unions must treat a negative account balance as

zero to determine the balance on which the annual percentage yield earned is calculated. (See commentary to § 707.7(a)(2).)

A. General formula.

1. *Accrued but uncredited dividends.* To calculate the annual percentage yield earned, accrued but uncredited dividends:

i. May not be included in the balance for statements that are issued at the same time or less frequently than the account's compounding and crediting frequency. For example, if monthly statements are sent for an account that compounds dividends daily and credits dividends monthly, the balance may not be increased each day to reflect the effect of daily compounding. Assume a credit union will pay $13.70 in dividends on $100,000 for the first day, $6.85 individends on $50,013.70 for the second day, and $3.43 in dividends on $25,020.55 for the third day. The sum of each day's balance is $175,000 (does not include accrued, but uncredited, dividends amounts $13.70, $6.85, and $3.43), thereby resulting in an average daily balance for the three days of $58,333.33.

ii. Must be included in the balance for succeeding statements if a statement is issued more frequently than compounded dividends are credited on an account. For example, if monthly statements are sent for an account that compounds dividends daily and credits dividends quarterly, the balance for the second monthly statement would include dividends that had accrued for the prior month. Assume a credit union will pay $411.78 in dividends on 30 days of $100,000, $427.28 in dividends on 31 days of $100,411.78, and $415.23 in dividends on 30 days of $100,839.06. The balance (average daily balance in the account for the period) for the second 31 days is $100,411.78.

2. *Rounding.* The dividends earned figure used to calculate the annual percentage yield earned must be rounded to two decimals to reflect the amount actually paid. For example, if the dividends earned for a statement period is $20.074 and the credit union pays the member $20.07, the credit union must use $20.07 (not $20.074) to calculate the annual percentage yield earned. For accounts that pay dividends based on the daily balance method, compound and credit dividends or interest quarterly, and send monthly statements, the credit union may, but need not, round accrued dividends to two decimals for calculating the "projected" or "anticipated" annual percentage yield earned on the first two monthly statements issued during the quarter. However, on the quarterly statement the dividends earned figure must reflect the amount actually paid.

3. *Compounding frequency using the average daily balance method.* Any compounding frequency, including daily compounding, can be used when calculating dividends using the average daily balance method. (See comment § 707.7(b), which does not require credit unions to compound or credit dividends at any particular frequency).

B. Special formula for use where periodic statement is sent more often than the period for which dividends are compounded.

1. *Statements triggered by Regulation E.* Credit unions may, but need not, use this formula to calculate the annual percentage yield earned for accounts that receive quarterly statements and that are subject to Regulation E's rule calling for monthly statements when an electronic fund transfer has occurred. They may do so even though no monthly statement was issued during a specific quarter. This formula must be used for accounts that compound and credit dividends quarterly and that receive monthly statements, triggered by Regulation E, which comply with the provisions of § 707.6.

2. *Days in compounding period.* Credit unions using the special annual percentage yield earned formula must use the actual number of days in the compounding period.

Appendix B to Appendix C of Part 707—Model Clauses and Sample Forms

1. *Modifications.* Credit unions that modify the model clauses will be deemed in compliance as long as they do not delete information required by TISA or regulation or rearrange the format so as to affect the substance or clarity of the disclosures.

2. *Format.* Credit unions may use inserts to a document (see Sample Form B–11) or fill-in blanks (see Sample Forms B–4 andB–5, which

use double underlining to indicate terms that have been filled in) to show current rates, fees or other terms.3. Disclosures for opening accounts. The sample forms illustrate the information that must be provided to a member when an account is opened, as required by § 707.4(a)(1). (See § 707.4(a)(2), which states the requirements for disclosing the annual percentage yield, the dividend rate, and the maturity of a term share account in responding to a member's request.)

4. *Compliance with Regulation E.* Credit unions may satisfy certain requirements under Part 707 with disclosures that meet the requirements of Regulation E. (See § 707.3(c).) The model clauses and sample forms do not give examples of disclosures that would be covered by both this regulation and Regulation E (such as disclosing the amount of a fee for ATM usage). Credit unions should consult appendix A to Regulation E for appropriate model clauses.

5. *Duplicate disclosures.* If a requirement such as a minimum balance applies to more than one account term (to obtain a bonus and determine the annual percentage yield, for example), credit unions need not repeat the requirement for each term, as long as it is clear which terms the requirement applies to.

6. *Guide to model clauses.* In the model clauses, italicized words indicate the type of disclosure a credit union should insert in the space provided (for example, a credit union might insert "March 25, 1995" in the blank for "(date)" disclosure). Brackets and diagonals ("/") indicate a credit union must choose the alternative that describes its practice (for example, [daily balance/average daily balance]).

7. *Sample forms.* The sample forms (B–4 through B–11) serve a purpose different from the model clauses. They illustrate various ways of adapting the model clauses to specific accounts. The clauses shown relate only to the specific transactions described.

Part 708a

Conversion of Insured Credit Unions to Mutual Savings Banks

§ 708a.1 Definitions.

As used in this part:

(a) *Credit union* has the same meaning as insured credit union in section 101 of the Federal Credit Union Act.

(b) *Mutual savings bank* and *savings association* have the same meaning as in section 3 of the Federal Deposit Insurance Act.

(c) *Federal banking agencies* have the same meaning as in section 3 of the Federal Deposit Insurance Act.

(d) *Senior management official* means a chief executive officer, an assistant chief executive officer, a chief financial officer, and any other senior executive officer as defined by the appropriate federal banking agency pursuant to section 32(f) of the Federal Deposit Insurance Act, 12 U.S.C. 1831i(f).

§ 708a.2 Authority to convert.

An insured credit union, with the approval of its members, may convert to a mutual savings bank or a savings association that is in mutual form without the prior approval of the NCUA, subject to applicable law governing mutual savings banks and savings associations and the other requirements of this part.

§ 708a.3 Board of directors and membership approval.

(a) The board of directors must approve a proposal to convert by majority vote and set a date for a vote on the proposal by the members of the credit union.

(b) The membership must approve the proposal to convert by the affirmative vote of a majority of those members who vote on such proposal.

§ 708a.4 Voting procedures.

(a) A member may vote on the proposal to convert in person at a special meeting held on the date set for the vote or by written ballot filed by the member. The vote on the conversion proposal must be by secret ballot and conducted by an independent entity. The independent entity must be a company with experience in conducting corporate elections. No official or senior manager of the credit union, or the immediate family members of any official or senior manager, may have any ownership interest in, or be employed by, the entity.

(b) A credit union that proposes to convert must provide written notice of its intent to convert to each member who is eligible to vote on the conversion. The notice to members must be submitted 90 calendar days, 60 calendar days, and 30 calendar days before the date of the membership vote on the conversion and a ballot must be submitted not less than 30 calendar days before the date of the vote.

(c) The notice to members must adequately describe the purpose and subject matter of the vote to be taken at the special meeting or by submission of the written ballot. The notice must clearly inform the member that the member may vote at the special meeting or by submitting the written ballot. The notice must state the date, time, and place of the meeting.

(d)(1) An adequate description of the purpose and subject matter of the member vote on conversion, as required by paragraph (c) of this section, must include:

(i) A disclosure that the conversion from a credit union to a mutual savings bank could lead to members losing their ownership interests in the credit union if the mutual savings bank subsequently converts to a stock institution and the members do not become stockholders;

(ii) A disclosure of how the conversion from a credit union to a mutual savings bank will affect members' voting rights; and

(iii) A disclosure of any conversion related economic benefit a director or senior management official may receive including receipt of or an increase in compensation and an explanation of any foreseeable stock related benefits associated with a subsequent conversion to a stock institution. The explanation of stock related benefits must include a comparison of the

opportunities to acquire stock that are available to officials and employees, with those opportunities available to the general membership.

(d)(2) In connection with the disclosures required by paragraphs (d)(1)(i) through (iii) of this section, the converting credit union must include an affirmative statement, that at the time of conversion to a mutual savings bank, the credit union does or does not intend to:

(i) Convert to a stock institution;

(ii) Provide any compensation to previously uncompensated directors or increase compensation or other conversion related benefits, including stock related benefits, to directors or senior management officials; and

(iii) Base member voting rights on account balances.

(e) A converting credit union must include the following disclosures with each written communication it sends to its members regarding the conversion. The disclosures must be offset from the other text by use of a border and at least one font size larger than any other text (exclusive of headings) used in the communication. Certain portions of the disclosures must be capitalized and bolded. A converting credit union may modify the disclosure with the prior consent of the Regional Director and, in the case of a state credit union, the appropriate state regulatory agency. The unmodified form of disclosure reads as follows:

The National Credit Union Administration, the federal government agency that supervises credit unions, requires [insert name of credit union] to provide the following disclosures.

1. **OWNERSHIP AND CONTROL.** In a credit union, every member has an equal vote in the election of directors and other matters concerning ownership and control. In a mutual savings bank, **ACCOUNT HOLDERS WITH LARGER BALANCES USUALLY HAVE MORE VOTES AND, THUS, GREATER CONTROL.**
2. **EXPENSES AND THEIR EFFECT ON RATES AND SERVICES.** Most credit union directors and committee members serve on a volunteer basis. Directors of a mutual savings bank are compensated. Credit unions are exempt from federal tax and most state taxes. Mutual savings banks pay taxes, including federal income tax. If [insert name of credit union] converts to a mutual savings bank, these **ADDITIONAL EXPENSES MAY CONTRIBUTE TO LOWER SAVINGS RATES, HIGHER LOAN RATES, OR ADDITIONAL FEES FOR SERVICES.**
3. **SUBSEQUENT CONVERSION TO STOCK INSTITUTION.** Conversion to a mutual savings bank is often the first step in a two-step process to convert to a stock-issuing bank or holding company. In a typical conversion to the stock form of ownership, the **EXECUTIVES OF THE INSTITUTION PROFIT BY OBTAINING STOCK FAR IN EXCESS OF THAT AVAILABLE TO THE INSTITUTION'S MEMBERS.**
4. **COSTS OF CONVERSION.** The costs of converting a credit union to a mutual savings bank are paid from the credit union's current and accumulated earnings. Because accumulated earnings are capital and represent members' ownership interests in a credit union, the conversion costs reduce members' ownership interests. As of [insert date], [insert name of credit union] estimates **THE CONVERSION WILL COST [INSERT DOLLAR AMOUNT] IN TOTAL.** That total amount is further broken down as follows: [itemize the costs of all expenses related to the conversion including printing fees, postage fees, advertising, consulting and professional fees, legal fees, staff time, the cost of holding a special meeting, conducting the vote, and any other expenses incurred].

§ 708a.5 Notice to NCUA.

(a) The credit union must provide the Regional Director for the region where the credit union is located with notice of its intent to convert during the 90 calendar day period preceding the date of the membership vote on the conversion.

(b)(1) The credit union must give notice to the Regional Director by providing a letter describing the material features of the conversion or a copy of the filing the credit union has made with another federal or state regulatory agency in which the credit union seeks that agency's approval of the conversion. The credit union must include with the notice to the Regional Director a copy of the notice the credit union provides to members under § 708a.4, as well as, the ballot form and all written materials the credit union has distributed or intends to distribute to the members. The term "written materials" includes written documentation or information of any sort, including electronic communications posted on a Web site.

(b)(2) A federally-insured State chartered credit union must include in its notice to NCUA a statement as to whether the State law under which it is chartered permits it to convert to a mutual savings bank and include a legal citation to the State law providing this authority. A federally-insured State chartered credit union will remain subject to any State law requirements for conversion that are more stringent than those this chapter imposes, including any internal governance requirements, such as the requisite membership vote for conversion and the determination of a member's eligibility to vote. If a federally-insured State chartered credit union relies for its authority to convert to a mutual savings bank on a State law parity provision, meaning a provision in State law permitting a State chartered credit union to operate with the same or similar authority as a federal credit union, it must include in its notice

a statement that its State regulatory authority agrees that it may rely on the State law parity provision as authority to convert. If a federally-insured state chartered credit union relies on a State law parity provision for authority to convert, it must indicate its State regulatory authority's position as to whether Federal law and regulations or State law will control internal governance issues in the conversion such as the requisite membership vote for conversion and the determination of a member's eligibility to vote.

(c) If it chooses, the credit union may provide the Regional Director notice of its intent to convert prior to the 90 calendar day period preceding the date of the membership vote on the conversion. In this case, the Regional Director will make a preliminary determination regarding the methods and procedures applicable to the membership vote. The Regional Director will notify the credit union within 30 calendar days of receipt of the credit union's notice of intent to convert if the Regional Director disapproves of the proposed methods and procedures applicable to the membership vote. The credit union's prior submission of the notice of intent does not relieve the credit union of its obligation to certify the results of the membership vote required by § 708a.6 or eliminate the right of the Regional Director to disapprove the actual methods and procedures applicable to the membership vote if the credit union fails to conduct the membership vote in a fair and legal manner.

§ 708a.6 Certification of vote on conversion proposal.

The board of directors of the converting credit union must certify the results of the membership vote to the Regional Director within 10 calendar days after the vote is taken. The board of directors must also certify at this time that the notice, ballot and other written materials provided to members were identical to those submitted pursuant to § 708a.5 or provide copies of any new or revised materials and an explanation of the reasons for the changes.

§ 708a.7 NCUA oversight of methods and procedures of membership vote.

(a) The Regional Director will issue a determination that the methods and procedures applicable to the membership vote are approved or disapproved within 10 calendar days of receipt from the credit union of the certification of the result of the membership vote required under § 708a.6.

(b) If the Regional Director disapproves of the methods by which the membership vote was taken or the procedures applicable to the membership vote, the Regional Director may direct that a new vote be taken.

(c) The Regional Director's review of the methods by which the membership vote was taken and the procedures applicable to the membership vote includes determining that the notice to members is accurate and not misleading, that all notices required by this section were timely, and that the membership vote was conducted in a fair and legal manner.

§ 708a.8 Other regulatory oversight of methods and procedures of membership vote.

The federal or state regulatory agency that will have jurisdiction over the financial institution after conversion must verify the membership vote and may direct that a new vote be taken, if it disapproves of the methods by which the membership vote was taken or the procedures applicable to the membership vote.

§ 708a.9 Completion of conversion.

(a) Upon receipt of approvals under § 708a.7 and § 708a.8 of this part, the credit union may complete the conversion transaction.

(b) Upon notification by the board of directors of the mutual savings bank or mutual savings association that the conversion transaction has been completed, the NCUA will cancel the insurance certificate of the credit union and, if applicable, the charter of the federal credit union.

§ 708a.10 Limit on compensation of officials.

No director or senior management official of an insured credit union may receive any economic benefit in connection with the conversion of the credit union other than compensation and other benefits paid to directors or senior management officials of the converted institution in the ordinary course of business.

§ 708a.11 Voting guidelines.

(a) A converting credit union must conduct its member vote on conversion in a fair and legal manner. These guidelines are not an exhaustive checklist that guarantees a fair and legal vote but are suggestions that provide a framework to help a credit union fulfill its regulatory obligations.

(b) While NCUA's conversion rule applies to all conversions of federally insured credit unions, federally-insured State chartered credit unions (FISCUs) are also subject to State law on conversions. NCUA's position is that a State legislature or State supervisory authority may impose conversion requirements more stringent or restrictive than NCUA's. States that permit this kind of conversion could have substantive and procedural requirements that vary from Federal law. For example, there could be different voting standards for approving a vote. While NCUA's rule requires a simple majority of those who vote to approve a conversion, some States have higher voting standards requiring two-thirds or more of those who vote. A FISCU should be careful to understand both Federal and State law to navigate the conversion process and conduct a proper vote.

(c)(1) Determining who is eligible to cast a ballot is fundamental to any vote. No conversion vote can be fair and legal if some members are improperly excluded. A converting credit union should be cautious to identify all eligible members and make certain they are included on its voting list. NCUA recommends that a converting credit union establish internal procedures to manage this task.

(2) A converting credit union should be careful to make certain its member list is accurate and complete. For example, when a credit union converts from paper record keeping to computer record keeping, some members' names may not transfer unless the credit union is careful in this regard. This same problem can arise when a credit union converts from one computer system to another where the software is not completely compatible.

(3) Problems with keeping track of who is eligible to vote can also arise when a credit union converts from a federal charter to a State charter or vice versa. NCUA is aware of an instance where a federal credit union used membership materials that allowed two or more individuals to open a joint account and also allowed each to become a member. The federal credit union later converted to a State chartered credit union that, like most other State chartered credit unions in its State, used membership materials that allowed two or more individuals to open a joint account but only allowed the first person listed on the account to become a member. The other individuals did not become members as a result of their joint account. To become members, those individuals were required to open another account where they were the first or only person listed on the account. Over time, some individuals who became members of the federal credit union as the second person listed on a joint account were treated like those individuals who were listed as the second person on a joint account opened directly with the State chartered credit union. Specifically, both of those groups were treated as non-members not entitled to vote. This example makes the point that a credit union must be diligent in maintaining a reliable membership list.

(d) NCUA's conversion rule requires a converting credit union to permit members to vote by written mail ballot or in person at a special meeting held for the purpose of voting on the conversion. Although most members may choose to vote by mail, a significant number may choose to vote in person. As a result, a converting credit union should be careful to conduct its special meeting in a manner conducive to accommodating all members that wish to attend. That includes selecting a meeting location that can accommodate the anticipated number of attendees and is conveniently located. The meeting should also be held on a day and time suitable to most members' schedules. A credit union should conduct its meeting in accordance with applicable federal and State law, its bylaws, Robert's Rules of Order or other appropriate parliamentary procedures, and determine before the meeting the nature and scope of any discussion to be permitted.

Part 708b

Mergers of Federally-Insured Credit Unions; Voluntary Termination or Conversion of Insured Status

§ 708b.1 Scope.

(a) Subpart A of this part prescribes the procedures for merging one or more credit unions with a continuing credit union where at least one of the credit unions is federally-insured.

(b) Subpart B of this part prescribes the procedures and notice requirements for termination of federal insurance or conversion of federal insurance to nonfederal insurance, including termination or conversion resulting from a merger.

(c) Subpart C prescribes required forms for use in conversion of federal insurance to nonfederal insurance.

(d) Nothing in this part restricts or otherwise impairs the authority of the NCUA to approve a merger pursuant to section 205(h) of the Act.

(e) This part does not address procedures or requirements that may be applicable under state law for a state credit union.

§ 708b.2 Definitions.

(a) *Continuing credit union* means the credit union that will continue in operation after the merger.

(b) *Convert, conversion,* and *converting,* when used in connection with insurance, refer to the act of canceling federal insurance and simultaneously obtaining insurance from another insurance carrier. They mean that after cancellation of federal insurance the credit union will be nonfederally-insured.

(c) *Federally-insured* means insured by the National Credit Union Administration (NCUA) through the National Credit Union Share Insurance Fund (NCUSIF).

(d) *Independent entity* means a company with experience in conducting corporate elections. No official or senior manager of the credit union, or the immediate family members of any official or senior manager, may have any ownership interest in, or be employed by, the entity.

(e) *Insurance* and *insured* refer to primary share or deposit insurance. These terms do not include excess share or deposit insurance as referred to in part 740 of this chapter.

(f) *Merging credit union* means the credit union that will cease to exist as an operating credit union at the time of the merger.

(g) *Nonfederally-insured* means insured by a private or cooperative insurance fund or guaranty corporation organized or chartered under state or territorial law.

(h) *Share insurance communication* means any written communication, excluding the forms in Subpart C of this Part, that is made by or on behalf of a federally-insured credit union that is intended to be read by two or more credit union members and that mentions share insurance conversion or termination. The term:

(1) Includes communications delivered or made available before, during, and after the credit union's board of directors decides to seek conversion or termination.

(2) Includes, but is not limited to, communications delivered or made available by mail, e-mail, and internet website posting.

(3) Does not include communications intended to be read only by the credit union's own employees or officials.

(i) *State credit union* means any credit union organized and operated according to the laws of any state, the several territories and possessions of the United States, or the Commonwealth of Puerto Rico. Accordingly, *state authority* means the appropriate state or territorial regulatory or supervisory authority for any such credit union.

(j) *Terminate, termination,* and *terminating,* when used in reference to insurance, refer to the act of canceling federal insurance and mean that the credit union will become uninsured.

(k) *Uninsured* means there is no share or deposit insurance available on the credit union accounts.

Subpart A—Mergers

§ 708b.101 Mergers generally.

(a) In any case where a merger will result in the termination of federal insurance or conversion to nonfederal insurance, the merging credit union must comply with the provisions of subparts B and C of this part in addition to this subpart A.

(b) A federally-insured credit union must have the prior written approval of the NCUA before merging with any other credit union.

(c) Where the continuing credit union is a federal credit union, it must be in compliance with the chartering policies of the NCUA.

(d) Where the continuing or merging credit union is a state credit union, the merger must be permitted by state law or authorized by the state authority.

(e) Where both the merging and continuing credit unions are federally-insured and the two credit unions have overlapping fields of membership, the continuing credit union must, within three months after completion of the merger, either:

(1) Notify all members of the continuing credit union of the potential loss of insurance coverage if they had overlapping membership,

(2) Notify all individuals and entities that were actually members of both credit unions of the potential loss of insurance coverage, or

(3) Determine which members of both credit unions may actually have uninsured funds six months after the merger and notify those members of the potential loss of insurance coverage.

§ 708b.102 Special provisions for federal insurance.

(a) Where the continuing credit union is federally-insured, the NCUSIF will assess a deposit and a prorated insurance premium (unless waived in whole or in part for all insured credit unions during that year) on the additional share accounts insured as a result of the merger of a nonfederally-insured or uninsured credit union with a federally-insured credit union.

(b) Where the continuing credit union is nonfederally-insured or uninsured but desires to be federally-insured as of the date of the merger, it must submit an application to the appropriate Regional Director when the merging credit union requests approval of the merger proposal. If the Regional Director approves the merger, the NCUSIF will assess a deposit and a prorated insurance premium (unless waived in whole or in part for all insured credit unions during that year) on any additional share accounts insured as a result of the merger.

(c) Where the continuing credit union is nonfederally-insured or uninsured and does not make application for insurance, but the merging credit union is federally-insured, the continuing credit union is entitled to a refund of the merging credit union's NCUSIF deposit and to a refund of the unused portion of the NCUSIF share insurance premium (if any). If the continuing credit union is uninsured, the NCUSIF will make the refund only after expiration of the one-year period of continued insurance coverage noted in paragraph (e) of this section.

(d) Where the continuing credit union is nonfederally-insured, NCUSIF insurance of the member accounts of a merging federally-insured credit union ceases as of the effective date of the merger.

(e) Where the continuing credit union is uninsured, NCUSIF insurance of the member accounts of the merging federally-insured credit union will continue for a period of one year, subject to the restrictions in section 206(d)(1) of the Act.

§ 708b.103 Preparation of merger plan.

(a) Upon the approval of a proposition for merger by the boards of directors of the credit unions, the two credit unions must prepare a plan for the proposed merger that includes:

(1) Current financial statements for both credit unions;

(2) Current delinquent loan summaries and analyses of the adequacy of the Allowance for Loan and Lease Losses account;

(3) Consolidated financial statements, including an assessment of the generally accepted accounting principles (GAAP) net worth of each credit union before the merger and the GAAP net worth of the continuing credit union after the merger;

(4) Analyses of share values;

(5) Explanation of any proposed share adjustments;

(6) Explanation of any provisions for reserves, undivided earnings or dividends;

(7) Provisions with respect to notification and payment of creditors;

(8) Explanation of any changes relative to insurance such as life savings and loan protection insurance and insurance of member accounts;

(9) Provisions for determining that all assets and liabilities of the continuing credit union will conform with the requirements of the Act (where the continuing credit union is a federal credit union); and

(10) Proposed charter amendments (where the continuing credit union is a federal credit union). These amendments, if any, will usually

pertain to the name of the credit union and the definition of its field of membership.

(b) [Reserved]

§ 708b.104 Submission of merger proposal to the NCUA.

(a) Upon approval of the merger plan by the boards of directors of the credit unions, the credit unions must submit the following information to the Regional Director:

(1) The merger plan, as described in this part;

(2) Resolutions of the boards of directors;

(3) Proposed Merger Agreement;

(4) Proposed Notice of Special Meeting of the Members (for merging federal credit unions);

(5) Copy of the form of Ballot to be sent to the members (for merging federal credit unions);

(6) Evidence that the state's supervisory authority approves the merger proposal (for states that require such agreement before NCUA approval);

(7) Application and Agreement for Insurance of Member Accounts (for continuing state credit unions desiring to become federally-insured);

(8) If the merging credit union has $50 million or more in assets on its latest call report, a statement about whether the two credit unions intend to make a Hart-Scott-Rodino Act premerger notification filing with the Federal Trade Commission and, if not, an explanation why not; and

(9) For mergers where the continuing credit union is not federally-insured and will not apply for federal insurance:

(i) A written statement from the continuing credit union that it "is aware of the requirements of 12 U.S.C. 1831t(b), including all notification and acknowledgment requirements"; and

(ii) Proof that the accounts of the credit union will be accepted for coverage by the nonfederal insurer (if the credit union will have nonfederal insurance).

(b) [Reserved]

§ 708b.105 Approval of merger proposal by the NCUA.

(a) In any case where the continuing credit union is federally-insured and the merging credit union is nonfederally-insured or uninsured, the NCUA will determine the potential risk to the NCUSIF.

(b) If the NCUA finds that the merger proposal complies with the provisions of this Part and does not present an undue risk to the NCUSIF, it may approve the proposal subject to any other specific requirements as it may prescribe to fulfill the intended purposes of the proposed merger. For mergers of federal credit unions into federally-insured credit unions, if the NCUA determines that the merging credit union is in danger of insolvency and that the proposed merger would reduce the risk or avoid a threatened loss to the NCUSIF, the NCUA may permit the merger to become effective without an affirmative vote of the membership of the merging credit union otherwise required by § 708b.106 of this part.

(c) NCUA may approve any proposed charter amendments for a continuing federal credit union contingent upon the completion of the merger. All charter amendments must be consistent with NCUA chartering policy.

§ 708b.106 Approval of the merger proposal by members.

(a) When the merging credit union is a federal credit union, the members must:

(1) Have the right to vote on the merger proposal in person at the annual meeting, if within 60 days after NCUA approval, or at a special meeting to be called within 60 days of NCUA approval, or by mail ballot, received no later than the date and time announced for the annual meeting or the special meeting called for that purpose.

(2) Be given advance notice of the meeting in accordance with the provisions of Article IV, Meetings of Members, Federal Credit Union Bylaws. The notice must:

(i) Specify the purpose of the meeting and the time and place;

(ii) Contain a summary of the merger plan, including, but not necessarily limited to, current financial statements for each credit union, a consolidated financial statement for the continuing credit union, analyses of share values, explanation of any proposed share adjustments, explanation of any changes relative to insurance such as life savings and loan protection insurance and insurance of member accounts;

(iii) State reasons for the proposed merger;

(iv) Provide name and location, including branches, of the continuing credit union;

(v) Inform the members that they have the right to vote on the merger proposal in person at the meeting or by written ballot to be received no later than the date and time announced for the annual meeting or the special meeting called for that purpose; and

(vi) Be accompanied by a Ballot for Merger Proposal.

(b) Approval of a proposal to merge a federal credit union into a federally-insured credit union requires the affirmative vote of a majority of the members of the merging credit union who vote on the proposal. If the continuing credit union is uninsured or nonfederally-insured, the voting requirements of subpart B apply. If the continuing credit union is nonfederally-insured, the merging credit union must use the form notice and ballot in subpart C of this part unless the Regional Director approves the use of different forms.

§ 708b.107 Certificate of vote on merger proposal.

The board of directors of the merging federal credit union must certify the results of the membership vote to the Regional Director within 10 days after the vote is taken. The certification must include the total number of members of record of the credit union, the number who voted on the merger, the number who voted in favor, and the number who voted against. If the continuing credit union is nonfederally-insured, the merging credit union must use the certification form in subpart C of this part unless the Regional Director approves the use of a different form.

§ 708b.108 Completion of merger.

(a) Upon approval of the merger proposal by the NCUA and by the state supervisory authority (where the continuing or merging credit union is a state credit union) and by the members of each credit union where required, the credit unions may complete the merger.

(b) Upon completion of the merger, the board of directors of the continuing credit union must certify the completion of the merger to the Regional Director within 30 days after the effective date of the merger.

(c) Upon the NCUA's receipt of certification that the merger has been completed, the NCUA will cancel the charter of the merging federal credit union (if applicable) and the insurance certificate of any merging federally-insured credit union.

Subpart B—Voluntary Termination or Conversion of Insured Status

§ 708b.201 Termination of insurance.

(a) A state credit union may terminate federal insurance, if permitted by state law, either on its own or by merging into an uninsured credit union.

(b) A federal credit union may terminate federal insurance only by merging into, or converting its charter to, an uninsured state credit union.

(c) A majority of the credit union's members must approve a termination of insurance by affirmative vote. The credit union must use an independent entity to collect and tally the votes and certify the results for all terminations, including terminations that involve a merger or charter conversion. The vote must be taken by secret ballot, meaning that no credit union employee or official can determine how a particular member voted.

(d) Termination of federal insurance requires the NCUA's prior written approval. A credit union must notify the NCUA and request approval of the termination through the Regional Director in writing at least 90 days before the proposed termination date and within one year after obtaining the membership vote. The notice to the NCUA must include:

(1) A written statement from the credit union that it "is aware of the requirements of 12 U.S.C. 1831t(b), including all notification and acknowledgment requirements;" and

(2) A certification of the member vote that must include the total number of members of record of the credit union, the number who voted in favor of the termination, and the number who voted against.

(e) The NCUA will approve or disapprove the termination in writing within 90 days after being notified by the credit union.

§ 708b.202 Notice to members of proposal to terminate insurance.

(a) When the board of directors of a federally-insured credit union adopts a resolution proposing to terminate federal insurance, including termination due to a merger or conversion of charter, it must provide its members with written notice of the proposal to terminate and of the date set for the membership vote. The first written communication following the resolution that is made by or on behalf of the credit union and that informs the members that the credit union will seek termination is the notice of the proposal to terminate. This notice must:

(1) Inform the members of the requirement for a membership vote and the date for the vote;

(2) Explain that the insurance provided by the NCUA is federal insurance and is backed by the full faith and credit of the United States government; and

(3) Include a conspicuous statement that if the termination or merger is approved, and the credit union, or the continuing credit union in the case of a merger, subsequently fails, the federal government does not guarantee the member will get his or her money back.

(b) The credit union must deliver the notice in person to each member, or mail it to each member at the address for the member as it appears on the records of the credit union, not more than 30 nor less than 7 days before the date of the vote. The membership must be given the opportunity to vote by mail ballot. The credit union may provide the notice of the proposal and the ballot to members at the same time.

(c) If the membership and the NCUA approve the proposition for termination of insurance, the credit union must give the members prompt and reasonable notice of termination.

§ 708b.203 Conversion of insurance.

(a) A federally-insured state credit union may convert to nonfederal insurance, if permitted by state law, either on its own or by merging into a nonfederally-insured credit union.

(b) A federal credit union may convert to nonfederal insurance only by merging into, or converting its charter to, a nonfederally-insured state credit union.

(c) Conversion to nonfederal insurance requires the prior written approval of the NCUA. After the credit union board of directors resolves to seek a conversion, the credit union must notify the Regional Director promptly, in writing, of the desired conversion and request NCUA approval of the conversion. The notification must be in the form specified in subpart C of this part, unless the Regional Director approves a different form. The credit union must provide this notification and request for approval to the Regional Director at least 14 days before the credit union notifies its members and seeks their vote and at least 90 days before the proposed conversion date. NCUA will approve or disapprove the conversion as described in paragraph (g) of this section.

(d) Approval of a conversion of federal to nonfederal insurance requires the affirmative vote of a majority of the credit union's members who vote on the proposition, provided at least 20 percent of the total membership participates in the voting. The credit union must use an independent entity to collect and tally the votes and certify the results for all share insurance conversions, including share insurance conversions that involve a merger or charter conversion. The vote must be taken by secret ballot, meaning that no credit union employee or official can determine how a particular member voted.

(e) For all conversions, the notice to the NCUA must include:

(1) A written statement from the credit union that it "it is aware of the requirements of 12 U.S.C. 1831t(b), including all notification and acknowledgment requirements;" and

(2) Proof that the nonfederal insurer is authorized to issue share insurance in the state where the credit union is located and that the insurer will insure the credit union.

(f) The board of directors of the credit union and the independent entity that conducts the membership vote must certify the results of the membership vote to the NCUA within 10 days after the deadline for receipt of votes. The certification must include the total number of members of record of the credit union, the number who voted on the conversion, the number who voted in favor of the conversion, and the number who voted against. The certification must be in the form specified in subpart C of this part.

(g) Generally, the NCUA will approve or disapprove the conversion in writing within 14 days after receiving the certification of the vote.

(h) For conversions by merger, the merging credit unions must follow the procedures specified in

subparts A and B of this part and use the forms specified in subpart C of this part. In the event the procedures of Subpart A and B conflict, the credit union must follow subpart B.

§ 708b.204 Notice to members of proposal to convert insurance.

(a) When the board of directors of a federally-insured credit union adopts a resolution proposing to convert from federal to nonfederal insurance, including an insurance conversion associated with a merger or conversion of charter, it must provide its members with written notice of the proposal to convert insurance and of the date set for the membership vote. The first written communication following this resolution that is made by or on behalf of the credit union and that informs the members that the credit union will seek conversion of insurance is the notice of the proposal to convert. This notice must:

(1) Inform the members of the requirement for a membership vote and the date for the vote;

(2) Explain that the insurance provided by the NCUA is federal insurance and is backed by the full faith and credit of the United States government, while the insurance provided by the nonfederal insurer is not guaranteed by the federal or any state government;

(3) Include a conspicuous statement that if the conversion or merger is approved, and the credit union, or the continuing credit union in the case of a merger, subsequently fails, the federal government does not guarantee the member will get his or her money back; and

(4) Be in the form set forth in subpart C of this part, unless the Regional Director approves a different form.

(b) The credit union must deliver the notice in person to each member or mail it to each member at the address for the member as it appears on the records of the credit union, not more than 30 nor less than 7 days before the date for the vote. The credit union must give the membership the opportunity to vote by mail ballot. The form of the ballot must be as set forth in subpart C of this part, unless the Regional Director approves the use of a different form. The notice of the proposal and the ballot may be provided to the members at the same time.

(c) If the membership and the NCUA approve the proposition for conversion of insurance, the credit union will give prompt and reasonable notice to the membership. The credit union must deliver the notice at least 30 days before the effective date of the conversion. The notice must identify the effective date of the conversion, and the first page must also include a conspicuous statement (*i.e.*, in bold and no smaller than any other font size used in the notice) that:

(1) The conversion will result in the loss of federal share insurance, and

(2) The credit union will, at any time before the effective date of conversion, permit all members who have share certificates or other term accounts to close the federally-insured portion of those accounts without an early withdrawal penalty.

§ 708b.205 Modifications to notice and ballot.

(a) Converting credit unions will use the form notice and ballot as provided in subpart C of this part unless the Regional Director approves the use of a different form.

(b) A converting credit union will provide the Regional Director with a copy of the notice and ballot, including any reasons for conversion and estimated costs of conversion, on or before the date the notice and ballot are mailed to the members.

(c) Federally-insured state credit unions may include additional language in the notice and ballot regarding state requirements for mergers, where appropriate.

§ 708b.206 Share insurance communications to members.

(a) Every share insurance communication must comply with § 740.2 of this chapter, which, in part, prohibits federally-insured credit unions from making any representation that is inaccurate or deceptive in any particular.

(b) Every share insurance communication about share insurance conversion must contain the following conspicuous statement: "IF YOU ARE A MEMBER OF THIS CREDIT UNION, YOUR ACCOUNTS ARE CURRENTLY INSURED BY THE NATIONAL CREDIT UNION ADMINISTRATION, A FEDERAL AGENCY. THIS FEDERAL INSURANCE IS BACKED BY THE FULL FAITH AND CREDIT OF THE UNITED STATES GOVERNMENT. IF THE CREDIT UNION CONVERTS TO PRIVATE INSURANCE AND THE CREDIT UNION FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE THAT

YOU WILL GET YOUR MONEY BACK." The statement must:

(1) Appear on the first page of the communication where conversion is discussed and, if the communication is on an internet website posting, the credit union must make reasonable efforts to make it visible without scrolling; and

(2) Must be in capital letters, bolded, offset from the other text by use of a border, and at least one font size larger than any other text (exclusive of headings) used in the communication.

(c) Every share insurance communication about share insurance termination must contain the following conspicuous statement: "IF YOU ARE A MEMBER OF THIS CREDIT UNION, YOUR ACCOUNTS ARE CURRENTLY INSURED BY THE NATIONAL CREDIT UNION ADMINISTRATION, A FEDERAL AGENCY. THIS FEDERAL INSURANCE IS BACKED BY THE FULL FAITH AND CREDIT OF THE UNITED STATES GOVERNMENT. IF THE CREDIT UNION TERMINATES ITS FEDERAL INSURANCE AND THE CREDIT UNION FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE THAT YOU WILL GET YOUR MONEY BACK." The statement must:

(1) Appear on the first page of the communication where termination is discussed and, if the communication is on an internet website posting, the credit union must make reasonable efforts to make it visible without scrolling; and

(2) Must be in capital letters, bolded, offset from the other text by use of a border, and at least one font size larger than any other text (exclusive of headings) used in the communication.

(d) A converting credit union must provide the Regional Director with a copy of any share insurance communication that the credit union will make during the voting period. The Regional Director must receive the copy at or before the time the credit union makes it available to members. The converting credit union must inform the Regional Director when the communication is to be made, to which members it will be directed, and how it will be disseminated. For purposes of this section, the voting period begins on the date of the board of director's resolution to seek conversion or termination and ends on the date the member voting closes.

(e) The Regional Director may take appropriate action, including disapproving a conversion, if he or she determines that a converting credit union, by inclusion or omission of information in a share insurance communication, materially mislead or misinformed its membership. For example, the Regional Director will treat any share insurance communication that compares the relative strength, safety, or claims paying ability of a private insurer with that of the National Credit Union Share Insurance Fund as materially misleading if the comparison fails to mention that the federal insurance provided by the NCUA is backed by the full faith and credit of the United States government.

Subpart C—Forms

§ 708b.301 Conversion of insurance (State Chartered Credit Union).

Unless the Regional Director approves the use of different forms, a state chartered credit union must use the forms in this section in connection with a conversion to nonfederal insurance.

(a) Form letter notifying NCUA of intent to convert:

(insert name), NCUA Regional Director

(insert address of NCUA Regional Director)

Re: Notice of Intent to Convert to Private Share Insurance

Dear Director (insert name):

In accordance with federal law at Title 12, United States Code Section 1785(b)(1)(D), I request the National Credit Union Administration approve the conversion of (insert name of credit union) from federal share insurance to private primary share insurance with (insert name of private insurance company).

On (insert date), the board of directors of (insert name of credit union) resolved to pursue the conversion from federal insurance to private insurance. A copy of the resolution is enclosed.

On (insert date), the credit union plans to solicit the vote of our members on the conversion. The credit union will employ (insert name, address, and telephone number of independent entity) to conduct the member vote. The credit union will use the form notice and ballot required by NCUA regulations, and will certify the results to NCUA as required by NCUA regulations.

Aside from the notice and ballot, the credit union (does)(does not) intend to provide its members with additional written information about the conversion. I understand that NCUA regulations forbid any communications to members, including

communications about NCUA insurance or private insurance, that are inaccurate or deceptive.

(Insert name of State) allows credit unions to obtain primary share insurance from (insert name of private insurance company). I have enclosed a copy of a letter from (insert name and title of state regulator) establishing that (insert name of private insurer) has the authority to provide (insert name of credit union) with primary share insurance.

I have enclosed a copy of a letter from (insert name of private insurer) indicating it has accepted (insert name of credit union) for primary share insurance and will insure the credit union immediately upon the date that it loses its federal share insurance.

I am aware of the requirements of 12 U.S.C. 1831t(b), including all notification and acknowledgment requirements.

The point of contact for conversion matters is (insert name and title of credit union employee), who can be reached at (insert telephone number).

Sincerely,

(signature)

Chief Executive Officer.

Enclosures

(b) Form notice to members of intent to convert and special meeting of members:

Notice of Proposal to Convert to Nonfederally-Insured Status and Special Meeting of Members

(Insert Name of Converting Credit Union)

On (insert date), the board of directors of your credit union approved a proposition to convert from federal share (deposit) insurance to private insurance. You are encouraged to attend a special meeting of our credit union at (insert address) on (insert time and date) to address this proposition.

Purpose of Meeting

The meeting has two purposes:

1. To consider and act upon a proposal to convert your account insurance from federal insurance to private insurance.

2. To approve the action of the Board of Directors in authorizing the officers of the credit union to carry out the proposed conversion.

Insurance Conversion

Currently, your accounts have share insurance provided by the National Credit Union Administration, an agency of the federal government. The basic federal coverage is up to $100,000, but accounts may be structured in different ways, such as joint accounts, payable-on-death accounts, or IRA accounts, to achieve federal coverage of much more than $100,000. If the conversion is approved, your federal insurance will terminate on the effective date of the conversion. Instead, your accounts in the credit union will be insured up to $(insert dollar amount) by (insert name of insurer), a corporation chartered by the State of (insert name of State). The federal insurance provided by the National Credit Union Administration is backed by the full faith and credit of the United States government. The private insurance you will receive from (insert name of insurer), however, is not guaranteed by the federal or any state or local government.

IF THIS CONVERSION IS APPROVED, AND THE (insert name of credit union) FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE YOU WILL GET YOUR MONEY BACK.

Also, because this conversion, if approved, would result in the loss of federal share insurance, the credit union will, at any time between the approval of the conversion and the effective date of conversion and upon request by the member, permit all members who have share certificates or other term accounts to close the federally-insured portion of those accounts without an early withdrawal penalty. (This is an optional sentence. It may be deleted without the approval of the Regional Director. The members must be informed about this right, however, as described in 12 CFR 708b.204(c).)

The board of directors has concluded that the proposed conversion is desirable for the following reasons: (insert reasons). (This is an optional paragraph. It may be deleted without the prior approval of the Regional Director.)

The proposed conversion will result in the following one-time cost associated with the conversion: (List the total estimated dollar amount, including (1) the cost of conducting the vote, (2) the

cost of changing the credit union's name and insurance logo, and (3) attorney and consultant fees.)

The conversion must have the approval of a majority of members who vote on the proposal, provided at least 20 percent of the total membership participates in the voting.

Enclosed with this Notice of Special Meeting is a ballot. If you cannot attend the meeting, please complete the ballot and return it to (insert name and address of independent entity conducting the vote) by no later than (insert time and date). To be counted, your ballot must reach us by that date and time.

By order of the board of directors.

(signature of Board Presiding Officer)

(insert title and date)

(c) Form ballot:

Ballot for Conversion to Nonfederally-Insured Status

Insert Name of Converting Credit Union)

Name of Member: (insert name)

Account Number: (insert account number)

The credit union must receive this ballot by (insert date and time for vote). Please mail or bring it to: (Insert name of independent entity and address)

I understand if the conversion of the (insert name of credit union) is approved, the National Credit Union Administration share (deposit) insurance I now have, up to $100,000, or possibly more if I use different accounts structures, will terminate upon the effective date of the conversion. Instead, my shares in the (insert name of credit union) will be insured up to $(insert dollar amount) by (insert name of insurer), a corporation chartered by the State of (insert name of state). The federal insurance provided by the National Credit Union Administration is backed by the full faith and credit of the United States Government. The private insurance provided by (insert name of insurer) is not.

I FURTHER UNDERSTAND THAT IF THIS CONVERSION IS APPROVED AND THE (insert name of credit union) FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE THAT I WILL GET MY MONEY BACK.

I vote on the proposal as follows (check one box):

[ ] Approve the conversion to private insurance and authorize the Board of Directors to take all necessary action to accomplish the conversion.

[ ] Do not approve the conversion to private insurance.

Signed: _____

(Insert printed member's name)

Date: _____

(d) Form certification of member vote to NCUA:

Certification of Vote on Conversion to Nonfederally-Insured Status

We, the undersigned officers of the (insert name of converting credit union), certify the completion of the following actions:

1. At a meeting on (insert date), the Board of Directors adopted a resolution to seek the conversion of our primary share insurance coverage from NCUA to (insert name of private insurer).

2. Not more than 30 nor less than 7 days before the date of the vote, copies of the notice of special meeting and the ballot, as approved by the National Credit Union Administration, were mailed to our members.

3. The credit union arranged for the conduct of a special meeting of our members at the time and place announced in the Notice to consider and act upon the proposed conversion.

4. At the special meeting, the credit union arranged for an explanation of the conversion to the members present at the special meeting.

5. The (insert name), an entity independent of the credit union, conducted the membership vote at the special meeting. The members voted as follows:

(insert) Number of total members

(insert) Number of members present at the special meeting

(insert) Number of members present who voted in favor of the conversion

(insert) Number of members present who voted against the conversion

(insert) Number of additional written ballots in favor of the conversion

(insert) Number of additional written ballots opposed to the conversion

(insert "20% or more") OR (insert "Less than 20%") of the total membership voted. Of those who voted, a majority voted (inset "in favor of") OR ("against") conversion.

The action of the members at the special meeting was recorded in the minutes.

This certification signed the (insert date).

(signature of Board Presiding Officer)
(insert typed name and title)
(signature of Board Secretary)
(insert typed name and title)

I (insert name), an officer of the (insert name of independent entity that conducted the vote), hereby certify that the information recorded in paragraph 5 above is accurate.

This certification signed the (insert date):

(signature of officer of independent entity)
(typed name, title, and phone number)

§ 708b.302 Conversion of Insurance (Federal Credit Union).

Unless the Regional Director approves the use of different forms, a federal credit union must use the following forms in this section in connection with a conversion to a nonfederally-insured state charter.

(a) Form letter notifying NCUA of intent to convert:

(insert name), NCUA Regional Director
(insert address of NCUA Regional Director)
Re: Notice of Intent to Convert to State Charter and to Private Share Insurance

Dear Director (insert name):

In accordance with federal law at Title 12, United States Code Section 1785(b)(1)(D), I request the National Credit Union Administration approve the conversion of (insert name of federal credit union) to a state charter in (insert name of state) and from federal share insurance to private primary share insurance with (insert name of private insurance company).

On (insert date), the board of directors of (insert name of credit union) resolved to pursue the charter conversion and the conversion from federal insurance to private insurance. A copy of the resolution is enclosed.

On (insert date), the credit union plans to solicit the vote of our members on the conversion. The credit union will employ (insert name, address, and telephone number of independent entity) to conduct the vote. The credit union will use the form notice and ballot required by NCUA regulations, and will certify the results to NCUA as required by NCUA regulations.

Aside from the notice and ballot, the credit union (does)(does not) intend to provide our members with additional written information about the conversion. I understand that NCUA regulations forbid any communications to members, including communications about NCUA insurance or private insurance, that are inaccurate or deceptive.

I have enclosed a copy of a letter from (insert name and title of state regulator) indicating approval of our conversion to a state charter.

(Insert name of State) allows credit unions to obtain primary share insurance from (insert name of private insurance company). I have enclosed a copy of a letter from (insert name and title of state regulator) establishing that (insert name of private insurer) has the authority to provide (insert name of credit union), after conversion to a state charter, with primary share insurance.

I have enclosed a copy of a letter from (insert name of private insurer) indicating it has accepted (insert name of credit union) for primary share insurance and will insure the credit union immediately upon the date that it loses its federal share insurance.

I am aware of the requirements of 12 U.S.C. 1831t(b), including all notification and acknowledgment requirements.

Enclosed you will also find other information required by NCUA's Chartering and Field of Membership Manual, Chapter 4, § III.C.

The point of contact for conversion matters is (insert name and title of credit union employee), who can be reached at (insert telephone number).

Sincerely,

(signature),
Chief Executive Officer.
Enclosures

(b) Form notice to members of intent to convert and special meeting of members:

Notice of Proposal to Convert to a State Charter and to Nonfederally-Insured Status and Special Meeting of Members

(Insert Name of Converting Credit Union)

On (insert date), the board of directors of your credit union approved a proposition to convert from federal share (deposit) insurance to private insurance and to convert from a federal credit union to a state-chartered credit union. You are encouraged to attend a special meeting of our credit union at (insert address) on (insert time and date) to address this proposition.

Purpose of Meeting

The meeting has two purposes:

1. To consider and act upon a proposal to convert your credit union from a federal charter to a state charter and your account insurance from federal insurance to private insurance.

2. To approve the action of the Board of Directors in authorizing the officers of the credit union to carry out the proposed conversion.

Insurance Conversion

Currently, your accounts have share insurance provided by the National Credit Union Administration, an agency of the federal government. The basic federal coverage is up to $100,000, but accounts may be structured in different ways, such as joint accounts, payable-on-death accounts, or IRA accounts, to achieve federal coverage of much more than $100,000. If the conversion is approved, your federal insurance will terminate on the effective date of the conversion. Instead, your accounts in the credit union will be insured up to $(insert dollar amount) by (insert name of insurer), a corporation chartered by the State of (insert name of State). The federal insurance provided by the National Credit Union Administration is backed by the full faith and credit of the United States government. The private insurance you will receive from (insert name of insurer), however, is not guaranteed by the federal or any state or local government.

IF THIS CONVERSION IS APPROVED, AND THE (insert name of credit union) FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE YOU WILL GET YOUR MONEY BACK.

Also, because this conversion, if approved, would result in the loss of federal share insurance, the credit union will, at any time between the approval of the conversion and the effective date of conversion and upon request of the member, permit all members who have share certificates or other term accounts to close the federally-insured portion of those accounts without an early withdrawal penalty. (This is an optional sentence. It may be deleted without the approval of the Regional Director. The members must be informed about this right, however, as described in 12 CFR 708b.204(c).)

The board of directors has concluded that the proposed conversion is desirable for the following reasons: (Insert reasons) (This is an optional paragraph. It may be deleted without the approval of the Regional Director.).

The proposed conversion will result in the following one-time cost associated with the conversion: (List the total estimated dollar amount, including (1) the cost of conducting the vote, (2) the cost of changing the credit union's name and insurance logo, and (3) attorney and consultant fees.)

The conversion must have the approval of a majority of members who vote on the proposal, provided at least 20 percent of the total membership participates in the voting.

Enclosed with this Notice of Special Meeting is a ballot. If you cannot attend the meeting, please complete the ballot and return it to (insert name and address of independent entity conducting the vote) by no later than (insert time and date). To be counted, your ballot must reach us by that date and time.

By order of the board of directors.

(signature of Board Presiding Officer)

(insert title and date)

(c) Form ballot:

Ballot for Conversion to State Charter and Nonfederally-Insured Status

(Insert Name of Converting Credit Union)

Name of Member: (insert name)

Account Number: (insert account number)

The credit union must receive this ballot by (insert date and time for vote). Please mail or bring it to: (Insert name of independent entity and address)

I understand if the conversion of the (insert name of credit union) is approved, the National Credit Union Administration share (deposit) insurance I now have, up to $100,000, or possibly more if I use different accounts structures, will terminate upon the effective date of the conversion. Instead, my shares in the (insert name of credit union) will be insured up to $(insert dollar amount) by (insert name of insurer), a corporation chartered by the State of (insert name of state). The federal insurance provided by the National Credit Union Administration is backed by the full faith and credit of the United States Government.

The private insurance provided by (insert name of insurer) is not.

I FURTHER UNDERSTAND THAT, IF THIS CONVERSION IS APPROVED AND THE (insert name of credit union) FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE THAT I WILL GET MY MONEY BACK.

I vote on the proposal as follows (check one box):

[ ] Approve the conversion of charter and conversion to private insurance and authorize the Board of Directors to take all necessary action to accomplish the conversion.

[ ] Do not approve the conversion of charter and the conversion to private insurance.

Signed: _____
(Insert printed member's name)

Date: _____

(d) Form certification to NCUA of member vote:

Certification of Vote on Conversion to State Charter and Nonfederally-Insured Status

We, the undersigned officers of the (insert name of converting credit union), certify the completion of the following actions:

1. At a meeting on (insert date), the Board of Directors adopted a resolution to seek the conversion of our credit union to a state charter and the conversion of our primary share insurance coverage from NCUA to (insert name of private insurer).

2. Not more than 30 nor less than 7 days before the date of the vote, copies of the notice of special meeting and ballot, as approved by the National Credit Union Administration, were mailed to our members.

3. The credit union arranged for the conduct of a special meeting of our members at the time and place announced in the Notice to consider and act upon the proposed conversion.

4. At the special meeting, the credit union arranged for an explanation of the conversion to the members present at the special meeting.

5. The (insert name), and entity independent of the credit union, conducted the membership vote at the special meeting. The members voted as follows:

(insert) Number of total members

(insert) Number of members present at the special meeting

(insert) Number of members present who voted in favor of the conversion

(insert) Number of members present who voted against the conversion

(insert) Number of additional written ballots in favor of the conversion

(insert) Number of additional written ballots opposed to the conversion

(insert "20% or more") OR (insert "Less than 20%") of the total membership voted. Of those who voted, a majority voted (inset "in favor of") OR ("against") conversion.

The action of the members at the special meeting was recorded in the minutes.

This certification signed the (insert date).

(signature of Board Presiding Officer)
(insert typed name and title)
(signature of Board Secretary)
(insert typed name and title)

I (insert name), an officer of the (insert name of independent entity that conducted the vote), hereby certify that the information recorded in paragraph 5 above is accurate.

This certification signed the (insert date):

(signature of officer of independent entity)
(typed name, title, and phone number)

§ 708b.303 Conversion of insurance through merger.

Unless the Regional Director approves the use of different forms, a federally-insured credit union that is merging into a nonfederally-insured credit union must use the forms in this section.

(a) Form notice to members of intent to merge and convert and special meeting of members:

Notice of Special Meeting on Proposal to Merge and Convert to Nonfederally-Insured Status

(Insert Name of Merging Credit Union)

On (insert date), the Board of Directors of your credit union approved a proposition to merge with

(insert name of continuing credit union) and to convert from federal share (deposit) insurance to private insurance. You are encouraged to attend a special meeting of our credit union at (insert address) on (insert time and date).

Purpose of Meeting

The meeting has two purposes:

1. To consider and act upon a proposal to merge our credit union with (insert name of continuing credit union), the continuing credit union.

2. To approve the action of the Board of Directors of our credit union in authorizing the officers of the credit union, subject to member approval, to carry out the proposed merger.

If this merger is approved, our credit union will transfer all its assets and liabilities to the continuing credit union. As a member of our credit union, you will become a member of the continuing credit union. On the effective date of the merger, you will receive shares in the continuing credit union for the shares you own now in our credit union.

Insurance Conversion

Currently, your accounts have share insurance provided by the National Credit Union Administration, an agency of the federal government. The basic federal coverage is up to $100,000, but accounts may be structured in different ways, such as joint accounts, payable-on-death accounts, or IRA accounts, to achieve federal coverage of much more than $100,000. If the merger is approved, your federal insurance will terminate on the effective date of the merger. Instead, your accounts in the credit union will be insured up to $(insert dollar amount) by (insert name of insurer), a corporation chartered by the State of (insert name of State). The federal insurance provided by the National Credit Union Administration is backed by the full faith and credit of the United States government. The private insurance you will receive from (insert name of insurer), however, is not guaranteed by the federal or any state or local government.

IF THIS MERGER IS APPROVED AND THE (insert name of continuing credit union) FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE YOU WILL GET YOUR MONEY BACK.

Also, because this merger, if approved, would result in the loss of federal share insurance, the (insert name of merging credit union) will, at any time between the approval of the merger and the effective date of merger and upon request of the member, permit all members who have share certificates or other term accounts to close the federally-insured portion of those accounts without an early withdrawal penalty. (This is an optional sentence. It may be deleted without the approval of the Regional Director. The members must be informed about this right, however, as described in 12 CFR 708b.204(c).)

Other Information Related to the Proposed Merger

The directors of the participating credit unions carefully analyzed the assets and liabilities of the participating credit unions and appraised each credit union's share values. The appraisal of the share values appears on the attached individual and consolidated financial statements of the participating credit unions.

The directors of the participating credit unions have concluded that the proposed merger is desirable for the following reasons: (insert reasons)

The Board of Directors of our credit union believes the merger should include/not include an adjustment in shares for the following reasons: (insert reasons)

The main office of the continuing credit union will be as follows: (insert location)

The branch office(s) of the continuing credit union will be as follows: (insert locations)

The merger must have the approval of a majority of members who vote on the proposal, provided at least 20 percent of the total membership participates in the voting.

Enclosed with this Notice of Special Meeting is a Ballot for Merger Proposal and Conversion to Nonfederally-insured Status. If you cannot attend the meeting, please complete the ballot and return it to (insert name of independent entity conducting vote) at (insert mailing address) by no later than (insert date and time). To be counted, your ballot must reach (insert name of inde-

pendent entity conducting vote) by the date and time announced for the meeting.

By order of the board of directors.

(signature of Board Presiding Officer)
(insert name and title of Board Presiding Officer) (insert date)

(b) Form ballot:

Ballot for Merger Proposal and Conversion to Nonfederally-Insured Status

Name of Member: (insert name)
Account Number: (insert account number)

The credit union must receive this ballot by (insert date and time for vote). Please mail or bring it to: (Insert name of independent entity and address)

I understand if the merger of conversion of the (insert name of merging credit union)into the (insert name of merging credit union is approved, the National Credit Union Administration share (deposit) insurance I now have, up to $100,000, or possibly more if I use different account structures, will terminate upon the effective date of the conversion. Instead, my shares in the (insert name of credit union) will be insured up to $(insert dollar amount) by (insert name of insurer), a corporation chartered by the State of (insert name of state). The federal insurance provided by the National Credit Union Administration is backed by the full faith and credit of the United States Government. The private insurance provided by (insert name of insurer) is not.

I FURTHER UNDERSTAND THAT, IF THIS MERGER IS APPROVED AND THE (insert name of continuing credit union) FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE THAT I WILL GET MY MONEY BACK.

I vote on the proposal as follows (check one box):

[ ] Approve the merger and the conversion to private insurance and authorize the Board of Directors to take all necessary action to accomplish the merger and conversion.

[ ] Do not approve the merger and the conversion to private insurance.

Signed: _____
(Insert printed member's name)

Date: _____

(c) Form certification of vote:

Certification of Vote on Merger Proposal and Conversion to Nonfederally-Insured Status of the (Insert Name of Merging Credit Union)

We, the undersigned officers of the (insert name of merging credit union), certify the completion of the following actions:

1. At a meeting on (insert date), the Board of Directors adopted a resolution approving the merger of our credit union with (insert name of continuing credit union).

2. Not more than 30 nor less than 7 days before the date of the vote, copies of the notice of special meeting and the ballot, as approved by the National Credit Union Administration, and a copy of the merger plan announced in the notice, were mailed to our members.

3. The credit union arranged for the conduct of a special meeting of our members at the time and place announced in the Notice to consider and act upon the proposed merger.

4. At the special meeting, the credit union arranged for an explanation of the merger proposal and any changes in federally-insured status to the members present at the special meeting.

5. The (insert name), and entity independent of the credit union, conducted the membership vote at the special meeting. At least 20 percent of our total membership voted and a majority of voting members favor the merger as follows:

(insert) Number of total members

(insert) Number of members present at the special meeting

(insert) Number of members present who voted in favor of the merger

(insert) Number of members present who voted against the merger

(insert) Number of additional written ballots in favor of the merger

(insert) Number of additional written ballots opposed to the merger

6. The action of the members at the special meeting was recorded in the minutes.

This certification signed the (insert date):

(signature of Board Presiding Officer)
(insert typed name and title)
(signature of Board Secretary)
(insert typed name and title)

I (insert name), an officer of the (insert name of independent entity that conducted the vote), hereby certify that the information recorded in paragraph 5 above is accurate.

This certification signed the (insert date):

(signature of officer of independent entity)
(typed name, title, and phone number)

Part 709

Involuntary Liquidation of Federal Credit Unions and Adjudication of Creditor Claims Involving Federally Insured Credit Unions in Liquidation

§ 709.0 Scope.

The rules and procedures in this part apply to charter revocations of federal credit unions under 12 U.S.C. 1787(a)(1)(A), (B), the involuntary liquidation and adjudication of creditor claims in all cases involving federally-insured credit unions, the treatment by the Board as conservator or liquidating agent of financial assets transferred in connection with a securitization or participation or of public funds held by a federally-insured credit union, and the allowance of prepayment fees to Federal Home Loan Banks under specified conditions. Remaining sections of this part are applicable to all federally insured credit unions. This part does not apply to share insurance claims arising out of the liquidation of a federally insured credit union. Insurance claims are decided pursuant to part 745 of this chapter.

§ 709.1 Definitions.

For the purposes of this Part, the following definitions apply:

(a) "General Counsel" means the General Counsel of the National Credit Union Administration or any attorney assigned to the General Counsel's staff.

(b) "Liquidating Agent" means the NCUA Board or person(s) appointed by it with delegated authority to carry out the liquidation of the credit union.

(c) "Insolvent" means insolvent as that term is defined in § 700.1(e)(1) of this chapter.

(d) "Claim" means a creditor's claim against the credit union in liquidation. This term does not include insurance claims arising out of the liquidation of a federally insured credit union. Insurance claims are decided pursuant to Part 745 of this Chapter.

(e) "Shareholder" means members, non-members, accountholders, or any other party or entity that is the owner of a share, share certificate or share draft account or the equivalent of such accounts under state law.

§ 709.2 NCUA Board as Liquidating Agent.

(a) The Board, as liquidating agent, by operation of law and without any conveyance or other instrument, act or deed, shall succeed to all the rights, titles, powers, and privileges of the credit union, and of its shareholders, officers, and directors, with respect to the credit union and its assets, and such shareholders, officers, or directors shall not thereafter have or exercise any such rights, powers, or privileges or act in connection with any assets or property of any nature of the credit union.

(b) The Board, as liquidating agent, shall take possession of and title to books, records, and assets of every description of such credit union to which such credit union has rights of possession and title to all offices and other facilities of such credit union.

§ 709.3 Challenge to Revocation of Charter and Involuntary Liquidation.

If a Federal credit union is determined to be insolvent and placed into liquidation pursuant to 12 U.S.C. § 1787, the Federal credit union may, not later than 10 days after the date on which the Board closes the credit union for liquidation, apply to the United States District Court for the judicial district in which the principal office of the credit union is located or the United States District Court for the District of Columbia for an order requiring the Board to show cause why it should not be prohibited from continuing such liquidation. Notwithstanding other provisions of this Part, the board of directors of the credit union may meet following the placing of the institution into liquidation for the sole purpose of considering and authorizing the filing of this action in the name of the credit union. No such action in the name of the credit union may be instituted without the authorization of the board of directors of the institution pursuant to a valid board of directors resolution. No credit union funds shall be available to pay expenses incurred in bringing a legal action to challenge the Board's liquidation action.

§ 709.4 Powers and Duties of Liquidating Agent.

(a) *Inventory of assets*—As soon as practicable after taking possession, the liquidating agent shall inventory the assets of such credit union as of the date of taking possession, showing the value as carried on the books of the credit union, and the security therefor, if any, a brief description of the assets and any security, and a record of the credit union's creditor and accounts liabilities.

(b) *Notice to creditors*—The liquidating agent shall promptly publish a notice to the credit union's creditors to present their claims, together with proof, to the liquidating agent by a date specified in the notice. This date shall be not less than 90 days after the publication of the notice. The liquidating agent shall republish such notice approximately one and two months, respectively, after the initial publication. At the time of initial publication, the liquidating agent shall mail a notice similar to the published notice to any creditor shown on the credit union's books at the last address appearing therein. If the liquidating agent discovers the name of a creditor whose name does not appear on the credit union's books, a notice similar to the published notice shall be mailed to such creditor within 30 days after the discovery of the name and address.

(c) *General*—The liquidating agent shall collect all obligations and money due such credit union and may, to the extent consistent with its appointment, do all things desirable or expedient in its discretion to wind up the affairs of the credit union including, but not limited to, the following:

(1) exercise all rights and powers of the credit union including, but not limited to, any rights and powers under any mortgage, deed of trust, chose in action, option, collateral note, contract, judgment or decree, or instrument of any nature;

(2) institute, prosecute, maintain, defend, intervene, and otherwise participate in any and all actions, suits, or other legal proceedings by and against the liquidating agent or the credit union or in which the liquidating agent, the credit union, or its creditors or shareholders, or any of them, shall have an interest, and in every way to represent the credit union, its shareholders and creditors, subject to the direction of General Counsel;

(3) employ on a salary or fee basis such persons as in the judgment of the liquidating agent are necessary or desirable to carry out its responsibilities and functions, including, but not limited to, appraisers and Certified Public Accountants, and pay the costs out of the assets of the liquidated credit union;

(4) employ or retain any attorney or attorneys designated by, or acceptable to, the General Counsel in connection with litigation or for legal advice and assistance, for the liquidation generally or in particular instances, and pay compensation and retainers of such attorney or attorneys, together with all expenses, including, but not limited to, the costs and expenses of any litigation, as approved by the General Counsel, out of the assets of the liquidated credit union;

(5) execute, acknowledge, and deliver any and all deeds, contracts, leases, assignments, bills of sale, releases, extensions, satisfactions, and other instruments necessary or proper for any purposes, including, but not limited to, the effectuation, termination, or transfer of real, personal or mixed property, or that shall be necessary or proper to liquidate the credit union, and any deed or other instrument executed pursuant to the authority hereby given shall be as valid and effective for all purposes as if the same had been executed as the act and deed of the credit union;

(6) with concurrence of General Counsel, disaffirm or repudiate any contract or lease to which the credit union is a party, the performance of which the liquidating agent, in his sole discretion, determines to be burdensome, and which disaffirmance or repudiation in the liquidating agent's sole discretion will promote the orderly administration of the credit union's affairs;

(7) deposit, withdraw, or transfer funds, and otherwise exercise complete control over all investment or depository accounts maintained by or for the credit union at financial depository or similar institutions;

(8) do such things, and have such rights, powers, privileges, immunities, and duties, whether or not otherwise granted in the rules and regulations of this Part 709, as shall be authorized, directed, conferred, or imposed from time to time by the Board, or as shall be conferred by the Federal Credit Union Act;

(9) exercise such other authority as is conferred by the Federal Credit Union Act; and

(10) where acting as liquidating agent for a state-chartered federally insured credit union, exercise all the rights, powers, and privileges granted by state law to such a liquidating agent.

(d) *Expenditure of funds of the liquidation*—The liquidating agent shall have power to:

(1) pay all costs and expenses of the liquidation as determined by the liquidating agent;

(2) pay off and discharge taxes and liens;

(3) pay out and expend such sums as are deemed necessary or advisable for or in connection with the preservation, maintenance, conservation, protection, remodeling, repair, rehabilitation, or improvement of any asset or property of any nature of the credit union or the liquidating agent;

(4) pay off and discharge any assessments, liens, claims, or charges of any kind against any asset or property of any nature on which the credit union or the liquidating agent has a lien by way of mortgage, deed of trust, pledge, or otherwise, or in which the credit union or liquidating agent has any interest;

(5) settle, compromise, or obtain the release of, for cash or other consideration, claims and demands against the credit union or the liquidating agent; and

(6) indemnify its employees and agents from the assets of the credit union against liabilities incurred in the good faith performance of their duties.

(e) *Assets, claims, and contracts*—The liquidating agent shall have power to:

(1) sell for cash or on terms, exchange, assign, or otherwise dispose of, in whole or in part, any or all of the assets and property of the credit union, real, personal and mixed, tangible and intangible, of any nature, including any mortgage, deed of trust, chose in action, bond, note, contract, judgment, or decree, share or certificate of share of stock or debt, owing to the credit union or the liquidating agent; and

(2) surrender, abandon, and release any chose in action, or other assets or property of any nature, whether the subject of pending litigation or not, and settle, compromise, modify, or release, for cash or other consideration, claims and demands in favor of the credit union or the liquidating agent.

§ 709.5 Payout Priorities in Involuntary Liquidation.

(a) Claimants whose claims are secured shall receive their security. To the extent their respective claims exceed the value of the security for those claims, as determined to the satisfaction of the liquidating agent, they shall each have an unsecured claim against the credit union having priority as provided in paragraph (b) of this section.

(b) Unsecured claims against the liquidation estate that are proved to the satisfaction of the liquidating agent shall have priority in the following order:

(1) administrative costs and expenses of liquidation;

(2) claims for wages and salaries, including vacation, severance, and sick leave pay;

(3) taxes legally due and owing to the United States or any state or subdivision thereof;

(4) debts due and owing the United States, including the National Credit Union Administration;

(5) general creditors, and secured creditors (to the extent that their respective claims exceed the value of the security for those claims);

(6) shareholders to the extent of their respective uninsured shares and the National Credit Union Share Insurance Fund to the extent of its payment of share insurance;

(7) in a case involving liquidation of a corporate credit union, membership capital of corporate credit unions;

(8) in a case involving liquidation of a low-income designated credit union, any outstanding secondary capital accounts issued pursuant to the authority of §§ 701.34 or 741.204(c) of this chapter, and

(9) in a case involving liquidation of a corporate credit union, paid-in capital.

(c) Priorities are to be based on the circumstances that exist on the date of liquidation.

(d) If the repudiation or disaffirmance of any contract or lease gives rise to a claim for damages, such claim shall be considered a general creditor claim under paragraph (b)(5) of this section and not a cost or expense of liquidation under paragraph (b)(1) of this section.

(e) All unsecured claims of any category or class or priority described in paragraphs (b)(1) through (b)(7) of this section shall be paid in full, or provisions made for such payment, before any claims of lesser priority are paid. If there are insufficient funds to pay all claims of a category or class, payment shall be made pro rata. Notwithstanding anything to the contrary herein, the liquidating agent may, at any time, and from time to time, prior to the payment in full of all claims of a category or class with higher priority, make such distributions to claimants in priority categories described in paragraphs (b)(1), (b)(2), (b)(3), (b)(4),

and (b)(5) of this section as the liquidating agent believes are reasonably necessary to conduct the liquidation, provided that the liquidating agent determines that adequate funds exist or will be recovered during the liquidation to pay in full all claims of any higher priority. If a surplus remains after making distribution in full on all allowed claims described in paragraphs (b)(1) through (b)(9) of this section, such surplus shall be distributed pro rata to the credit union's shareholders.

§ 709.6 Initial Determination of Creditor Claims by the Liquidating Agent.

(a)(1) Any party wishing to submit a claim against the liquidated credit union must submit a written proof of claim in accordance with the requirements set forth in the notice to creditors. A failure to submit a written claim within the time provided in the notice to creditors shall be deemed a waiver of said claim and claimant shall have no further rights or remedies with respect to such claim.

(2) Notwithstanding paragraph (a)(1) of this section, the liquidating agent may, at his discretion, consider an untimely claim provided the following two criteria are present: (i) the claimant did not receive notice of the appointment of the liquidating agent in time to file a claim before the date provided for in the notice; and (ii) the claim is filed in time to permit payment of the claim.

(b) The liquidating agent may require submission of supplemental evidence by the claimant and by interested parties in the event of a dispute concerning a claim against any asset of the liquidated credit union. In requiring the submission of supplemental evidence, the liquidating agent may set such limitations of time, scope, and size as the liquidating agent deems reasonable in the circumstances, and may refuse to include in the record submissions or portions of submissions not in compliance with such limitations or requirements. The liquidating agent shall compile such written record of a claim or dispute as, in its discretion, is deemed sufficient to provide a reasonable basis for allowing or disallowing a claim or resolving a dispute. This written record shall be considered the administrative record.

(c) The liquidating agent shall determine whether to allow or disallow a claim and shall notify the claimant within 180 days from the date a claim against a credit union is filed pursuant to paragraph (a)(1) of this section. This 180-day period may be extended by written agreement between the claimant and the liquidating agent. Failure by the liquidating agent to determine a claim and notify the claimant within the 180-day period or, if the period is extended, within the extended period, shall be deemed a denial of the claim.

(d) If a claim or any portion thereof is disallowed, the notice to the claimant shall contain a statement of the reasons for the disallowance and an explanation of appeal rights pursuant to Section 709.7 of this Part.

(e) Notice of any determination with respect to a claim shall be sufficient if mailed to the most recent address of the claimant which appears:

(1) on the credit union's books;

(2) in the claim filed by the claimant; or

(3) in the documents submitted in the proof of claim.

(f) In the event the liquidating agent disallows all or part of a claim, the liquidating agent shall file with the Board, or its designated agent, a report of its determination. This report shall become part of the record and shall include the notice to the claimant and findings on all issues raised and decided by the liquidating agent.

§ 709.7 Procedures for Appeal of Initial Determination.

In order to appeal all or part of an initial decision which disallows a claim, in whole or in part, a claimant must, within 60 days of the mailing of the initial determination, file an administrative appeal pursuant to Section 709.8 of this Part, or file suit against the liquidated credit union in the United States District Court for the District of Columbia or in the United States District Court having jurisdiction over the place where the credit union's principal place of business is located, or continue an action commenced before the appointment of the liquidating agent. If the claimant does not appeal or file or continue a suit, any disallowance shall be final and the claimant shall have no further rights or remedies with respect to such claim.

§ 709.8 Administrative Appeal of the Initial Determination.

(a) *General*—A claimant requesting an administrative appeal may request review pursuant to any of the procedures listed in paragraphs (b) or (c) of this section. Any appeal of the initial deter-

mination must be in writing and must specify what type of appeal the claimant requests. The determination of whether to agree to a request for administrative appeal shall rest solely with the Board, which shall notify the claimant of its decision in writing. The 60-day period for filing a lawsuit in United States District Court, provided for in Section 709.7 of this Part, shall be tolled from the date of claimant's request for an administrative appeal to the date of the Board's decision regarding that request.

(b) *Hearing on the record*—Except as provided herein, any hearing requested pursuant to this section shall be conducted in accordance with the provisions of Subpart A, Part 747, of this Chapter. The Board shall render a final decision with respect to such claim after consideration of the hearing record and recommended decision. The Board's determination shall be subject to judicial review under Chapter 7 of Title 5, United States Code. Any claimant seeking judicial review of the Board's final decision under this paragraph must file a petition in the court of appeals for the circuit in which the principal office of the credit union is located, or in the United States Court of Appeals for the District of Columbia Circuit, within 30 days of the date of the Board's final decision. If a claimant does not file a petition before the end of the 30-day period, the Board's decision shall be final, and the claimant shall have no further rights or remedies with respect to such claim.

(1) *Burden of proof*—In any hearing on the record, the burden of proof to establish entitlement to any modification of the initial determination shall rest solely upon the claimant.

(2) *Order of procedure*—In any hearing on the record, at the time for opening arguments, counsel for the claimant shall argue first, and at the time for closing arguments, counsel for the claimant shall argue last.

(c) *Alternative dispute resolution*—Paragraphs (c) (1) and (2) of this section list alternatives for dispute resolution which may be available at the discretion of the Board. From time to time, the NCUA Board may authorize additional alternative dispute resolution processes.

(1) *Appeal to the Board*—Pursuant to this paragraph (c)(1), the claimant may file an appeal with the NCUA Board within the time provided for in Section 709.7. The appeal must be in writing and filed with the Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428. There shall be no personal appearance before the Board in connection with an appeal under this paragraph (c)(1).

(i) *Content of appeal*—Any appeal must include:

(A) a statement of the facts on which the appeal is based;

(B) a statement of the basis for the initial determination to which the claimant objects and the alleged error in such determination, including citations to applicable statutes and regulations;

(C) any other evidence relied upon by the claimant which was not previously provided to the liquidating agent.

(ii) *Procedures for review of the appeal*—

(A) Within 60 days of the date of the Board's receipt of an appeal, pursuant to paragraph (c)(1) of this section, the Board may request in writing that the claimant submit supplemental evidence in support of its appeal. If additional evidence is requested, the claimant shall have 45 days from the date of issuance of such request to provide such additional information. Failure by the claimant to provide such additional information may, as determined solely by the Board, result in denial of the claimant's appeal.

(B) Within 60 days from the date of the Board's receipt of an appeal, pursuant to paragraph (c)(1) of this section, the claimant may amend or supplement the appeal in writing. In the event the claimant does amend or supplement the appeal, the provisions of paragraph (c)(1)(ii)(A) of this section, with respect to requests for additional information and responses to such requests, shall apply with equal force to any such amendment or supplement to an appeal.

(iii) *Determination on appeal*—

(A) Within 180 days from the date of receipt of an appeal by the Board, the Board shall issue a decision allowing or disallowing claimant's appeal.

(B) The decision by the Board on appeal shall be provided to the claimant in writing, stating the reasons for the decision, and shall constitute a final agency decision regarding the claimant's claim.

(C) Failure by the Board to issue a decision on appeal of the claimant's claim within the 180-day period provided for under paragraph (c)(1)(iii)(A) shall be deemed to be denial of such appeal for the purposes of paragraph (c)(1)(iv) of this section.

(iv) *Judicial review*—

(A) For the purposes of seeking judicial review of actions taken pursuant to paragraph (c)(1) of this section, only a determination on appeal issued by the NCUA Board pursuant to this section shall constitute a final determination regarding a claim.

(B) A final determination by the Board is reviewable in accordance with the provisions of Chapter 7, Title 5, United States Code, by the United States Court of Appeals for the District of Columbia or the court of appeals for the Federal judicial circuit where the credit union's principal place of business is located. Any request for judicial review under this subparagraph must be filed within 60 days of the date of the Board's final decision. If any claimant fails to file before the end of the 60-day period, the Board's decision shall be final, and the claimant shall have no further rights or remedies with respect to such claim.

(2) The following additional procedures for dispute resolution may be made available at the sole discretion of the Board: mediation; nonbinding arbitration; and neutral fact finding.

§ 709.9 Expedited Determination of Creditor Claims.

(a) *General*—The provisions of this section establish procedures under which claimants may request expedited relief in lieu of the procedures set forth in Section 709.6 of this Part. A claimant shall be entitled to expedited determination of a claim only upon a showing that there exists a legally valid and enforceable or perfected security interest in assets of the liquidated credit union and that irreparable injury will occur if the routine claims procedure is followed.

(b) *Filing of request for expedited relief*—All requests for expedited relief must be filed within 30 days from the date of mailing, by the liquidating agent, of the notice to the creditor concerned. The request shall be deemed to be filed when received by the Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428. A copy of the request must be simultaneously served upon the liquidating agent for the credit union concerned. There shall be no right of personal appearance before the Board in connection with any claim submitted under this paragraph.

(c) *Content of request for expedited relief*—Any Request for Expedited Relief must contain the following:

(1) a clear and concise statement of the facts and issues on which the request is based;

(2) a clear and concise statement describing the nature of any security interests in any assets of the credit union;

(3) a clear and concise statement of the probable, imminent and irreparable harm likely to occur if expedited relief is not granted;

(4) an assessment of the likelihood of success on the merits of the underlying claim, including statutory citations and relevant documentation supporting the merits of the claim;

(5) any other relevant documentation that supports the request;

(6) citations to applicable statutes, regulations, or other legal authority; and

(7) a signed statement certifying that a copy of the request has been mailed or hand delivered to the liquidating agent on or before the day that the request was filed with the Board.

(d) *Burden of proof*—The burden of proving entitlement to expedited relief rests at all times with the requester.

(e) *Additional information*—The Board may order the filing of additional information and/or documentation in order to make its determination. Such filing shall be on a date certain, and failure to provide the additional documentation or information may constitute the sole grounds for denial of the request.

(f) *Decision*—Before the end of the 90-day period beginning on the date a request is filed, the Board shall render its decision and provide it to the requester. The Board will determine whether to grant expedited review and allow or disallow the claim or whether such claim should be resolved pursuant to the claims process described in Section 709.6 of this Part.

(1) *Expedited review denied*—A decision by the Board that expedited review is not appropriate shall be final and the claim shall be decided pursuant to the claims adjudication process set forth in Section 709.6 of this Part.

(2) *Expedited review granted*—If expedited review is granted, the Board shall decide the claim. If the claim is disallowed, in whole or part, the decision shall contain a statement of each reason for the disallowance and the procedure for obtaining judicial review.

(g) *Period for filing or renewing suit*—Any claimant who files a request for expedited relief shall be permitted to file a suit, or to continue a suit filed before the appointment of the liquidating agent, seeking a determination of the claimant's

rights with respect to its security interest after the earlier of:

(1) the end of the 90-day period beginning on the date of the filing of a request for expedited relief; or

(2) the date the Board denies all or part of the claim.

§ 709.10 Treatment by conservator or liquidating agent of financial assets transferred in connection with a securitization or participation.

(a) *Definitions.* (1) *Beneficial interest* means debt or equity (or mixed) interests or obligations of any type issued by a special purpose entity that entitle their holders to receive payments that depend primarily on the cash flow from financial assets owned by the special purpose entity.

(2) *Financial asset* means cash or a contract or instrument that conveys to one entity a contractual right to receive cash or another financial instrument from another entity.

(3) *Legal isolation* means that transferred financial assets have been put presumptively beyond the reach of the transferor, its creditors, a trustee in bankruptcy, or a receiver, either by a single transaction or a series of transactions taken as a whole.

(4) *Participation* means the transfer or assignment of an undivided interest in all or part of a loan or a lease from a seller, known as the "lead," to a buyer, known as the "participant," without recourse to the lead, under an agreement between the lead and the participant. *Without recourse* means that the participation is not subject to any agreement that requires the lead to repurchase the participant's interest or to otherwise compensate the participant due to a default on the underlying obligation.

(5) *Securitization* means the issuance by a special purpose entity of beneficial interests:

(i) The most senior class of which at time of issuance is rated in one of the four highest categories assigned to long-term debt or in an equivalent short-term category (within either of which there may be sub-categories or gradations indicating relative standing) by one or more nationally recognized statistical rating organizations; or

(ii) Which are sold in transactions by an issuer not involving any public offering for purposes of section 4 of the Securities Act of 1933, as amended, or in transactions exempt from registration under such Act under 17 CFR 230.91 through 230.905 (Regulation S) thereunder (or any successor regulation).

(6) *Special purpose entity* means a trust, corporation, or other entity demonstrably distinct from the federally-insured credit union that is primarily engaged in acquiring and holding (or transferring to another special purpose entity) financial assets, and in activities related or incidental thereto, in connection with the issuance by such special purpose entity (or by another special purpose entity that acquires financial assets directly or indirectly from such special purpose entity) of beneficial interests.

(b) The Board, by exercise of its authority to disaffirm or repudiate contracts under 12 U.S.C. 1787(c), will not reclaim, recover, or recharacterize as property of the credit union or the liquidation estate any financial assets transferred to another party by a federally-insured credit union in connection with a securitization or participation, provided that a transfer meets all conditions for sale accounting treatment under generally accepted accounting principles, other than the "legal isolation" condition addressed by this section.

(c) Paragraph (b) of this section will not apply unless the federally-insured credit union received adequate consideration for the transfer of financial assets at the time of the transfer, and the documentation effecting the transfer of financial assets reflects the intent of the parties to treat the transaction as a sale, and not as a secured borrowing, for accounting purposes.

(d) Paragraph (b) of this section will not be construed as waiving, limiting, or otherwise affecting the power of the Board, as conservator or liquidating agent, to disaffirm or repudiate any agreement imposing continuing obligations or duties upon the federally-insured credit union in conservatorship or the liquidation estate.

(e) Paragraph (b) of this section will not be construed as waiving, limiting or otherwise affecting the rights or powers of the Board to take any action or to exercise any power not specifically limited by this section, including, but not limited to, any rights, powers or remedies of the Board regarding transfers taken in contemplation of the credit union's insolvency or with the intent to hinder, delay, or defraud the credit union or the creditors of such credit union, or that is a fraudulent transfer under applicable law.

(f) The Board will not seek to avoid an otherwise legally enforceable securitization agreement or

participation agreement executed by a federally-insured credit union solely because such agreement does not meet the "contemporaneous" requirement of sections 207(b)(9) and 208(a)(3) of the Federal Credit Union Act.

(g) This section may be repealed by the NCUA upon 30 days notice and opportunity for comment provided in the **Federal Register**, but any such repeal or amendment will not apply to any transfers of financial assets made in connection with a securitization or participation that was in effect before such repeal or modification. For purposes of this paragraph, a securitization would be in effect on the earliest date that the most senior level of beneficial interests is issued, and a participation would be in effect on the date that the parties executed the participation agreement.

§ 709.11 Treatment by conservator or liquidating agent of collateralized public funds.

An agreement to provide for the lawful collateralization of funds of a federal, state, or local governmental entity or of any depositor or member referred to in section 207(k)(2)(A) of the Act will not be deemed to be invalid under sections 207(b)(9) and 208(a)(3) of the Act solely because such agreement was not executed contemporaneously with the acquisition of collateral or with any changes, increases, or substitutions in the collateral made in accordance with such agreement, provided the following conditions are met:

(a) The agreement was undertaken in the ordinary course of business, not in contemplation of insolvency, and with no intent to hinder, delay or defraud the credit union or its creditors;

(b) The secured obligation represents a bona fide and arm's length transaction;

(c) The secured party or parties are not insiders or affiliates of the credit union;

(d) The grant or creation of the security interest was for adequate consideration; and,

(e) The security agreement evidencing the security interest is in writing, was approved by the credit union's board of directors, and has been continuously an official record of the credit union from the time of its execution.

§ 709.12 Prepayment Fees to Federal Home Loan Bank.

The Board as conservator or liquidating agent of a federally-insured credit union in receipt of any extension of credit from a Federal Home Loan Bank will allow a claim for a prepayment fee by the Bank if:

(a) The claim is made pursuant to a written contract that provides for a prepayment fee but the prepayment fee allowed by the Board will not exceed the present value of the loss attributable to the difference between the contract rate of the secured borrowing and the reinvestment rate then available to the Bank; and

(b) The indebtedness owed to the Bank is secured by sufficient collateral in which a perfected security interest in favor of the Bank exists or as to which the Bank's security interest is entitled to priority under section 306(d) of the Competitive Equality Banking Act of 1987, 12 U.S.C. 1430(e) footnote (1), or otherwise so that the aggregate of the outstanding principal on the advances secured by the collateral, the accrued but unpaid interest on the outstanding principal and the prepayment fee applicable to the advances can be paid in full from the amounts realized from the collateral. For purposes of this paragraph, the adequacy of the collateral will be determined as of the date the prepayment fees are due and payable under the terms of the written contract.

§ 709.13 Treatment of swap agreements in liquidation or conservatorship.

The Board has determined that a swap agreement, as defined in the Federal Deposit Insurance Act at 12 U.S.C. 1821(e)(8)(D)(vi), is a qualified financial contract for purposes of the special treatment for qualified financial contracts provided in 12 U.S.C. 1787(c). Any master agreement for any swap agreement, together with all supplements to such master agreement, will be treated as one swap agreement.

Part 710

Voluntary Liquidation

§ 710.0 Scope.

This Part prescribes the requirements that must be followed to accomplish the voluntary liquidation of a Federal credit union. Federally insured state credit unions are only subject to the notification requirement provided in § 710.9; voluntary liquidation is to be accomplished in accordance with state law or procedures established by the state regulatory authority.

§ 710.1 Definitions.

For the purpose of this Part, the following definitions apply:

(a) *Voluntary liquidation* means the dissolution of a solvent Federal credit union with the assets being sold or collected, liabilities paid, and shares distributed under the direction of the board of directors or its duly appointed liquidating agent.

(b) *Liquidation date* means the date the members vote to approve liquidation.

(c) *Liquidating agent* means the person or persons, including any legally recognized entity, appointed by the board of directors to liquidate the Federal credit union.

§ 710.2 Responsibility for Conducting Voluntary Liquidation.

(a) The board of directors shall be responsible for conserving the assets, for expediting the liquidation, and for equitable distribution of the assets to the members.

(b) After voting to present the question of liquidation to the members, the board of directors may appoint a liquidating agent and delegate all or part of the board's responsibility to such agent and authorize reasonable compensation for the services provided.

(c) The board of directors shall determine that the liquidating agent and all persons who handle or have access to funds of the Federal credit union are adequately covered by surety bond and that either such coverage remains in effect, or the discovery period is extended, for at least four months after final distribution of assets.

(d) Within three days after the decision of the board of directors to submit the question of liquidation to the members, the Regional Director will be notified in writing, setting forth in detail the reasons for the proposed action. A balance sheet and income statement as of the previous month-end will be included with the notification. During the liquidation process, financial statements will be submitted to the Regional Director as requested.

(e) Promptly after the decision to present the question of liquidation to the members, the board of directors or liquidating agent shall develop a written plan for the liquidation of the assets and payment of shares (liquidation plan). The plan should provide for the liquidation of assets and payment of creditors and shareholders within one year of the liquidation date. If the liquidation period is projected to exceed one year, an explanation must be provided in the liquidation plan. A copy of the liquidation plan will be mailed to the Regional Director within 30 days of the date the board of directors votes to present the question of liquidation to the members.

§ 710.3 Approval of the Liquidation Proposal by Members.

(a) When the board of directors decides to present the question of liquidation to the members, it shall act promptly to obtain the members' approval. The members shall be given advance notice of the membership meeting at which the liquidation proposal is to be submitted, in accordance with the provisions of Article V of the Federal Credit Union Bylaws. The notice shall:

(1) Inform members that they have the right to vote on the liquidation proposal in person at the membership meeting called for that purpose or by written ballot to be received no later than the time and date indicated on the notice.

(2) Include or be accompanied by a ballot for the liquidation proposal.

(b) The liquidation proposal must be approved by the affirmative vote of a majority of the Federal credit union members who vote on the proposal.

(c) If the members do not approve the liquidation, the board of directors, or if delegated the authority, the liquidating agent, must decide within seven days whether the Federal credit union should resume operations or, if good cause exists, to resubmit the question of liquidation to the members.

(d) If the members approve the liquidation, neither the members nor the board of directors may rescind the decision to liquidate unless the Regional Director concurs in the rescission.

(e) The Regional Director will be notified in writing of the results of the membership vote on the voluntary liquidation proposal within three days of the date of the vote.

§ 710.4 Transaction of Business During Liquidation.

(a) Immediately upon decision by the board of directors to present the question of liquidation to the members, payments on shares, withdrawal of shares (except for transfer of shares to loans and interest), transfer of shares to another share account, granting of loans, and making of investments other than short-term investments shall be suspended pending action by the members on the proposal to liquidate. Collection of loans and interest, payment of necessary expenses, clearing of share drafts and credit card charges will continue.

(b) Upon approval of the members, payments on shares, withdrawal of shares (except for transfer of shares to loans and interest), transfer of shares to another share account, granting of loans, and making of investments other than short-term investments shall be discontinued permanently. Collection of loans and interest and payment of necessary expenses will continue during the period of liquidation. Members will be notified to discontinue the use of share drafts and credit cards, and items will not be cleared 15 days from the liquidation date.

(c) Approval of the Regional Director must be obtained prior to consummating any sale of assets which would not provide sufficient funds to pay shareholders at par.

§ 710.5 Notice of Liquidation to Creditors.

(a) When approval for liquidation is obtained from the members, the board of directors or the liquidating agent shall cause notice to be given to creditors to present their claims.

(1) Federal credit unions with assets in excess of $5 million as of the month-end prior to the liquidation date shall publish the notice once a week in each of three successive weeks, in a newspaper of general circulation, in each county in which the Federal credit union maintains an office or branch for the transaction of business on the liquidation date. The first notice shall be published within seven days of the liquidation date.

(2) Federal credit unions with assets in excess of $500,000 but less than $5 million as of the month-end prior to the liquidation date shall publish the notice once, in a newspaper of general circulation, in each county in which the Federal credit union maintains an office or branch for the transaction of business on the liquidation date. The notice shall be published within seven days of the liquidation date.

(3) Federal credit unions with assets less than $500,000 as of the month-end prior to the liquidation date shall not be required to publish the notice.

(b) Within 10 days of the liquidation date, a copy of the notice of liquidation shall be mailed to all creditors reflected on the records of the Federal credit union.

(c) Creditors shall be provided 30 days from the liquidation date to submit their claims.

§ 710.6 Distribution of Assets.

(a) With the approval of the Regional Director, a partial pro rata distribution of the Federal credit union's assets may be made to its members from cash funds available on authorization by the board of directors or liquidating agent. Payment of a partial distribution may exclude member accounts of less than $25.00.

(b) After all assets of the Federal credit union have been converted to cash or found to be worthless and all loans and debts owing to it have been collected or found to be uncollectible and all obligations of the Federal credit union have been paid, with the exception of shares due its members, the books shall be closed and the pro rata distribution to the members shall be computed. The computation shall be based on the total amount in each share account.

(c) Promptly after the pro rata distribution to members has been computed, checks shall be drawn for the amounts to be distributed to each

member. The checks shall be mailed to the members at their last known address or handed to them in person.

(d) Unclaimed share accounts, unpaid claims, and unpaid claims of members or creditors who failed to cash their final distribution checks shall be trusteed or escheated in accordance with the laws of the state in which the member or creditor resides.

(e) The Regional Director will be notified in writing within three days when the final distribution of assets to the members is started.

§ 710.7 Retention of Records.

(a) The board of directors or liquidating agent shall appoint a custodian for the Federal credit union's records which are to be retained after the final distribution of assets.

(b) All records of the liquidated Federal credit union necessary to establish that creditors were paid and that assets were equitably distributed to the members shall be retained by the custodian for a period of five years following the date of charter cancellation.

§ 710.8 Certificate of Dissolution and Liquidation.

Within 120 days after the final distribution of assets to members is started, a duly executed Certificate of Dissolution and Liquidation shall be filed with the Regional Director.

§ 710.9 Federally Insured State Credit Unions.

A federally insured state credit union will notify the Regional Director in writing within three days after the board of directors' decision to liquidate is made. A balance sheet and income statement as of the previous month-end and a copy of any liquidation plan will be included with the notification to the Regional Director.

Part 711

Management Official Interlocks

§ 711.1 Authority, Purpose and Scope.

(a) *Authority.* This part is issued under the provisions of the Depository Institution Management Interlocks Act (Interlocks Act) (12 U.S.C. 3201 *et seq*).

(b) *Purpose.* The purpose of the Interlocks Act and this part is to foster competition by generally prohibiting a management official from serving two nonaffiliated depository organizations in situations where the management interlock likely would have an anticompetitive effect.

(c) *Scope.* This part applies to management officials of federally insured credit unions. Section 711.4(c) exempts a management official of a credit union from the prohibitions of the Interlocks Act when the individual serves as a management official of another credit union. Therefore, the Interlocks Act prohibitions contained in this part only apply to a management official of a credit union when that individual also serves as a management official of another type of depository organization (usually a bank or thrift).

§ 711.2 Definitions.

For purposes of this part, the following definitions apply:

(a) *Affiliate.* (1) The term *affiliate* has the meaning given in section 202 of the Interlocks Act (12 U.S.C. 3201). For purposes of that section 202, shares held by an individual include shares held by members of his or her immediate family. "Immediate family" means spouse, mother, father, child, grandchild, sister, brother, or any of their spouses, whether or not any of their shares are held in trust.

(2) For purposes of section 202(3)(B) of the Interlocks Act (12 U.S.C. 3201(3)(B)), an affiliate relationship involving a depository institution based on common ownership does not exist if the appropriate federal supervisory agency determines, after giving the affected persons the opportunity to respond, that the asserted affiliation was established in order to avoid the prohibitions of the Interlocks Act and does not represent a true commonality of interest between the depository organizations. In making this determination, the appropriate Federal supervisory agency considers, among other things, whether a person, including members of his or her immediate family, whose shares are necessary to constitute the group owns a nominal percentage of the shares of one of the organizations and the percentage is substantially disproportionate to that person's ownership of shares in the other organization.

(b) *Area median income* means:

(1) The median family income for the metropolitan statistical area (MSA), if a depository organization is located in an MSA; or

(2) The statewide nonmetropolitan median family income, if a depository organization is located outside an MSA.

(c) *Community* means a city, town, or village, and contiguous or adjacent cities, towns, or villages.

(d) *Contiguous or adjacent cities, towns, or villages* means cities, towns, or villages whose borders touch each other or whose borders are within 10 road miles of each other at their closest points. The property line of an office located in an unincorporated city, town, or village is the boundary line of that city, town, or village for the purpose of this definition.

(e) *Depository holding company* means a bank holding company or a savings and loan holding company (as more fully defined in section 202 of the Interlocks Act (12 U.S.C. 3201) having its principal office located in the United States.

(f) *Depository institution* means a commercial bank (including a private bank), a savings bank, a trust company, a savings and loan association, a building and loan association, a homestead association, a cooperative bank, an industrial bank, or a credit union, chartered under the laws of the United States and having a principal office located in the United States. Additionally, a United States office, including a branch or agency, of a foreign commercial bank is a depository institution.

(g) *Depository institution affiliate* means a depository institution that is an affiliate of a depository organization.

(h) *Depository organization* means a depository institution or a depository holding company.

(i) *District bank* means any State bank operating under the Code of Law of the District of Columbia.

(j) *Low- and moderate-income areas* means census tracts (or, if an area is not in a census tract, block numbering areas delineated by the United States Bureau of the Census) where the median family income is less than 100 percent of the area median income.

(k) *Management official.* (1) The term *management official* means:

(i) A director;

(ii) An advisory or honorary director of a depository institution with total assets of $100 million or more;

(iii) A senior executive officer as that term is defined in 12 CFR 701.14(b)(2), or a person holding an equivalent position regardless of title;

(iv) A branch manager;

(v) A trustee of a depository organization under the control of trustees; and

(vi) Any person who has a representative or nominee serving in any of the capacities in this paragraph (m)(1).

(2) The term *management official* does not include:

(i) A person whose management functions relate exclusively to the business of retail merchandising or manufacturing;

(ii) A person whose management functions relate principally to the business outside the United States of a foreign commercial bank; or

(iii) A person described in the provisions of section 202(4) of the Interlocks Act (12 U.S.C. 3201(4)) (referring to an officer of a State-chartered savings bank, cooperative bank, or trust company that neither makes real estate mortgage loans nor accepts savings).

(l) *Office* means a principal or branch office of a depository institution located in the United States. *Office* does not include a representative office of a foreign commercial bank, an electronic terminal, or a loan production office.

(m) *Person* means a natural person, corporation, or other business entity.

(n) *Relevant metropolitan statistical area (RMSA)* means an MSA, a primary MSA, or a consolidated MSA that is not comprised of designated primary MSAs to the extent that these terms are defined and applied by the Office of Management and Budget.

(o) *Representative or nominee* means a natural person who serves as a management official and has an obligation to act on behalf of another person with respect to management responsibilities. NCUA will find that a person has an obligation to act on behalf of another person only if the first person has an agreement, express or implied, to act on behalf of the second person with respect to management responsibilities. NCUA will determine, after giving the affected persons an opportunity to respond, whether a person is a *representative or nominee.*

(p) *Total assets.* (1) The term *total assets* means assets measured on a consolidated basis and reported in the most recent fiscal year-end Consolidated Report of Condition and Income.

(2) The term *total assets* does not include:

(i) Assets of a diversified savings and loan holding company as defined by section 10(a)(1)(F) of the Home Owners' Loan Act (12 U.S.C. 1467a(a)(1)(F)) other than the assets of its depository institution affiliate;

(ii) Assets of a bank holding company that is exempt from the prohibitions of section 4 of the Bank Holding Company Act of 1956 pursuant to an order issued under section 4(d) of that Act (12 U.S.C. 1843(d)) other than the assets of its depository institution affiliate; or

(iii) Assets of offices of a foreign commercial bank other than the assets of its United States branch or agency.

(q) *United States* includes any State or territory of the United States of America, the District of Columbia, Puerto Rico, Guam, American Samoa, and the Virgin Islands.

§ 711.3 Prohibitions.

(a) *Community.* A management official of a depository organization may not serve at the same time as a management official of an unaffiliated depository organization if the depository organizations in question (or a depository institution affiliate thereof) have offices in the same community.

(b) *RMSA.* A management official of a depository organization may not serve at the same time as a management official of an unaffiliated depository organization if the depository organizations in question (or a depository institution affiliate thereof) have offices in the same RMSA and each depository organization has total assets of $20 million or more.

(c) *Major Assets.* A management official of a depository organization with total assets exceeding

$2.5 billion (or any affiliate thereof) may not serve at the same time as a management official of an unaffiliated depository organization with total assets exceeding $1.5 billion (or any affiliate thereof), regardless of the location of the two depository organizations. The NCUA will adjust these thresholds, as necessary, based on year-to-year change in the average of the Consumer Price Index for the Urban Wage Earners and Clerical Workers, not seasonally adjusted, with rounding to the nearest $100 million. The NCUA will announce the revised thresholds by publishing a notice in the **Federal Register**.

§ 711.4 Interlocking relationships permitted by statute.

The prohibitions of § 711.3 do not apply in the case of any one or more of the following organizations or to a subsidiary thereof:

(a) A depository organization that has been placed formally in liquidation, or which is in the hands of a receiver, conservator, or other official exercising a similar function;

(b) A corporation operating under section 25 or section 25A of the Federal Reserve Act (12 U.S.C. 601 *et seq.* and 12 U.S.C. 611 *et seq.*, respectively) (Edge Corporations and Agreement Corporations);

(c) A credit union being served by a management official of another credit union;

(d) A depository organization that does not do business within the United States except as an incident to its activities outside the United States;

(e) A State-chartered savings and loan guaranty corporation;

(f) A Federal Home Loan Bank or any other bank organized solely to serve depository institutions (a bankers' bank) or solely for the purpose of providing securities clearing services and services related thereto for depository institutions and securities companies;

(g) A depository organization that is closed or is in danger of closing as determined by the appropriate Federal depository institutions regulatory agency and is acquired by another depository organization. This exemption lasts for five years, beginning on the date the depository organization is acquired; and

(h)(1) A diversified savings and loan holding company (as defined in section 10(a)(1)(F) of the Home Owners' Loan Act (12 U.S.C. 1467a(a)(1)(F)) with respect to the service of a director of such company who also is a director of an unaffiliated depository organization if:

(i) Both the diversified savings and loan holding company and the unaffiliated depository organization notify their appropriate Federal depository institutions regulatory agency at least 60 days before the dual service is proposed to begin; and

(ii) The appropriate regulatory agency does not disapprove the dual service before the end of the 60-day period.

(2) The NCUA Board or its designee may disapprove a notice of proposed service if it finds that:

(i) The service cannot be structured or limited so as to preclude an anticompetitive effect in financial services in any part of the United States;

(ii) The service would lead to substantial conflicts of interest or unsafe or unsound practices; or

(iii) The notificant failed to furnish all the information required by NCUA.

(3) The NCUA Board or its designee may require that any interlock permitted under this paragraph (h) be terminated if a change in circumstances occurs with respect to one of the interlocked depository organizations that would have provided a basis for disapproval of the interlock during the notice period.

§ 711.5 Small market share exemption.

(a) *Exemption.* A management interlock that is prohibited by § 711.3(a) or § 711.3(b) is permissible, provided:

(1) The interlock is not prohibited by § 711.3(c); and

(2) The depository organizations (and their depository institution affiliates) hold, in the aggregate, no more than 20% of the deposits, in each RMSA or community in which the depository organizations (or their depository institution affiliates) are located. The amount of deposits will be determined by reference to the most recent annual Summary of Deposits published by the FDIC. This information is available on the Internet at http://www.fdic.gov.

(b) *Confirmation and records.* Each depository organization must maintain records sufficient to support its determination of eligibility for the exemption under paragraph (a) of this section, and must reconfirm that determination on an annual basis.

§ 711.6 General exemption.

(a) *Exemption.* NCUA may, by agency order issued following receipt of an application, exempt an interlock from the prohibitions in § 711.3, if NCUA finds that the interlock would not result in a monopoly or substantial lessening of competition, and would not present other safety and soundness concerns.

(b) *Presumptions.* In reviewing applications for an exemption under this section, NCUA will apply a rebuttable presumption that an interlock will not result in a monopoly or substantial lessening of competition if the depository organization seeking to add a management official:

(1) Primarily serves, low- and moderate-income areas;

(2) Is controlled or managed by persons who are members of a minority group or women;

(3) Is a depository institution that has been chartered for less than two years; or

(4) Is deemed to be in "troubled condition" as defined in § 701.14(b)(3) of this chapter.

(c) *Duration.* Unless a shorter expiration period is provided in the NCUA approval, an exemption permitted by paragraph (a) of this section may continue so long as it would not result in a monopoly or substantial lessening of competition, or be unsafe or unsound. If the NCUA grants an interlock exemption in reliance upon a presumption under paragraph (b) of this section, the interlock may continue for three years, unless otherwise provided in the approval.

§ 711.7 Change in circumstances.

(a) *Termination.* A management official shall terminate his or her service if a change in circumstances causes the service to become prohibited. A change in circumstances may include, but is not limited to, an increase in asset size of an organization, a change in the delineation of the RMSA or community, the establishment of an office, an increase in the aggregate deposits of the depository organization, or an acquisition, merger, consolidation, or reorganization of the ownership structure of a depository organization that causes a previously permissible interlock to become prohibited.

(b) *Transition period.* A management official described in paragraph (a) of this section may continue to serve the depository organization involved in the interlock for 15 months following the date of the change in circumstances. NCUA may shorten this period under appropriate circumstances.

§ 711.8 Enforcement.

Except as provided in this section, NCUA administers and enforces the Interlocks Act with respect to federally insured credit unions, and may refer any case of a prohibited interlocking relationship involving these entities to the Attorney General of the United States to enforce compliance with the Interlocks Act and this part.

Part 712

Credit Union Service Organizations (CUSOs)

§ 712.1 What does this part cover?

This part establishes when a Federal credit union (FCU) can invest in and make loans to CUSOs. CUSOs are subject to review by NCUA. This part does not apply to corporate credit unions that have CUSOs subject to § 704.11 of this title. This part does not apply to state-chartered credit unions or the subsidiaries of state-chartered credit unions that do not have FCU investments or loans.

§ 712.2 How much can an FCU invest in or loan to CUSOs, and what parties may participate?

(a) *Investments.* An FCU's total investments in CUSOs must not exceed, in the aggregate, 1% of its paid-in and unimpaired capital and surplus as of its last calendar year-end financial report.

(b) *Loans.* An FCU's total loans to CUSOs must not exceed, in the aggregate, 1% of its paid-in and unimpaired capital and surplus as of its last calendar year-end financial report. Loan authority is independent and separate from the 1% investment authority of subsection (a) of this section.

(c) *Parties.* An FCU may invest in or loan to a CUSO by itself, or with non-credit union parties.

(d) *Measurement for calculating regulatory limitation.* For purposes of paragraphs (a) and (b) of this section:

(1) *Paid-in and unimpaired capital and surplus* means shares plus post-closing, undivided earnings (this does not include regular reserves or special reserves required by law, regulation or special agreement between the credit union and its regulator or share insurer); and

(2) Total investments in and total loans to CUSOs will be measured consistent with GAAP.

(e) *Divestiture.* If the limitations in paragraph (a) of this section are reached or exceeded because of the profitability of the CUSO and the related GAAP valuation of the investment under the equity method, without an additional cash outlay by the FCU, divestiture is not required. An FCU may continue to invest up to 1% without regard to the increase in the GAAP valuation resulting from a CUSO's profitability.

§ 712.3 What are the characteristics of and what requirements apply to CUSOs?

(a) *Structure.* An FCU can invest in a CUSO only if the CUSO is structured as a corporation, limited liability company, or limited partnership. An FCU may only participate in a limited partnership as a limited partner. For purposes of this part, "corporation" means a legally incorporated corporation as established and maintained under relevant federal or state law. For purposes of this part, "limited partnership" means a legally established limited partnership as established and maintained under relevant state law. For purposes of this part, "limited liability company" means a legally established limited liability company as established and maintained under relevant state law, provided that the FCU obtains written legal advice that the limited liability company is a recognized legal entity under the applicable laws of the state of formation and that the limited liability company is established in a manner that will limit potential exposure of the FCU to no more than the amount of funds invested in, or loaned to, the CUSO.

(b) *Customer base.* An FCU can invest in or loan to a CUSO only if the CUSO primarily serves credit unions, its membership, or the membership of credit unions contracting with the CUSO.

(c) *Federal credit union accounting for financial reporting purposes.* An FCU must account for its investments in or loans to a CUSO in conformity with "generally accepted accounting principles" (GAAP).

(d) *CUSO accounting; audits and financial statements; NCUA access to information.* An FCU must obtain written agreements from a CUSO, prior to investing in or lending to the CUSO, that the CUSO will:

(1) Account for all its transactions in accordance with GAAP;

(2) Prepare quarterly financial statements and obtain an annual opinion audit, by a licensed Certified Public Accountant, on its financial statements in accordance with "generally accepted auditing standards" (GAAS); and

(3) Provide NCUA and its representatives with complete access to any books and records of the CUSO and the ability to review CUSO internal controls, as deemed necessary by NCUA in carrying out its responsibilities under the Act.

(e) *Other laws.* A CUSO must comply with applicable Federal, state and local laws.

§ 712.4 What must an FCU and a CUSO do to maintain separate corporate identities?

(a) *Corporate separateness.* An FCU and a CUSO must be operated in a manner that demonstrates to the public the separate corporate existence of the FCU and the CUSO. Good business practices dictate that each must operate so that:

(1) Its respective business transactions, accounts, and records are not intermingled;

(2) Each observes the formalities of its separate corporate procedures;

(3) Each is adequately financed as a separate unit in the light of normal obligations reasonably foreseeable in a business of its size and character;

(4) Each is held out to the public as a separate enterprise;

(5) The FCU does not dominate the CUSO to the extent that the CUSO is treated as a department of the FCU; and

(6) Unless the FCU has guaranteed a loan obtained by the CUSO, all borrowings by the CUSO indicate that the FCU is not liable.

(b) *Legal opinion.* Prior to an FCU investing in a CUSO, the FCU must obtain written legal advice as to whether the CUSO is established in a manner that will limit potential exposure of the FCU to no more than the loss of funds invested in, or lent to, the CUSO. In addition, if a CUSO in which an FCU has an investment plans to change its structure under § 712.3(a), an FCU must also obtain prior, written legal advice that the CUSO will remain established in a manner that will limit potential exposure of the FCU to no more than the loss of funds invested in, or loaned to, the CUSO. The legal advice must address factors that have led courts to "pierce the corporate veil" such as inadequate capitalization, lack of separate corporate identity, common boards of directors and employees, control of one entity over another, and lack of separate books and records. The legal advice may be provided by independent legal counsel of the investing FCU or the CUSO.

§ 712.5 What activities and services are preapproved for CUSOs?

NCUA may at any time, based upon supervisory, legal, or safety and soundness reasons, limit any CUSO activities or services, or refuse to permit any CUSO activities or services. Otherwise, an FCU may invest in, loan to, and/or contract with only those CUSOs that are sufficiently bonded or insured for their specific operations and engaged in the preapproved activities and services related to the routine daily operations of credit unions. The specific activities listed within each preapproved category are provided in this section as illustrations of activities permissible under the particular category, not as an exclusive or exhaustive list.

(a) *Checking and currency services:*

(1) Check cashing;

(2) Coin and currency services; and

(3) Money order, savings bonds, travelers checks, and purchase and sale of U.S. Mint commemorative coins services;

(b) *Clerical, professional and management services:*

(1) Accounting services;

(2) Courier services;

(3) Credit analysis;

(4) Facsimile transmissions and copying services;

(5) Internal audits for credit unions;

(6) Locator services;

(7) Management and personnel training and support;

(8) Marketing services;

(9) Research services; and

(10) Supervisory committee audits;

(c) *Business loan origination;*

(d) *Consumer mortgage loan origination;*

(e) *Electronic transaction services:*

(1) Automated teller machine (ATM) services;

(2) Credit card and debit card services;

(3) Data processing;

(4) Electronic fund transfer (EFT) services;

(5) Electronic income tax filing;

(6) Payment item processing;

(7) Wire transfer services; and

(8) Cyber financial services;

(f) *Financial counseling services:*

(1) Developing and administering Individual Retirement Accounts (IRA), Keogh, deferred compensation, and other personnel benefit plans;

(2) Estate planning;
(3) Financial planning and counseling;
(4) Income tax preparation;
(5) Investment counseling; and
(6) Retirement counseling;

(g) *Fixed asset services:*
(1) Management, development, sale, or lease of fixed assets; and
(2) Sale, lease, or servicing of computer hardware or software;

(h) *Insurance brokerage or agency:*
(1) Agency for sale of insurance;
(2) Provision of vehicle warranty programs; and
(3) Provision of group purchasing programs;

(i) *Leasing:*
(1) Personal property; and
(2) Real estate leasing of excess CUSO property;

(j) *Loan support services:*
(1) Debt collection services;
(2) Loan processing, servicing, and sales; and
(3) Sale of repossessed collateral;

(k) *Record retention, security and disaster recovery services:*
(1) Alarm-monitoring and other security services;
(2) Disaster recovery services;
(3) Microfilm, microfiche, optical and electronic imaging, CD–ROM data storage and retrieval services;
(4) Provision of forms and supplies; and
(5) Record retention and storage;

(l) *Securities brokerage services;*

(m) *Shared credit union branch (service center) operations;*

(n) *Student loan origination;*

(o) *Travel agency services;*

(p) *Trust and trust-related services:*
(1) Acting as administrator for prepaid legal service plans;
(2) Acting as trustee, guardian, conservator, estate administrator, or in any other fiduciary capacity; and
(3) Trust services.

(q) *Real estate brokerage services.*

(r) *CUSO investments in non-CUSO service providers:* In connection with providing a permissible service, a CUSO may invest in a non-CUSO service provider. The amount of the CUSO's investment is limited to the amount necessary to participate in the service provider, or a greater amount if necessary to receive a reduced price for goods or services.

§ 712.6 What activities and services are prohibited for CUSOs?

General. CUSOs must not acquire control of, either directly or indirectly, another depository financial institution, nor invest in shares, stocks, or obligations of an insurance company, trade association, liquidity facility or similar organization, corporation, or association.

§ 712.7 What must an FCU do to add activities or services that are not preapproved?

In order for an FCU to invest in and/or loan to a CUSO that offers an unpreapproved activity or service, the FCU must first receive NCUA Board approval. The request for NCUA Board approval of an unpreapproved activity or service must include a full explanation and complete documentation of the activity or service and how that activity or service is associated with routine credit union operations. The request must be submitted jointly to your Regional Office and to the Secretary of the Board. The request will be treated as a petition to amend § 712.5 and NCUA will request public comment or otherwise act on the petition within 60 days after receipt. Before you engage in the petition process, you should seek an advisory opinion from NCUA's Office of General Counsel as to whether a proposed activity is already covered by one of the authorized categories without filing a petition to amend the regulation.

§ 712.8 What transaction and compensation limits might apply to individuals related to both an FCU and a CUSO?

(a) *Officials and Senior Management Employees.* The officials, senior management employees, and their immediate family members of an FCU that has outstanding loans or investments in a CUSO must not receive any salary, commission, investment income, or other income or compensation from the CUSO either directly or indirectly, or from any person being served through the CUSO. This provision does not prohibit such FCU officials or senior management employees from assisting in the operation of a CUSO, provided the officials or senior management employees are not compensated by the CUSO. Further, the CUSO may reimburse the FCU for the services

provided by such FCU officials and senior management employees only if the account receivable of the FCU due from the CUSO is paid in full at least every 120 days. For purposes of this paragraph (a), "official" means affiliated credit union directors or committee members. For purposes of this paragraph (a), "senior management employee" means affiliated credit union chief executive officer (typically this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (e.g. Assistant President, Vice President, or Assistant Treasurer/Manager) and the chief financial officer (Comptroller). For purposes of this paragraph (a), "immediate family member" means a spouse or other family members living in the same household.

(b) *Employees.* The prohibition contained in paragraph (a) of this section also applies to FCU employees not otherwise covered if the employees are directly involved in dealing with the CUSO unless the FCU's board of directors determines that the FCU employees' positions do not present a conflict of interest.

(c) *Others.* All transactions with business associates or family members of FCU officials, senior management employees, and their immediate family members, not specifically prohibited by paragraphs (a) and (b) of this section must be conducted at arm's length and in the interest of the FCU.

§ 712.9 When must an FCU comply with this part?

(a) *Investments.* An FCU's investments in CUSOs in existence prior to April 1, 1998, must conform with this part not later than April 1, 2001, unless the Board grants prior approval to continue such investment for a stated period.

(b) *Loans.* An FCU's loans to CUSOs in existence prior to April 1, 1998, must conform with this part not later than April 1, 2001, unless:

(1) The Board grants prior approval to continue the FCU's loan for a stated period; or

(2) Under the terms of its loan agreement, the FCU cannot require accelerated repayment without breaching the agreement.

Part 713

Fidelity Bond and Insurance Coverage for Federal Credit Unions

§ 713.1 What is the scope of this section?

This section provides the requirements for fidelity bonds for Federal credit union employees and officials and for other insurance coverage for losses such as theft, holdup, vandalism, etc., caused by persons outside the credit union.

§ 713.2 What are the responsibilities of a credit union's board of directors under this section?

The board of directors of each Federal credit union must at least annually review its fidelity and other insurance coverage to ensure that it is adequate in relation to the potential risks facing the credit union and the minimum requirements set by the Board.

§ 713.3 What bond coverage must a credit union have?

At a minimum, your bond coverage must:

(a) Be purchased in an individual policy from a company holding a certificate of authority from the Secretary of the Treasury; and

(b) Include fidelity bonds that cover fraud and dishonesty by all employees, directors, officers, supervisory committee members, and credit committee members.

§ 713.4 What bond forms may be used?

(a) The following basic bonds may be used without prior NCUA Board approval:

Credit union form No.	Carrier
Credit Union Blanket Bond Standard Form 23 of the Surety Association of America (revised May 1950).	Various.
Extended Form 23	USFG.
100	CUMIS (only approved for corporate credit union use).
200	CUMIS.
300	CUMIS.
400	CUMIS.
AIG 23	National Union Fire Insurance Co. of Pitts., PA.
Reliance Preferred Form 23	Reliance Insurance Company.
Form 31	ITT Hartford.
Form 24 with Credit Union Endorsement.	Continental (only approved for corporate credit union use).
Form 40325	St. Paul Fire and Marine.
Form F2350	Fidelity & Deposit Co. Of Maryland.
Form 9993 (6/97)	Progressive Casualty Insurance Co.
Credit Union Blanket Bond (1/96).	Cooperativas de Seguros Multiples de Puerto Rico.

(b) To use any of the following, you need prior written approval from the Board:

(1) Any other basic bond form; or

(2) Any rider or endorsement that limits coverage of approved basic bond forms.

§ 713.5 What is the required minimum dollar amount of coverage?

(a) The minimum required amount of fidelity bond coverage for any single loss is computed based on a Federal credit union's total assets.

Assets	Minimum bond
$0 to $10,000	Coverage equal to the credit union's assets.
$10,001 to $1,000,000	$10,000 for each $100,000 or fraction thereof.
$1,000,001 to $50,000,000	$100,000 plus $50,000 for each million or fraction over $1,000,000.
$50,000,001 to $295,000,000	$2,550,000 plus $10,000 for each million or fraction thereof over $50,000,000.
Over $295,000,000	$5,000,000.

(b) This is the minimum coverage required, but a Federal credit union's board of directors should purchase additional coverage when circumstances, such as cash on hand or cash in transit, warrant.

(c) While the above is the required minimum amount of bond coverage, credit unions should maintain increased coverage equal to the greater

of either of the following amounts within thirty days of discovery of the need for such increase:

(1) The amount of the daily cash fund, i.e. daily cash plus anticipated daily money receipts on the credit union's premises, or

(2) The total amount of the credit union's money in transit in any one shipment.

(3) Increased coverage is not required pursuant to paragraph (c) of this section, however, when the credit union temporarily increased its cash fund because of unusual events which cannot reasonably be expected to recur.

(d) Any aggregate limit of liability provided for in a fidelity bond policy must be at least twice the single loss limit of liability. This requirement does not apply to optional insurance coverage.

(e) Any proposal to reduce your required bond coverage must be approved in writing by the NCUA Board at least twenty days in advance of the proposed effective date of the reduction.

§ 713.6 What is the permissible deductible?

(a)(1) The maximum amount of allowable deductible is computed based on a Federal credit union's asset size, as follows:

Assets	Maximum deductible
$0–$100,000	No deductibles allowed.
$100,001–$250,000	$1,000.
$250,001–$1,000,000	$2,000.
Over $1,000,001	$2,000 plus 1/1000 of total assets up to a maximum deductible of $200,000.

(2) The deductibles may apply to one or more insurance clauses in a policy. Any deductibles in excess of the above amounts must receive the prior written permission of the NCUA Board.

(b) A deductible may not exceed 10 percent of a credit union's Regular Reserve unless a separate Contingency Reserve is set up for the excess. In computing the maximum deductible, valuation accounts such as the allowance for loan losses cannot be considered.

§ 713.7 May the NCUA Board require a credit union to secure additional insurance coverage?

The NCUA Board may require additional coverage when the Board determines that a credit union's current coverage is inadequate. The credit union must purchase this additional coverage within 30 days.

Part 714

Leasing

§ 714.1 What does this part cover?

This part covers the standards and requirements that you, a federal credit union, must follow when engaged in the leasing of personal property.

§ 714.2 What are the permissible leasing arrangements?

(a) You may engage in direct leasing. In direct leasing, you purchase personal property from a vendor, becoming the owner of the property at the request of your member, and then lease the property to that member.

(b) You may engage in indirect leasing. In indirect leasing, a third party leases property to your member and you then purchase that lease from the third party for the purpose of leasing the property to your member. You do not have to purchase the leased property if you comply with the requirements of § 714.3.

(c) You may engage in open-end leasing. In an open-end lease, your member assumes the risk and responsibility for any difference in the estimated residual value and the actual value of the property at lease end.

(d) You may engage in closed-end leasing. In a closed-end lease, you assume the risk and responsibility for any difference in the estimated residual value and the actual value of the property at lease end. However, your member is always responsible for any excess wear and tear and excess mileage charges as established under the lease.

§ 714.3 Must you own the leased property in an indirect leasing arrangement?

You do not have to own the leased property in an indirect leasing arrangement if:

(a) You obtain a full assignment of the lease. A full assignment is the assignment of all the rights, interests, obligations, and title in a lease to you, that is, you become the owner of the lease;

(b) You are named as the sole lienholder of the leased property;

(c) You receive a security agreement, signed by the leasing company, granting you a sole lien in the leased property and the right to take possession and dispose of the leased property in the event of a default by the lessee, a default in the leasing company's obligations to you, or a material adverse change in the leasing company's financial condition; and

(d) You take all necessary steps to record and perfect your security interest in the leased property. Your state's Commercial Code may treat the automobiles as inventory, and require a filing with the Secretary of State.

§ 714.4 What are the lease requirements?

(a) Your lease must be a net lease. In a net lease, your member assumes all the burdens of ownership including maintenance and repair, licensing and registration, taxes, and insurance;

(b) Your lease must be a full payout lease. In a full payout lease, you must reasonably expect to recoup your entire investment in the leased property, plus the estimated cost of financing, from the lessee's payments and the estimated residual value of the leased property at the expiration of the lease term; and

(c) The amount of the estimated residual value you rely upon to satisfy the full payout lease requirement may not exceed 25% of the original cost of the leased property unless the amount above 25% is guaranteed. Estimated residual value is the projected value of the leased property at lease end. Estimated residual value must be reasonable in light of the nature of the leased property and all circumstances relevant to the leasing arrangement.

§ 714.5 What is required if you rely on an estimated residual value greater than 25% of the original cost of the leased property?

If the amount of the estimated residual value you rely upon to satisfy the full payout lease requirement of § 714.4(b) exceeds 25% of the original cost of the leased property, a financially capable party must guarantee the excess. The guarantor may be the manufacturer. The guarantor may also be an insurance company with an A.M. Best rating of at least a B+, or with at least the equivalent of an A.M. Best B+ rating from another major rating company. You must obtain or have on file financial documentation demonstrating that the guarantor has the resources to meet the guarantee.

§ 714.6 Are you required to retain salvage powers over the leased property?

You must retain salvage powers over the leased property. Salvage powers protect you from a loss and provide you with the power to take action if there is an unanticipated change in conditions that threatens your financial position by significantly increasing your exposure to risk. Salvage powers allow you:

(a) As the owner and lessor, to take reasonable and appropriate action to salvage or protect the value of the property or your interests arising under the lease; or

(b) As the assignee of a lease, to become the owner and lessor of the leased property pursuant to your contractual rights, or take any reasonable and appropriate action to salvage or protect the value of the property or your interests arising under the lease.

§ 714.7 What are the insurance requirements applicable to leasing?

(a) You must maintain a contingent liability insurance policy with an endorsement for leasing or be named as the co-insured if you do not own the leased property. Contingent liability insurance protects you should you be sued as the owner of the leased property. You must use an insurance company with a nationally recognized industry rating of at least a B+.

(b) Your member must carry the normal liability and property insurance on the leased property. You must be named as an additional insured on the liability insurance policy and as the loss payee on the property insurance policy.

§ 714.8 Are the early payment provisions, or interest rate provisions, applicable in leasing arrangements?

You are not subject to the early payment provisions set forth in § 701.21(c)(6) of this chapter. You are also not subject to the interest rate provisions in § 701.21(c)(7).

§ 714.9 Are indirect leasing arrangements subject to the purchase of eligible obligation limit set forth in § 701.23 of this chapter?

Your indirect leasing arrangements are not subject to the eligible obligation limit if they satisfy the provisions of § 701.23(b)(3)(iv) that require that you make the final underwriting decision and that the lease contract is assigned to you very soon after it is signed by the member and the dealer or leasing company.

§ 714.10 What other laws must you comply with when engaged in leasing?

You must comply with the Consumer Leasing Act, 15 U.S.C. 1667–67f, and its implementing regulation, Regulation M, 12 CFR part 213. You must comply with state laws on consumer leasing, but only to the extent that the state leasing laws are consistent with the Consumer Leasing Act, 15 U.S.C. 1667e, or provide the member with greater protections or benefits than the Consumer Leasing Act. You are also subject to the lending rules set forth in § 701.21 of this chapter, except as provided in § 714.8 and § 714.9 of this part. The lending rules in § 701.21 address the preemption of other state and federal laws that impact on credit transactions.

Part 715

Supervisory Committee Audits and Verifications

§ 715.1 Scope of this part.

This part implements section 202(a)(6)(D) of the Federal Credit Union Act, 12 U.S.C. 1782(a)(6)(D), as added by section 201(a) of the Credit Union Membership Access Act, Pub. L. No. 105–219, 112 Stat. 918 (1998). This part prescribes the responsibilities of the Supervisory Committee to obtain an annual audit of the credit union according to its charter type and asset size, and to conduct a verification of members' accounts.

§ 715.2 Definitions used in this part.

As used in this part:

(a) *Balance sheet audit* refers to the examination of a credit union's assets, liabilities, and equity under generally accepted auditing standards (GAAS) by an independent public accountant for the purpose of opining on the fairness of the presentation on the balance sheet. Credit unions required to file call reports consistent with GAAP should ensure the audited balance sheet is likewise prepared on a GAAP basis. The opinion under this type of engagement would not address the fairness of the presentation of the credit union's income statement, statement of changes in equity (including comprehensive income), or statement of cash flows.

(b) *Compensated person* refers to any accounting/auditing professional, excluding a credit union employee, who is compensated for performing more than one supervisory committee audit and/or verification of members' accounts per calendar year.

(c) *Financial statements* refers to a presentation of financial data, including accompanying notes, derived from accounting records of the credit union, and intended to disclose a credit union's economic resources or obligations at a point in time, or the changes therein for a period of time, in conformity with GAAP, as defined herein, or regulatory accounting procedures. Each of the following is considered to be a financial statement: a balance sheet or statement of financial condition; statement of income or statement of operations; statement of undivided earnings; statement of cash flows; statement of changes in members' equity; statement of revenue and expenses; and statement of cash receipts and disbursements.

(d) *Financial statement audit* (also known as an "opinion audit") refers to an audit of the financial statements of a credit union performed in accordance with GAAS by an independent person who is licensed by the appropriate State or jurisdiction. The objective of a financial statement audit is to express an opinion as to whether those financial statements of the credit union present fairly, in all material respects, the financial position and the results of its operations and its cash flows in conformity with GAAP, as defined herein, or regulatory accounting practices.

(e) *GAAP* is an acronym for "generally accepted accounting principles" which refers to the conventions, rules, and procedures which define accepted accounting practice. GAAP includes both broad general guidelines and detailed practices and procedures, provides a standard by which to measure financial statement presentations, and encompasses not only accounting principles and practices but also the methods of applying them.

(f) *GAAS* is an acronym for "generally accepted auditing standards" which refers to the standards approved and adopted by the American Institute of Certified Public Accountants which apply when an "independent, licensed certified public accountant" audits financial statements. Auditing standards differ from auditing procedures in that "procedures" address acts to be performed, whereas "standards" measure the quality of the performance of those acts and the objectives to be achieved by use of the procedures undertaken. In addition, auditing standards address the auditor's professional qualifications as well as the judgment exercised in performing the audit and in preparing the report of the audit.

(g) *Independent* means the impartiality necessary for the dependability of the compensated auditor's findings. Independence requires the exercise of fairness toward credit union officials, members, creditors and others who may rely upon the report of a supervisory committee audit report.

(h) *Internal control* refers to the process, established by the credit union's board of directors, offi-

cers and employees, designed to provide reasonable assurance of reliable financial reporting and safeguarding of assets against unauthorized acquisition, use, or disposition. A credit union's internal control structure consists of five components: control environment; risk assessment; control activities; information and communication; and monitoring. Reliable financial reporting refers to preparation of Call Reports (NCUA Forms 5300 and 5310) that meet management's financial reporting objectives. Internal control over safeguarding of assets against unauthorized acquisition, use, or disposition refers to prevention or timely detection of transactions involving such unauthorized access, use, or disposition of assets which could result in a loss that is material to the financial statements.

(i) *Reportable conditions* refers to a matter coming to the attention of the independent, compensated auditor which, in his or her judgment, represents a significant deficiency in the design or operation of the internal control structure of the credit union, which could adversely affect its ability to record, process, summarize, and report financial data consistent with the representations of management in the financial statements.

(j) *Report on Examination of Internal Control over Call Reporting* refers to an engagement in which an independent, licensed, certified public accountant or public accountant, consistent with attestation standards, examines and reports on management's written assertions concerning the effectiveness of its internal control over financial reporting in its most recently filed semiannual or year-end Call Report, with a concentration in high risk areas. For credit unions, such high risk areas most often include: lending activity; investing activity; and cash handling and deposit-taking activity.

(k) *State-licensed person* refers to a certified public accountant or public accountant who is licensed by the State or jurisdiction where the credit union is principally located to perform accounting or auditing services for that credit union.

(l) *Supervisory committee* refers to a supervisory committee as defined in Section 111(b) of the Federal Credit Union Act, 12 U.S.C. 1761(b). For some federally-insured state chartered credit unions, the "audit committee" designated by state statute or regulation is the equivalent of a supervisory committee.

(m) *Supervisory committee audit* refers to an engagement under either § 715.5 or § 715.6 of this part.

(n) *Working papers* refers to the principal record, in any form, of the work performed by the auditor and/or supervisory committee to support its findings and/or conclusions concerning significant matters. Examples include the written record of procedures applied, tests performed, information obtained, and pertinent conclusions reached in the engagement, proprietary audit programs, analyses, memoranda, letters of confirmation and representation, abstracts of credit union documents, reviewer's notes, if retained, and schedules or commentaries prepared or obtained in the course of the engagement.

§ 715.3 General responsibilities of the Supervisory Committee.

(a) *Basic.* The supervisory committee is responsible for ensuring that the board of directors and management of the credit union—

(1) Meet required financial reporting objectives and

(2) Establish practices and procedures sufficient to safeguard members' assets.

(b) *Specific.* To carry out the responsibilities set forth in paragraph (a) of this section, the supervisory committee must determine whether:

(1) Internal controls are established and effectively maintained to achieve the credit union's financial reporting objectives which must be sufficient to satisfy the requirements of the supervisory committee audit, verification of members' accounts and its additional responsibilities;

(2) The credit union's accounting records and financial reports are promptly prepared and accurately reflect operations and results;

(3) The relevant plans, policies, and control procedures established by the board of directors are properly administered; and

(4) Policies and control procedures are sufficient to safeguard against error, conflict of interest, self-dealing and fraud.

(c) *Mandates.* In carrying out the responsibilities set forth in paragraphs (a) and (b) of this section, the Supervisory Committee must:

(1) Ensure that the credit union adheres to the measurement and filing requirements for reports filed with the NCUA Board under § 741.6 of this chapter;

(2) Perform or obtain a supervisory committee audit, as prescribed in § 715.4 of this part;

(3) Verify or cause the verification of members' passbooks and accounts against the records of the credit union, as prescribed in § 715.8 of this part;

(4) Act to avoid imposition of sanctions for failure to comply with the requirements of this part, as prescribed in § 715.11 and § 715.12 of this part.

§ 715.4 Audit responsibility of the Supervisory Committee.

(a) *Annual audit requirement.* A federally-insured credit union is required to obtain an annual supervisory committee audit which occurs at least once every calendar year (period of performance) and must cover the period elapsed since the last audit period (period effectively covered).

(b) *Financial statement audit option.* Any federally-insured credit union, whether Federally- or State-chartered and regardless of asset size, may choose to fulfill its Supervisory Committee audit responsibility by obtaining an annual audit of its financial statements performed in accordance with GAAS by an independent person who is licensed to do so by the State or jurisdiction in which the credit union is principally located. (A "financial statement audit" is distinct from a "supervisory committee audit," although a financial statement audit is included among the options for fulfilling the supervisory committee audit requirement. *Compare* § 715.2(c) and (j).)

(c) *Other audit options.* A federally insured credit union which does not choose to obtain a financial statement audit as permitted by subsection (b) must fulfill its supervisory audit responsibility under either of § 715.5 or § 715.6 of this part, whichever is applicable. *See* Table 1. For purposes of this part, a credit union's asset size is the amount of total assets reported in the year-end Call Report (NCUA form 5300) filed for the calendar year-end immediately preceding the period under audit.

Type of Charter	*Asset Size*	*Minimum Audit Required to Fulfill Supervisory Audit Responsibility* [1]	*Part 715 section*
Federal charter	$500 Million or more	Financial statement audit per GAAS by independent, State-licensed person	§ 715.5
	Less than $500 Million but greater than $10 Million	Either financial statement audit or other supervisory committee audit options	
	$10 Million or less	Either of three supervisory committee audit options	
State charter	$500 Million or more	Financial statement audit per GAAS by independent, State-licensed person	§ 715.6
	Less than $500 Million	Either of three supervisory committee audit options unless audit prescribed by State law is more stringent	

[1] The Supervisory Committee audit responsibility under Part 715 can always be fulfilled by obtaining a financial statement audit. § 715.4(b).

§ 715.5 Audit of Federal Credit Unions.

(a) *Total assets of $500 million or greater.* To fulfill its Supervisory Committee audit responsibility, a federal credit union having total assets of $500 million or greater must obtain an annual audit of its financial statements performed in accordance with GAAS by an independent person who is licensed to do so by the State or jurisdiction in which the credit union is principally located.

(b) *Total assets of less than $500 million but more than $10 million.* To fulfill its Supervisory Committee audit responsibility, a Federally-chartered credit union having total assets of less than $500 million but more than $10 Million which does not choose to obtain an audit under § 715.5(a), must obtain an annual supervisory committee audit as prescribed in § 715.7.

(c) *Total assets of $10 million or less.* To fulfill its Supervisory Committee audit responsibility, a Federally-chartered credit union having total assets of $10 million or less must obtain an annual Supervisory Committee audit as prescribed in § 715.7.

(d) *Other requirements.* A federally chartered credit union, regardless of which audit it is required to obtain under this section, must meet other applicable requirements of this part.

§ 715.6 Audit of Federally-insured State-chartered credit unions.

(a) *Total assets of $500 million or greater.* To fulfill its Supervisory Committee audit responsibility, a federally-insured State-chartered credit union having total assets of $500 million or greater must obtain an annual audit of its financial statements performed in accordance with GAAS by an independent person who is licensed to do so by the State or jurisdiction in which the credit union is principally located.

(b) *Total assets of less than $500 million.* To fulfill its Supervisory Committee audit responsibility, a federally-insured State-chartered credit union having total assets of less than $500 million must obtain either an annual supervisory committee audit as prescribed under either § 715.6(a) or § 715.7, or an audit as prescribed by the State or jurisdiction in which the credit union is principally located, whichever audit is more stringent.

(c) *Other requirements.* A federally-insured, state-chartered credit union, regardless of which audit it is required to obtain under this section, must meet other applicable requirements of this part except §§ 715.5 and 715.12.

§ 715.7 Supervisory Committee audit alternatives to a financial statement audit.

A credit union which is not required to obtain a financial statement audit may fulfill its supervisory committee responsibility by any one of the following engagements:

(a) *Balance sheet audit.* A balance sheet audit, as defined in § 715.2(a), performed by a person who is licensed to do so by the State or jurisdiction in which the credit union is principally located; or

(b) *Report on Examination of Internal Control over Call Reporting.* An engagement and report on management's written assertions concerning the effectiveness of internal control over financial reporting in the credit union's most recently filed semiannual or year-end call report (NCUA Form 5300), as defined in § 715.2(j), performed by a person who is licensed to do so by the State or jurisdiction in which the credit union is principally located, and in which management specifies the criteria on which it based its evaluation of internal control; or

(c) *Audit per Supervisory Committee Guide.* An audit performed by the supervisory committee, its internal auditor, or any other qualified person (such as a certified public accountant, public accountant, league auditor, credit union auditor consultant, retired financial institutions examiner, etc.) in accordance with the procedures prescribed in NCUA's *Supervisory Committee Guide.* Qualified persons who are not State-licensed cannot provide assurance services under this subsection.

§ 715.8 Requirements for verification of accounts and passbooks.

(a) *Verification obligation.* The Supervisory Committee shall, at least once every two years, cause the passbooks (including any book, statements of account, or other record approved by the NCUA Board) and accounts of the members to be verified against the records of the treasurer of the credit union.

(b) *Methods.* Any of the following methods may be used to verify members' passbooks and accounts, as appropriate:

(1) *Controlled verification.* A controlled verification of 100 percent of members' share and loan accounts;

(2) *Statistical method.* A sampling method which provides for:

(i) Random selection:

(ii) A sample which is representative of the population from which it was selected;

(iii) An equal chance of selecting each dollar in the population;

(iv) Sufficient accounts in both number and scope on which to base conclusions concerning management's financial reporting objectives; and

(v) Additional procedures to be performed if evidence provided by confirmations alone is not sufficient.

(3) *Non-statistical method.* When the verification is performed by an Independent person licensed by the State or jurisdiction in which the credit union is principally located, the auditor may choose among the sampling methods set forth in paragraphs (b)(1) and (2) of this section and non-statistical sampling methods consistent with GAAS if such methods provide for:

(i) Sufficient accounts in both number and scope on which to base conclusions concerning management's financial reporting objectives to provide assurance that the General Ledger accounts are fairly stated in relation to the financial statements taken as a whole;

(ii) Additional procedures to be performed by the auditor if evidence provided by confirmations alone is not sufficient; and

(iii) Documentation of the sampling procedures used and of their consistency with GAAS (to be provided to the NCUA Board upon request).

(c) *Retention of records.* The supervisory committee must retain the records of each verification of members' passbooks and accounts until it completes the next verification of members' passbooks and accounts.

§ 715.9 Assistance from outside, compensated person.

(a) *Unrelated to officials.* A compensated auditor who performs a Supervisory Committee audit on behalf of a credit union shall not be related by blood or marriage to any management employee, member of either the board of directors, the Supervisory Committee or the credit committee, or loan officer of that credit union.

(b) *Engagement letter.* The engagement of a compensated auditor to perform all or a portion of the scope of a financial statement audit or supervisory committee audit shall be evidenced by an engagement letter. In all cases, the engagement must be contracted directly with the Supervisory Committee. The engagement letter must be signed by the compensated auditor and acknowledged therein by the Supervisory Committee prior to commencement of the engagement.

(c) *Contents of letter.* The engagement letter shall:

(1) Specify the terms, conditions, and objectives of the engagement;

(2) Identify the basis of accounting to be used;

(3) If a Supervisory Committee Guide audit, include an appendix setting forth the procedures to be performed;

(4) Specify the rate of, or total, compensation to be paid for the audit;

(5) Provide that the auditor shall, upon completion of the engagement, deliver to the Supervisory Committee a written report of the audit and notice in writing, either within the report or communicated separately, of any internal control reportable conditions and/or irregularities or illegal acts, if any, which come to the auditor's attention during the normal course of the audit (i.e., no notice required if none noted);

(6) Specify a target date of delivery of the written reports, such target date not to exceed 120 days from date of calendar or fiscal year-end under audit (period covered), unless the supervisory committee obtains a waiver from the supervising NCUA Regional Director;

(7) Certify that NCUA staff and/or the State credit union supervisor, or designated representatives of each, will be provided unconditional access to the complete set of original working papers, either at the offices of the credit union or at a mutually agreed upon location, for purposes of inspection; and

(8) Acknowledge that working papers shall be retained for a minimum of three years from the date of the written audit report.

(d) *Complete scope.* If the engagement is to perform a *Supervisory Committee Guide* audit intended to fully meet the requirements of § 715.7(c), the engagement letter shall certify that the audit will address the complete scope of that engagement;

(e) *Exclusions from scope.* If the engagement is to perform a *Supervisory Committee Guide* audit which will exclude any item required by the applicable section, the engagement letter shall:

(1) Identify the excluded items;

(2) State that, because of the exclusion(s), the resulting audit will not, by itself, fulfill the scope of a supervisory committee audit; and

(3) Caution that the supervisory committee will remain responsible for fulfilling the scope of

a supervisory committee audit with respect to the excluded items.

§ 715.10 Audit report and working paper maintenance and access.

(a) *Audit report.* Upon completion and/or receipt of the written report of a financial statement audit or a supervisory committee audit, the Supervisory Committee must verify that the audit was performed and reported in accordance with the terms of the engagement letter prescribed herein. The Supervisory Committee must submit the report(s) to the board of directors, and provide a summary of the results of the audit to the members of the credit union orally or in writing at the next annual meeting of the credit union. If a member so requests, the Supervisory Committee shall provide the member access to the full audit report. If the National Credit Union Administration ("NCUA") so requests, the Supervisory Committee shall provide NCUA a copy of each of the audit reports it receives or produces.

(b) *Working papers.* The supervisory committee shall be responsible for preparing and maintaining, or making available, a complete set of original working papers supporting each supervisory committee audit. The supervisory committee shall, upon request, provide NCUA staff unconditional access to such working papers, either at the offices of the credit union or at a mutually agreeable location, for purposes of inspecting such working papers.

§ 715.11 Sanctions for failure to comply with this part.

(a) *Sanctions.* Failure of a supervisory committee and/or its independent compensated auditor or other person to comply with the requirements of this section, or the terms of an engagement letter required by this section, is grounds for:

(1) The regional director to reject the supervisory committee audit and provide a reasonable opportunity to correct deficiencies;

(2) The regional director to impose the remedies available in § 715.12, provided any of the conditions specified therein is present; and

(3) The NCUA Board to seek formal administrative sanctions against the supervisory committee and/or its independent, compensated auditor pursuant to section 206(r) of the Federal Credit Union Act, 12 U.S.C. 1786(r).

(b) *State Charters.* In the case of a federally-insured state chartered credit union, NCUA shall provide the state regulator an opportunity to timely impose a remedy satisfactory to NCUA before exercising it authority under § 741.202 of this chapter to impose a sanction permitted under paragraph (a) of this section.

§ 715.12 Statutory audit remedies for Federal credit unions.

(a) *Audit by alternative licensed person.* The NCUA Board may compel a federal credit union to obtain a supervisory committee audit which meets the minimum requirements of § 715.5 or § 715.7, and which is performed by an independent person who is licensed by the State or jurisdiction in which the credit union is principally located, for any fiscal year in which any of the following three conditions is present:

(1) The Supervisory Committee has not obtained an annual financial statement audit or performed a supervisory committee audit; or

(2) The Supervisory Committee has obtained a financial statement audit or performed a supervisory committee audit which does not meet the requirements of part 715 including those in § 715.8.

(3) The credit union has experienced serious and persistent recordkeeping deficiencies as defined in paragraph (c) of this section.

(b) *Financial statement audit required.* The NCUA Board may compel a federal credit union to obtain a financial statement audit performed in accordance with GAAS by an independent person who is licensed by the State or jurisdiction in which the credit union is principally located (even if such audit is not required by § 715.5), for any fiscal year in which the credit union has experienced serious and persistent recordkeeping deficiencies as defined in paragraph (c) of this section. The objective of a financial statement audit performed under this paragraph is to reconstruct the records of the credit union sufficient to allow an unqualified or, if necessary, a qualified opinion on the credit union's financial statements. An adverse opinion or disclaimer of opinion should be the exception rather than the norm.

(c) "*Serious and persistent recordkeeping deficiencies.*" A record-keeping deficiency is "serious" if the NCUA Board reasonably believes that the board of directors and management of the credit union have not timely met financial reporting objectives and established practices and procedures sufficient to safeguard members' assets. A serious recordkeeping deficiency is "persistent" when it continues beyond a usual, expected or reasonable period of time.

Part 716

Privacy of Consumer Financial Information and Appendix

§ 716.1 Purpose and scope.

(a) *Purpose.* This part governs the treatment of nonpublic personal information about consumers by the credit unions listed in paragraph (b) of this section. This part:

(1) Requires a credit union to provide notice to members about its privacy policies and practices;

(2) Describes the conditions under which a credit union may disclose nonpublic personal information about consumers to nonaffiliated third parties; and

(3) Provides a method for consumers to prevent a credit union from disclosing that information to most nonaffiliated third parties by "opting out" of that disclosure, subject to the exceptions in §§ 716.13, 716.14, and 716.15.

(b) *Scope.* (1) This part applies only to nonpublic personal information about individuals who obtain financial products or services for personal, family or household purposes. This part does not apply to information about companies or about individuals who obtain financial products or services for business, commercial or agricultural purposes. This part applies to federally-insured credit unions. This part refers to a federally-insured credit union as "you" or "the credit union."

(2) Nothing in this part modifies, limits, or supersedes the standards governing individually identifiable financial information promulgated by the Secretary of Health and Human Services under the authority of §§ 262 and 264 of the Health Insurance Portability and Accountability Act of 1996 (42 U.S.C. 1320d–1320d–8).

§ 716.2 Rule of construction.

The examples in this part and the sample clauses in appendix A of this part are not exclusive. Compliance with an example or use of a sample clause, to the extent applicable, constitutes compliance with this part.

§ 716.3 Definitions.

As used in this part, unless the context requires otherwise:

(a)(1) *Affiliate* means any company that controls, is controlled by, or is under common control with another company.

(2) *Examples.* (i) An affiliate of a federal credit union is a credit union service organization (CUSO), as provided in 12 CFR part 712, that is controlled by the federal credit union.

(ii) An affiliate of a federally-insured, state-chartered credit union is a company that is controlled by the credit union.

(b)(1) *Clear and conspicuous* means that a notice is reasonably understandable and designed to call attention to the nature and significance of the information in the notice.

(2) *Examples.* (i) *Reasonably understandable.* You make your notice reasonably understandable if you:

(A) Present the information contained in the notice in clear, concise sentences, paragraphs and sections;

(B) Use short, explanatory sentences or bullet lists whenever possible;

(C) Use definite, concrete, everyday words and active voice whenever possible;

(D) Avoid multiple negatives;

(E) Avoid legal and highly technical business terminology wherever possible; and

(F) Avoid explanations that are imprecise and readily subject to different interpretations.

(ii) *Designed to call attention.* You design your notice to call attention to the nature and significance of the information in it if you:

(A) Use a plain-language heading to call attention to the notice;

(B) Use a typeface and type size that are easy to read;

(C) Provide wide margins and ample line spacing;

(D) Use boldface or italics for key words; and

(E) In a form that combines your notice with other information, use distinctive type size, style, and graphic devices, such as shading or sidebars.

(iii) *Notices on web sites.* If you provide notices on a web page, you design your notice to

call attention to the nature and significance of the information in it if you use text or visual cues to encourage scrolling down the page if necessary to view the entire notice and ensure that other elements on the web site (such as text graphics, hyperlinks or sound) do not distract attention form the notice, and you either:

(A) Place the notice on a screen frequently accessed by consumers, such as a home page or a page on which transactions are conducted; or

(B) Place a link on a screen frequently accessed by consumers, such as a home page or a page on which transactions are conducted, that connects directly to the notice and is labeled appropriately to convey the importance, nature and relevance of the notice.

(c) *Collect* means to obtain information that you organize or can retrieve by the name of an individual or by identifying number, symbol, or other identifying particular assigned to the individual, irrespective of the source of the underlying information.

(d) *Company* means any corporation, limited liability company, business trust, general or limited partnership, association or similar organization.

(e)(1) *Consumer* means an individual who obtains or has obtained a financial product or service from you, that is to be used primarily for personal, family or household purposes, or that individual's legal representative.

(2) *Examples.* (i) An individual who provides nonpublic personal information to you in connection with obtaining or seeking to obtain credit union membership is your consumer regardless of whether you establish a member relationship.

(ii) An individual who provides nonpublic personal information to you in connection with using your ATM is your consumer.

(iii) If you hold ownership or servicing rights to an individual's loan, the individual is your consumer, even if you hold those rights in conjunction with one or more financial institutions. (The individual is also a consumer with respect to the other financial institutions involved). This applies, even if you, or another financial institution with those rights, hire an agent to collect on the loan or to provide processing or other services.

(iv) An individual who is a consumer of another financial institution is not your consumer solely because you act as agent for, or provide processing or other services to, that financial institution.

(v) An individual is not your consumer solely because he or she is a participant or a beneficiary of an employee benefit plan that you sponsor or for which you act as a trustee or fiduciary.

(f) *Consumer reporting agency* has the same meaning as in section 603(f) of the Fair Credit Reporting Act (15 U.S.C. 1681a(f)).

(g) *Control* of a company means:

(1) Ownership, control, or power to vote 25 percent or more of the outstanding shares of any class of voting security of the company, directly or indirectly, or acting through one or more other persons;

(2) Control in any manner over the election of a majority of the directors, trustees or general partners (or individuals exercising similar functions) of the company; or

(3) The power to exercise, directly or indirectly, a controlling influence over the management or policies of the company, as the NCUA determines. With respect to state-chartered credit unions, NCUA will consult with the appropriate state regulator prior to making its determination.

(4) *Example.* NCUA will presume a credit union has a controlling influence over the management or policies of a CUSO, if the CUSO is 67% owned by credit unions.

(h) *Credit union* means a federal or state-chartered credit union that the National Credit Union Share Insurance Fund insures.

(i) *Customer* means a consumer who has a customer relationship with a financial institution other than a credit union.

(j) *Customer relationship* means a continuing relationship between a consumer and a financial institution other than a credit union.

(k) *Federal functional regulator* means—

(1) The National Credit Union Administration Board;

(2) The Board of Governors of the Federal Reserve System;

(3) The Office of the Comptroller of the Currency;

(4) The Board of Directors of the Federal Deposit Insurance Corporation;

(5) The Director of the Office of Thrift Supervision; and

(6) The Securities and Exchange Commission.

(l)(1) *Financial institution* means any institution the business of which is engaging in activities that are financial in nature or incidental to such finan-

cial activity as described in section 4(k) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(k)).

(2) Examples of financial institutions may include, but are not limited to: credit unions; banks; insurance companies; securities brokers, dealers, and underwriters; loan brokers and servicers; tax planners and preparation services; personal property appraisers; real estate appraisers; career counselors for employees in financial occupations; digital signature services; courier services; real estate settlement services; manufacturers of computer software and hardware; and travel agencies operated in connection with financial services.

(3) *Financial institution* does not include:

(i) Any person or entity with respect to any financial activity that is subject to the jurisdiction of the Commodity Futures Trading Commission under the Commodity Exchange Act (7 U.S.C. 1 *et seq.*);

(ii) The Federal Agricultural Mortgage Corporation or any entity chartered and operating under the Farm Credit Act of 1971 (12 U.S.C. 2001 *et seq.*); or

(iii) Institutions chartered by Congress specifically to engage in securitizations, secondary market sales (including sales of servicing rights) or similar transactions related to a transaction of a consumer, as long as such institutions do not sell or transfer nonpublic personal information to a nonaffiliated third party.

(m)(1) *Financial product or service* means any product or service that a financial holding company could offer by engaging in an activity that is financial in nature or incidental to such a financial activity under section 4(k) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(k)).

(2) *Financial service* includes your evaluation or brokerage of information that you collect in connection with a request or an application from a consumer for a financial product or service.

(n) *Member* means a consumer who has a member relationship with you. For purposes of this part only, it will include certain nonmembers.

(o)(1) *Member relationship* means a continuing relationship between a consumer and you under which you provide one or more financial products or services to the consumer that are to be used primarily for personal, family or household purposes. As noted in the examples, this will include certain consumers that are not your members.

(2) *Examples.* (i) A consumer has a continuing relationship with you if the consumer:

(A) Is your member as defined in your bylaws;

(B) Is a nonmember who has a share, share draft, or credit card account with you jointly with a member;

(C) Is a nonmember who has a loan that you service;

(D) Is a nonmember who has an account with you and you are a credit union that has been designated as a low-income credit union; or

(E) Is a nonmember who has an account in a federally-insured, state-chartered credit union pursuant to state law.

(ii) A consumer does not, however, have a member relationship with you if the consumer is a nonmember and:

(A) The consumer only obtains a financial product or service in isolated transactions, such as using your ATM to withdraw cash from an account maintained at another financial institution or purchasing travelers checks; or

(B) You sell the consumer's loan and do not retain the rights to service that loan.

(p)(1) *Nonaffiliate third party* means any person except:

(i) Your affiliate; or

(ii) A person employed jointly by you and any company that is not your affiliate (but nonaffiliated third party includes the other company that jointly employs the person).

(q)(1) *Nonpublic personal information* means:

(i) Personally identifiable financial information; and

(ii) Any list, description or other grouping of consumers (and publicly available information pertaining to them) that is derived using any personally identifiable financial information.

(2) *Nonpublic personal information* does not include:

(i) Publicly available information, except as included on a list described in paragraph (q)(1)(ii) of this section; or

(ii) Any list, description, or other grouping of consumers (and publicly available information pertaining to them) that is derived without using any personally identifiable financial information, other than publicly available information.

(3) *Examples of lists.* (i) Nonpublic personal information includes any list of individuals' names and street addresses that is derived in whole or in part using personally identifiable financial information, other than publicly available information, such as account numbers.

(ii) Nonpublic personal information does not include any list of individuals' names and addresses that contains only publicly available information, is not derived using personally identifiable financial information, other than publicly available information, either in whole or in part, and is not disclosed in a manner that indicates that any of the individuals on the list is a consumer of a credit union, other than publicly available information.

(r)(1) *Personally identifiable financial information* means any information:

(i) A consumer provides to you to obtain a financial product or service from you;

(ii) About a consumer resulting from any transaction involving a financial product or service between you and a consumer; or

(iii) You otherwise obtain about a consumer in connection with providing a financial product or service to that consumer.

(2) Personally identifiable financial information does not include publicly available information.

(3) *Examples.* (i) *Information included.* Personally identifiable financial information includes:

(A) Information a consumer provides to you on an application to obtain membership, a loan, credit card or other financial product or service;

(B) Account balance information, payment history, overdraft history, and credit or debit card purchase information;

(C) The fact that an individual is or has been one of your members or has obtained a financial product or service from you;

(D) Any information about your consumer if it is disclosed in a manner that indicates that the individual is or has been your consumer;

(E) Any information that a consumer provides to you or that you or your agent otherwise obtain in connection with collecting on a loan or servicing a loan;

(F) Any information you collect through an Internet "cookie" (an information collecting device from a web server); and

(G) Information from a consumer report.

(ii) *Information not included.* Personally identifiable financial information does not include:

(A) A list of names and addresses of customers of an entity that is not a financial institution; and

(B) Information that does not identify a consumer, such as aggregate information or blind data that does not contain personal identifiers such as account numbers, names, or addresses.

(s)(1) *Publicly available information* means any information that you have a reasonable basis to believe is lawfully made available to the general public from:

(i) Federal, state or local government records;

(ii) Widely distributed media; or

(iii) Disclosures to the general public that are required to be made by federal, state or local law.

(2) *Reasonable basis.* You have a reasonable basis to believe that information is lawfully made available to the general public if you have taken steps to determine:

(i) That the information is of the type that is available to the general public; and

(ii) Whether an individual can direct that the information not be made available to the general public and, if so, that your member or consumer has not done so.

(3) *Examples.* (i) *Government records.* Publicly available information in government records includes information in government real estate records and security interest filings.

(ii) *Widely distributed media.* Publicly available information from widely distributed media includes information from a telephone book, a television or radio program, a newspaper or a web site that is available to the general public on an unrestricted basis. A web site is not restricted merely because an Internet service provider or site operator requires a fee or a password, so long as access is available to the general public.

(iii) *Reasonable basis.* (1) You have a reasonable basis to believe that mortgage information is lawfully made available to the general public if you have determined that the information is of the type included on the public record in the jurisdiction where the mortgage would be recorded.

(2) You have a reasonable basis to believe that an individual's telephone number is lawfully made available to the general public if you have located the telephone number in the telephone book or have been informed by the consumer that the telephone number is not unlisted.

(t) *You* means a federally-insured credit union.

Subpart A—Privacy and Opt Out Notices

§ 716.4 Initial privacy notice to consumers required.

(a) *Initial notice requirement.* You must provide a clear and conspicuous notice that accurately reflects your privacy policies and practices to a:

(1) *Member*, not later than when you establish a member relationship, except as provided in paragraph (e) of this section; and

(2) *Consumer*, before you disclose any nonpublic personal information about the consumer to any nonaffiliated third party, if you make such a disclosure other than as authorized by §§ 716.14 and 716.15.

(b) *When initial notice to a consumer is not required.* You are not required to provide an initial notice to a consumer under paragraph (a) of this section if:

(1) You do not disclose any nonpublic personal information about the consumer to any nonaffiliated third party, other than as authorized by §§ 716.14 and 716.15; and

(2) You do not have a member relationship with the consumer.

(c) *When you establish a member relationship.* (1) *General rule*. You establish a member relationship when you and the consumer enter into a continuing relationship.

(2) *Special rule for loans*. You establish a member relationship with a consumer when you originate, or acquire the servicing rights to a loan to the consumer for personal, household or family purposes and that is the only basis for the member relationship. If you subsequently transfer the servicing rights to that loan to another financial institution, the member relationship transfers with the servicing rights.

(3)(i) *Examples of establishing member relationship*. You establish a member relationship when the consumer:

(A) Becomes your member under your bylaws;

(B) Is a nonmember and opens a credit card account with you jointly with a member under your procedures;

(C) Is a nonmember and executes the contract to open a share or share draft account with you or obtains credit from you jointly with a member, including an individual acting as a guarantor;

(D) Is a nonmember and opens an account with you and you are a credit union designated as a low-income credit union;

(E) Is a nonmember and opens an account with you pursuant to state law and you are a state-chartered credit union.

(ii) *Examples of loan rule*. You establish a member relationship with a consumer who obtains a loan for personal, family, or household purposes when you:

(A) Originate the loan to the consumer and retain the servicing rights; or

(B) Purchase the servicing rights to the consumer's loan.

(d) *Existing members*. When an existing member obtains a new financial product or service that is to be used primarily for personal, family, or household purposes, you satisfy the initial notice requirements of paragraph (a) of this section as follows:

(1) You may provide a revised policy notice, under § 716.8, that covers the member's new financial product or service; or

(2) If the initial, revised, or annual notice that you most recently provided to that member was accurate with respect to the new financial product or service, you do not need to provide a new privacy notice under paragraph (a) of this section.

(e) *Exceptions to allow subsequent delivery of notice.* (1) You may provide the initial notice required by paragraph (a)(1) of this section within a reasonable time after you establish a member relationship if:

(i) Establishing the member relationship is not at the member's election;

(ii) Providing notice not later than when you establish a member relationship would substantially delay the member's transaction and the member agrees to receive the notice at a later time.

(2) *Examples of exceptions*. (i) *Not at member's election*. Establishing a member relationship is not at the member's election if you acquire a member's deposit liability from another financial institution and the member does not have a choice about your acquisition.

(ii) *Substantial delay of member's transaction*. Providing notice not later than when you establish a member relationship would substantially delay the member's transaction when:

(A) You and the individual agree over the telephone to enter into a member relationship involving prompt delivery of the financial product or service; or

(B) You establish a member relationship with an individual under a program authorized by Title IV of the Higher Education Act of 1965 (20 U.S.C. 1070 *et seq.*) or similar student loan programs where loan proceeds are disbursed promptly without prior communication between you and the member.

(iii) *No substantial delay of member's transaction.* Providing notice not later than when you establish a member relationship would not substantially delay the member's transaction when the relationship is initiated in person at your office or through other means by which the member may view the notice, such as on a web site.

(f)(1) *Joint relationships.* If two or more consumers jointly obtain a financial product or service, other than a loan, from you, you may satisfy the requirements of paragraph (a) of this section by providing one initial notice to those consumers jointly.

(2) *Special rule for loans.* (i) You are required to provide an initial notice to a borrower or guarantor on a loan if you share his or her nonpublic personal information with nonaffiliated third parties other than for purposes under §§ 716.13, 716.14 and 716.15. (ii) You may satisfy the annual notice requirements of § 716.6 by providing one notice to those borrowers and guarantors jointly.

(g) *Delivery.* When you are required to deliver an initial privacy notice by this section, you must deliver it according to the methods in § 716.9. If you use a short-form initial notice for nonmember consumers according to § 716.6(c), you may deliver your privacy notice according to § 716.6(c)(3).

§ 716.5 Annual privacy notice to members required.

(a)(1) *General rule.* You must provide a clear and conspicuous notice to members that accurately reflects your privacy policies and practices not less than annually during the continuation of the member relationship. *Annually* means at least once in any period of 12 consecutive months during which that relationship exists. You may define the 12-consecutive-month period, but you must apply it to the member on a consistent basis.

(2) *Example.* You provide a notice annually if you define the 12-consecutive-month period as a calendar year and provide the annual notice to the member once in each calendar year following the calendar year in which you provide the initial notice. For example, if a member opens an account on any day of year one, you must provide an annual notice to that member by December 31 of year two.

(b) (1) *Termination of member relationship.* You are not required to provide an annual notice to a former member.

(2) *Examples.* Your member becomes your former member when:

(i) An individual is no longer your member as defined in your bylaws;

(ii) In the case of a nonmember's share or share draft account, the account is inactive under the credit union's policies;

(iii) In the case of a nonmember's closed-end loan, the loan is paid in full, you charge off the loan, or you sell the loan without retaining servicing rights;

(iv) In the case of a credit card relationship or other open-end credit relationship with a nonmember, you no longer provide any statements or notices to the nonmember concerning that relationship or you sell the credit card receivables without retaining servicing rights; or

(v) You have not communicated with the nonmember about the relationship for a period of twelve consecutive months, other than to provide annual privacy notices or promotional material.

(c) *Delivery.* When you are required to deliver an annual privacy notice by this section, you must deliver it according to the methods in § 716.9.

§ 716.6 Information to be included in initial and annual privacy notices.

(a) *General rule.* The initial and annual privacy notices under §§ 716.4 and 716.5 must include each of the following items of information that applies to you or to the consumers to whom you send your privacy notice, in addition to any other information you wish to provide:

(1) The categories of nonpublic personal information that you collect;

(2) The categories of nonpublic personal information that you disclose;

(3) The categories of affiliates and nonaffiliated third parties to whom you disclose nonpublic personal information, other than those parties to whom you disclose information under §§ 716.14 and 716.15;

(4) The categories of nonpublic personal information about your former members that

you disclose and the categories of affiliates and nonaffiliated third parties to whom you disclose it, other than those parties to whom you disclose information under §§ 716.14 and 716.15;

(5) If you disclose nonpublic personal information to a nonaffiliated third party under § 716.13 (and no other exception applies to that disclosure), a separate statement of the categories of information you disclose and the categories of third parties with whom you have contracted;

(6) An explanation of the consumer's right under § 716.10(a) to opt out of the disclosure of nonpublic personal information to nonaffiliated third parties, including the methods by which the consumer may exercise that right at that time;

(7) Any disclosures that you make under section 603(d)(2)(A)(iii) of the Fair Credit Reporting Act (15 U.S.C. 1681a(d)(2)(A)(iii)) (that is, notices regarding the ability to opt out of disclosure of information among affiliates);

(8) Your policies and practices with respect to protecting the confidentiality and security of nonpublic personal information; and

(9) Any disclosures you make under paragraph (b) of this section.

(b) *Description of nonaffiliated third parties subject to exceptions.* If you disclose nonpublic personal information to third parties as authorized under §§ 716.14 and 716.15, you are not required to list those exceptions in the initial or annual privacy notices required by §§ 716.4 and 716.5. When describing the categories with respect to those parties, you are required to state only that you make disclosures to other nonaffiliated third parties as permitted by law.

(c) *Short-form initial notice with opt out notice for nonmember consumers.* (1) You may satisfy the initial notice requirements in §§ 716.4(a)(2), 716.7(b), and 716.7(c) for a consumer who is not a member by providing a short-form initial notice at the same time as you deliver an opt out notice as required in § 716.7.

(2) A short-form initial notice must:

(i) Be clear and conspicuous;

(ii) State that your privacy notice is available upon request; and

(iii) Explain a reasonable means by which the consumer may obtain that notice.

(3) You must deliver your short-form initial notice according to § 716.9. You are not required to deliver your privacy notice with your short form initial notice. You instead may simply provide the consumer a reasonable means to obtain your privacy notice. If a consumer who receives your short-form notice requests your privacy notice, you must deliver your privacy notice according to § 716.9.

(4) *Examples of obtaining privacy notice.* You provide a reasonable means by which a consumer may obtain a copy of your privacy notice if you:

(i) Provide a toll-free telephone number that the consumer may call to request the notice; or

(ii) For a consumer who conducts business in person at your office, maintain copies of the notice on hand that you provide to a consumer immediately upon request.

(d) *Future disclosures.* Your notice may include:

(1) Categories of nonpublic personal information that you reserve the right to disclose in the future, but do not currently disclose; and

(2) Categories of affiliates or nonaffiliated third parties to whom you reserve the right in the future to disclose, but to whom you do not currently disclose, nonpublic personal information.

(e) *Examples.* (1) *Categories of nonpublic personal information that you collect.*

You satisfy the requirement to categorize the nonpublic personal information that you collect if you list the following categories, as applicable:

(i) Information from the consumer;

(ii) Information about the consumer's transactions with you or your affiliates;

(iii) Information about the consumer's transactions with nonaffiliated third parties; and

(iv) Information from a consumer reporting agency.

(2) *Categories of nonpublic personal information you disclose.* (i) You satisfy the requirement to categorize the nonpublic personal information that you disclose if you list the categories described in paragraph (e)(1) of this section, as applicable, and a few examples to illustrate the types of information in each category.

(ii) If you reserve the right to disclose all of the nonpublic personal information about consumers that you collect, you may simply state that fact without describing the categories or examples of the nonpublic personal information you disclose.

(3) *Categories of affiliates and nonaffiliated third parties to whom you disclose.* You satisfy the requirement to categorize the affiliates and

nonaffiliated third parties to whom you disclose nonpublic personal information if you list the following categories, as applicable, and a few examples to illustrate the types of third parties in each category.

(i) Financial service providers;

(ii) Non-financial companies; and

(iii) Others.

(4) *Disclosures under exception for service providers and joint marketers.* If you disclose nonpublic personal information under the exception in § 716.13 to a nonaffiliated third party to market products or services that you offer alone or jointly with another financial institution, you satisfy the disclosure requirement of paragraph (a)(5) of this section if you:

(i) List the categories of nonpublic personal information you disclose, using the same categories and examples you used to meet the requirements of paragraphs (a)(2) of this section, as applicable; and

(ii) State whether the third party is:

(A) A service provider that performs marketing services on your behalf or on behalf of you and another financial institution; or

(B) A financial institution with whom you have a joint marketing agreement.

(5) *Simplified notices.* If you do not disclose, and do not intend to disclose, nonpublic personal information about members or former members to affiliates or nonaffiliated third parties except as authorized under §§ 716.14 and 716.15, you may simply state that fact, in addition to the information you must provide under paragraphs (a)(1), (a)(8), (a)(9) and (c) of this section.

(6) *Confidentiality and security.* You describe your policies and practices with respect to protecting the confidentiality and security of nonpublic personal information if you do both of the following:

(i) Describe in general terms who is authorized to have access to the information.

(ii) State whether you have security practices and procedures in place to ensure the confidentiality of the information in accordance with your policy. You are not required to describe technical information about the safeguards you use.

(7) *Joint notice with affiliates.* You may provide a joint notice from you and one or more of your affiliates or other financial institutions, as specified in the notice, as long as the notice is accurate with respect to you and the other institution.

§ 716.7 Form of opt out notice to consumers and opt out methods.

(a)(1) *Form of opt out notice.* If you are required to provide an opt out notice under § 716.10(a)(1), you must provide a clear and conspicuous notice to each of your consumers that accurately explains the right to opt out under that section. The notice must state:

(i) That you disclose or reserve the right to disclose nonpublic personal information about your consumer to a nonaffiliated third party;

(ii) That the consumer has the right to opt out of that disclosure; and

(iii) A reasonable means by which the consumer may exercise the opt out right.

(2) *Examples.* (i) *Adequate opt out notice.* You provide adequate notice that the consumer can opt out of the disclosure of nonpublic personal information to a nonaffiliated third party if you:

(A) Identify all of the categories of nonpublic personal information that you disclose or reserve the right to disclose and all of the categories of nonaffiliated third parties to whom you disclose the information, as described in § 716.6(a)(2) and (3) and state that the consumer can opt out of the disclosure of that information; and

(B) Identify the financial products or services that the consumer obtains from you, either singly or jointly, to which the opt out direction would apply.

(ii) *Reasonable opt out means.* You provide a reasonable means to exercise an opt out right if you:

(A) Designate check-off boxes in a prominent position on the relevant forms with the opt out notice;

(B) Include a reply form together with the opt out notice;

(C) Provide an electronic means to opt out, such as a form that can be sent via electronic mail or a process at your web site, if the consumer agrees to the electronic delivery of information; or

(D) Provide a toll-free telephone number that consumers may call to opt out.

(iii) *Unreasonable opt out means.* You *do not* provide a reasonable means of opting out if:

(A) The only means of opting out is for the consumer to write his or her own letter to exercise that opt out right; or

(B) The only means of opting out as described in any notice subsequent to the initial notice is to use a check-off box that was provided with the initial notice but not included with the subsequent notice.

(iv) *Specific opt out means.* You may require each consumer to opt out through a specific means, as long as that means is reasonable for that consumer.

(b) *Same form as initial notice permitted.* You may provide the opt out notice together with or on the same written or electronic form as the initial notice you provide in accordance with § 716.4.

(c) *Initial notice required when opt out notice delivered subsequent to initial notice.* If you provide the opt out notice later than required for the initial notice in accordance with § 716.4, you must also include a copy of the initial notice in writing or, if the consumer agrees, electronically.

(d) *Joint relationships.* (1) If two or more consumers jointly obtain a financial product or service, other than a loan, from you, you may provide only a single opt out notice. Your opt out notice must explain how you will treat an opt out direction by a joint consumer as explained in the examples in paragraph (d)(5) of this section.

(2) Any of the joint consumers may exercise the right to opt out. You may either:

(i) Treat an opt out direction by a joint consumer to apply to all of the associated joint consumers; or

(ii) Permit each joint consumer to opt out separately.

(3) If you permit each joint consumer to opt out separately, you must permit one of the joint consumers to opt out on behalf of all of the joint consumers.

(4) You may not require all joint consumers to opt out before you implement any opt out direction.

(5) *Example.* If John and Mary have a joint share account with you and arrange for you to send statements to John's address, you may do any of the following, but you must explain in your opt out notice which opt out policy you will follow:

(i) Send a single opt out notice to John's address, but you must accept an opt out direction from either John or Mary.

(ii) Treat an opt out direction by either John or Mary as applying to the entire account. If you do so, and John opts out, you may not require Mary to opt out as well before implementing John's opt out direction.

(iii) Permit John and Mary to make different opt out directions. If you do so, and if John and Mary both opt out, you must permit one or both of them to notify you in a single response (such as on a form or through a telephone call).

(6) *Special rule for loans.* (i) You are required to provide an initial opt out notice to a borrower or guarantor on a loan if you share his or her nonpublic personal information with nonaffiliated third parties other than for purposes under §§ 716.13, 716.14 and 716.15.

(ii) You may satisfy your annual opt out notice requirement by providing one notice to those borrowers and guarantors jointly.

(e) *Time to comply with opt out.* You must comply with the consumer's opt out direction as soon as reasonably practicable after you receive it.

(f) *Continuing right to opt out.* A consumer may exercise the right to opt out at any time.

(g) *Duration of consumer's opt out direction.* (1) A consumer's direction to opt out under this section is effective until the consumer revokes it in writing or, if the consumer agrees, electronically.

(2) When a member relationship terminates, the member's opt out direction continues to apply to the nonpublic personal information that you collected during or related to the relationship. If the individual subsequently establishes a new member relationship with you, the opt out direction that applied to the former relationship does not apply to the new relationship.

(h) *Delivery.* When you are required to deliver an opt out notice by this section, you must deliver it according to the methods in § 716.9.

§ 716.8 Revised privacy notices.

(a) *General rule.* Except as otherwise authorized in this part, you must not, directly or through any affiliate, disclose any nonpublic personal information about a consumer to a nonaffiliated third party other than as described in the initial notice that you provided to that consumer under § 716.4, unless:

(1) You have provided to the consumer a revised notice that accurately describes your policies and practices;

(2) You have provided to the consumer a new opt out notice;

(3) You have given the consumer a reasonable opportunity, before you disclose the information to the nonaffiliated third party, to opt out of the disclosure; and

(4) The consumer does not opt out.

(b) *Examples.* (1) Except as otherwise permitted by §§ 716.13, 716.14 and 716.15, you must provide a revised notice if you—

(i) Disclose a new category of nonpublic personal information to any nonaffiliated third party;

(ii) Disclose nonpublic personal information to a new category of nonaffiliated third party; or

(iii) Disclose nonpublic personal information about a former member to a nonaffiliated third party, and that former member has not had the opportunity to exercise an opt out right regarding that disclosure.

(2) A revised notice is not required if you disclose nonpublic personal information to a new nonaffiliated third party that you adequately described in your prior notice.

(c) *Delivery.* When you are required to deliver a revised privacy notice by this section, you must deliver it according to the methods in § 716.9.

§ 716.9 Delivering privacy and opt out notices.

(a) *How to provide notices.* You must provide any privacy notices and opt out notices, including short-form initial notices, that this part requires so that each consumer can reasonably be expected to receive actual notice in writing or, if the consumer agrees, electronically.

(b) (1) *Examples of reasonable expectation of actual notice.* You may reasonably expect that a consumer will receive actual notice if you:

(i) Hand-deliver a printed copy of the notice to the consumer;

(ii) Mail a printed copy of the notice to the last known address of the consumer;

(iii) For the consumer who conducts transactions electronically, post the notice on the electronic site and require the consumer to acknowledge receipt of the notice as a necessary step to obtaining a particular financial product or service;

(iv) For an isolated transaction with the consumer, such as an ATM transaction, post the notice on the ATM screen and require the consumer to acknowledge receipt of the notice as a necessary step to obtaining the particular financial product or service.

(2) *Examples of unreasonable expectations of actual notice.* You may not, however, reasonably expect that a consumer will receive actual notice if you:

(i) Only post a sign in your branch or office or generally publish advertisements of your privacy policies and practices;

(ii) Send the notice via electronic mail to a consumer who does not obtain a financial product or service from you electronically.

(c) *Annual notices only.* You may reasonably expect that a member will receive actual notice of your annual privacy notice if:

(1) The member uses your web site to access financial products and services electronically and agrees to receive notices at your web site and you post your current privacy notice continuously in a clear and conspicuous manner on your web site; or

(2) The member has requested that you refrain from sending any information regarding the member relationship, and your current privacy notice remains available to the member upon request.

(d) *Oral description of notice insufficient.* You may not provide any notice required by this part solely by orally explaining the notice, either in person or over the telephone.

(e) *Retention or accessibility of notices for members.* (1) For members only, you must provide the initial notice required by § 716.4 (a)(1), the annual notice required by § 716.5(a) and the revised notice required by § 716.8 so that the member can retain them or obtain them later in writing or, if the member agrees, electronically.

(2) *Examples of retention or accessibility.* You provide the privacy notice to the member so that the member can retain it or obtain it later if you:

(i) Hand-deliver a printed copy of the notice to the member;

(ii) Mail a printed copy of the notice to the last known address of the member upon request of the member; or

(iii) Make your current privacy notice available on a web site (or a link to another web site) for the member who obtains a financial product or service electronically and agrees to receive the notice at the web site.

Subpart B—Limits on Disclosures

§ 716.10 Limits on disclosure of nonpublic personal information to nonaffiliated third parties.

(a)(1) *Conditions for disclosure.* Except as otherwise authorized in this part, you may not, directly or through any affiliate, disclose any nonpublic personal information about a consumer to a nonaffiliated third party unless:

(i) You have provided to the consumer an initial notice as required under § 716.4;

(ii) You have provided to the consumer an opt out notice as required in § 716.7;

(iii) You have given the consumer a reasonable opportunity, before you disclose the information to the nonaffiliated third party, to opt out of the disclosure; and

(iv) The consumer does not opt out.

(2) *Opt out definition.* Opt out means a direction by the consumer that you not disclose nonpublic personal information about that consumer to a nonaffiliated third party, other than as permitted by §§ 716.13, 716.14 and 716.15.

(3) *Examples of reasonable opportunity to opt out.* You provide a consumer with a reasonable opportunity to opt out if:

(i) *By mail.* You mail the notices required in paragraph (a)(1) of this section to the consumer and allow the consumer to opt out by mailing a form, calling a toll-free telephone number, or any other reasonable means within 30 days from the date you mailed the notices.

(ii) *By electronic means.* A member opens an on-line account with you and agrees to receive the notices required in paragraph (a)(1) of this section electronically, and you make the notices available to the member on your web site and allow the member to opt out by any reasonable means within 30 days after the date that the member acknowledges receipt of the notices.

(iii) *Isolated transaction with consumer.* For an isolated transaction, such as the purchase of a traveler's check by a consumer, you provide the consumer with a reasonable opportunity to opt out if you provide the notices required in paragraph (a)(1) of this section at the time of the transaction and request that the consumer decide, as a necessary part of the transaction, whether to opt out before completing the transaction.

(b) *Application of opt out to all consumers and all nonpublic personal information.* (1) You must comply with this section, regardless of whether you and the consumer have established a member relationship.

(2) Unless you comply with this section, you may not, directly or through an affiliate, disclose any nonpublic personal information about a consumer that you have collected, regardless of whether you collected it before or after receiving the direction to opt out from the consumer.

(c) *Partial opt out.* You may allow a consumer to select certain nonpublic personal information or certain nonaffiliated third parties with respect to which the consumer wishes to opt out.

§ 716.11 Limits on redisclosure and reuse of information.

(a)(1) *Information you receive under an exception.* If you receive nonpublic personal information from a nonaffiliated financial institution under an exception in § 716.14 or 716.15 of this part, your disclosure and use of that information is limited as follows:

(i) You may disclose the information to the affiliates of the financial institution from which you received the information; and

(ii) You may disclose the information to your affiliates, but your affiliates may, in turn, disclose and use the information only to the extent that you may disclose and use the information; and

(iii) You may disclose and use the information pursuant to an exception in § 716.14 or 716.15 in the ordinary course of business to carry out the activity covered by the exception under which you received the information.

(2) *Example.* If you receive a member list from a credit union in order to provide correspondent services under the exception in § 716.14(a), you may disclose that information under any exception in § 716.14 or 716.15 in order to provide those services. For example, you could disclose the information in response to a properly authorized subpoena or to your attorneys, accountants, and auditors. You could not disclose that information to a third party for marketing purposes or use that information for your own marketing purposes.

(b)(1) *Information you receive outside of an exception.* If you receive nonpublic personal information from a nonaffiliated financial institution

other than under an exception in § 716.14 or 716.15 of this part, you may disclose the information only:

(i) To the affiliates of the financial institution from which you received the information;

(ii) To your affiliates, but your affiliates may, in turn, disclose the information only to the extent that you can disclose the information;

(iii) To any other person, if the disclosure would be lawful if made directly to that person by the financial institution from which you received the information; and

(iv) Pursuant to an exception in § 716.14 or 716.15.

(2) *Example.* If you obtain a customer list from a nonaffiliated financial institution outside of the exceptions in §§ 716.14 and 716.15,

(i) You may use the list for your own purposes;

(ii) You may disclose that list to another non-affiliated third party only if the financial institution from which you purchased the list could have disclosed the list to that third party, that is you may disclose the list in accordance with the privacy policy of the financial institution from which you received the list, as limited by the opt out direction of each consumer whose nonpublic personal information you intend to disclose; and

(iii) You may disclose that list as permitted by § 716.14 or 716.15, such as to your attorneys or accountants.

(c) *Information you disclose under an exception.* If you disclose nonpublic personal information to a nonaffiliated third party under an exception in § 716.14 or 716.15 of this part, the disclosure and use of that information by the third party is limited as follows:

(1) The third party may disclose the information to your affiliates;

(2) The third party may disclose the information to its affiliates, but its affiliates may, in turn, disclose and use the information only to the extent that the third party may disclose and use the information; and

(3) The third party may disclose and use the information pursuant to an exception in § 716.14 or 716.15 in the ordinary course of business to carry out the activity covered by the exception under which it received the information.

(d) *Information you disclose outside of an exception.* If you disclose nonpublic personal information to a nonaffiliated third party other than under an exception in § 716.14 or 716.15 of this part, the third party may disclose the information only:

(1) To your affiliates;

(2) To its affiliates, but its affiliates, in turn, may disclose the information only to the extent the third party can disclose the information;

(3) To any other person, if the disclosure would be lawful if made directly to that person by you; and

(4) Pursuant to an exception in § 716.14 or 716.15.

§ 716.12 Limits on sharing of account number information for marketing purposes.

(a) *General prohibition on disclosure of account numbers.* You must not, directly or through an affiliate, disclose, other than to a consumer reporting agency, an account number or similar form of access number or access code for a consumer's credit card account, share account or transaction account to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing through electronic mail to the consumer.

(b) *Exceptions.* Paragraph (a) of this section does not apply if you disclose an account number or similar form of access number or access code:

(1) To your agent or service provider solely in order to perform marketing for your own products or services, as long as the agent or service provider cannot directly initiate charges to the account; or

(2) To a participant in a private label credit card program or an affinity or similar program where the participants in the program are identified to the member when the member enters into the program.

(c) *Examples.* (1) *Account number.* An account number, or similar form of access number or access code, does not include a number or code in an encrypted form, as long as you do not provide the recipient with a means to decode the number or code.

(2) *Transaction account.* A transaction account is an account other than a share or credit card account. A transaction account does not include an account to which a third party cannot initiate a charge.

Subpart C—Exceptions

§ 716.13 Exception to opt out requirements for service providers and joint marketing.

(a) *General rule.* (1) The opt out requirements in §§ 716.7 and 716.10 do not apply when you provide nonpublic personal information to a nonaffiliated third party to perform services for you or functions on your behalf, if you:

(i) Provide the initial notice in accordance with § 716.4; and

(ii) Enter into a contractual agreement with the third party that prohibits the third party from disclosing or using the information other than to carry out the purposes for which you disclosed the information, including use under an exception in § 716.14 or 716.15 in the ordinary course of business to carry out those purposes.

(2) *Example.* If you disclose nonpublic personal information under this section to a financial institution with which you perform joint marketing, your contractual agreement with that institution meets the requirements of paragraph (a)(1)(ii) of this section if it prohibits the institution from disclosing or using the nonpublic personal information except as necessary to carry out the joint marketing or under an exception in § 716.14 or 716.15 in the ordinary course of business to carry out that joint marketing.

(b) *Service may include joint marketing.* The services that a nonaffiliated third party performs for you under paragraph (a) of this section may include marketing of your own products or services or marketing of financial products or services offered pursuant to joint agreements between you and one or more financial institutions.

(c) *Definition of joint agreement.* For purposes of this section, *joint agreement* means a written contract pursuant to which you and one or more financial institutions jointly offer, endorse, or sponsor a financial product or service.

§ 716.14 Exceptions to notice and opt out requirements for processing and servicing transactions.

(a) *Exceptions for processing transactions at consumer's request.* The requirements for initial notice in § 716.4(a)(2), the opt out in §§ 716.7 and 716.10 and service providers and joint marketing in § 716.13 do not apply if you disclose nonpublic personal information as necessary to effect, administer, or enforce a transaction that a consumer requests or authorizes, or in connection with:

(1) Servicing or processing a financial product or service that a consumer requests or authorizes;

(2) Maintaining or servicing the consumer's account with you, or with another entity as part of a private label credit card program or other extension of credit on behalf of such entity; or

(3) A proposed or actual securitization, secondary market sale (including sales of servicing rights) or similar transaction related to a transaction of the consumer.

(b) *Necessary to effect, administer, or enforce a transaction* means that the disclosure is:

(1) Required, or is one of the lawful or appropriate methods, to enforce your rights or the rights of other persons engaged in carrying out the financial transaction or providing the product or service; or

(2) Required, or is a usual, appropriate or acceptable method:

(i) To carry out the transaction or the product or service business of which the transaction is a part, and record, service or maintain the consumer's account in the ordinary course of providing the financial service or financial product;

(ii) To administer or service benefits or claims relating to the transaction or the product or service business of which it is a part;

(iii) To provide a confirmation, statement or other record of the transaction, or information on the status or value of the financial service or financial product to the consumer or the consumer's agent or broker;

(iv) To accrue or recognize incentives or bonuses associated with the transaction that are provided by you or any other party;

(v) In connection with:

(A) The authorization, settlement, billing, processing, clearing, transferring, reconciling or collection of amounts charged, debited, or otherwise paid using a debit, credit or other payment card, check or account number, or by other payment means;

(B) The transfer of receivables, accounts or interests therein; or

(C) The audit of debit, credit or other payment information.

§ 716.15 Other exceptions to notice and opt out requirements.

(a) *Exceptions to opt out requirements.* The requirements for initial notice to consumers in § 716.4(a)(2), the opt out in §§ 716.7 and 716.10 and service providers and joint marketing in § 716.13 do not apply when you disclose nonpublic personal information:

(1) With the consent or at the direction of the consumer, provided that the consumer has not revoked the consent or direction;

(2)(i) To protect the confidentiality or security of your records pertaining to the consumer, service, product or transaction;

(ii) To protect against or prevent actual or potential fraud, unauthorized transactions, claims or other liability;

(iii) For required institutional risk control or for resolving consumer disputes or inquiries;

(iv) To persons holding a legal or beneficial interest relating to the consumer; or

(v) To persons acting in a fiduciary or representative capacity on behalf of the consumer;

(3) To provide information to insurance rate advisory organizations, guaranty funds or agencies, agencies that are rating you, persons that are assessing your compliance with industry standards, and your attorneys, accountants, and auditors;

(4) To the extent specifically permitted or required under other provisions of law and in accordance with the Right to Financial Privacy Act of 1978 (12 U.S.C. 3401 *et seq.*), to law enforcement agencies (including a federal functional regulator, the Secretary of the Treasury, with respect to 31 U.S.C. Chapter 53, Subchapter II (Records and Reports on Monetary Instruments and Transactions) and 12 U.S.C. Chapter 21 (Financial Recordkeeping), a state insurance authority, with respect to any person domiciled in that insurance authority's state that is engaged in providing insurance, and the Federal Trade Commission), self-regulatory organizations, or for an investigation on a matter related to public safety;

(5)(i) To a consumer reporting agency in accordance with the Fair Credit Reporting Act (15 U.S.C. 1681 *et seq.*), or

(ii) From a consumer report reported by a consumer reporting agency;

(6) In connection with a proposed or actual sale, merger, transfer, or exchange of all or a portion of a business or operating unit if the disclosure of nonpublic personal information concerns solely consumers of such business or unit; or

(7)(i) To comply with federal, state or local laws, rules and other applicable legal requirements;

(ii) To comply with a properly authorized civil, criminal or regulatory investigation, or subpoena or summons by federal, state or local authorities; or

(iii) To respond to judicial process or government regulatory authorities having jurisdiction over you for examination, compliance or other purposes as authorized by law.

(b) *Examples of consent and revocation of consent.* (1) A consumer may specifically consent to your disclosure to a nonaffiliated insurance company of the fact that the consumer has applied to you for a mortgage so that the insurance company can offer homeowner's insurance to the consumer.

(2) A consumer may revoke consent by subsequently exercising the right to opt out of future disclosures of nonpublic personal information as permitted under § 716.7(f).

Subpart D—Relation to Other Laws; Effective Date

§ 716.16 Protection of Fair Credit Reporting Act.

Nothing in this part shall be construed to modify, limit, or supersede the operation of the Fair Credit Reporting Act (15 U.S.C. 1681 *et seq.*), and no inference shall be drawn on the basis of the provisions of this part regarding whether information is transaction or experience information under section 603 of that Act.

§ 716.17 Relation to state laws.

(a) *In general.* This part shall not be construed as superseding, altering, or affecting any statute, regulation, order or interpretation in effect in any state, except to the extent that such state statute, regulation, order or interpretation is inconsistent

with the provisions of this part, and then only to the extent of the inconsistency.

(b) *Greater protection under state law.* For purposes of this section, a state statute, regulation, order or interpretation is not inconsistent with the provisions of this part if the protection such statute, regulation, order or interpretation affords any consumer is greater than the protection provided under this part, as determined by the Federal Trade Commission, after consultation with the National Credit Union Administration, on the Federal Trade Commission's own motion or upon the petition of any interested party.

§ 716.18 Effective date; transition rule.

(a) *Effective date.* This part is effective November 13, 2000. In order to provide sufficient time for you to establish policies and systems to comply with the requirements of this part, the National Credit Union Administration Board has extended the time for compliance with this part until July 1, 2001.

(b)(1) *Notice requirement for consumers who were your members on the compliance date.* By July 1, 2001, you must provide an initial notice, as required by § 716.4, to consumers who are your members on July 1, 2001.

(2) *Example.* You provide an initial notice to consumers who are your members on July 1, 2001, if, by that date, you have established a system for providing an initial notice to all new members and have mailed the initial notice to all your existing members.

(c) *Two-year grandfathering of service agreements.* Until July 1, 2002, a contract that you have entered into with a nonaffiliated third party to perform services for you or functions on your behalf satisfies the provisions of § 716.13(a)(2) of this part, even if the contract does not include a requirement that the third party maintain the confidentiality of nonpublic personal information, as long as the agreement was entered into on or before July 1, 2000.

Appendix A to Part 716—Sample Clauses

Credit unions, including a group of affiliates that use a common privacy notice, may use the following sample clauses, if the clause is accurate for each institution that uses the notice.

A–1—Categories of information you collect (all credit unions)

You may use this clause, as applicable, to meet the requirement of § 716.6(a)(1) to describe the categories of nonpublic personal information you collect.

Sample Clause A–1:

We collect nonpublic personal information about you from the following sources:

- Information we receive from you on applications or other forms;
- Information about your transactions with us, our affiliates, or others; and
- Information we receive from a consumer reporting agency.

A–2—Categories of information you disclose (credit unions that disclose outside of the exceptions)

You may use one of these clauses, as applicable, to meet the requirement of § 716.6(a)(2) to describe the categories of nonpublic personal information you disclose. These clauses may be used if you disclose nonpublic personal information other than as permitted by the exceptions in §§ 716.13, 716.14, and 716.15.

Sample Clause A–2, Alternative 1:

We may disclose the following kinds of nonpublic personal information about you:

- Information we receive from you on applications or other forms, such as [*provide illustrative examples, such as "your name, address, social security number, assets, and income"*];
- Information about your transactions with us, our affiliates, or others, such as [*provide illustrative examples, such as "your account balance, payment history, parties to transactions, and credit card usage"*]; and
- Information we receive from a consumer reporting agency, such as [*provide illustrative examples, such as "your creditworthiness and credit history"*].

Sample Clause A–2, Alternative 2:

We may disclose all of the information that we collect, as described [*describe location in the notice, such as "above" or "below"*].

A–3—Categories of information you disclose and parties to whom you disclose (credit unions that do not disclose outside of the exceptions)

You may use this clause, as applicable, to meet the requirements of § 716.6(a)(2), (3) and (4) to describe the categories of nonpublic personal information about members and former members that you disclose and the categories of affiliates and nonaffiliated third parties to whom you disclose. This clause may be used if you do not disclose nonpublic personal information to any party, other than as permitted by the exceptions in §§ 716.14, and 716.15.

Sample Clause A–3:

We do not disclose any nonpublic personal information about our members and former members to anyone, except as permitted by law.

A–4—Categories of parties to whom you disclose (credit unions that disclose outside of the exceptions)

You may use this clause, as applicable, to meet the requirement of § 716.6(a)(3) to describe the categories of affiliates and nonaffiliated third parties to whom you disclose nonpublic personal information. This clause may be used if you disclose nonpublic personal information other than as permitted by the exceptions in §§ 716.13, 716.14, and 716.15, as well as when permitted by the exceptions in §§ 716.14, and 716.15.

Sample Clause A–4:

We may disclose nonpublic personal information about you to the following types of third parties:

- Financial service providers, such as [*provide illustrative examples, such as "mortgage bankers, securities broker-dealers, and insurance agents"*];
- Non-financial companies, such as [*provide illustrative examples, such as "retailers, direct marketers, airlines, and publishers"*]; and
- Others, such as [*provide illustrative examples, such as "non-profit organizations"*].

We may also disclose nonpublic personal information about you to nonaffiliated third parties as permitted by law.

A–5—Service provider/joint marketing exception

You may use one of these clauses, as applicable, to meet the requirements of § 716.6(a)(5) related to the exception for service providers and joint marketers in § 716.13. If you disclose nonpublic personal information under this exception, you must describe the categories of nonpublic personal information you disclose and the categories of third parties with whom you have contracted.

Sample Clause A–5, Alternative 1:

We may disclose the following information to companies that perform marketing services on our behalf or to other financial institutions with whom we have joint marketing agreements:

- Information we receive from you on applications or other forms, such as [*provide illustrative examples, such as "your name, address, social security number, assets, and income"*];
- Information about your transactions with us, our affiliates, or others, such as [*provide illustrative examples, such as "your account balance, payment history, parties to transactions, and credit card usage"*]; and
- Information we receive from a consumer reporting agency, such as [*provide illustrative examples, such as "your creditworthiness and credit history"].*

Sample Clause A–5, Alternative 2:

We may disclose all of the information we collect, as described [*describe location in the notice, such as "above" or "below"*] to companies that perform marketing services on our behalf or to other financial institutions with whom we have joint marketing agreements.

A–6—Explanation of opt out right (credit unions that disclose outside of the exceptions)

You may use this clause, as applicable, to meet the requirement of § 716.6(a)(6) to provide an explanation of the consumer's right to opt out of the disclosure of nonpublic personal information to nonaffiliated third parties, including the method(s) by which the consumer may exercise that right. This clause may be used if you disclose nonpublic personal information other than as permitted by the exceptions in §§ 716.13, 716.14, and 716.15.

Sample Clause A–6:

If you prefer that we not disclose nonpublic personal information about you to nonaffiliated third parties, you may opt out of those disclosures, that is, you may direct us not to make those disclosures

(other than disclosures permitted by law). If you wish to opt out of disclosures to nonaffiliated third parties, you may [*describe a reasonable means of opting out, such as "call the following toll-free number: (insert number)*].

A–7—Confidentiality and security (all credit unions)

You may use this clause, as applicable, to meet the requirement of § 716.6(a)(8) to describe your policies and practices with respect to protecting the confidentiality and security of nonpublic personal information.

Sample Clause A–7:

We restrict access to nonpublic personal information about you to [*provide an appropriate description, such as "those employees who need to know that information to provide products or services to you"*]. We maintain physical, electronic, and procedural safeguards that comply with federal regulations to guard your nonpublic personal information.

Part 717

Fair Credit Reporting

Subpart A—General Provisions

§ 717.1–717.2 [Reserved]

§ 717.3 Definitions.

As used in this part, unless the context requires otherwise:

(a) [Reserved]
(b) [Reserved]
(c) [Reserved]
(d) [Reserved]
(e) *Consumer* means an individual.
(f) [Reserved]
(g) [Reserved]
(h) [Reserved]
(i) [Reserved]
(j) [Reserved]
(k) [Reserved]
(l) [Reserved]
(m) [Reserved]
(n) [Reserved]
(o) *You* means a Federal credit union.

Subpart I—Duties of Users of Consumer Reports Regarding Identity Theft

§ 717.80–717.82 [Reserved]

§ 717.83 Disposal of consumer information.

(a) *In general.* You must properly dispose of any consumer information that you maintain or otherwise possess in a manner consistent with the Guidelines for Safeguarding Member Information, in appendix A to part 748 of this chapter.

(b) *Examples.* Appropriate measures to properly dispose of consumer information include the following examples. These examples are illustrative only and are not exclusive or exhaustive methods for complying with this section.

(1) Burning, pulverizing, or shredding papers containing consumer information so that the information cannot practicably be read or reconstructed.

(2) Destroying or erasing electronic media containing consumer information so that the information cannot practicably be read or reconstructed.

(c) *Rule of construction.* This section does not:

(1) Require you to maintain or destroy any record pertaining to a consumer that is not imposed under any other law; or

(2) Alter or affect any requirement imposed under any other provision of law to maintain or destroy such a record.

(d) *Definitions.* As used in this section:

(1) *Consumer information* means any record about an individual, whether in paper, electronic, or other form, that is a consumer report or is derived from a consumer report and that is maintained or otherwise possessed by or on behalf of the credit union for a business purpose. Consumer information also means a compilation of such records. The term does not include any record that does not identify an individual.

(i) *Consumer information* includes:

(A) A consumer report that you obtain;

(B) Information from a consumer report that you obtain from your affiliate after the consumer has been given a notice and has elected not to opt out of that sharing;

(C) Information from a consumer report that you obtain about an individual who applies for but does not receive a loan, including any loan sought by an individual for a business purpose;

(D) Information from a consumer report that you obtain about an individual who guarantees a loan (including a loan to a business entity); or

(E) Information from a consumer report that you obtain about an employee or prospective employee.

(ii) *Consumer information* does not include:

(A) Aggregate information, such as the mean credit score, derived from a group of consumer reports; or

(B) Blind data, such as payment history on accounts that are not personally identifiable, you use for developing credit scoring models or for other purposes.

(2) *Consumer report* has the same meaning as set forth in the Fair Credit Reporting Act, 15 U.S.C. 1681a(d). The meaning of consumer report is broad and subject to various definitions, conditions and exceptions in the Fair Credit Reporting Act. It includes written or oral communications from a consumer reporting agency to a third party of information used or collected for use in establishing eligibility for credit or insurance used primarily for personal, family or household purposes, and eligibility for employment purposes. Examples include credit reports, bad check lists, and tenant screening reports.

Part 721

Incidental Powers

§ 721.1 What does this part cover?

This part authorizes a federal credit union (you) to engage in activities incidental to your business as set out in this part. This part also describes how interested parties may request a legal opinion on whether an activity is within a federal credit union's incidental powers or apply to add new activities or categories to the regulation. An activity approved in a legal opinion to an interested party or as a result of an application by an interested party to add new activities or categories is recognized as an incidental powers activity for all federal credit unions. This part does not apply to the activities of corporate credit unions.

§ 721.2 What is an incidental powers activity?

An incidental powers activity is one that is necessary or requisite to enable you to carry on effectively the business for which you are incorporated. An activity meets the definition of an incidental power activity if the activity:

(a) Is convenient or useful in carrying out the mission or business of credit unions consistent with the Federal Credit Union Act;

(b) Is the functional equivalent or logical outgrowth of activities that are part of the mission or business of credit unions; and

(c) Involves risks similar in nature to those already assumed as part of the business of credit unions.

§ 721.3 What categories of activities are preapproved as incidental powers necessary or requisite to carry on a credit union's business?

The categories of activities in this section are preapproved as incidental to carrying on your business under § 721.2. The examples of incidental powers activities within each category are provided in this section as illustrations of activities permissible under the particular category, not as an exclusive or exhaustive list.

(a) *Certification services.* Certification services are services whereby you attest or authenticate a fact for your members' use. Certification services may include such services as notary services, signature guarantees, certification of electronic signatures, and share draft certifications.

(b) *Correspondent services.* Correspondent services are services you provide to other credit unions that you are authorized to perform for your members or as part of your operation. These services may include loan processing, loan servicing, member check cashing services, disbursing share withdrawals and loan proceeds, cashing and selling money orders, performing internal audits, and automated teller machine deposit services.

(c) *Electronic financial services.* Electronic financial services are any services, products, functions, or activities that you are otherwise authorized to perform, provide, or deliver to your members but performed through electronic means. Electronic services may include automated teller machines, electronic fund transfers, online transaction processing through a web site, web site hosting services, account aggregation services, and Internet access services to perform or deliver products or services to members.

(d) *Excess capacity.* Excess capacity is the excess use or capacity remaining in facilities, equipment, or services that: You properly invested in or established, in good faith, with the intent of serving your members; and you reasonably anticipate will be taken up by the future expansion of services to your members. You may sell or lease the excess capacity in facilities, equipment or services such as office space, employees and data processing.

(e) *Financial counseling services.* Financial counseling services means advice, guidance or services that you offer to your members to promote thrift or to otherwise assist members on financial matters. Financial counseling services may include income tax preparation service, electronic tax filing for your members, counseling regarding estate and retirement planning, investment counseling, and debt and budget counseling.

(f) *Finder activities.* Finder activities are activities in which you introduce or otherwise bring together outside vendors with your members so that

the two parties may negotiate and consummate transactions. Finder activities may include offering third party products and services to members through the sale of advertising space on your web site, account statements and receipts, or selling statistical or consumer financial information to outside vendors to facilitate the sale of their products to your members.

(g) *Loan-related products.* Loan-related products are the products, activities or services you provide to your members in a lending transaction that protect you against credit-related risks or are otherwise incidental to your lending authority. These products or activities may include debt cancellation agreements, debt suspension agreements, letters of credit and leases.

(h) *Marketing activities.* Marketing activities are the activities or means you use to promote membership in your credit union and the products and services you offer to your members. Marketing activities may include advertising and other promotional activities such as raffles, membership referral drives, and the purchase or use of advertising.

(i) *Monetary instrument services.* Monetary instrument services are services that enable your members to purchase, sell, or exchange various currencies. These services may include the sale and exchange of foreign currency and U.S. commemorative coins. You may also use accounts you have in foreign financial institutions to facilitate your members' transfer and negotiation of checks denominated in foreign currency or engage in monetary transfer services for your members.

(j) *Operational programs.* Operational programs are programs that you establish within your business to establish or deliver products and services that enhance member service and promote safe and sound operation. Operational programs may include electronic funds transfers, remote tellers, point of purchase terminals, debit cards, payroll deduction, pre-authorized member transactions, direct deposit, check clearing services, savings bond purchases and redemptions, tax payment services, wire transfers, safe deposit boxes, loan collection services, and service fees.

(k) *Stored value products.* Stored value products are alternate media to currency in which you transfer monetary value to the product and create a medium of exchange for your members' use. Examples of stored value products include stored value cards, public transportation tickets, event and attraction tickets, gift certificates, prepaid phone cards, postage stamps, electronic benefits transfer script, and similar media.

(l) *Trustee or custodial services.* Trustee or custodial services are services in which you are authorized to act under any written trust instrument or custodial agreement created or organized in the United States and forming part of a tax-advantaged savings plan, as authorized under the Internal Revenue Code. These services may include acting as a trustee or custodian for member retirement, education and health savings accounts.

§ 721.4 How may a credit union apply to engage in an activity that is not preapproved as within a credit union's incidental powers?

(a) *Application contents.* To engage in an activity that may be within an FCU's incidental powers but that does not fall within a preapproved category listed in § 721.3, you may submit an application by certified mail, return receipt requested, to the NCUA Board. Your application must describe the activity, your explanation, consistent with the test provided in paragraph (c) of this section, of why this activity is within your incidental powers, your plan for implementing the proposed activity, any state licenses you must obtain to conduct the activity, and any other information necessary to describe the proposed activity adequately. Before you engage in the petition process you should seek an advisory opinion from NCUA's Office of General Counsel, as to whether a proposed activity fits into one of the authorized categories or is otherwise within your incidental powers without filing a petition to amend the regulation.

(b) *Processing of application.* Your application must be filed with the Secretary of the NCUA Board. NCUA will review your application for completeness and will notify you whether additional information is required or whether the activity requested is permissible under one of the categories listed in § 721.3. If the activity falls within a category provided in § 721.3, NCUA will notify you that the activity is permissible and treat the application as withdrawn. If the activity does not fall within a category provided in § 721.3, NCUA staff will consider whether the proposed activity is legally permissible. Upon a recommendation by NCUA staff that the activity is within a credit union's incidental powers, the NCUA Board may amend § 721.3 and will request public comment on the establishment of a new category of activities within § 721.3. If the activity proposed in your ap-

plication fails to meet the criteria established in paragraph (c) of this section, NCUA will notify you within a reasonable period of time.

(c) *Decision on application.* In determining whether an activity is authorized as an appropriate exercise of a federal credit union's incidental powers, the Board will consider:

(1) Whether the activity is convenient or useful in carrying out the mission or business of credit unions consistent with the Act;

(2) Whether the activity is the functional equivalent or logical outgrowth of activities that are part of the mission or business of credit unions; and

(3) Whether the activity involves risks similar in nature to those already assumed as part of the business of credit unions.

§ 721.5 What limitations apply to a credit union engaging in activities approved under this part?

You must comply with any applicable NCUA regulations, policies, and legal opinions, as well as applicable state and federal law, if an activity authorized under this part is otherwise regulated or conditioned.

§ 721.6 May a credit union derive income from activities approved under this part?

You may earn income for those activities determined to be incidental to your business.

§ 721.7 What are the potential conflicts of interest for officials and employees when credit unions engage in activities approved under this part?

(a) *Conflicts.* No official, employee, or their immediate family member may receive any compensation or benefit, directly or indirectly, in connection with your engagement in an activity authorized under this part, except as otherwise provided in paragraph (b) of this section. This section does not apply if a conflicts of interest provision within another section of this chapter applies to a particular activity; in such case, the more specific conflicts of interest provision controls. For example: An official or employee that refers loan-related products offered by a third-party to a member, in connection with a loan made by you, is subject to the conflicts of interest provision in § 701.21(c)(8) of this chapter.

(b) *Permissible payments.* This section does not prohibit:

(1) Payment, by you, of salary to your employees;

(2) Payment, by you, of an incentive or bonus to an employee based on your overall financial performance;

(3) Payment, by you, of an incentive or bonus to an employee, other than a senior management employee or paid official, in connection with an activity authorized by this part, provided that your board of directors establishes written policies and internal controls for the incentive program and monitors compliance with such policies and controls at least annually; and

(4) Payment, by a person other than you, of any compensation or benefit to an employee, other than a senior management employee or paid official, in connection with an activity authorized by this part, provided that your board of directors establishes written policies and internal controls regarding third-party compensation and determines that the employee's involvement does not present a conflict of interest.

(c) *Business associates and family members.* All transactions with business associates or family members not specifically prohibited by paragraph (a) of this section must be conducted at arm's length and in the interest of the credit union.

(d) *Definitions.* For purposes of this part, the following definitions apply.

(1) *Senior management employee* means your chief executive officer (typically, this individual holds the title of President or Treasurer/Manager), any assistant chief executive officers (e.g. Assistant President, Vice President, or Assistant Treasurer/Manager), and the chief financial officer (Comptroller).

(2) *Official* means any member of your board of directors, credit committee or supervisory committee.

(3) *Immediate family member* means a spouse or other family member living in the same household.

Part 722

Appraisals

§ 722.1 Authority, Purpose, and Scope.

(a) *Authority.* Part 722 is issued by the National Credit Union Administration ("NCUA") under Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA") (Pub. L. No. 101–73, 103 Stat. 183, 1989) and 12 U.S.C. 1757 and 1766.

(b) *Purpose and Scope.* (1) Title XI provides protection for federal financial and public policy interests in real estate-related transactions by requiring real estate appraisals used in connection with federally related transactions to be performed in writing, in accordance with uniform standards, by appraisers whose competency has been demonstrated and whose professional conduct will be subject to effective supervision. This Part implements the requirements of Title XI and applies to all federally related transactions entered into by the National Credit Union Administration or by federally insured credit unions ("regulated institutions").

(2) This Part:

(i) identifies which real estate-related financial transactions require the services of an appraiser;

(ii) prescribes which categories of federally related transactions shall be appraised by a state-certified appraiser and which by a state-licensed appraiser; and

(iii) prescribes minimum standards for the performance of real estate appraisals in connection with federally related transactions under the jurisdiction of the National Credit Union Administration.

§ 722.2 Definitions.

(a) "Appraisal" means a written statement independently and impartially prepared by a qualified appraiser setting forth an opinion as to the market value of an adequately-described property as of a specific date(s), supported by the presentation and analysis of relevant market information.

(b) "Appraisal Foundation" means the Appraisal Foundation established on November 30, 1987, as a not-for-profit corporation under the laws of Illinois.

(c) "Appraisal Subcommittee" means the Appraisal Subcommittee of the Federal Financial Institutions Examination Council.

(d) "Complex 1-to-4 family residential property appraisal" means one in which the property to be appraised, the form of ownership, or market conditions are atypical.

(e) "Federally related transaction" means any real estate-related financial transaction entered into on or after August 9, 1990, that:

(1) the National Credit Union Administration, or any federally insured credit union, engages in or contracts for; and

(2) requires the services of an appraiser.

(f) "Market value" means the most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably and as suming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

(1) buyer and seller are typically motivated;

(2) both parties are well informed or well advised, and acting in what they consider their own best interests;

(3) a reasonable time is allowed for exposure in the open market;

(4) payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and

(5) the price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.

(g) "Real estate or real property" means an identified parcel or tract of land, including easements, rights of way, undivided or future interests and similar rights in a parcel or tract of land, but does not include mineral rights, timber rights, and growing crops, water rights and similar interests severable from the land when the transaction does not involve the associated parcel or tract of land.

(h) "Real estate-related financial transaction" means any transaction involving:

(1) the sale, lease, purchase, investment in or exchange of real property, including interests in property, or the financing thereof; or

(2) the refinancing of real property or interests in real property; or

(3) the use of real property or interests in property as security for a loan or investment, including mortgage-backed securities.

(i) "State-certified appraiser" means any individual who has satisfied the requirements for certification in a state or territory whose criteria for certification as a real estate appraiser currently meet the minimum criteria for certification issued by the Appraiser Qualification Board of the Appraisal Foundation. No individual shall be a state-certified appraiser unless such individual has achieved a passing grade upon a suitable examination administered by a state or territory that is consistent with and equivalent to the Uniform State Certification Examination issued or endorsed by the Appraiser Qualification Board. In addition, the Appraisal Subcommittee must not have issued a finding that the policies, practices, or procedures of a state or territory are inconsistent with Title XI of FIRREA. The National Credit Union Administration may, from time to time, impose additional qualification criteria for certified appraisers performing appraisals in connection with federally related transactions within its jurisdiction.

(j) "State-licensed appraiser" means any individual who has satisfied the requirements for licensing in a state or territory where the licensing procedures comply with Title XI of FIRREA and where the Appraisal Subcommittee has not issued a finding that the policies, practices, or procedures of the state or territory are inconsistent with Title XI. The NCUA may, from time to time, impose additional qualification criteria for licensed appraisers performing appraisals in connection with federally related transactions within its jurisdiction.

(k) "Tract development" means a project of five units or more that is constructed or is to be constructed as a single development.

(l) "Transaction value" means:

(1) for loans or other extensions of credit, the amount of the loan or extension of credit;

(2) for sales, leases, purchases, and investments in or exchanges of real property, the market value of the real property interest involved; and

(3) for the pooling of loans or interests in real property for resale or purchase, the amount of the loan or market value of the real property calculated with respect to each such loan or interest in real property.

§ 722.3 Appraisals required; transactions requiring a State certified or licensed appraiser.

(a) *Appraisals required.* An appraisal performed by a State certified or licensed appraiser is required for all real estate-related financial transactions except those in which:

(1) The transaction value is $250,000 or less;

(2) A lien on real property has been taken as collateral through an abundance of caution and where the terms of the transaction as a consequence have not been made more favorable than they would have been in the absence of a lien;

(3) A lien on real estate has been taken for purposes other than the real estate's value;

(4) A lease of real estate is entered into, unless the lease is the economic equivalent of a purchase or sale of the leased real estate;

(5) The transaction involves an existing extension of credit at the credit union, provided that:

(i) There is no advancement of new monies, other than funds necessary to cover reasonable closing costs; and

(ii) There has been no obvious and material change in market conditions or physical aspects of the property that threatens the adequacy of the credit union's real estate collateral protection after the transaction;

(6) The transaction involves the purchase, sale, investment in, exchange of, or extension of credit secured by, a loan or interest in a loan, pooled loans, or interests in real property, including mortgage-backed securities, and each loan or interest in a loan, pooled loan, or real property interest met the requirements of this regulation, if applicable, at the time of origination;

(7) The transaction is wholly or partially insured or guaranteed by a United States government agency or United States government sponsored agency;

(8) The transaction either:

(i) Qualifies for sale to a United States government agency or United States government sponsored agency; or

(ii) Involves a residential real estate transaction in which the appraisal conforms to the Federal National Mortgage Association or Federal Home Loan Mortgage Corporation appraisal standards applicable to that category of real estate; or

(9) The regional director has granted a waiver from the appraisal requirement for a category of loans meeting the definition of a member business loan.

(b) *Transactions Requiring a State-Certified Appraiser.*

(1) (All transactions of $1,000,000 or more) All federally related transactions having a transaction value of $1,000,000 or more shall require an appraisal prepared by a state-certified appraiser.

(2) (Nonresidential transactions) All federally related transactions having a transaction value of more than $250,000, other than those involving appraisals of 1-to-4 family residential properties, shall require an appraisal prepared by a state-certified appraiser.

(3) (Complex residential transactions of $250,000 or more) All complex 1-to-4 family residential property appraisals rendered in connection with federally related transactions shall require a state-certified appraiser if the transaction value is $250,000 or more. A regulated institution may presume that appraisals of 1-to-4 family residential properties are not complex unless the institution has readily available information that a given appraisal will be complex. The regulated institution shall be responsible for making the final determination of whether the appraisal is complex. If, during the course of the appraisal, a licensed appraiser identifies factors that would result in the property, form of ownership, or market conditions being considered atypical, then either:

(i) the regulated institution may ask the licensed appraiser to complete the appraisal and have a certified appraiser approve and cosign the appraisal; or

(ii) the institution may engage a certified appraiser to complete the appraisal.

(c) *Transactions Requiring Either a State-Certified or -Licensed Appraiser.* All appraisals for federally related transactions not requiring the services of a state-certified appraiser shall be prepared by either a state-certified appraiser or a state-licensed appraiser.

(d) *Valuation requirement.* Secured transactions exempted from appraisal requirements pursuant to paragraphs (a)(1) and (a)(5) of this section and not otherwise exempted from this regulation or fully insured shall be supported by a written estimate of market value, as defined in this part, performed by an individual having no direct or indirect interest in the property, and qualified and experienced to perform such estimates of value for the type and amount of credit being considered.

(e) *Appraisals to address safety and soundness concerns.* NCUA reserves the right to require an appraisal under this part whenever the agency believes it is necessary to address safety and soundness concerns.

§ 722.4 Minimum appraisal standards.

For federally related transactions, all appraisals shall, at a minimum:

(a) Conform to generally accepted appraisal standards as evidenced by the Uniform Standards of Professional Appraisal Practice (USPAP) promulgated by the Appraisal Standards Board of the Appraisal Foundation, 1029 Vermont Ave., NW., Washington, DC 20005;

(b) Be written and contain sufficient information and analysis to support the institution's decision to engage in the transaction;

(c) Analyze and report appropriate deductions and discounts for proposed construction or renovation, partially leased buildings, non-market lease terms, and tract developments with unsold units;

(d) Be based upon the definition of market value as set forth in § 722.2(f); and

(e) Be performed by State licensed or certified appraisers in accordance with requirements set forth in this part.

§ 722.5 Appraiser Independence.

(a) *Staff Appraiser.* If an appraisal is prepared by a staff appraiser, that appraiser must be independent of the lending, investment, and collection functions and not involved, except as an appraiser, in the federally related transaction, and have no direct or indirect interest, financial or otherwise, in the property. If the only qualified persons available to perform an appraisal are involved in the lending, investment, or collection functions of the credit union, the credit union shall take appropriate steps to ensure that the appraisers exercise independent judgment. Such steps include, but are not limited to, prohibiting an individual from performing an appraisal in connection with feder-

ally related transactions in which the appraiser is otherwise involved.

(b) *Fee Appraisers.* (1) If an appraisal is prepared by a fee appraiser, the appraiser shall be engaged directly by the credit union or its agent and have no direct or indirect interest, financial or otherwise, in the property or the transaction.

(2) A credit union also may accept an appraisal that was prepared by an appraiser engaged directly by another financial services institution; if:

(i) the appraiser has no direct or indirect interest, financial or otherwise, in the property or transaction; and

(ii) the credit union determines that the appraisal conforms to the requirement of this part and is otherwise acceptable.

§ 722.6 Professional Association Membership; Competency.

(a) *Membership in Appraisal Organization.* A state-certified appraiser or a state-licensed appraiser may not be excluded from consideration for an assignment for a federally related transaction solely by virtue of membership or lack of membership in any particular appraisal organization.

(b) *Competency.* All staff and fee appraisers performing appraisals in connection with federally related transactions must be state-certified or -licensed as appropriate. However, a state-certified or -licensed appraiser may not be considered competent solely by virtue of being certified or licensed. Any determination of competency shall be based upon the individual's experience and educational background as they relate to the particular appraisal assignment for which he or she is being considered.

§ 722.7 Enforcement.

Credit unions and institution-affiliated parties, including staff appraisers, may be subject to removal and/or prohibition orders, cease-and-desist orders, and the imposition of civil money penalties pursuant to Section 1786 of the Federal Credit Union Act, or any other applicable law.

Part 723

Member Business Loans

§ 723.1 What is a member business loan?

(a) *General rule.* A member business loan includes any loan, line of credit, or letter of credit (including any unfunded commitments) where the borrower uses the proceeds for the following purposes:

(1) Commercial;

(2) Corporate;

(3) Other business investment property or venture; or

(4) Agricultural.

(b) *Exceptions to the general rule.* The following are not member business loans:

(1) A loan fully secured by a lien on a 1 to 4 family dwelling that is the member's primary residence;

(2) A loan fully secured by shares in the credit union making the extension of credit or deposits in other financial institutions;

(3) Loan(s) to a member or an associated member which, when the net member business loan balances are added together, are equal to less than $50,000;

(4) A loan where a federal or state agency (or its political subdivision) fully insures repayment, or fully guarantees repayment, or provides an advance commitment to purchase in full; or

(5) A loan granted by a corporate credit union to another credit union.

(c) *Loans to credit unions and credit union service organizations.* This part does not apply to loans made by federal credit unions to credit unions and credit union service organizations. This part does not apply to loans made by a federally insured, state-chartered credit union to credit unions and credit union service organizations if the credit union's supervisory authority determines that state law grants authority to lend to these entities other than the general authority to grant loans to members.

(d) *Purchase of member loans and member loan participations.* Any interest a credit union obtains in a loan that was made by another lender to the credit union's member is a member business loan, for purposes of this rule and the risk weighting standards of part 702 of this chapter to the same extent as if made directly by the credit union to its member.

(e) *Purchases of nonmember loans and nonmember loan participations.* Any interest a credit union obtains in a nonmember loan, pursuant to § 701.22 or part 742 of this chapter or other authority, is treated the same as a member business loan for purposes of this rule and the risk weighting standards under part 702 of this chapter, except that the effect of such interest on a credit union's aggregate member business loan limit will be as set forth in § 723.16(b) of this part.

§ 723.2 What are the prohibited activities?

(a) *Who is ineligible to receive a member business loan?* You may not grant a member business loan to the following:

(1) Your chief executive officer (typically this individual holds the title of President or Treasurer/Manager);

(2) Any assistant chief executive officers (e.g., Assistant President, Vice President, or Assistant Treasurer/Manager);

(3) Your chief financial officer (Comptroller); or

(4) Any associated member or immediate family member of anyone listed in paragraphs (a) (1) through (3) of this section.

(b) *Equity agreements/joint ventures.* You may not grant a member business loan if any additional income received by the credit union or senior management employees is tied to the profit or sale of the business or commercial endeavor for which the loan is made.

(c) *Loans to compensated directors.* A credit union may not grant a member business loan to a compensated director unless the board of directors approves granting the loan and the compensated director is recused from the decision making process.

§ 723.3 What are the requirements for construction and development lending?

Except as provided in § 723.4 or unless your Regional Director grants a waiver, loans granted for the construction or development of commercial or residential property are subject to the following additional requirements.

(a) The aggregate of the net member business loan balances for all construction and development loans must not exceed 15% of net worth. In determining the aggregate balances for purposes of this limitation, a credit union may exclude any loan made to finance the construction of a single-family residence if a prospective homeowner has contracted to purchase the property and may also exclude a loan to finance the construction of one single-family residence per member-borrower or group of associated member-borrowers, irrespective of the existence of a contractual commitment from a prospective homeowner to purchase the property.

(b) The borrower must have a minimum of 25% equity interest in the project being financed, the value of which is determined by the market value of the project at the time the loan is made, except that this requirement will not apply in the case of a loan made to finance the construction of a single-family residence if a prospective homeowner has contracted to purchase the property and in the case of one loan to a member-borrower or group of associated member-borrowers to finance the construction of a single-family residence, irrespective of the existence of a contractual commitment from a prospective homeowner to purchase the property. Instead, the collateral requirements of § 723.7 will apply; and

(c) The funds may be released only after onsite, written inspections by qualified personnel and according to a preapproved draw schedule and any other conditions as set forth in the loan documentation.

§ 723.4 What other regulations apply to member business lending?

(a) The provisions of § 701.21(a) through (g) and part 702 of this chapter apply to member business loans granted by credit unions to the extent they are consistent with this part. Except as required by part 741 of this chapter, federally insured State-chartered credit unions are not required to comply with the provisions of § 701.21(a) through (g) of this chapter.

(b) If a federal credit union makes a member business loan as part of a Small Business Administration guaranteed loan program with loan requirements that are less restrictive than those required by NCUA, then the federal credit union may follow the loan requirements of the relevant Small Business Administration guaranteed loan program to the extent they are consistent with this part. A federally insured State-chartered credit union that is subject to this part and makes a member business loan as part of a Small Business Administration guaranteed loan program with loan requirements that are less restrictive than those required by NCUA may follow the loan requirements of the relevant Small Business Administration guaranteed loan program to the extent they are consistent with this part if its state supervisory authority has determined that the credit union has authority to do so under State law.

(c) The collateral and security requirements of § 723.3 and § 723.7 do not apply to member business loans made as part of a Small Business Administration guaranteed loan program.

§ 723.5 How do you implement a member business loan program?

(a) *Generally.* The board of directors must adopt specific business loan policies and review them at least annually. The board must also use the services of an individual with at least two years direct experience with the type of lending the credit union will be engaging in. The experience must provide the credit union sufficient expertise given the complexity and risk exposure of the loans in which the credit union intends to engage. Credit unions do not have to hire staff to meet the requirements of this section but must ensure that the expertise is available. A credit union can meet the experience requirement through various approaches. For example, a credit union can use the services of a credit union service organization (CUSO), an employee of another credit union, an independent contractor, or other third parties. However, the actual decision to grant a loan must reside with the credit union.

(b) *Conflicts of Interest.* Any third party used by a credit union to meet the requirements of paragraph (a) of this section must be independent from the transaction and is prohibited from having a

participation in the loan or an interest in the collateral securing the loan that the third party is responsible for reviewing, with the following exceptions:

(1) The third party may provide a service to the credit union related to the transaction, such as loan servicing;

(2) The third party may provide the requisite experience to the credit union and purchase a loan or a participation interest in a loan originated by the credit union that the third party reviewed; or

(3) A credit union may use the services of a CUSO that otherwise meets the requirements of paragraph (a) of this section even though the CUSO is not independent from the transaction, provided the credit union has a controlling financial interest in the CUSO as determined under Generally Accepted Accounting Principles.

§ 723.6 What must your member business loan policy address?

At a minimum, your policy must address the following:

(a) The types of business loans you will make;

(b) Your trade area;

(c) The maximum amount of your assets, in relation to net worth, that you will invest in secured and unsecured business loans;

(d) The maximum amount of your assets, in relation to net worth, that you will invest in a given category or type of business loan;

(e) The maximum amount of your assets, in relation to net worth, that you will loan to any one member or group of associated members, subject to § 723.7(c)(2) and § 723.8;

(f) The qualifications and experience of personnel (minimum of 2 years) involved in making and administering business loans;

(g) A requirement to analyze and document the ability of the borrower to repay the loan consistent with appropriate underwriting and due diligence standards, which also addresses the need for periodic financial statements, credit reports, and other data when necessary to analyze future loans and lines of credit, such as, borrower's history and experience, balance sheet, cash flow analysis, income statements, tax data, environmental impact assessment, and comparison with industry averages, depending upon the loan purpose;

(h) The collateral requirements must include:

(1) Loan-to-value ratios;

(2) Determination of value;

(3) Determination of ownership;

(4) Steps to secure various types of collateral; and

(5) How often the credit union will reevaluate the value and marketability of collateral;

(i) The interest rates and maturities of business loans;

(j) General loan procedures which include:

(1) Loan monitoring;

(2) Servicing and follow-up; and

(3) Collection;

(k) Identification of those individuals prohibited from receiving member business loans.

§ 723.7 What are the collateral and security requirements?

(a) Except as provided in § 723.4 or unless your Regional Director grants a waiver, all member business loans, except those made under paragraphs (c), (d), and (e) of this section, must be secured by collateral as follows:

(1) The maximum loan-to-value ratio for all liens must not exceed 80% unless the value in excess of 80% is covered through private mortgage insurance or equivalent type of insurance, or insured, guaranteed, or subject to advance commitment to purchase by an agency of the federal government, an agency of a state or any of its political subdivisions, but in no case may the ratio exceed 95%;

(2) A borrower may not substitute any insurance, guarantee, or advance commitment to purchase by any agency of the federal government, a state or any political subdivision of such state for the collateral requirements of this paragraph.

(b) Principals, other than a not for profit organization as defined by the Internal Revenue Service Code (26 U.S.C. 501) or those where the Regional Director grants a waiver, must provide their personal liability and guarantee. Federal credit unions and federally insured state-chartered credit unions that meet RegFlex standards, as determined pursuant to Part 742 of this Chapter, are exempt from this requirement and may make their own determination whether to require the personal liability and guarantee of principals.

(c) You may make unsecured member business loans under the following conditions:

(1) You are well capitalized as defined by § 702.102(a)(1) of this chapter;

(2) The aggregate of the unsecured outstanding member business loans to any one member or group of associated members does not exceed the lesser of $100,000 or 2.5% of your net worth; and

(3) The aggregate of all unsecured outstanding member business loans does not exceed 10% of your net worth.

(d) You are exempt from the provisions of paragraphs (a), (b), and (c) of this section with respect to credit card line of credit programs offered to nonnatural person members that are limited to routine purposes normally made available under those programs.

(e) You may make vehicle loans under this part without complying with the loan-to-value ratios in this section, provided that the vehicle is a car, van, pick-up truck, or sports utility vehicle and not part of a fleet of vehicles.

§ 723.8 How much may one member or a group of associated members borrow?

Unless your Regional Director grants a waiver for a higher amount, the aggregate amount of net member business loan balances to any one member or group of associated members must not exceed the greater of:

(a) 15% of the credit union's net worth; or

(b) $100,000.

§ 723.9 Removed and Reserved.

§ 723.10 What waivers are available?

You may seek a waiver for a category of loans in any of the following areas:

(a) Appraisal requirements under § 722.3;

(b) Aggregate construction and development loans limits under § 723.3(a);

(c) Minimum borrower equity requirements for construction and development loans under § 723.3(b);

(d) Loan-to-value ratio requirements for business loans under § 723.7(a);

(e) Requirement for personal liability and guarantee under § 723.7(b);

(f) Maximum unsecured business loans to one member or group of associated members under § 723.7(c)(2);

(g) Maximum aggregate unsecured member business loan limit under § 723.7(c)(3); and

(h) Maximum aggregate net member business loan balance to any one member or group of associated members under § 723.8.

§ 723.11 How do you obtain a waiver?

To obtain a waiver, a federal credit union must submit a request to the Regional Director (a corporate federal credit union submits the waiver request to the Director of the Office of Corporate Credit Unions). A state chartered federally insured credit union must submit the request to its state supervisory authority. If the state supervisory authority approves the request, the state regulator will forward the request to the Regional Director (or if appropriate the Director of the Office of Corporate Credit Unions). A waiver is not effective until it is approved by the Regional Director (or in the case of a corporate federal credit union the Director of the Office of Corporate Credit Unions). The waiver request must contain the following:

(a) A copy of your business lending policy;

(b) The higher limit sought (if applicable);

(c) An explanation of the need to raise the limit (if applicable);

(d) Documentation supporting your ability to manage this activity; and

(e) An analysis of the credit union's prior experience making member business loans, including as a minimum:

(1) The history of loan losses and loan delinquency;

(2) Volume and cyclical or seasonal patterns;

(3) Diversification;

(4) Concentrations of credit to one borrower or group of associated borrowers in excess of 15% of net worth;

(5) Underwriting standards and practices;

(6) Types of loans grouped by purpose and collateral; and

(7) The qualifications of personnel responsible for underwriting and administering member business loans.

§ 723.12 What will NCUA do with my waiver request?

Your Regional Director (or the Director of the Office of Corporate Credit Unions) will:

(a) Review the information you provided in your request;

(b) Evaluate the level of risk to your credit union;

(c) Consider your credit union's historical CAMEL composite and component ratings when evaluating your request; and

(d) Notify you whenever your waiver request is deemed complete. Notify you of the action taken within 45 calendar days of receiving a complete request from the federal credit union or the state supervisory authority. If you do not receive notification within 45 calendar days of the date the complete request was received by the regional office, the credit union may assume approval of the waiver request.

§ 723.13 What options are available if the NCUA Regional Director denies my waiver request or a portion of it?

You may appeal the Regional Director's (or the Director of the Office of Corporate Credit Unions) decision in writing to the NCUA Board. Your appeal must include all information requested in § 723.11 and why you disagree with your Regional Director's (or the Office of Corporate Credit Union Director's) decision.

§ 723.14 Removed and Reserved.

§ 723.15 Removed and Reserved.

§ 723.16 What is the aggregate member business loan limit for a credit union?

(a) *General.* The aggregate limit on a credit union's net member business loan balances is the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets. Net worth is all of the credit union's retained earnings. Retained earnings normally includes undivided earnings, regular reserves and any other appropriations designated by management or regulatory authorities. Loans that are exempt from the definition of member business loans are not counted for the purpose of the aggregate loan limit.

(b) *Effect of nonmember loans and nonmember participations.* If a credit union holds any nonmember loans or nonmember loan participation interests that would constitute a member business loan if made to a member, those loans will affect the credit union's aggregate limit on net member business loan balances as follows:

(1) The total of the credit union's net member business loan balances and the nonmember loan balances must not exceed the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets, unless the credit union has first received approval from the NCUA regional director.

(2) To request approval from the NCUA regional director, a credit union must submit an application that:

(i) Includes a current copy of the credit union's member business loan policies;

(ii) Confirms that the credit union is in compliance with all other aspects of this rule;

(iii) States the credit union's proposed limit on the total amount of nonmember loans and participation interests that the credit union may acquire if the application is granted; and

(iv) Attests that the acquisition of nonmember loans and participations is not being used, in conjunction with one or more other credit unions, to have the effect of trading member business loans that would otherwise exceed the aggregate limit.

(3) A federal credit union must submit its request for approval to the regional director (a corporate federal credit union submits its request to the Director of the Office of Corporate Credit Unions). A state chartered federally insured credit union must submit the request to its state supervisory authority. If the state supervisory authority approves the request, the state regulator will forward the application and its decision to the regional director (or if appropriate, the Director of the Office of Corporate Credit Unions). An approved application is not effective until it is approved by the regional director (or in the case of a corporate federal credit union the Director of the Office of Corporate Credit Unions). The regional director will issue a decision within 30 days of receipt of a federal credit union's completed application or within 30 days of receipt of a completed application and the state supervisory authority's approval for a state chartered federally insured credit union.

§ 723.17 Are there any exceptions to the aggregate loan limit?

There are three circumstances where a credit union qualifies for an exception from the aggregate

limit. Loans that are excepted from the definition of member business loans are not counted for the purpose of the exceptions. The three exceptions are:

(a) Credit unions that have a low-income designation or participate in the Community Development Financial Institutions program;

(b) Credit unions that were chartered for the purpose of making member business loans and can provide documentary evidence (such evidence includes but is not limited to the original charter, original bylaws, original business plan, original field of membership, board minutes and loan portfolio);

(c) Credit unions that have a history of primarily making member business loans, meaning that either member business loans comprise at least 25% of the credit union's outstanding loans (as evidenced in any call report filed between January 1995 and September 1998 or any equivalent documentation including financial statements) or member business loans comprise the largest portion of the credit union's loan portfolio (as evidenced in any call report filed between January 1995 and September 1998 or any equivalent documentation including financial statements). For example, if a credit union makes 23% member business loans, 22% first mortgage loans, 22% new automobile loans, 20% credit card loans, and 13% total other real estate loans, then the credit union meets this exception.

§ 723.18 How do I obtain an exception?

To obtain the exception, a federal credit union must submit documentation to the Regional Director, demonstrating that it meets the criteria of one of the exceptions. A state chartered federally insured credit union must submit documentation to its state supervisory authority. The state supervisory authority will forward its decision to NCUA. The exception does not expire unless revoked by the state supervisory authority for a state chartered federally insured credit union or the Regional Director for a federal credit union. If an exception request is denied for a federal credit union, it may be appealed to the NCUA Board within 60 days of the denial by the Regional Director. Until the NCUA Board acts on the appeal, the credit union can continue to make new member business loans.

§ 723.19 What are the recordkeeping requirements?

You must separately identify member business loans in your records and in the aggregate on your financial reports.

§ 723.20 How can a state supervisory authority develop and enforce a member business loan regulation?

(a) The NCUA Board may exempt federally insured state chartered credit unions in a given state from NCUA's member business loan rule if NCUA approves the state's rule for use for state chartered federally insured credit unions. In making this determination, the Board is guided by safety and soundness considerations and reviews whether the state regulation minimizes the risk and accomplishes the overall objectives of NCUA's member business loan rule in this part. Specifically, the Board will focus its review on:

(1) The definition of a member business loan;

(2) Loan to one borrower limits;

(3) Written loan policies;

(4) Collateral and security requirements;

(5) Construction and development lending; and

(6) Loans to senior management.

(b) To receive NCUA's approval of a state's member business loan rule, the state supervisory authority must submit its rule to the NCUA regional office. After reviewing the rule, the region will forward the request to the NCUA Board for a final determination.

§ 723.21 Definitions.

For purposes of this part, the following definitions apply:

Associated member is any member with a shared ownership, investment, or other pecuniary interest in a business or commercial endeavor with the borrower.

Construction or development loan is a financing arrangement for acquiring property or rights to property, including land or structures, with the intent to convert it to income-producing property

such as residential housing for rental or sale; commercial use; industrial use; or similar uses.

Immediate family member is a spouse or other family member living in the same household.

Loan-to-value ratio is the aggregate amount of all sums borrowed including outstanding balances plus any unfunded commitment or line of credit from all sources on an item of collateral divided by the market value of the collateral used to secure the loan.

Net member business loan balance means the outstanding loan balance plus any unfunded commitments, reduced by 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 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 and qualifying for true sales accounting under generally accepted accounting principles.

Net worth is retained earnings as defined under Generally Accepted Accounting Principles. Retained earnings normally includes undivided earnings, regular reserves and any other appropriations designated by management or regulatory authorities.

Part 724

Trustees and Custodians of Pension Plans

§ 724.1 Federal credit unions acting as trustees and custodians of certain tax-advantaged savings plans.

A federal credit union is authorized to act as trustee or custodian, and may receive reasonable compensation for so acting, under any written trust instrument or custodial agreement created or organized in the United States and forming part of a tax-advantaged savings plan which qualifies or qualified for specific tax treatment under sections 223, 401(d), 408, 408A and 530 of the Internal Revenue Code (26 U.S.C. 223, 401(d), 408, 408A and 530), for its members or groups of its members, provided the funds of such plans are invested in share accounts or share certificate accounts of the Federal credit union. Federal credit unions located in a territory, including the trust territories, or a possession of the United States, or the Commonwealth of Puerto Rico, are also authorized to act as trustee or custodian for such plans, if authorized under sections 223, 401(d), 408, 408A and 530 of the Internal Revenue Code as applied to the territory or possession under similar provisions of territorial law. All funds held in a trustee or custodial capacity must be maintained in accordance with applicable laws and rules and regulations as may be promulgated by the Secretary of Labor, the Secretary of the Treasury, or any other authority exercising jurisdiction over such trust or custodial accounts. The Federal credit union shall maintain individual records for each participant which show in detail all transactions relating to the funds of each participant or beneficiary.

§ 724.2 Self-Directed Plans.

A federal credit union may facilitate transfers of plan funds to assets other than share and share certificates of the credit union, provided the conditions of § 724.1 are met and the following additional conditions are met:

(a) all contributions of funds are initially made to a share or share certificate account in the Federal credit union;

(b) any subsequent transfer of funds to other assets is solely at the direction of the member and the Federal credit union exercises no investment discretion and provides no investment advice with respect to plan assets (i.e., the credit union performs only custodial duties); and

(c) the member is clearly notified of the fact that National Credit Union Share Insurance Fund coverage is limited to funds held in share or share certificate accounts of NCUSIF-insured credit unions.

§ 724.3 Appointment of Successor Trustee or Custodian.

Any plan operated pursuant to this Part shall provide for the appointment of a successor trustee or custodian by a person, committee, corporation, or organization other than the Federal credit union or any person acting in his capacity as a director, employee or agent of the Federal credit union upon notice from the Federal credit union or the Board that the Federal credit union is unwilling or unable to continue to act as trustee or custodian.

Part 725

Central Liquidity Facility

§ 725.1 Scope.

This Part contains the regulations implementing the National Credit Union Central Liquidity Facility Act, Subchapter III of the Federal Credit Union Act. The National Credit Union Administration Central Liquidity Facility is a mixed-ownership Government corporation within the National Credit Union Administration. It is managed by the National Credit Union Administration Board and is owned by its member credit unions. The purpose of the Facility is to improve the general financial stability of credit unions by meeting their liquidity needs and thereby encourage savings, support consumer and mortgage lending and provide basic financial resources to all segments of the economy.

§ 725.2 Definitions.

As used in this Part:

(a) "Agent" means an Agent member of the Facility.

(b) "Agent group" means an Agent member of the Facility consisting of a group of central credit unions, one of which is designated as the group's "Agent group representative" and authorized to transact business with the Facility on behalf of the group or any member of the group.

(c) "Agent loan" means an advance of funds by an Agent to a member natural person credit union to meet liquidity needs which have been the basis for a Facility advance.

(d) "Central credit union" means a Federal or state-chartered credit union primarily serving other credit unions. A credit union is primarily serving other credit unions when the total dollar amount of the shares and deposits received from other credit unions plus loans to other credit unions exceeds 50 percent of the total dollar amount of all shares and deposits plus loans during the qualifying period, as defined in subsection (p) of this section.

(e) "Facility" or "Central Liquidity Facility" means the National Credit Union Administration Central Liquidity Facility.

(f) "Facility advance" means an advance of funds by the Facility to a Regular or Agent member.

(g) "Facility lending officer" means any employee of the Facility or the National Credit Union Administration who has been designated by the NCUA Board as a Facility lending officer.

(h) "Liquid assets" means the following unpledged assets:

(1) cash on hand;

(2) share or deposit accounts with remaining maturities of one year or less maintained in central credit unions or institutions insured by the Federal Deposit Insurance Corporation or Federal Savings and Loan Insurance Corporation;

(3) investments in obligations of the United States or any agency thereof, or securities fully guaranteed as to principal and interest thereby, which are authorized under 12 U.S.C. § 1757(7) and which have a remaining maturity of one year or less;

(4) common trust investments and similar investments in funds or securities authorized for Federal credit unions, the objectives of which are to provide daily liquidity for participating credit unions;

(5) shares in the National Credit Union Administration Central Liquidity Facility or in special share accounts authorized by Section 725.7 of this Part;

(6) in the case of a federally-insured state-chartered credit union, any asset held in satisfaction of liquidity requirements imposed by applicable state law or regulation; and

(7) balances maintained by federally-insured credit unions in a Federal Reserve bank, or in a pass-through account to a Federal Reserve bank, pursuant to the requirements of Section 19(b) of the Federal Reserve Act (12 U.S.C. § 461(b)).

(i) "Liquidity needs" means the needs of credit unions primarily serving natural persons for:

(1) short-term adjustment credit available to assist in meeting temporary requirements for funds or to cushion more persistent outflows of funds pending an orderly adjustment of credit union assets and liabilities;

(2) seasonal credit available for longer periods to assist in meeting seasonal needs for

funds arising from a combination of expected patterns of movement in share and deposit accounts and loans; and

(3) protracted adjustment credit available in the event of unusual or emergency circumstances of a longer term nature resulting from national, regional or local difficulties.

(j) "Management policies" means policies of a credit union with respect to membership, shares, deposits, dividends, interest rates, lending, investing, borrowing, safeguarding of assets, hiring, training and supervision of employees, and general operating and control practices and procedures.

(k) "Member" means a Regular or Agent member of the Facility, unless the context indicates otherwise.

(l) "Member natural person credit union" means a natural person credit union which is a member of an Agent or of any central credit union in an Agent group. Member natural person credit unions are not members of the Facility unless they are also Regular members of the Facility.

(m) "Natural person credit union" means a Federal or state-chartered credit union primarily serving natural persons. A credit union is primarily serving natural persons if it is not a central credit union as defined in subsection (d) of this section.

(n) "NCUA Board" or "Board" means the National Credit Union Administration Board.

(o) *Paid-in and unimpaired capital and surplus* means shares and deposits plus post-closing, undivided earnings. This does not include regular reserves or special reserves required by law, regulation or special agreement between the credit union and its regulator or share insurer.

(p) "Qualifying Period" means:

(1) for initial qualification, any 7 months out of the 12 months immediately preceding the month in which application is made to become a member of the Facility; and

(2) for qualification during each subsequent calendar year, any 7 months out of the previous calendar year.

(q) "Stock subscription" means the stock subscription required for membership in the Facility. "Total subscribed Facility stock" is the sum of all members' stock subscriptions.

§ 725.3 Regular Membership.

(a) A natural person credit union may become a Regular member of the Facility by:

(1) making application on a form approved by the Facility;

(2) subscribing to capital stock of the Facility in an amount equal to one-half of 1 percent of the credit union's paid-in and unimpaired capital and surplus, as determined in accordance with subsection 725.5(b) of this Part, and forwarding with its completed application funds equal to one-half of this stock subscription;[1] and

(3) furnishing the following reports and documents with the completed membership application;

(i) a copy of the credit union's financial and statistical report for the most recent calendar month; and

(ii) copies of the credit union's charter and bylaws, unless the credit union is federally chartered.

(b) A credit union which becomes a Regular member of the Facility after February 23, 1980, may not receive Facility advances without approval of the NCUA Board for a period of six months after becoming a member. This subsection shall not apply to any credit union which becomes a Regular member of the Facility within six months after such credit union is chartered, or which has had access to Facility funds through an Agent member of the Facility at any time within six months prior to becoming a Regular member of the Facility.

§ 725.4 Agent Membership.

(a) A central credit union or a group of central credit unions may become an Agent member of the Facility by (in the case of a group of central credit unions, each central credit union in the group must do each of the following except for paragraph (a)(2) of this section, which shall be done by the Agent group representative):

[1] A credit union which submits its application for membership prior to October 1, 1979, is not required to forward these funds to the Facility until October 1, 1979.

(1) making application on a form approved by the Facility;

(2) subscribing to the capital stock of the Facility in an amount equal to one-half of 1 percent of the paid-in and unimpaired capital and surplus (as determined in accordance with subsection 725.5(b) of this Part) of all the central credit union's or central credit union group's member natural person credit unions, except those which are Regular members of the Facility or which have access to the Facility through, and are included in the stock subcription of, another Agent.[2] Upon approval of the application, the Agent shall forward funds equal to one-half of this initial stock subscription to the Facility;[3]

(3) furnishing the following reports and documents with the completed membership application:

(i) a copy of the central credit union's financial and statistical report for the most recent calendar month;

(ii) copies of the central credit union's charter and bylaws, unless such credit union is federally chartered; and

(iii) a list of all the central credit union's member natural person credit unions.

(4) agreeing to submit to the supervision of the NCUA Board and to comply with all regulations and reporting requirements which the NCUA Board shall prescribe for Agent members;

(5) agreeing to submit to periodic unrestricted examinations by the NCUA Board or its designee; and

(6) obtaining the written approval of the NCUA Board.

(b) The NCUA Board may approve a central credit union or group of central credit unions as an Agent member of the Facility, provided the NCUA Board is satisfied that such credit union or credit union group meets certain criteria, including but not limited to the following (in the case of a group of central credit unions, each central credit union in the group must meet these criteria):

(1) the management policies are in writing, approved by the central credit union's board of directors, and reviewed annually by such board;

(2) adequate internal controls are in place to assure accurate and timely reporting of transactions and the safeguarding of assets;

(3) the financial condition of the central credit union is sound with adequate reserves for losses;

(4) surety bond coverage provides protection for the central credit union while the central credit union is performing the duties of an Agent member of the Facility;

(5) management has demonstrated its ability to use such techniques as cash flow analysis, budgeting, and projections of sources and uses of funds to manage the affairs of the central credit union efficiently and in conformity with sound business practices; and

(6) there are no practices, procedures, policies, or other factors that would result in discrimination by the central credit union among natural person credit unions or inhibit its ability to act independ- ently in its role as an Agent member of the Facility.

(c) Each Agent, or in the case of an Agent group, each central credit union in the group, must:

(1) maintain records related to Facility activity in conformity with requirements prescribed by the NCUA Board from time to time; and

(2) submit such reports as may be required by the Facility to determine financial soundness, quality and level of service, and conformity with established guidelines and procedures.

(d) Each Agent, or in the case of an Agent group, each central credit union in the group, must have on an annual basis a third party independent audit of its books and records and provide the Facility with copies of the report of such audit. The auditor selected must be recognized by a state or territorial licensing authority as possessing the requisite knowledge and experience to perform audits.

(e) Within 30 days after a natural person credit union becomes a member of a central credit union which is an Agent or a member of an Agent group, the agent, or in the case of an Agent group, the agent group representative, shall subscribe to additional capital stock of the Facility in an amount equal to one-half of 1 percent of such credit union's paid-in and unimpaired capital and surplus, and shall forward funds equal to one-half of this stock subscription to the Facility. This subsection shall

[2] A natural person credit union which is a member of more than one Agent member of the Facility must designate through which Agent it will deal with the Facility, and the designated Agent will be responsible for including the capital and surplus of such credit union in the calculation of its stock subscription.

[3] If the application is approved prior to October 1, 1979, these funds are not required to be forwarded to the Facility until October 1, 1979.

not apply if the natural person credit union is a Regular member of the Facility or has access to the Facility through, and is included in the stock subscription of, another Agent.

(f) A central credit union or group of central credit unions which becomes an Agent member of the Facility after February 23, 1980, may not receive a Facility advance without approval of the NCUA Board for a period of six months after becoming a member. This subsection shall not apply to any central credit union which becomes an Agent member or a member of an Agent group within six months after such credit union has been an Agent or a member of another Agent group.

(g) Agent members will be compensated for the services they perform for the Facility in a manner to be specified by the NCUA Board.

§ 725.5 Capital Stock.

(a) The capital stock of the Facility is divided into nonvoting shares having a par value of $50 each. The Facility issues whole and fractional shares. Shares are issued in book entry form upon receipt of payment for such shares, and cannot be transferred or hypothecated except to the Facility.

(b) The capital stock subscriptions provided for in Sections 725.3 and 725.4 shall be:

(1) based on an arithmetic average of paid-in and unimpaired capital and surplus over the six months preceding application for membership, and

(2) adjusted at the close of each calendar year in accordance with an arithmetic average of paid-in and unimpaired capital and surplus over the twelve months in such calendar year. Payments for adjustments to the capital stock subscription must be received by the Facility no later than March 31 of the following year.

(c) That part of a member's stock subscription which is not paid-in shall be held by the member on call of the NCUA Board and shall be invested in liquid assets.

(d) Any member may at any time purchase additional shares of capital stock in the Facility. Any shares in excess of the member's required paid-in portion of its stock subscription can be redeemed by the member as long as the member maintains investments in other assets sufficient to meet the requirement of paragraph (c) of this section. The member's required paid-in portion of its stock subscription includes one-half of its stock subscription plus any "calls" that may have been issued by the NCUA Board against the "on-call" portion of such stock subscription.

(e) Dividends will be paid on capital stock at such times and rates as are determined by the NCUA Board. The NCUA Board shall declare such dividends no less frequently than annually. All issued (paid for) capital stock shall share in dividend distributions without preference. Payment of dividends will be made by the issuance of capital stock to the member in the amount of the dividend.

§ 725.6 Termination of Membership.

(a) A member of the Facility whose stock subscription constitutes less than 5 percent of total subscribed Facility stock may withdraw from membership in the Facility six months after notifying the NCUA Board in writing of its intention to do so.

(b) A member of the Facility whose stock subscription constitutes 5 percent or more of total subscribed Facility stock may withdraw from membership in the Facility twenty-four months after notifying the NCUA Board in writing of its intention to do so.

(c) The NCUA Board may terminate membership in the Facility if, after the opportunity for a hearing, the NCUA Board determines the member has failed to comply with any provision of the National Credit Union Central Liquidity Facility Act or any regulation issued pursuant thereto. If membership is terminated under this subsection, the credit union will be required to obtain the approval of the NCUA Board before becoming a member of the Facility again. Such approval will be granted only if the NCUA Board is satisfied that the credit union will comply with such Act and regulations.

(d)(1) If membership is terminated under any provision of this section, the terminated member's stock shall be redeemed upon termination. In such event, the Facility may retain any amount owed to the Facility by the member.

(2) When a member natural person credit union withdraws from membership in a central credit union which is an Agent or a member of an Agent group, the stock subscription of the Agent, or in the case of an Agent group, the stock subscription of the Agent group representative, will be adjusted after the waiting period which would apply under subsection (a) or (b) of

this section if the withdrawing credit union were a member of the Facility.

§ 725.7 Special Share Accounts in Federally Chartered Agent Members.

(a) A federally chartered Agent member of the Facility may require its member natural person credit unions to establish and maintain special share accounts in the Agent member to reimburse it for the portion of the Agent's Facility stock subscription which is attributable to the paid-in and unimpaired capital and surplus of each such natural person credit union.

(b) The amount which the Agent member requires each member natural person credit union to maintain in such special share accounts shall be based on a uniform percentage of the paid-in and unimpaired capital and surplus of such credit unions, and shall not exceed the amount of the Agent's stock subscription which is attributable to the capital and surplus of each such credit union. An Agent shall not permit a member to maintain in a special share account any amounts in excess of the required amount.

(c) A natural person credit union that withdraws from membership in an Agent member or that becomes a Regular member of the Facility, shall be entitled to the return of all amounts in its special share account upon withdrawal from membership in the Agent or upon becoming a Regular member, as applicable.

[Sections 725.8 through 725.16 Reserved for future use.]

§ 725.17 Applications for Extensions of Credit.

(a) A Regular member may apply for a Facility advance to meet its liquidity needs by filing an application on a Facility-approved form, or by any other method approved by the Facility.

(b)(1) An Agent member may apply for a Facility advance by filing an application on a Facility-approved form, or by any other method approved by the Facility.[4]

(2) The Agent's application shall be based on the following:

(i) approved applications to the Agent by its member natural person credit unions for pending loans to meet liquidity needs; or

(ii) outstanding loans previously made by the Agent to meet liquidity needs of its member natural person credit unions; or

(iii) such other demonstrable liquidity needs as the NCUA Board may specify.

(3) An Agent shall not submit an application to the Facility based on the liquidity needs of any member natural person credit union which has not agreed to the repayment, security and credit reporting terms prescribed by the Facility for Agent loans;

(4) Any loan to meet liquidity needs which have been or will be the basis for an application by the Agent for a Facility advance must be applied for on an application form approved by the Facility.

(5) Unless approved by the Facility, an Agent shall not submit an application to the Facility based on the liquidity needs of any credit union which became a member natural person credit union of the Agent after February 23, 1980, unless such credit union has been a member natural person credit union of the Agent for six months, was chartered within six months before becoming a member natural person credit union of the Agent, or had access to the Facility either as a Regular member or through another Agent within six months before becoming a member natural person credit union of the Agent.

(c) In emergency circumstances, the applications for extensions of credit required under subsection (a) and paragraphs (b)(1) and (b)(4) of this section may be verbal, but must be confirmed within five working days by an application as required by such subsection or paragraphs.

(d) Applications of Regular and Agent members shall be filed with a Facility lending officer. Each application for credit which is completed and properly filed will be approved or denied within five working days after the receipt.

§ 725.18 Creditworthiness.

(a) Prior to Facility approval of each application of a Regular member for a Facility advance, the Facility shall consider the creditworthiness of such member.

(b) Prior to an Agent's approval of each application of a member natural person credit union for an extension of credit on which an application by the Agent to the Facility will be based, an Agent shall consider the creditworthiness of such member natural person credit union.

(c) Specific characteristics of an uncreditworthy credit union include, but are not limited to, insol-

[4] If the Agent is an Agent group, the application must be filed by the Agent group representative, and any Facility advance will be made to the Agent group representative.

vency as defined by § 700.2(e)(1) of this chapter, unsatisfactory practices in extending credit, lower than desirable reserve levels, high expense ratio, failure to repay previous Facility advances as agreed, excessive dependence on borrowed funds, inadequate cash management policies and planning, or any other relevant characteristics creating a less than satisfactory condition. The presence of one or more of these characteristics will not necessarily mean that a credit union will be considered uncreditworthy.

(d) A natural person credit union (whether a Regular member of the Facility or a member natural person credit union) which does not meet the Facility creditworthiness standards may be limited in or denied the use of advances for its liquidity needs.

§ 725.19 Collateral Requirements.

(a) Each Facility advance and each Agent loan shall be secured by a first priority security interest in collateral of the credit union with a net book value at least equal to 110% of all amounts due under the applicable Facility advance or Agent loan, or by guarantee of the National Credit Union Share Insurance Fund.

(b) The Facility may accept as collateral for each Facility advance to a Regular member, a security interest in all assets of the Regular member; provided however, that the value of any assets in which any third party has a perfected security interest that is superior to the security interest of the Facility shall be excluded for purposes of complying with the requirements of paragraph (a) of this section.

(c) The Facility may accept as collateral for each Facility advance to an Agent member, a security interest in the Agent loans for which the Facility advance was made; provided however, that the collateral for such Agent loan meets the requirements of paragraph (a) of this section.

§ 725.20 Repayment, Security and Credit Reporting Agreements; Other Terms and Conditions.

(a) Regular and Agent members, or in the case of an Agent group, the Agent group representative, shall sign the repayment, security and credit reporting agreements prescribed by the Facility, and all Facility advances to Regular and Agent members shall be governed by the terms and conditions of such agreements.

(b) All Agent loans shall be made subject to the repayment, security and credit reporting terms prescribed by the Facility for Agent loans.

(c) Other terms and conditions applicable to Facility advances and Agent loans will be specified in confirmations of credit provided in connection with such advances and loans, and/or in operating circulars of the Facility.

§ 725.21 Modification of Agreements.

The repayment, security, and credit reporting terms under which Facility advances and Agent loans will be made, as provided in section 725.20 of this Part, shall be subject to modification from time to time as the NCUA Board may determine. Any change in such terms shall be published in the FEDERAL REGISTER and shall apply to all advances disbursed by the Facility after the effective date of the change.

§ 725.22 Advances to Insurance Organizations.

(a) In accordance with policies established by the NCUA Board, the Facility may advance funds to a State credit union share or deposit insurance corporation, guaranty credit union, guaranty association, or similar organization. Requests for such advances shall be supported by an application which sets forth and supports the need for the advance.

(b) Advances under subsection (a) shall be subject to the approval of the NCUA Board and shall be made subject to the following terms:

(1) the advance shall be fully secured,

(2) the maturity of the advance shall not exceed 12 months,

(3) the advance shall not be renewable at maturity, and

(4) the funds advanced shall not be relent at an interest rate exceeding that imposed by the Facility

§ 725.23 Other Advances.

(a) The NCUA Board may authorize extensions of credit to members of the Facility for purposes other than liquidity needs if the NCUA Board, the Board of Governors of the Federal Reserve System, and the Secretary of the Treasury concur in a determination that such extensions of credit are in the national economic interest.

(b) Extensions of credit approved under the conditions of paragraph (a) of this section shall be subject to such terms and conditions as shall be established by the NCUA Board.

Part 740

Accuracy of Advertising and Notice of Insured Status

§ 740.0 Scope.

This part applies to all federally insured credit unions. It prescribes the requirements for the official sign insured credit unions must display and the requirements with regard to the official advertising statement insured credit unions must include in their advertisements. It requires that all other kinds of advertisements be accurate. It also establishes requirements for advertisements of excess insurance.

§ 740.1 Definitions.

(a) *Account* or *accounts* as used in this part means share, share certificate or share draft accounts (or their equivalent under state law, as determined by the Board in the case of insured state credit unions) of a member (which includes other credit unions, public units, and nonmembers where permitted under the Act) in a credit union of a type approved by the Board which evidences money or its equivalent received or held by a credit union in the usual course of business and for which it has given or is obligated to give credit to the account of the member.

(b) *Insured credit union* as used in this part means a credit union insured by the National Credit Union Administration (NCUA).

§ 740.2 Accuracy of advertising.

No insured credit union may use any advertising (which includes print, electronic, or broadcast media, displays and signs, stationery, and other promotional material) or make any representation which is inaccurate or deceptive in any particular, or which in any way misrepresents its services, contracts, or financial condition, or which violates the requirements of § 707.8 of this subchapter, if applicable. This provision does not prohibit an insured credit union from using a trade name or a name other than its official charter name in advertising or signage, so long as it uses its official charter name in communications with NCUA and for share certificates or certificates of deposit, signature cards, loan agreements, account statements, checks, drafts and other legal documents.

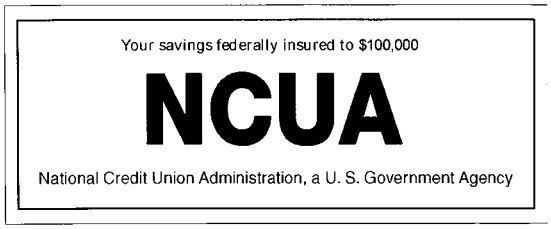
§ 740.3 Advertising of excess insurance.

Any advertising that mentions share or savings account insurance provided by a party other than the NCUA must clearly explain the type and amount of such insurance and the identity of the carrier and must avoid any statement or implication that the carrier is affiliated with the NCUA or the federal government.

§ 740.4 Requirements for the official sign.

(a) Each insured credit union must continuously display the official sign described in paragraph (b) of this section at each station or window where insured account funds or deposits are normally received in its principal place of business and in all its branches, 30 days after its first day of operation as an insured credit union. Each insured credit union must also display the official sign on its Internet page, if any, where it accepts deposits or open accounts, but it may vary the font sizes from that depicted in paragraph (b) of this section to ensure its legibility.

(b) The official sign shall be as depicted below:



(1) NCUA will automatically supply all insured credit unions an initial supply of official signs with a blue background and white let-

tering at no cost for compliance with paragraph (a) of this section. If the initial supply is not adequate, the insured credit unions must immediately request additional signs from NCUA. Any credit union that does not have an adequate supply but requests additional signs from NCUA will not be considered to have violated paragraph (a) of this section unless the credit union fails to display the signs after receiving them.

(2) Insured credit unions may purchase additional signs from commercial suppliers in additional colors, materials and sizes, for uses other than those required by paragraph (a) of this section.

(c) An insured credit union must not receive account funds at any teller's station or window where any noninsured credit union or institution receives deposits. Excepted from this prohibition are credit union centers, service centers, or branches servicing more than one credit union where only some of the credit unions are insured by the NCUA. In such instances, immediately above or beside each official sign there must be another sign stating, "Only the following credit unions serviced by this facility are federally insured by the NCUA — " (the full name of each credit union insured will follow the word NCUA). The lettering must be of such size and print to be clearly legible to all members conducting share or share deposit transactions.

(d) The Board may require any insured credit union, upon at least 30 days' written notice, to change the wording of its official signs in a manner deemed necessary for the protection of shareholders or others.

(e) For purposes of this section, the terms "branch," "station," "teller station," and "window" do not include automated teller machines or point of sale terminals.

§ 740.5 Requirements for the official advertising statement.

(a) Each insured credit union must include the official advertising statement, prescribed in paragraph (b) of this section, in all of its advertisements, including on its main Internet page, except as provided in paragraph (c) of this section.

(1) An insured credit union must include the official advertising statement in its advertisements thirty (30) days after its first day of operations as an insured credit union unless the Regional Director grants it an extension.

(2) If advertising copy without the official advertising statement is on hand on the date the requirements of this section become operative, the insured credit union may use an overstamp or other means to include the official advertising statement until the supplies are exhausted.

(b) The official advertising statement is in substance as follows: This credit union is federally insured by the National Credit Union Administration. The short title "Federally insured by NCUA" and a reproduction of the official sign may be used by insured credit unions at their option as the official advertising statement. The official advertising statement must be in a size and print that is clearly legible.

(c) The following advertisements need not include the official advertising statement:

(1) Statements of condition and reports of condition of an insured credit union which are required to be published by state or federal law or regulation;

(2) Credit union supplies such as stationery (except when used for circular letters), envelopes, deposit slips, checks, drafts, signature cards, account passbooks, and noninsurable certificates;

(3) Signs or plates in the credit union office or attached to the building or buildings in which the offices are located;

(4) Listings in directories;

(5) Advertisements not setting forth the name of the insured credit union;

(6) Display advertisements in credit union directories, provided the name of the credit union is listed on any page in the directory with a symbol or other descriptive matter indicating it is insured;

(7) Joint or group advertisements of credit union services where the names of insured credit unions and noninsured credit unions are listed and form a part of such advertisement;

(8) Advertisements by radio that do not exceed thirty (30) seconds in time;

(9) Advertisements by television, other than display advertisements, that do not exceed thirty (30) seconds in time;

(10) Advertisements that because of their type or character would be impractical to include the official advertising statement, including but not limited to, promotional items such as calendars, matchbooks, pens, pencils, and key chains;

(11) Advertisements that contain a statement to the effect that the credit union is insured by the National Credit Union Administration, or that its accounts and shares or members are insured by the Administration to the maximum of $100,000 for each member or shareholder;

(12) Advertisements that do not relate to member accounts, including but not limited to advertisements relating to loans by the credit union, safekeeping box business or services, traveler's checks on which the credit union is not primarily liable, and credit life or disability insurance.

(d) The non-English equivalent of the official advertising statement may be used in any advertisement provided that the Regional Director gives prior approval to the translation.

Part 741

Requirements for Insurance

§ 741.0 Scope.

The provisions of this part apply to federal credit unions, federally insured state-chartered credit unions, and credit unions making application for insurance of accounts pursuant to Title II of the Act, unless the context of a provision indicates its application is otherwise limited. This part prescribes various requirements for obtaining and maintaining federal insurance and the payment of insurance premiums and capitalization deposit. Subpart A of this part contains substantive requirements that are not codified elsewhere in this chapter. Subpart B of this part lists additional regulations, set forth elsewhere in this chapter as applying to federal credit unions, that also apply to federally insured state-chartered credit unions. As used in this part, "insured credit union" means a credit union whose accounts are insured by the National Credit Union Share Insurance Fund (NCUSIF).

Subpart A—Regulations that Apply to Both Federal Credit Unions and Federally Insured State-Chartered Credit Unions and That are not Codified Elsewhere in NCUA's Regulations

§ 741.1 Examination.

As provided in Sections 201 and 204 of the Act (12 U.S.C. 1781 and 1784), the NCUA Board is authorized to examine any insured credit union or any credit union making application for insurance of its accounts. Such examination may require access to all records, reports, contracts to which the credit union is a party, and information concerning the affairs of the credit union. Upon request, such documentation must be provided to the NCUA Board or its representative. Any credit union which makes application for insurance will be required to pay the cost of such examination and processing. To the maximum extent feasible, the NCUA Board will utilize examinations conducted by state regulatory agencies.

§ 741.2 Maximum borrowing authority.

(a) Any credit union which makes application for insurance of its accounts pursuant to Title II of the Act, or any insured credit union, must not borrow, from any source, an aggregate amount in excess of 50 per centum of its paid-in and unimpaired capital and surplus (shares and undivided earnings, plus net income or minus net loss).

(b) A federally insured state-chartered credit union may apply to the regional director for a waiver of paragraph (a) of this section up to the amount permitted under the applicable state law or by the state regulator. The waiver request must include:

(1) Written approval from the state regulator;

(2) A detailed analysis of the safety and soundness implications of the proposed waiver;

(3) A proposed aggregate dollar amount or percentage of paid-in and unimpaired capital and surplus limitation; and

(4) An explanation demonstrating the need to raise the limit.

(c) The regional director will approve the waiver request if the proposed borrowing limit will not adversely affect the safety and soundness of the federally insured state-chartered credit union.

§ 741.3 Criteria.

In determining the insurability of a credit union which makes application for insurance and in continuing the insurability of its accounts pursuant to Title II of the Act, the following criteria shall be applied:

(a) *Reserves*—(1) *General rule.* State-chartered credit unions are subject to section 216 of the Act, 12 U.S.C. 1790d, and to part 702 and subpart L of part 747 of this chapter.

(2) *Special reserve for nonconforming investments.* State-chartered credit unions (except state-chartered corporate credit unions) are required to establish an additional special reserve for investments if those credit unions

are permitted by their respective state laws to make investments beyond those authorized in the Act or the NCUA Rules and Regulations. For any investment other than loans to members and obligations or securities expressly authorized in Title I of the Act and part 703 of this chapter, as amended, state-chartered credit unions (except state-chartered corporate credit unions) are required to establish and maintain at the end of each accounting period and prior to payment of any dividend, an Appropriation for Non-conforming Investments in an amount at least equal to the net excess of book value over current market value of the investments. If the market value cannot be determined, an amount equal to the full book value will be established. When at the end of any dividend period, the amount in the Appropriation for Non-conforming Investments exceeds the difference between book value and market value, the board of directors may authorize the transfer of the excess to Undivided Earnings.

(b) *Financial condition and policies.* The following factors are to be considered in determining whether the credit union's financial condition and policies are both safe and sound:

(1) The existence of unfavorable trends which may include excessive losses on loans (i.e., losses which exceed the regular reserve or its equivalent [in the case of state-chartered credit unions] plus other irrevocable reserves established as a contingency against losses on loans), the presence of special reserve accounts used specifically for charging off loan balances of deceased borrowers, and an expense ratio so high that the required transfers to reserves create a net operating loss for the period or that the net gain after these transfers is not sufficient to permit the payment of a nominal dividend;

(2) The existence of written lending policies, including adequate documentation of secured loans and the protection of security interests by recording, bond, insurance, or other adequate means, adequate determination of the financial capacity of borrowers and co-makers for repayment of the loan, and adequate determination of value of security on loans to ascertain that said security is adequate to repay the loan in the event of default;

(3) Investment policies which are within the provisions of applicable law and regulations, i.e., the Act and part 703 of this chapter for federal credit unions and the laws of the state in which the credit union operates for state-chartered credit unions, except state-chartered corporate credit unions. State-chartered corporate credit unions are permitted to make only those investments that are in conformance with part 704 of this chapter and applicable state laws and regulations;

(4) The presence of any account or security, the form of which has not been approved by the Board, except for accounts authorized by state law for state-chartered credit unions.

(c) *Fitness of management.* The officers, directors, and committee members of the credit union must have conducted its operations in accordance with provisions of applicable law, regulations, its charter and bylaws. No person shall serve as a director, officer, committee member, or employee of an insured credit union who has been convicted of any criminal offense involving dishonesty or breach of trust, except with the written consent of the Board.

(d) *Insurance of member accounts would not otherwise involve undue risk to the NCUSIF.* The credit union must maintain adequate fidelity bond coverage as specified in § 741.201. Any circumstances which may be unique to the particular credit union concerned shall also be considered in arriving at the determination of whether or not an undue risk to the NCUSIF is or may be present. For purposes of this section, the term "undue risk to the NCUSIF" is defined as a condition which creates a probability of loss in excess of that normally found in a credit union and which indicates a reasonably foreseeable probability of the credit union becoming insolvent because of such condition, with a resultant claim against the NCUSIF.

(e) *Powers and purposes.* The credit union must not perform services other than those which are consistent with the promotion of thrift and the creation of a source of credit for its members, except as otherwise permitted by law or regulation.

(f) *Letter of disapproval.* A credit union whose application for share insurance is disapproved shall receive a letter indicating the reasons for such disapproval, a citation of the authority for such disapproval, and suggested methods by which the applying credit union may correct its deficiencies and thereby qualify for share insurance.

(g) Nothing in this section shall preclude the NCUA Board from imposing additional terms or conditions pursuant to the insurance agreement.

§ 741.4 Insurance premium and one percent deposit.

(a) *Scope.* This section implements the requirements of Section 202 of the Act (12 U.S.C. 1782) providing for capitalization of the NCUSIF through the maintenance of a deposit by each insured credit union in an amount equaling one percent of its insured shares and payment of an insurance premium.

(b) *Definitions.* For purposes of this section:

(1) *Available assets ratio* means the ratio of:

(i) The amount determined by subtracting all liabilities of the NCUSIF, including contingent liabilities for which no provision for losses has been made, from the sum of cash and the market value of unencumbered investments authorized under 12 U.S.C. 1783(c), to:

(ii) The aggregate amount of the insured shares in all insured credit unions.

(iii) Shown as an abbreviated mathematical formula, the available assets ratio is:

$$\frac{\text{(cash + market value of unencumbered investments) – (liabilities + contingent liabilities for which no provision for losses has been made)}}{\text{aggregate amount of all insured shares from final reporting period of calendar year}}$$

(2) *Equity ratio* means the ratio of:

(i) The amount of NCUSIF's capitalization, meaning insured credit unions' one percent capitalization deposits plus the retained earnings balance of the NCUSIF (less contingent liabilities for which no provision for losses has been made) to:

(ii) The aggregate amount of the insured shares in all insured credit unions.

(iii) Shown as an abbreviated mathematical formula, the equity ratio is:

$$\frac{\text{insured credit unions' 1.0\% capitalization deposits + (NCUSIF's retained earnings – contingent liabilities for which no provision for losses has been made)}}{\text{aggregate amount of all insured shares}}$$

(3) *Insured shares* means the total amount of a credit union's share, share draft and share certificate accounts, or their equivalent under state law (which may include deposit accounts), authorized to be issued to members, other credit unions, public units, or nonmembers (where permitted under the Act or equivalent state law). "Insured shares" does not include amounts in excess of insurance coverage as provided in part 745 of this chapter; and

(4) *Normal operating level* means an equity ratio not less than 1.2 percent and not more than 1.5 percent, as established by action of the NCUA Board.

(5) *Reporting period* means calendar year for credit unions with total assets of less than $50,000,000 and means semiannual period for credit union with total assets of $50,000,000 or more.

(c) *One percent deposit.* Each insured credit union shall maintain with the NCUSIF during each reporting period a deposit in an amount equaling one percent of the total of the credit union's insured shares at the close of the preceding reporting period. For credit unions with total assets of less than $50,000,000, insured shares will be measured and adjusted annually based on the insured shares reported in the credit union's semiannual 5300 report due in January of each year. For credit unions with total assets of $50,000,000 or more, insured shares will be measured and adjusted semiannually based on the insured shares reported in the credit union's quarterly 5300 reports due in January and July of each year.

(d) *Insurance premium charges.* (1) *In general.* Each insured credit union will pay to the NCUSIF, on dates the NCUA Board determines, but not more than twice in any calendar year, an insurance premium in an amount stated as a percentage of insured shares, which will be the same for all insured credit unions.

(2) *Relation of premium charge to equity ratio of NCUSIF.* (i) The NCUA Board may assess a premium charge only if the NCUSIF's equity ratio is less than 1.3 percent and the pre-

mium charge does not exceed the amount necessary to restore the equity ratio to 1.3 percent.

(ii) If the equity ratio of NCUSIF falls below 1.2 percent, the NCUA Board is required to assess a premium in an amount it determines is necessary to restore the equity ratio to, and maintain that ratio at, 1.2 percent.

(e) *Distribution of NCUSIF equity.* If, as of the end of a calendar year, the NCUSIF exceeds its normal operating level and its available assets ratio exceeds 1.0 percent, the NCUA Board will make a proportionate distribution of NCUSIF equity to insured credit unions. The distribution will be the maximum amount possible that does not reduce the NCUSIF's equity ratio below its normal operating level and does not reduce its available assets ratio below 1.0 percent. The distribution will be after the calendar year and in the form determined by the NCUA Board. The form of the distribution may include a waiver of insurance premiums, premium rebates, or distributions from NCUSIF equity in the form of dividends. The NCUA Board will use the aggregate amount of the insured shares from all insured credit unions from the final reporting period of the calendar year in calculating the NCUSIF's equity ratio and available assets ratio for purposes of this paragraph.

(f) *Invoices.* The NCUA provides invoices to all federally insured credit unions stating any change in the amount of a credit union's one percent deposit and the computation and funding of any premium payment due. Invoices for federal credit unions also include any annual operating fees that are due. Invoices are calculated based on a credit union's insured shares as of the most recently ended reporting period. The invoices may also provide for any distribution the NCUA Board declares in accordance with paragraph (e) of this section, resulting in a single net transfer of funds between a credit union and the NCUA.

(g) *New charters.* A newly-chartered credit union that obtains share insurance coverage from the NCUSIF during the calendar year in which it has obtained its charter shall not be required to pay an insurance premium for that calendar year. The credit union shall fund its one percent deposit on a date to be determined by the NCUA Board in the following calendar year, but shall not participate in any distribution from NCUSIF equity related to the period prior to the credit union's funding of its deposit.

(h) *Conversion to Federal insurance.* An existing credit union that converts to insurance coverage with the NCUSIF shall immediately fund its one percent deposit based on the total of its insured shares as of the close of the month prior to conversion and, if any premiums have been assessed in that calendar year, will pay a prorated premium amount to reflect the remaining number of months in that calendar year. The credit union will be entitled to a prorated share of any distribution from NCUSIF equity declared subsequent to the credit union's conversion.

(i) *Mergers of nonfederally insured credit unions.* Where a nonfederally insured credit union merges into a federally insured credit union, the continuing federally insured credit union shall immediately pay to the NCUSIF a prorated insurance premium (unless waived in whole or in part for all federally insured credit unions), and an additional one percent deposit based upon the increase in insured shares resulting from the merger.

(j) *Return of deposit.* Any insolvent credit union that is closed for involuntary liquidation will not be entitled to a return of its deposit. Any solvent credit union that is closed due to involuntary liquidation shall be entitled to a return of its deposit prior to final distribution of member shares. Any other credit union whose insurance coverage with the NCUSIF terminates will be entitled to a return of the full amount of its deposit immediately after the final date on which any shares of the credit union are insured, except that the NCUA Board reserves the right to delay payment by up to one year if it determines that immediate payment would jeopardize the financial condition of the NCUSIF. This includes termination of insurance due to mergers and consolidations. A credit union that receives a return of its deposit during a calendar year shall have the option of leaving a nominal sum on deposit with the NCUSIF until the next distribution from NCUSIF equity and will thus qualify for a prorated share of the distribution.

(k) *Assessment of administrative fee and interest for delinquent payment.* Each federally insured credit union shall pay to the NCUA an administrative fee, the costs of collection, and interest on any delinquent payment of its capitalization deposit or insurance premium. A payment will be considered delinquent if it is postmarked later than the date stated in the invoice provided to the credit union. The NCUA may waive or abate charges or collection of interest, if circumstances warrant.

(1) The administrative fee for a delinquent payment shall be an amount as fixed from time to time by the NCUA Board based upon the

administrative costs of such delinquent payments to the NCUA in the preceding year.

(2) The costs of collection shall be calculated as the actual hours expended by NCUA personnel multiplied by the average hourly cost of the salaries and benefits of such personnel.

(3) The interest rate charged on any delinquent payment shall be the U.S. Department of the Treasury Tax and Loan Rate in effect on the date when the payment is due as provided in 31 U.S.C. 3717.

§ 741.5 Notice of termination of excess insurance coverage.

In the event of a credit union's termination of share insurance coverage other than that provided by the NCUSIF, the credit union must notify all members in writing of such termination at least thirty days prior to the effective date of termination.

§ 741.6 Financial and statistical and other reports.

(a) Each operating insured credit union must file with the NCUA a quarterly Financial and Statistical Report on or before January 22 (as of the previous December 31), April 22 (as of the previous March 31), July 22 (as of the previous June 30), and October 22 (as of the previous September 30) of each year. Insured credit unions with assets of $10 million or greater must file all quarterly reports on Form NCUA 5300. Insured credit unions with assets of less than $10 million must file their first (due April 22) and third (due October 22) quarter reports on Form NCUA 5300SF or Form NCUA 5300 and their second (due July 22) and fourth (due January 22) quarter reports on Form NCUA 5300.

(b) *Consistency with GAAP.* The accounts of financial statements and reports required to be filed quarterly under paragraph (a) of this section must reflect GAAP if the credit union has total assets of $10 million or greater, but may reflect regulatory accounting principles other than GAAP if the credit union has total assets of less than $10 million (except that a Federally-insured State-chartered credit union may be required by its state credit union supervisor to follow GAAP regardless of asset size).

(c) *GAAP sources.* GAAP means generally accepted accounting principles, as defined in § 715.2(e) of this chapter. GAAP is distinct from GAAS, which means generally accepted auditing standards, as defined in § 715.2(f) of this chapter. Authoritative sources of GAAP include, but are not limited to, pronouncements of the Financial Accounting Standards Board (FASB) and its predecessor organizations, the Accounting Standards Executive Committee (AcSEC) of the American Institute of Certified Public Accountants (AICPA), the FASB's Emerging Issues Task Force (EITF), and the applicable AICPA Audit and Accounting Guide.

(d) Insured credit unions shall, upon written notice from the NCUA Board or Regional Director, file such financial or other reports in accordance with instructions contained in such notice.

§ 741.7 Conversion to a state-chartered credit union.

Any federal credit union that petitions to convert to a state-chartered federally insured credit union is required to apply to the Regional Director for continued insurance of its accounts and meet the requirements as stated in the Act and this part. If the application for continued insurance is not approved, such insurance will terminate subject to the conditions set forth in section 206(d) of the Act.

§ 741.8 Purchase of assets and assumption of liabilities.

(a) Any credit union insured pursuant to Title II of the Act must apply for and receive approval from the NCUA Board before either purchasing or acquiring loans or assuming or receiving an assignment of deposits, shares, or liabilities from:

(1) Any credit union that is not insured pursuant to Title II of the Act;

(2) Any other financial-type institution (including depository institutions, mortgage banks, consumer finance companies, insurance companies, loan brokers, and other loan sellers or liability traders); or

(3) Any successor in interest to any institution identified in paragraph (a)(1) or (a)(2) of this section.

(b) Approval is not required for:

(1) Purchases of student loans or real estate secured loans to facilitate the packaging of a pool of loans to be sold or pledged on the secondary market under § 701.23(b)(1) (iii) or (iv) of this chapter or comparable state law for state-chartered credit unions, or purchases of member

loans under § 701.23(b)(1)(i) of this chapter or comparable state law for state-chartered credit unions; or

(2) Assumptions or receipt of deposits, shares or liabilities as rollovers or transfers of member retirement accounts or in which an NCUSIF-insured credit union perfects a security interest in connection with an extension of credit to any member.

§ 741.9 Uninsured membership shares.

Any credit union that is insured pursuant to Title II of the Act may not offer membership shares that, due to the terms and conditions of the account, are not eligible for insurance coverage. This prohibition does not apply to shares that are uninsured solely because the amount is in excess of the maximum insurance coverage provided pursuant to part 745 of this chapter.

§ 741.10 Disclosure of share insurance.

Any credit union which is insured pursuant to Title II of the Act and is permitted by state law to accept nonmember shares or deposits from sources other than other credit unions and public units (or, for low-income designated credit unions, any nonmembers), shall identify such nonmember accounts as nonmember shares or deposits on any statement or report required by the NCUA Board for insurance purposes. Immediately after a state-chartered credit union receives notice from NCUA that its member accounts are federally insured, the credit union shall advise any present nonmember share and deposit holders by letter that their accounts are not insured by the NCUSIF. Also, future nonmember share and deposit fund holders will be so advised by letter as they open accounts.

§ 741.11 Foreign branching.

(a) *Application and Prior NCUA Approval Required.* Any credit union insured under Title II of the Act must apply for and receive approval from the regional director before establishing a credit union branch outside the United States unless the foreign branch is located on a United States military instillation or embassy outside the United States. The regional director will have 60 days to approve or deny the request.

(b) *Contents of Application.* The application must include a business plan, written approval by the state supervisory agency if the applicant is a state-chartered credit union, and documentation evidencing written permission from the host country to establish the branch that explicitly recognizes NCUA's authority to examine and take any enforcement action, including conservatorship and liquidation actions.

(c) *Contents of Business Plan.* The written business plan must address the following:

(1) Analysis of market conditions in the area where the branch is to be established;

(2) The credit union's plan for addressing foreign currency risk;

(3) Operating facilities, including office space/equipment and supplies;

(4) Safeguarding of assets, bond coverage, insurance coverage, and records preservation;

(5) Written policies regarding the branch (shares, lending, capital, charge-offs, collections);

(6) The field of membership or portion of the field of membership to be served through the foreign branch and the financial needs of the members to be served and services and products to be provided;

(7) Detailed *pro forma* financial statements for branch operations (balance sheet and income and expense projections) for the first and second year including assumptions;

(8) Internal controls including cash disbursal procedures for shares and loans at the branch;

(9) Accounting procedures used to identify branch activity and performance; and

(10) Foreign income taxation and employment law.

(d) *Revocation of Approval.* A state regulator that revokes approval of the branch office must notify NCUA of the action once it issues the notice of revocation. The regional director may revoke approval of the branch office for failure to follow the business plan in a material respect or for substantive and documented safety and soundness reasons. If the regional director revokes the approval, the credit union will have six months from the date of the revocation letter to terminate the operations of the branch. The credit union can appeal this revocation directly to the NCUA Board within 30 days of the date of the revocation letter.

(e) *Insurance Coverage.* Accounts at foreign branches are insured by the NCUSIF only if de-

nominated in U.S. dollars and only if payable, by the terms of the account agreement, at a U.S. office of the credit union. If the host country requires insurance from its own system, accounts will not be insured by the National Credit Union Share Insurance Fund.

Subpart B—Regulations Codified Elsewhere in NCUA's Regulations as Applying to Federal Credit Unions That Also Apply to Federally Insured State-Chartered Credit Unions

§ 741.201 Minimum fidelity bond requirements.

(a) Any credit union which makes application for insurance of its accounts pursuant to Title II of the Act must possess the minimum fidelity bond coverage stated in part 713 of this chapter in order for its application for such insurance to be approved and for such insurance coverage to continue. A federally insured credit union whose fidelity bond coverage is terminated shall mail notice of such termination to the Regional Director not less than 35 days prior to the effective date of such termination.

(b) Corporate credit unions must comply with § 704.17 of this chapter in lieu of part 713 of this chapter.

§ 741.202 Audit and verification requirements.

(a) The supervisory committee of each credit union insured pursuant to Title II of the Act shall make or cause to be made an audit of the credit union at least once every calendar year covering the period elapsed since the last audit. The audit must fully meet the applicable requirements set forth in part 715 of this chapter or applicable state laws, whichever requirement is more stringent.

(b) Each credit union which is insured pursuant to Title II of the Act shall verify or cause to be verified, under controlled conditions, all passbooks and accounts with the records of the financial officer not less frequently than once every 2 years. The verification must fully meet the requirements set forth in § 715.8 of this chapter.

§ 741.203 Minimum loan policy requirements.

Any credit union which is insured pursuant to Title II of the Act must:

(a) Adhere to the requirements stated in part 723 of this chapter concerning member business loans, § 701.21(c)(8) of this chapter concerning prohibited fees, and § 701.21(d)(5) of this chapter concerning nonpreferential loans. State-chartered, NCUSIF-insured credit unions in a given state are exempt from these requirements if the state supervisory authority for that state adopts substantially equivalent regulations as determined by the NCUA Board or, in the case of the member business loan requirements, if the state supervisory authority adopts member business loan regulations that are approved by the NCUA Board pursuant to § 723.20. In nonexempt states, all required NCUA reviews and approvals will be handled in coordination with the state credit union supervisory authority; and

(b) Adhere to the requirements stated in part 722 of this chapter concerning appraisals.

§ 741.204 Maximum public unit and nonmember accounts, and low-income designation.

Any credit union that is insured, or that makes application for insurance, pursuant to Title II of the Act must:

(a) Adhere to the requirements of § 701.32 of this chapter regarding public unit and nonmember accounts, provided it has the authority to accept such accounts. Requests by federally insured state-chartered credit unions for an exemption from the limitation of § 701.32 of this chapter will be made and reviewed on the same basis as that provided in § 701.32 of this chapter for federal credit unions, provided, however that NCUA will not grant an exemption without the concurrence of the appropriate state regulator.

(b) Obtain a low-income designation in order to accept nonmember accounts, other than from public units or other credit unions, provided it has the authority to accept such accounts under state law. The state regulator shall make the low-income designation with the concurrence of the appropriate regional director. The designation will

be made and reviewed by the state regulator on the same basis as that provided in § 701.34(a) of this chapter for federal credit unions. Removal of the designation by the state regulator for such credit unions shall be with the concurrence of NCUA.

(c) Receive secondary capital accounts only if the credit has a low-income designation pursuant to paragraph (b) of this section, and then only in accordance with the terms and conditions authorized for Federal credit unions pursuant to § 701.34 of this chapter and to the extent not inconsistent with applicable state law and regulation. State chartered federally insured credit unions offering secondary capital accounts must submit the plan required by § 701.34 to both the state supervisory authority and the NCUA Regional Director.

§ 741.205 Reporting requirements for credit unions that are newly chartered or in troubled condition.

Any federally insured credit union chartered for less than 2 years or any credit union defined to be in troubled condition as set forth in § 701.14(b)(3) of this chapter must adhere to the requirements stated in § 701.14(c) of this chapter concerning the prior notice and NCUA review. Federally insured state-chartered credit unions must submit required information to both the appropriate NCUA Regional Director and their state supervisor. NCUA will consult with the state supervisor before making its determination pursuant to § 701.14 (d)(2) and (f) of this chapter. NCUA will notify the state supervisor of its approval/disapproval no later than the time that it notifies the affected individual pursuant to § 701.14(d)(1) of this chapter.

§ 741.206 Corporate credit unions.

Any corporate credit union insured pursuant to Title II of the Act shall adhere to the requirements of part 704 of this chapter.

§ 741.207 Community development revolving loan program for credit unions.

Any credit union which is insured pursuant to Title II of the Act and is a "participating credit union," as defined in § 705.3 of this chapter, shall adhere to the requirements stated in part 705 of this chapter.

§ 741.208 Mergers of federally insured credit unions: voluntary termination or conversion of insured status.

Any credit union which is insured pursuant to Title II of the Act and which merges with another credit union or non-credit union institution, and any state-chartered credit union which voluntarily terminates its status as a federally-insured credit union, or converts from federal insurance to other insurance from a government or private source authorized to insure member accounts, shall adhere to the applicable requirements stated in section 206 of the Act and parts 708a and 708b of this chapter concerning mergers and voluntary termination or conversion of insured status.

§ 741.209 Management official interlocks.

Any credit union which is insured pursuant to Title II of the Act shall adhere to the requirements stated in part 711 of this chapter concerning management official interlocks, issued under the provisions of the Depository Institution Management Interlocks Act (12 U.S.C. 3201 et seq.).

§ 741.210 Central liquidity facility.

Any credit union which is insured pursuant to Title II of the Act and is a member of the Central Liquidity Facility, shall adhere to the requirements stated in part 725 of this chapter.

§ 741.211 Advertising.

Any credit union which is insured pursuant to Title II of the Act shall adhere to the requirements prescribed by part 740 of this chapter.

§ 741.212 Share insurance.

(a) Member share accounts received by any credit union which is insured pursuant to Title II of the Act in its usual course of business, including regular shares, share certificates, and share draft accounts, are insured subject to the limitations and rules in subpart A of part 745 of this chapter.

(b) The payment of share insurance and the appeal process applicable to any credit union which is insured pursuant to Title II of the Act are addressed in subpart B of part 745 of this chapter.

§ 741.213 Administrative actions, adjudicative hearings, rules of practice and procedure.

Any credit union which is insured pursuant to Title II of the Act shall adhere to the applicable rules of practice and procedures for administrative actions and adjudicative hearings prescribed by part 747 of this chapter. Subpart E of part 747 of this chapter applies only to federal credit unions.

§ 741.214 Report of crime or catastrophic act and Bank Secrecy Act compliance.

Any credit union which is insured pursuant to Title II of the Act shall adhere to the requirements stated in part 748 of this chapter.

§ 741.215 Records preservation program.

Any credit union which is insured pursuant to Title II of the Act shall maintain a records preservation program as prescribed by part 749 of this chapter.

§ 741.216 Flood insurance.

Any credit union which is insured pursuant to Title II of the Act shall adhere to the requirements stated in part 760 of this chapter.

§ 741.217 Truth in savings.

Any credit union which is insured pursuant to Title II of the Act shall adhere to the requirements stated in part 707 of this chapter.

§ 741.218 Involuntary liquidation and creditor claims.

Any credit union which is insured pursuant to Title II of the Act shall adhere to the applicable provisions in part 709 of this chapter. Section 709.3 of this chapter applies only to federal credit unions.

§ 741.219 Investment requirements.

Any credit union which is insured pursuant to Title II of the Act must adhere to the requirements stated in part 703 of this chapter concerning transacting business with corporate credit unions.

§ 741.220 Privacy of consumer financial information.

Any credit union which is insured pursuant to Title II of the Act must adhere to the requirements stated in part 716 of this chapter.

§ 741.221 Suretyship and guaranty requirements.

Any credit union, which is insured pursuant to Title II of the Act, must adhere to the requirements in § 701.20 of this chapter. State-chartered, NCUSIF-insured credit unions may only enter into suretyship and guaranty agreements to the extent authorized under state law.

Part 742

Regulatory Flexibility Program

§ 742.1 What is NCUA's Regulatory Flexibility Program?

NCUA's Regulatory Flexibility Program (RegFlex) exempts credit unions with a current net worth of nine percent (or if a credit union is subject to a risk-based net worth requirement under § 702.103 of this chapter, it must be 200 basis points over its risked based net worth level or nine percent, whichever is higher) and a CAMEL rating of 1 or 2, for two consecutive examinations, from all or part of identified NCUA regulations. The Regulatory Flexibility Program also grants eligible credit unions additional powers.

§ 742.2 How do I become eligible for the Regulatory Flexibility Program?

Eligibility is automatic as soon as the credit union meets the net worth and CAMEL criteria. If a credit union is a CAMEL 3 (or CAMEL 1 or 2 for less than two consecutive cycles) with a net worth in excess of 9 percent or if the credit union is a CAMEL 1 or 2 with a net worth under 9 percent (or if a credit union is subject to a risk-based net worth requirement under § 702.103 of this chapter, and it does not exceed 200 basis points over its risk based net worth level), it can apply to the regional director for a RegFlex designation, in whole or in part.

§ 742.3 Will NCUA notify me when I am eligible for the Regulatory Flexibility Program?

Yes. Once this rule is effective, NCUA will notify all RegFlex eligible credit unions. Subsequent notifications of eligibility will occur after an application for a RegFlex designation or as part of the examination process.

§ 742.4 From what NCUA regulations will I be exempt?

(a) RegFlex credit unions are exempt from the provisions of the following NCUA regulations without restrictions or limitations: § 701.25, § 701.32(b) and (c), § 701.36(a), § 703.5(b)(1)(ii) and (2), § 703.12(c), § 703.16(b), and § 723.7(b) of this chapter.

(b) RegFlex credit unions are exempt from the provisions of the following NCUA regulations with certain restrictions or limitations:

(1) Section 703.13(d)(3) of this chapter, provided the value of the investments that mature later than the borrowing repurchase transaction does not exceed 100 percent of the Federal credit union's net worth; and

(2) Section 703.16(d) of this chapter provided:

(i) The issuer of the security is domestic;

(ii) The security is rated in one of the two highest rating categories by at least one nationally-recognized statistical rating organization;

(iii) The security meets the definition of mortgage related security as defined in 15 U.S.C. 78c(a)(41) and the definition of commercial mortgage related security as defined in § 703.2 of this chapter;

(iv) The security's underlying pool of loans contains more than 50 loans with no one loan representing more than 10 percent of the pool; and

(v) The aggregate total of commercial mortgage related securities purchased by the Federal credit union does not exceed 50 percent of its net worth.

§ 742.5 What additional authority will I be granted?

Notwithstanding the general limitations in § 701.23 of this chapter, RegFlex credit unions are eligible to purchase any auto loan, credit card loan, member business loan, student loan or mortgage loan from any federally insured credit union as long as the loans are loans that the purchasing credit union is empowered to grant. RegFlex credit unions are authorized to keep these loans in their portfolio. If a RegFlex credit union is purchasing

the eligible obligations of a liquidating credit union, the loans purchased cannot exceed 5% of the unimpaired capital and surplus of the purchasing credit union.

§ 742.6 How can I lose my RegFlex eligibility?

Eligibility may be lost in two ways. First, the credit union no longer meets the RegFlex criteria set forth in § 742.1. When this event occurs, the credit union must cease using the additional authority granted by this rule. Second, the regional director for substantive and documented safety and soundness reasons may revoke a credit union's RegFlex authority in whole or in part. The regional director must give a credit union written notice stating the reasons for this action. The revocation is effective as soon as the regional director's determination has been received by the credit union.

§ 742.7 What is the appeal process?

A credit union has 60 days from the date of the regional director's determination to revoke a credit union's RegFlex authority (in whole or in part) to appeal the action to NCUA's Supervisory Review Committee. The regional director's determination will remain in effect unless the Supervisory Review Committee issues a different determination. If the credit union is dissatisfied with the decision of the Supervisory Review Committee, the credit union has 60 days from the issuance of this decision to appeal to the NCUA Board.

§ 742.8 If I lose my RegFlex authority, will my past actions be grandfathered?

Any action by the credit union under the RegFlex authority will be grandfathered. Any actions subsequent to losing the RegFlex authority must meet NCUA's regulatory requirements. This does not diminish NCUA's authority to require a credit union to divest its investments or assets for substantive safety and soundness reasons.

Part 745

Share Insurance and Appendix

Subpart A—Clarification and Definition of Account Insurance Coverage

§ 745.0 Scope.

The regulation and appendix contained in this Part describe the insurance coverage of various types of member accounts. In general, all types of member share accounts received by the credit union in its usual course of business, including regular shares, share certificates, and share draft accounts, represent equity and are insured. For the purposes of applying the rules in this Part, it is presumed that the owner of funds in an account is an insured credit union member or otherwise eligible to maintain an insured account in a credit union. These rules do not extend insurance coverage to persons not entitled to maintain an insured account or to account relationships that have not been approved by the Board as an insured account. Where there are multiple owners of a single account, generally only that part which is allocable to the member(s) is insured.

§ 745.1 Definitions.

(a) The terms "account" or "accounts" as used in this Part mean share, share certificate or share draft accounts (or their equivalent under state law, as determined by the Board in the case of insured state credit unions) of a member (which includes other credit unions, public units and nonmembers where permitted under the Act) in a credit union of a type approved by the Board which evidences money or its equivalent received or held by a credit union in the usual course of business and for which it has given or is obligated to give credit to the account of the member.

(b) The terms "member" or "members" as used in this Part mean those persons enumerated in the credit union's field of membership who have been elected to membership in accordance with the Act or state law in the case of state credit unions. It also includes those nonmembers permitted under the Act to maintain accounts in an insured credit union, including nonmember credit unions and nonmember public units and political subdivisions.

(c) The term "public unit" means the United States, any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Panama Canal Zone, any territory or possession of the United States, any county, municipality, or political subdivision thereof, or any Indian tribe as defined in Section 3(c) of the Indian Financing Act of 1974.

(d) The term "political subdivision" includes any subdivision of a public unit, as defined in (c) above, or any principal department of such public unit, (1) the creation of which subdivision or department has been expressly authorized by state statute, (2) to which some functions of government have been delegated by state statute, and (3) to which funds have been allocated by statute or ordinance for its exclusive use and control. It also includes drainage, irrigation, navigation improvement, levee, sanitary, school or power districts and bridge or port authorities, and other special districts created by state statute or compacts between the states. Excluded from the term are subordinate or nonautonomous divisions, agencies, or boards within principal departments.

§ 745.2 General Principles Applicable in Determining Insurance of Accounts.

(a) General: This Part provides for determination by the Board of the amount of members' insured accounts. The rules for determining the insurance coverage of accounts maintained by members in the same or different rights and capacities in the same insured credit union are set forth in the following provisions of this Part. The Appendix provides examples of the application of these rules to various factual situations. While the provisions of this part govern in determining share insurance coverage, to the extent local law enters into a share insurance determination, the local law of the jurisdiction in which the insured credit union's principal office is located will control over the local

law of other jurisdictions where the insured credit union has offices or service facilities.

(b) The regulations in this Part in no way are to be interpreted to authorize any type of account that is not authorized by Federal law or regulation or State law or regulation or by the bylaws of a particular credit union. The purpose is to be as inclusive as possible of all situations.

(c) Records: (1) The account records of the insured credit union shall be conclusive as to the existence of any relationship pursuant to which the funds in the account are deposited and on which a claim for insurance coverage is founded. Examples would be trustee, agent, custodian, or executor. No claim for insurance based on such a relationship will be recognized in the absence of such disclosure.

(2) If the account records of an insured credit union disclose the existence of a relationship which may provide a basis for additional insurance, the details of the relationship and the interest of other parties in the account must be ascertainable either from the records of the credit union or the records of the member maintained in good faith and in the regular course of business.

(3) The account records of an insured credit union in connection with a trust account shall disclose the name of both the settlor (grantor) and the trustee of the trust and shall contain an account signature card executed by the trustee.

(4) The interests of the co-owners of a joint account shall be deemed equal, unless otherwise stated on the insured credit union's records in the case of a tenancy in common.

(d) Valuation of trust interests: (1) Trust interests in the same trust deposited in the same account will be separately insured if the value of the trust interest is capable of determination, without evaluation of contingencies, except for those covered by the present worth tables and rules of calculation for their use set forth in § 20.2031–7 of the Federal Estate Tax Regulations (26 C.F.R. 20.2031–7).

(2) In connection with any trust in which certain trust interests are not capable of evaluation in accordance with the foregoing rule, payment by the Board to the trustee with respect to all such trust interests shall not exceed the basic insured amount of $100,000.

(3) Each trust interest in any trust established by two or more settlors shall be deemed to be derived from each settlor pro rata to his contribution to the trust.

(4) The term "trust interest" means the interest of a beneficiary in an irrevocable express trust, whether created by trust instrument or statute, but does not include any interest retained by the settlor.

(e) *Continuation of insurance coverage following the death of a member.* The death of a member will not affect the member's share insurance coverage for a period of six months following death unless the member's share accounts are restructured in that time period. If the accounts are restructured during the six-month grace period, or upon the expiration of the six months if not restructured, the share insurance coverage will be provided on the basis of actual ownership of the accounts in accordance with the provisions of this part. The operation of this grace period, however, will not result in a reduction of coverage.

(f) *Continuation of separate share insurance coverage after merger of insured credit unions.* Whenever the liability to pay the member accounts of one or more insured credit unions is assumed by another insured credit union, whether by merger, consolidation, other statutory assumption or contract: The insured status of the credit unions whose member account liability has been assumed terminates, for purposes of this section, on the date of receipt by NCUA of satisfactory evidence of the assumption; and the separate insurance of member accounts assumed continues for six months from the date the assumption takes effect or, in the case of a share certificate, the earliest maturity date after the six-month period. In the case of a share certificate that matures within the six-month grace period that is renewed at the same dollar amount, either with or without accrued dividends having been added to the principal amount, and for the same term as the original share certificate, the separate insurance applies to the renewed share certificate until the first maturity date after the six-month period. A share certificate that matures within the six-month grace period that is renewed on any other basis, or that is not renewed, is separately insured only until the end of the six-month grace period.

§ 745.3 Single Ownership Accounts.

(a) Funds owned by an individual and deposited in the manner set forth below shall be added together and insured up to $100,000 in the aggregate.

(1) *Individual accounts.* Funds owned by an individual (or by the husband-wife community

of which the individual is a member) and deposited in one or more accounts in the individual's own name shall be insured up to $100,000 in the aggregate.

(2) *Accounts held by agents or nominees.* Funds owned by a principal and deposited in one or more accounts in the name or names of agents or nominees shall be added to any individual account of the principal and insured up to $100,000 in the aggregate.

(3) *Custodial loan accounts.* Loan payments received by a Federal credit union prior to remittance to other parties to whom the loan was sold pursuant to Section 107(13) of the Federal Credit Union Act and Section 701.23 of NCUA's Regulations shall be considered to be funds owned by the borrower and shall be added to any individual accounts of the borrower and insured up to $100,000 in the aggregate.

(b) Funds held by a guardian, custodian, or conservator for the benefit of his ward or for the benefit of a minor under a Uniform Gifts to Minors Act and deposited in one or more accounts in the name of the guardian, custodian, or conservator are insured up to $100,000 in the aggregate, separately from any other accounts of the guardian, custodian, conservator, ward, or minor.

§ 745.4 Revocable trust accounts.

(a) For purposes of this part, the term "revocable trust account" includes a testamentary account, tentative or "Totten" trust account, "payable-on-death" account, or any similar account which evidences an intention that the funds shall pass on the death of the owner of the funds to a named beneficiary.

(b) If the named beneficiary of a revocable trust account is a spouse, child, grandchild, parent, brother or sister of the account owner, the account shall be insured up to $100,000 in the aggregate as to each such beneficiary, separately from any other accounts of the owner or beneficiary, regardless of the membership status of the beneficiary.

(c) If the named beneficiary of a revocable trust account is other than the spouse, child, grandchild, parent, brother or sister of the account owner, the funds corresponding to that beneficiary shall be treated as an individually owned account of the owner, aggregated with any other individually owned accounts of the owner, and insured up to $100,000. For example, if A establishes an account payable upon death to his nephew, the account would be insured as an individual account owned by A. Similarly, if B establishes an account payable upon death to her husband, son and nephew, two-thirds of the account balance would be eligible for revocable trust account coverage up to $200,000 corresponding to the two qualifying beneficiaries, the spouse and child. The amount corresponding to the non-qualifying beneficiary, the nephew, would be deemed to be owned by B as an individual account and insured accordingly.

(d) For purposes of this section, the term "child" includes the biological, adopted or step-child of the owner; the term "grandchild" includes the biological, adopted or step-child of any of the owner's children; the term "parent" includes the biological, adoptive or step-parent of the owner; the term "brother" includes a full brother, half brother, brother through adoption or step-brother; and the term "sister" includes a full sister, half sister, sister through adoption or step-sister.

(e) *Living Trusts.* Insurance treatment under this section also applies to revocable trust accounts held in connection with a so-called "living trust," meaning a formal trust that an owner creates and retains control over during his or her lifetime. If a named beneficiary in a living trust is a qualifying beneficiary under this section, then the share account held in connection with the living trust may be eligible for share insurance under this section, assuming compliance with all the provisions of this part. This coverage applies only if, at the time an insured credit union fails, a qualifying beneficiary would be entitled to his or her interest in the trust assets upon the grantor's death and that ownership interest would not depend upon the death of another beneficiary. If there is more than one grantor, the beneficiary's entitlement to the trust assets must be upon the death of the last grantor. The coverage provided in this paragraph (e) is irrespective of any other conditions in the trust that might prevent a beneficiary from acquiring an interest in the share account upon the account owner's death. The rules in paragraph (c) of this section on the interests of non-qualifying beneficiaries apply to living trust accounts. For living trust accounts that provide for a life estate interest for designated beneficiaries and a remainder interest for other beneficiaries, unless otherwise indicated in the trust, each life estate holder and each remainder-man will be deemed to have equal interests in the trust assets for share insurance purposes. Coverage will then be provided under the rules in this paragraph (e) up to $100,000 per qualifying beneficiary. For a living trust account to qualify for coverage provided under this paragraph (e), the records of the

credit union must reflect that the funds in the account are held pursuant to a formal revocable trust, but the credit union's records need not indicate the names of the beneficiaries of the living trust or their ownership interests in the trust. Effective April 1, 2004, this paragraph (e) will apply to all living trust accounts, unless, upon an insured credit union failure, a member who established a living trust before April 1, 2004, chooses coverage under the previous living trust account rules. For any insured credit union failures occurring between February 19, 2004 and April 1, 2004, the NCUA will apply the living trust account rules in this revised paragraph (e) if doing so would benefit living trust account holders of such insured credit union.

(f) *Joint revocable trust accounts.* Where an account described in paragraph (a) of this section is established by more than one owner and held for the benefit of others, some or all of whom are within the qualifying degree of kinship, the respective interests of each owner held for the benefit of each qualifying beneficiary will be separately insured up to $100,000. The interest of each co-owner will be deemed equal unless otherwise stated in the share account records of the federally-insured credit union. Interests held for non-qualifying beneficiaries will be added to the individual accounts of the owners. Where a husband and a wife establish a revocable trust account naming themselves as the sole beneficiaries, the account will not be insured according to the provisions of this section, but will instead be insured in accordance with the joint account provisions of § 745.8.

§ 745.5 Accounts Held by Executors or Administrators.

Funds of a decedent held in the name of the decedent or in the name of the executor or administrator of the decedent's estate and deposited in one or more accounts shall be insured up to $100,000 in the aggregate for all such accounts, separately from the individual accounts of the beneficiaries of the estate or of the executor or administrator.

§ 745.6 Accounts Held by a Corporation, Partnership or Unincorporated Association.

Accounts of a corporation, partnership, or unincorporated association engaged in any independent activity shall be insured up to $100,000 in the aggregate. The account of a corporation, partnership, or unincorporated association not engaged in an independent activity shall be deemed to be owned by the person or persons owning such corporation or comprising such partnership or unincorporated association and, for account insurance purposes, the interest of each person in such an account shall be added to any other account individually owned by such person and insured up to $100,000 in the aggregate. For purposes of this section, "independent activity" means an activity other than one directed solely at increasing insurance coverage.

§ 745.7 (Reserved)

§ 745.8 Joint ownership accounts.

(a) *Separate insurance coverage.* Qualifying joint accounts, whether owned as joint tenants with right of survivorship, as tenants by the entireties, as tenants in common, or by husband and wife as community property, shall be insured separately from accounts individually owned by any of the co-owners. The interest of a co-owner in all qualifying joint accounts shall be added together and the total for that co-owner shall be insured up to $100,000.

(b) *Qualifying joint accounts.* A joint account is a qualifying joint account if each of the co-owners has personally signed a membership or account signature card and has a right of withdrawal on the same basis as the other co-owners. The signature requirement does not apply to share certificates, or to any accounts maintained by an agent, nominee, guardian, custodian or conservator on behalf of two or more persons if the records of the credit union properly reflect that the account is so maintained.

(c) *Failure to qualify.* A joint account that does not meet the requirements for a qualifying joint account shall be treated as owned by the named persons as individuals and the actual ownership interest of each such person in such account shall be added to any other accounts individually owned by such person and insured up to $100,000 in the aggregate. An account will not fail to qualify as a joint account if a joint owner is a minor and applicable state law limits or restricts a minor's withdrawal rights.

(d) *Nonmember joint owners.* A nonmember may become a joint owner with a member on a joint account with right of survivorship. The nonmem-

ber's interest in such accounts will be insured in the same manner as the member joint-owner's interest.

§ 745.9–1 Trust Accounts.

(a) For purposes of this section, "trust" refers to an irrevocable trust.

(b) All trust interests (as defined in subsection 745.2(d)(4)), for the same beneficiary, deposited in an account and established pursuant to valid trust agreements created by the same settlor (grantor) shall be added together and insured up to $100,000 in the aggregate, separately from other accounts of the trustee of such trust funds or the settlor or beneficiary of such trust arrangements.

(c) This section applies to trust interests created in Coverdell Education Savings Accounts, formerly Education IRAs, established in connection with section 530 of the Internal Revenue Code (26 U.S.C. 530).

§ 745.9–2 IRA/Keogh Accounts.

(a) The present vested ascertainable interest of a participant or designated beneficiary in a trust or custodial account maintained pursuant to a pension or profit-sharing plan described under section 401(d) (Keogh account), section 408(a) (IRA) and section 408A (Roth IRA) of the Internal Revenue Code (26 U.S.C. 401(d), 408(a) and 408A), or similar provisions of law applicable to a U.S. territory or possession, will be insured up to $100,000 separately from other accounts of the participant or designated beneficiary. For insurance purposes, IRA and Roth IRA accounts will be combined together and insured in the aggregate up to $100,000. A Keogh account will be separately insured from an IRA account, Roth IRA account or, where applicable, aggregated IRA and Roth IRA accounts.

§ 745.9–3 Deferred Compensation Accounts.

Funds deposited by an employer pursuant to a deferred compensation plan (including § 401(K) of the Internal Revenue Code) shall be insured up to $100,000 as to the interest of each plan participant who is a member, separately from other accounts of the participant or employer.

§ 745.10 Public Unit Accounts.

(a) Public funds invested in Federal credit unions and federally-insured state credit unions authorized to accept such investments shall be insured as follows:

(1) Each official custodian of funds of the United States lawfully investing the same in a federally-insured credit union will be separately insured in the amount of:

(i) Up to $100,000 in the aggregate for all share draft accounts; and

(ii) Up to $100,000 in the aggregate for all share certificate and regular share accounts;

(2) Each official custodian of funds of any state of the United States or any county, municipality, or political subdivision thereof lawfully investing the same in a federally-insured credit union in the same state will be separately insured in the amount of:

(i) Up to $100,000 in the aggregate for all share draft accounts; and

(ii) Up to $100,000 in the aggregate for all share certificate and regular share accounts;

(3) Each official custodian of funds of the District of Columbia lawfully investing the same in a federally-insured credit union in the District of Columbia will be separately insured in the amount of:

(i) Up to $100,000 in the aggregate for all share draft accounts; and

(ii) Up to $100,000 in the aggregate for all share certificate and regular share accounts;

(4) Each official custodian of funds of the Commonwealth of Puerto Rico, the Panama Canal Zone, or any territory or possession of the United States, or any county, municipality, or political subdivision thereof lawfully investing the same in a federally-insured credit union in Puerto Rico, the Panama Canal Zone, or any such territory or possession, respectively, will be separately insured in the amount of:

(i) Up to $100,000 in the aggregate for all share draft accounts; and

(ii) Up to $100,000 in the aggregate for all share certificate and regular share accounts;

(5) Each official custodian of tribal funds of any Indian tribe (as defined in section 3(c) of the Indian Financing Act of 1974) or agency thereof lawfully investing the same in a federally-insured credit union will be separately insured in the amount of:

(i) Up to $100,000 in the aggregate for all share draft accounts; and

(ii) Up to $100,000 in the aggregate for all share certificate and regular share accounts;

(b) Each official custodian referred to in paragraphs (a)(2), (3), and (4) of this section lawfully investing such funds in share accounts in a federally-insured credit union outside of their respective jurisdictions shall be separately insured up to $100,000 in the aggregate for all such accounts regardless of whether they are share draft, share certificate or regular share accounts.

(c) For purposes of this section, if the same person is an official custodian of more than one public unit, he shall be separately insured with respect to the public funds held by him for each such unit, but he shall not be separately insured with respect to all public funds of the same public unit by virtue of holding different offices in such unit or by holding such funds for different purposes. Where an officer, agent or employee of a public unit has custody of certain funds which by law or under a bond indenture are required to be set aside to discharge a debt owed to the holders of notes or bonds issued by the public unit, any investment of such funds in an account in a federally-insured credit union will be deemed to be a share account established by a trustee of trust funds of which the noteholders or bondholders are pro rata beneficiaries, and the beneficial interest of each noteholder or bondholder in the share account will be separately insured up to $100,000.

(d) For purposes of this section, "lawfully investing" means pursuant to the statutory or regulatory authority of the custodian or public unit.

§ 745.11 Accounts Evidenced by Negotiable Instruments.

If any insured account obligation of a credit union is evidenced by a negotiable certificate account, negotiable draft, negotiable cashier's or officer's check, negotiable certified check, or negotiable traveler's check or letter of credit, the owner of such account obligation will be recognized for all purposes of a claim for insured accounts to the same extent as if his name and interest were disclosed on the records of the credit union provided the instrument was in fact negotiated to such owner prior to the date of the closing of the credit union. Affirmative proof of such negotiation must be offered in all cases to substantiate the claim.

§ 745.12 Account Obligations for Payment of Items Forwarded for Collection by Depository Institution Acting as Agent.

Where a closed credit union has become obligated for the payment of items forwarded for collection by a depository institution acting solely as agent, the owner of such items will be recognized for all purposes of a claim for insured accounts to the same extent as if his name and interest were disclosed on the records of the credit union when such claim for insured accounts, if otherwise payable, has been established by the execution and delivery of prescribed forms. Such depository institution forwarding such items for the owners thereof will be recognized as agent for such owners for the purpose of making an assignment of the rights of such owners against the closed insured credit union to the Board and for the purpose of receiving payment on behalf of such owners.

§ 745.13 Notification to Members/Shareholders.

Each insured credit union shall provide notice to its members concerning NCUA insurance coverage of member accounts. This may be accomplished by placing either a copy of Part 745 of these rules, the Appendix, or one or more copies of the NCUA brochure "Your Insured Funds" in each branch office and main office of the credit union. Copies of these materials shall also be made available to members upon request. For purposes of this section, an automated teller machine or point of sale terminal is not a branch office.

APPENDIX TO PART 745—EXAMPLES OF INSURANCE COVERAGE AFFORDED ACCOUNTS IN CREDIT UNIONS INSURED BY THE NATIONAL CREDIT UNION SHARE INSURANCE FUND

What is the Purpose of this Appendix?

The following examples illustrate insurance coverage on accounts maintained in the same federally-insured credit union. They are intended to cover various types of ownership interests and combinations of accounts which may occur in connection with funds invested in insured credit unions. These examples interpret the rules for insurance of accounts contained in 12 C.F.R. Part 745.

The examples, as well as the rules which they interpret, are predicated upon the assumption that, (1) invested funds are actually owned in the manner indicated on the credit union's records and (2) the owner of funds in an account is a credit union member or otherwise eligible to maintain an insured account in a credit union. If available evidence shows that ownership is different from that on the institution's records, the National Credit Union Share Insurance Fund may pay claims for insured accounts on the basis of actual rather than ostensible ownership. Further, the examples and the rules which they interpret do not extend insurance coverage to persons otherwise not entitled to maintain an insured account or to account relationships that have not been approved by the Board as an insured account.

A. How are Single Ownership Accounts Insured?

All funds owned by an individual member (or, in a community property state, by the husband-wife community of which the individual is a member) and invested in one or more individual accounts are added together and insured to the $100,000 maximum. This is true whether the accounts are maintained in the name of the individual member owning the funds, in the name of the member's agent or nominee, or in a custodial loan account on behalf of the member as a borrower. (§§ 745.3(a)(1), (2) and (3).) All such accounts are added together and insured as one individual account. Funds held in one or more accounts in the name of a guardian, custodian, or conservator for the benefit of a ward or minor are added together and insured up to $100,000. However, such account or accounts will not be added to any other individual accounts of the guardian, custodian, conservator, ward, or minor for purposes of determining insurance coverage. (§ 745.3(b).)

Example 1

Question: Members A and B, husband and wife, each maintain an individual account containing $100,000. In addition, they hold a joint account containing $100,000. What is the insurance coverage?

Answer: Each account is separately insured up to $100,000 for a total coverage of $300,000. The coverage would be the same whether the individual accounts contain funds owned as community property or as individual property of the spouses (§ 745.3(a)(1) and § 745.8(a)).

Example 2

Question: Members H and W, husband and wife, reside in a community property share. H maintains a $100,000 account consisting of his separately-owned funds and invests $100,000 of community property funds in another account, both of which are in his name alone. What is the insurance coverage?

Answer: The two accounts are added together and insured to a total of $100,000. $100,000 is uninsured (§ 745.3(a)(1)).

Example 3

Question: Member A has $92,500 invested in an individual account, and his agent, Member B, invests $25,000 of A's funds in a properly designated agency account. B also holds a $100,000 individual account. What is the insurance coverage?

Answer: A's individual account and the agency account are added together and insured to the $100,000 maximum, leaving $17,500 uninsured. The investment of funds through an agent does

not result in additional insurance coverage for the principal (§ 745.3(a)(2)). B's individual account is insured separately from the agency account (§ 745.3(a)(1)). However, if the account records of the credit union do not show the agency relationship under which the funds in the $25,000 account are held, the $25,000 in B's name could, at the option of the NCUSIF, be added to his individual account and insured to $100,000 in the aggregate, leaving $25,000 uninsured (§ 745.2(c)).

Example 4

Question: Member A holds a $100,000 individual account. Member B holds two accounts in his own name, the first containing $25,000 and the second containing $92,500. In processing the claims for payment of insurance on these accounts, the NCUSIF discovers that the funds in the $25,000 account actually belong to A and that B had invested these funds as agent for A, his undisclosed principal. What is the insurance coverage?

Answer: Since the available evidence shows that A is the actual owner of the funds in the $25,000 account, those funds would be added to the $100,000 individual account held by A (rather than to B's $92,500 account) and insured to the $100,000 maximum, leaving $25,000 uninsured. (§ 745.3(a)(2).) B's $92,500 individual account would be separately insured.

Example 5

Question: Member C, a minor, maintains an individual account of $750. C's grandfather makes a gift to him of $100,000, which is invested in another account by C's father, designated on the credit union's records as custodian under a Uniform Gift to Minors Act. C's father, also a member, maintains an individual account of $100,000. What is the insurance coverage? Answer: C's individual account and the custodian account held for him by his father are each separately insured: the $100,000 maximum on the custodian account, and $750 on his individual account. The individual account held by C's father is also separately insured to the $100,000 maximum. (§§ 745.3(a)(1) and (b).)

Example 6

Question: Member G, a court-appointed guardian, invests in a properly designated account $100,000 of funds in his custody which belong to member W, his ward. W and G each maintain $25,000 individual accounts. What is the insurance coverage?

Answer: W's individual account and the guardianship account in G's name are each insured to $100,000 providing W with $125,000 in insured funds. G's individual account is also separately insured. (§§ 745.3(a)(1) and (b).)

Example 7

Question: X Credit Union acts as a servicer of FHA, VA, and conventional mortgage loans made to its members but sold to other parties. Each month X receives loan payments, for remittance to the other parties, from approximately 2,000 member mortgagors. The monies received each month total $1,000,000 and are maintained in a custodial loan account. What is the insurance coverage?

Answer: X Credit Union acts as custodian for the 2,000 individual mortgagors. The interest of each mortgagor is separately insured as his individual account (but added to any other individual accounts which the mortgagor holds in the Credit Union) (§ 745.3(a)(3)).

B. How are Revocable Trust Accounts Insured?

The term "revocable trust account" includes a testamentary account, tentative or "Totten" trust account, "payable-on-death" account, or any similar account which evidences an intention that the funds shall pass on the death of the owner of the funds to a named beneficiary. If the named beneficiary is a spouse, child, grandchild, parent, brother or sister (as defined in subsection 745.4(d)) of the owner, the funds in all such accounts are insured for the owner up to $100,000 in the aggregate as to each such beneficiary. If the named beneficiary of a revocable trust account is other than the spouse, child, grandchild, parent, brother or sister of the account owner, the funds corresponding to that beneficiary shall be treated as an individually owned account of the owner, aggregated with any other individually owned accounts of the owner, and insured up to $100,000. In the case

of a revocable trust account, the person who holds the power of revocation is deemed to be the owner of the funds in the account. If a revocable trust account is held in the name of a fiduciary other than the owner of the funds, any other accounts held by the fiduciary are insured separately from such revocable trust account.

Example 1

Question: Member H invests $200,000 in a revocable trust account with his son, S, and his daughter, D, as named beneficiaries. What is the insurance coverage?

Answer: Since S and D are children of H, the owner of the account, the funds are insured up to $100,000 as to each beneficiary (§ 745.4(b)). Assuming that S and D have equal beneficial interests ($100,000 each), H is fully insured for this account.

Example 2

Question: Member H invests $100,000 in each of four "payable-on-death" accounts. Under the terms of each account contract, H has the right to withdraw any or all of the funds in the account at any time. Any funds remaining in the account at the time of H's death are to be paid to a named beneficiary. The respective beneficiaries of the four accounts are H's wife, his mother, his brother, and his nephew. H also holds an individual account containing $100,000. What is the insurance coverage?

Answer: The accounts payable on death to H's wife, mother and brother are each separately insured to the $100,000 maximum (Sec. 745.4(b)). The account payable to H's nephew is added to H's individual account and insured to $100,000 in the aggregate, leaving $100,000 uninsured (Sec. 745.4(c)).

Example 3

Question: Members H and W jointly invest in a "payable-on-death" account for the benefit of their son, S, and daughter, D. The account is held by H and W with right of survivorship. What is the maximum insurance coverage available on the account?

Answer: Since S and D are the children of H and W, the account will be insured up to $100,000 as to each beneficiary separately from any accounts of the owners, H and W (§ 745.4(b)). H would be entitled to $100,000 insurance for S and $100,000 for D. W would be entitled to the same coverage for a total of $400,000 on the account. However, upon the death of either H or W, insurance coverage would be reduced to $200,000.

Example 4

Question: Member H invests $200,000 in a revocable trust account held in connection with a living trust with his son, S, and his daughter, D, as named beneficiaries. What is the insurance coverage?

Answer: Since S and D are children of H, the owner of the account, the funds would normally be insured under the rules governing revocable trust accounts up to $100,000 as to each beneficiary, (§ 745.4(b)). However, because this account is held in connection with a living trust whose named beneficiaries are qualifying beneficiaries under § 745.4, it must be scrutinized to determine whether the account complies with all other provisions of this part. Assuming that the account complies with all other requirements of this part, then it will be treated as any other revocable trust. In this instance, it will be insured up to $100,000 as to each beneficiary (§ 745.4(e)). Assuming that S and D have equal beneficial interests ($100,000 each), H is fully insured for this account.

Example 5

Question: H creates a living trust providing for his wife to have a life estate interest in the trust assets with the remaining assets going to their two children upon the wife's death. The assets in the trust are $300,000 and a living trust share account is opened for that full amount. What is the coverage amount?

Answer: Unless otherwise indicated in the trust, each beneficiary (all of whom here are qualifying beneficiaries) would be deemed to own an equal share of the $300,000; hence, the full amount would be insured. This result would be the same even if the wife has the power to invade the principal of the trust, inasmuch as defeating contingencies are not relevant for insurance purposes.

C. How are Accounts Held by Executors or Administrators Insured?

All funds belonging to a decedent and invested in one or more accounts, whether held in

the name of the decedent or in the name of his executor or administrator, are added together and insured to the $100,000 maximum. Such funds are insured separately from the individual accounts of any of the beneficiaries of the estate or of the executor or administrator.

Example 1

Question: Member A, administrator of Member D's estate, sells D's automobile and invests the proceeds of $12,500 in an account entitled "A Administrator of the estate of D." A has an individual account in that same credit union containing $100,000. Prior to his death, D had opened an individual account of $100,000. What is the insurance coverage?

Answer: The $12,500 is added to D's individual account and insured to $100,000, leaving $12,500 uninsured. A's individual account is separately insured for $100,000 (§ 745.5).

D. How are Accounts Held by a Corporation, Partnership or Unincorporated Association Insured?

All funds invested in an account or accounts by a corporation, a partnership or an unincorporated association engaged in any independent activity are added together and insured to the $100,000 maximum. The term "independent activity" means any activity other than the one directed solely at increasing coverage. If the corporation, partnership or unincorporated association is not engaged in an independent activity, any account held by the entity is insured as if owned by the persons owning or comprising the entity, and the imputed interest of each such person is added for insurance purposes to any individual account which he maintains.

Example 1

Question: Member X Corporation maintains a $100,000 account. The stock of the corporation is owned by members A, B, C, and D in equal shares. Each of these stockholders also maintains an individual account of $100,000 with the same credit union. What is the insurance coverage?

Answer: Each of the five accounts would be separately insured to $100,000 if the corporation is engaged in an independent activity and has not been established merely for the purpose of increasing insurance coverage. The same would be true if the business were operated as a bona fide partnership instead of as a corporation (§ 745.6). However, if X corporation was not engaged in an independent activity, then $25,000 (1/4 interest) would be added to each account of A, B, C, and D. The accounts of A, B, C, and D would then each be insured to $100,000, leaving $25,000 in each account uninsured.

Example 2

Question: Member C College maintains three separate accounts with the same credit union under the titles: "General Operating Fund," "Teachers Salaries," and "Building Fund." What is the insurance coverage?

Answer: Since all of the funds are the property of the college, the three accounts are added together and insured only to the $100,000 maximum (§ 745.6).

Example 3

Question: The men's club of X Church carries on various social activities in addition to holding several fund-raising campaigns for the church each year. The club is supported by membership dues. Both the club and X Church maintain member accounts in the same credit union. What is the insurance coverage?

Answer: The men's club is an unincorporated association engaged in an independent activity. If the club funds are, in fact, legally owned by the club itself and not the church, each account is separately insured to the $100,000 maximum (§ 745.6).

Example 4

Question: The PQR Union, a member of the ABC Federal Credit Union, has three locals in a certain city. Each of the locals maintains an account containing funds belonging to the parent organization. All three accounts are in the same insured credit union. What is the insurance coverage?

Answer: The three accounts are added together and insured up to the $100,000 maximum (§ 745.6).

E. How are Public Unit Accounts Insured?

For insurance purposes, the official custodian of funds belonging to a public unit, rather than the public unit itself, is insured as the account holder. All funds belonging to a public unit and invested by the same custodian in a federally-insured credit union are categorized as either share draft accounts or share certificate and regular share accounts. If these accounts are invested in a federally-insured credit union located in the jurisdiction from which the official custodian derives his authority, then the share draft accounts will be insured separately from the share certificate and regular share accounts. Under this circumstance, all share draft accounts are added together and insured to the $100,000 maximum and all share certificate and regular share accounts are also added together and separately insured up to the $100,000 maximum. If, however, these accounts are invested in a federally-insured credit union located outside of the jurisdiction from which the official custodian derives his authority, then insurance coverage is limited to $100,000 for all accounts regardless of whether they are share draft, share certificate or regular share accounts. If there is more than one official custodian for the same public unit, the funds invested by each custodian are separately insured. If the same person is custodian of funds for more than one public unit, he is separately insured with respect to the funds of each unit held by him in properly designated accounts.

For insurance purposes, a "political subdivision" is entitled to the same insurance coverage as any other public units. "Political subdivision" includes any subdivision of a public unit or any principal department of such unit (1) the creation of which has been expressly authorized by state statute, (2) to which some functions of government have been allocated by state statute, and (3) to which funds have been allocated by statute or ordinance for its exclusive use and control.

Example 1

Question: As Comptroller of Y Consolidated School District, A maintains a $125,000 account in the credit union containing school district funds. He also maintains his own $100,000 member account in the same credit union. What is the insurance coverage?

Answer: The two accounts will be separately insured, assuming the credit union's records indicate that the account containing the school district funds is held by A in a fiduciary capacity. Thus, $100,000 of the school's funds and the entire $100,000 in A's personal account will be insured (§§ 745.10(a)(2) and 745.3).

Example 2

Question: A, as city treasurer, and B, as chief of the city police department, each have $100,000 in city funds invested in custodial accounts. What is the insurance coverage?

Answer: Assuming that both A and B have official custody of the city funds, each account is separately insured to the $100,000 maximum (§ 745.10(a)(2)).

Example 3

Question: A is Treasurer of X County and collects certain tax assessments, a portion of which must be paid to the state under statutory requirement. A maintains an account for general funds which belong to the State Treasurer. The credit union's records indicate that the separate account contains funds held for the State. What is the insurance coverage?

Answer: Since two public units own the funds held by A, the accounts would each be separately insured to the $100,000 maximum (§ 745.10(a)(2)).

Example 4

Question: A city treasurer invests city funds in each of the following accounts: "General Operating Account," "School Transportation Fund," "Local Maintenance Fund," and "Payroll Fund." Each account is available to the custodian upon demand. By administrative direction, the city treasurer has allocated the funds for the use of and control by separate departments of the city. What is the insurance coverage?

Answer: All of the accounts are added together and insured in the aggregate to $100,000. Because the allocation of the city's funds is not by statute or ordinance for the specific use of and control by separate departments of the city, separate insurance coverage to the

maximum of $100,000 is not afforded to each account (§§ 745.1(d) and 745.10(a)(2)).

Example 5

Question: A, the custodian of retirement funds of a military exchange, invests $1,000,000 in an account in an insured credit union. The military exchange, a non-appropriated fund instrumentally of the United States, is deemed to be a public unit. The employees of the exchange are the beneficiaries of the retirement funds but are not members of the credit union. What is the insurance coverage?

Answer: Because A invested the funds on behalf of a public unit, in his capacity as custodian, those funds qualify for $100,000 share insurance even though A and the public unit are not within the credit union's field of membership. Since the beneficiaries are neither public units nor members of the credit union they are not entitled to separate share insurance. Therefore, $900,000 is uninsured (§ 745.10(a)(1)).

Example 6

Question: A is the custodian of the County's employee retirement funds. He deposits $1,000,000 in retirement funds in an account in an insured credit union. The "beneficiaries" of the retirement fund are not themselves public units nor are they within the credit union's field of membership. What is the insurance coverage?

Answer: Because A invested the funds on behalf of a public unit, in his capacity as custodian, those funds qualify for $100,000 share insurance even though A and the public unit are not within the credit union's field of membership. Since the beneficiaries are neither public units nor members of the credit union they are not entitled to separate share insurance. Therefore, $900,000 is uninsured (§ 745.10(a)(2)).

Example 7

Question: A county treasurer establishes the following share draft accounts in an insured credit union each with $100,000:

"General Operating Fund"
"County Roads Department Fund"
"County Water District Fund"
"County Public Improvement District Fund"
"County Emergency Fund"

What is the insurance coverage?

Answer: The "County Roads Department," "County Water District" and "County Public Improvement District" accounts would each be separately insured to $100,000 if the funds in each such account have been allocated by law for the exclusive use of a separate county department or subdivision expressly authorized by State statute. Funds in the "General Operating" and "Emergency Fund" accounts would be added together and insured in the aggregate to $100,000, if such funds are for countywide use and not for the exclusive use of any subdivision or principal department of the county, expressly authorized by State statute (§§ 745.1(d) and 745.10(a)(2)).

Example 8

Question: A, the custodian of Indian tribal funds, lawfully invests $1,000,000 in an account in an insured credit union on behalf of 15 different tribes; the records of the credit union show that no tribe's interest exceeds $100,000. A, as official custodian, also invests $1,000,000 in the same credit union on behalf of 100 individual indians, who are not members; each indian's interest is $10,000. What is the insurance coverage?

Answer: Because each tribe is considered a separate public unit, the custodian of each tribe, even though the same person, is entitled to separate insurance for each tribe (§ 745.10(a)(5)). Since the credit union's records indicate no tribe has more than $100,000 in the account, the $1,000,000 would be fully insured as 15 separate tribal accounts. If any one tribe had more than a $100,000 interest in the funds, it would be insured only to $100,000 and any excess would be uninsured. However, the $1,000,000 invested on behalf of the individual indians would not be insured since the individual indians are neither public units nor, in the example, members of the credit union. If A is the custodian of the funds in his capacity as an official of a governmental body that qualified as a public unit, then the account would be insured for $100,000 leaving $900,000 uninsured.

Example 9

Question: A, an official custodian of funds of a state of the United States, lawfully invests $250,000 of state funds in a federally-insured credit union located in the state from which he

derives his authority as an official custodian. What is the insurance coverage?

Answer: If A invested the entire $250,000 in a share draft account, then $100,000 would be insured and $150,000 would be uninsured. If A invested $125,000 in share draft accounts and another $125,000 in share certificate and regular share accounts, then A would be insured for $100,000 for the share draft accounts and $100,000 for the share certificate and regular share accounts leaving $50,000 uninsured (§ 745.10(a)(2)). If A had invested the $250,000 in a federally-insured credit union located outside the state from which he derives his authority as an official custodian, then $100,000 would be insured for all accounts regardless of whether they were share draft, share certificate or regular share accounts, leaving $150,000 uninsured (§ 745.10(b)).

F. How are Joint Accounts Insured?

The interest of a co-owner in all accounts held under any form of joint ownership valid under state law (whether as joint tenants with right of survivorship, tenants by the entireties, tenants in common, or by husband and wife as community property) is insured up to $100,000. This insurance is separate from that afforded individual accounts held by any of the co-owners.

An account is insured as a joint account only if each of the co-owners has personally signed a membership card or an account signature card and possesses the same withdrawal rights as the other co-owners. (The signature requirement does not apply to share certificates, or to any accounts maintained by an agent, nominee, guardian, custodian or conservator on behalf of two or more persons. However, the records of the credit union must show that the account is being maintained for joint owners. There is also another exception in the case of a minor discussed below.) An account owned jointly which does not qualify as a joint account for insurance purposes is insured as if owned by the named persons as individuals. In that case, the actual ownership interest in the account of each person is added to any other accounts individually owned by such person and insured up to $100,000 in the aggregate.

Any individual, including a minor, may be a co-owner of a joint account. Although, generally, each co-owner must have signed an account signature card and must have the same rights of withdrawal as other co-owners in order for the account to qualify for separate joint account insurance, there is an exception for minors. If state law limits or restricts a minor's withdrawal rights—for example, a minimum age requirement to make a withdrawal—the account will still be insured as a joint account.

The interests of a co-owner in all joint accounts that qualify for separate insurance coverage are insured up to the $100,000 maximum. For insurance purposes, the co-owners of any joint account are deemed to have equal interests in the account, except in the case of a tenancy in common. With a tenancy in common, equal interests are presumed unless otherwise stated on the records of the credit union.

Example 1

Question: Members A and B maintain an account as joint tenants with right of survivorship and, in addition, each holds an individual account. Is each account separately insured?

Answer: If both A and B have signed the membership or signature card and possess equal withdrawal rights with respect to the joint funds, their interests in the joint account are separately insured from their interests in the individual accounts. (§ 745.8 (a) and (b).) If the joint account is represented by a share certificate, their individual signatures are not required for that account.

Example 2

Question: Members H and W, husband and wife, reside in a community property state. Each holds an individual account and, in addition, they hold a qualifying joint account. The funds in all three accounts consist of community property. Is each account separately insured?

Answer: Yes. An account in the individual name of a spouse will be insured up to $100,000 whether the funds consist of community property or separate property of the spouse. A joint account containing community property is separately insured. Thus, community property can be used for individual accounts in the name of each spouse and for a joint account in the name of both spouses. In this example, each individual account is insured up to $100,000 (§ 745.3(a)(1)), and the interests of both the husband and wife in the joint account are each insured up to $100,000 (§ 745.8(a)).

Example 3

Question: Two accounts of $100,000 each are held by a member husband and his wife under the following names: John Doe and Mary Doe, husband and wife, as joint tenants with right of survivorship. Mrs. John Doe and John Q. Doe (community property). How much insurance do the husband and wife have?

Answer: They have $200,000 of insurance. Both the husband and wife are deemed to have a one half interest ($50,000) in each account. (§ 745.2(c)(4).) The husband's interest in both accounts would be added together and insured for $100,000. The wife's insurance coverage would be determined the same way. (§ 745.8(a).)

Example 4

Question: The following accounts are held by members A, B and C, each of whom has personally executed signature cards for the accounts in which he has an interest. Each co-owner of a joint account possesses the necessary withdrawals rights.

1. A, as an individual—$100,000.
2. B, as an individual—$100,000.
3. C, as an individual—$100,000.
4. A and B, as joint tenants w/r/o survivorship—$90,000.
5. A and C, as joint tenants w/r/o survivorship—$90,000.
6. B and C, as joint tenants w/r/o survivorship—$90,000.
7. A, B and C, as joint tenants w/r/o survivorship—$90,000.

What is the insurance coverage?

Answer: Accounts numbered 1, 2 and 3 are each separately insured for $100,000 as individual accounts held by A, B and C, respectively (§ 745.3(a)(1)). The interest of the co-owners of each joint account are deemed equal for insurance purposes (§ 745.2(c)(4)). A's interest in accounts numbered 4, 5, and 7 are added together for insurance purposes (§ 745.8(e)). Thus, A has an interest of $45,000 in account No. 4, $45,000 in account No. 5 and $30,000 in account No. 7, for a total joint account interest of $120,000, of which $100,000 is insured. The interest of B and C are similarly insured.

Example 5(a)

Question: A, B and C hold accounts as set forth in Example 4. Members A and B are husband and wife; C, their minor child, has failed to sign the signature card for Account No. 7. In Account No. 5, according to the terms of the account, C cannot make a withdrawal without A's written consent. (This is not a limitation imposed under state law.) In Account No. 6, the signatures of both B and C are required for withdrawal. A has provided all of the funds for Accounts numbered 5 and 7 and under state law has the entire actual ownership interest in these two accounts. What is the insurance coverage?

Answer: If any of the co-owners of a joint account have failed to meet any of the joint account requirements, the account is not a qualifying joint account. Instead, the account is treated as if it consisted of commingled individual accounts of each of the co-owners in accordance with his or her actual ownership interest in the funds, as determined under applicable state law. (§ 745.8(c).)

Account No. 5 is not a qualifying joint account because C does not have equal withdrawal rights with A. Based on the terms of the account, C can only make a withdrawal if he has A's written consent. Account No. 7 is not a qualifying joint account because C did not personally sign the signature card. Therefore, all of the funds in Accounts 5 and 7 are treated as individually owned by A and added to A's individual account, Account No. 1. For insurance purposes then, A has $280,000 in one individual account that is insured for $100,000, leaving $180,000 uninsured.

Account 6 is a qualifying joint account for insurance purposes since each co-owner has the right to withdraw funds on the same basis. Account 4 is also a qualifying joint account. A's interest in Account 4 is insured for $45,000. B's interest of $45,000 in Account 4 is added to her interest of $45,000 in Account 6 and insured for $90,000. C's interest in Account 6 is insured for $45,000.

Example 5(b)

Question: Assume the same accounts as Example 5(a) except that, on Account No. 5, C's right to make a withdrawal is limited by state law which precludes a minor from making a

withdrawal without the co-owner's written consent. What is the insurance coverage?

Answer: In this situation, Accounts 4, 5, and 6 all qualify as joint accounts. A, B, and C will each have $90,000 of insured funds based on: A's interest in Account 4 ($45,000) and 5 ($45,000), B's interest in Accounts 4 ($45,000) and 6 ($45,000), and C's interest in Accounts 5 ($45,000) and 6 ($45,000). As in Example 5(a), Account No. 7 does not qualify as a joint account and would be added to A's individual account for insurance purposes.

G. How are Trust Accounts and Retirement Accounts Insured?

A trust estate is the interest of a beneficiary in an irrevocable express trust, whether created by trust instrument or statute, that is valid under state law. Thus, funds invested in an account by a trustee under an irrevocable express trust are insured on the basis of the beneficial interests under such trust. The interest of each beneficiary in an account (or accounts) established under such a trust arrangement is insured to $100,000 separately from other accounts held by the trustee, the settlor (grantor), or the beneficiary. However, in cases where a beneficiary has an interest in more than one trust arrangement created by the same settlor, the interests of the beneficiary in all accounts established under such trusts are added together for insurance purposes, and the beneficiary's aggregate interest derived from the same settlor is separately insured to the $100,000 maximum.

A beneficiary's interest in an account established pursuant to an irrevocable express trust arrangement is insured separately from other beneficial interests (trust estates) invested in the same account if the value of the beneficiary's interest (trust estate) can be determined (as of the date of a credit union's insolvency) without evaluation of contingencies except for those covered by the present worth tables and rules of calculation for their use set forth in § 20.2031–10 of the Federal Estate Tax Regulations (26 C.F.R. 20–2031–10). If any trust estates in such an account cannot be so determined, the insurance with respect to all such trust estates together shall not exceed the basic insured amount of $100,000.

In order for insurance coverage of trust accounts to be effective in accordance with the foregoing rules, certain recordkeeping requirements must be met. In connection with each trust account, the credit union's records must indicate the name of both the settlor and the trustee of the trust and must contain an account signature card executed by the trustee indicating the fiduciary capacity of the trustee. In addition, the interests of the beneficiaries under the trust must be ascertainable from the records of either the credit union or the trustee, and the settlor or beneficiary must be a member of the credit union. If there are two or more settlors or beneficiaries, then either all the settlors or all the beneficiaries must be members of the credit union.

Although each ascertainable trust estate is separately insured, it should be noted that in short-term trusts the insurable interest or interests may be very small, since the interests are computed only for the duration of the trust. Thus, if a trust is made irrevocable for a specified period of time, the beneficial interest will be calculated in terms of the length of time stated. A reversionary interest retained by the settlor is treated in the same manner as an individual account of the settlor.

As stated, the trust must be valid under local law. A trust which does not meet local requirements, such as one imposing no duties on the trustee or conveying no interest to the beneficiary, is of no effect for insurance purposes. An account in which such funds are invested is considered to be an individual account.

An account established pursuant to a revocable trust arrangement is insured as a form of individual account and is treated under Section B, supra, dealing with Testamentary Accounts.

IRA and Keogh accounts are separately insured, each up to $100,000. Although credit unions may serve as trustees or custodians for self-directed IRA, Roth IRA and Keogh accounts, once the funds in those accounts are taken out of the credit union, they are no longer insured.

In the case of an employee retirement fund where only a portion of the fund is placed in a credit union account, the amount of insurance available to an individual member/beneficiary on his interest in the account will be in proportion to his interest in the entire employee retirement fund. If, for example, the member's interest represents 10% of the entire plan funds, then he is presumed to have only a 10% interest in the plan account. Said another way, if a member has a vested interest of $10,000 in a

municipal employees retirement plan and the trustee invests 25% of the total plan funds in a credit union, the member would be insured for only $2,500 on that credit union account. There is an exception, however. The member would be insured for $10,000 if the trustee can document, through records maintained in the ordinary course of business, that individual beneficiary's interests are segregated and the total vested interest of the member was, in fact, invested in that account.

Example 1

Question: Member S invests $45,000 in trust for B, the beneficiary. S also has an individual account containing $90,000 in the same credit union. What is the insurance coverage?

Answer: Both accounts are fully insured. The trust account is separately insured from the individual account of S (§§ 745.3(a)(1) and 745.9–1).

Example 2

Question: S invests funds in trust for A, B, C, D, and E. A, B, and C are members of the credit union, D, E, and S are not. What is the insurance coverage?

Answer: This is an uninsurable account. Where there is more than one settlor or more than one beneficiary, all the settlors or all the beneficiaries must be members to establish this type of account. Since D, E and S are not members, this account cannot legally be established or insured.

Example 3

Question: Member S invests $500,000 in trust for ABC Employees Retirement Fund. Some of the beneficiaries are members and some are not. What is the insurance coverage?

Answer: The account is insured as to the determinable interests of each member beneficiary to a maximum of $100,000 per member. Member interests not capable of evaluation and nonmember interests shall be added together and insured to a maximum of $100,000 in the aggregate (§ 745.9–1).

Example 3(a)

Question: Member S is trustee for the ABC Employees Retirement Fund containing $1,000,000. Member A has a determinable interest of $90,000 in the Fund (9% of the total). S invests $500,000 of the Fund in trust in an insured credit union and the remaining $500,000 elsewhere. Some of the beneficiaries of the Fund are members of the credit union and some are not. S does not segregate each employee's interest in the Fund. What is the insurance coverage?

Answer: The account is insured as to determinable interest of each member beneficiary, adjusted in proportion to the Fund's investment in the credit union. A's insured interest in the account is $45,000, or 9% of $500,000. This reflects the fact that only 50% of the Fund is in the account and A's interest in the account is in the same proportion as his interest in the overall plan. Each beneficiary who is a member would be similarly insured. Members' interests not capable of evaluation and nonmembers' interests are added together and insured to a maximum of $100,000 in the aggregate (§ 745.9–1).

Example 4

Question: Member A has an individual account of $100,000 and establishes an IRA and accumulates $50,000 in that account. Subsequently A becomes self-employed and establishes a Keogh account in the same credit union and accumulates $100,000 in that account. What is the insurance coverage?

Answer: Each of A's accounts would be separately insured for up to $100,000. In the example, A would be fully insured for $250,000 (§§ 745.3(a)(1) and 745.9–2).

Example 5

Question: Member A has a self-directed IRA account with $70,000 in it. The FCU is the trustee of the account. Member transfers $40,000 into a blue chip stock; $30,000 remains in the FCU. What is the insurance coverage?

Answer: Originally, the full $70,000 in A's IRA account is insured. The $40,000 is no longer insured once it is moved out of the FCU. The $30,000 remaining in the FCU is insured (§ 745.9–2).

Subpart B—Payment of Share Insurance and Appeals

§ 745.200 General.

(a) *Payment.* In the event of the liquidation of an insured credit union, the Board will promptly determine the insured accountholders thereof and the amount of the insured account or accounts of each such accountholder. Payment may be in cash, or its equivalent, or may be made by making available to each accountholder a transferred account in a new federally-insured credit union in the same community or in another federally-insured credit union or institution in an amount equal to the accountholder's insured account. Notwithstanding the foregoing, the Board may withhold payment of such portion of the insured account of any member as may be required to provide for payment of any direct or indirect liability to the closed credit union or the liquidating agent, which is not offset against a claim due from such credit union, pending the determination and payment of such liability by the member or any person liable therefor.

(b) *Amount of insurance.* The amount of insurance on an insured account shall be determined in accordance with the provisions of Subpart A of this part and the Federal Credit Union Act. For the purpose of determining insurance coverage, dividends earned in the ordinary course of business and posted to share accounts for any prior accounting or dividend period shall be deemed to be principal under this part. Dividends earned or accrued in the ordinary course of business, but not posted to share accounts, may be paid at the discretion of the liquidating agent. In making such determination, the liquidating agent will take into consideration whether the failure to post dividends earned or accrued was due to the fraud, embezzlement or accounting errors of credit union personnel. The liquidating agent may require an accountholder to submit documentation supporting any claim for unposted dividends not otherwise evidenced in the credit union records. However, in no event will dividend amounts be considered as principal for insurance purposes pursuant to this section if not consistent with the amounts paid on similar classes of shares.

(c) *Multiple accounts.* In the event an insured member holds more than one insured account in the same capacity, and the aggregate amount of such accounts (including share draft accounts held in such capacity) exceeds the amount of insurance afforded thereon, the insurance coverage will be prorated among the member's interest in all accounts held in the same capacity. In the case of individual accounts, the insurance proceeds shall be paid to the holder of the account, whether or not the holder is the beneficial owner. In the case of accounts which are owned jointly, the insurance proceeds shall be paid to the owners jointly. In the case of trust estates, the insurance proceeds shall be paid to the indicated trustee unless otherwise provided for in the trust instrument or under state law. In the case of corporations, partnerships and unincorporated associations engaged in an independent activity, the insurance proceeds shall be paid to the indicated holder of the account. Where insurance payment is in the form of a transferred account to another insured institution, the same rules shall be applied.

(d) *Computing time.* In computing any period of time prescribed by this subpart, the provisions of § 747.12(a) shall apply.

§ 745.201 Processing of Insurance Claims.

(a) *Delegations of authority.* The Agent for the Liquidating Agent ("Liquidating Agent") or his or her designee is authorized to make initial determinations with respect to insurance claims pursuant to the principles set forth in this Part, and to act on requests for reconsideration of the initial determination.

(b) *Initial determination.* In the event the Liquidating Agent determines that all or a portion of an accountholder's account is uninsured, the Liquidating Agent shall so notify the accountholder in writing, stating the reason(s) for such initial determination, and shall provide the accountholder with a certificate of claim in liquidation in the amount of the uninsured account from the Board in its capacity as Liquidating Agent for the insured credit union to enable the accountholder to share in the proceeds of the liquidation of the credit union, if any, up to the amount of the uninsured account.

(c) *Request for Reconsideration.* An accountholder may, at his or her option, request reconsideration from the Liquidating Agent of the initial determination within 30 days of the date of the initial determination, or directly appeal the initial determination to the Board pursuant to § 745.202 of this subpart. The Liqui-

dating Agent shall act on the request for reconsideration within 30 days from its receipt.

§ 745.202 Appeal.

(a) *Time for filing.* Within 60 days after issuance of an initial determination, or of the determination on a request for reconsideration by the liquidating agent, the accountholder may appeal by filing with the Board a written request for appeal. The appeal may be filed with the Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

(b) *Content of request.* Any appeal must include:

(1) a statement of the facts on which the claim for insurance is based;

(2) a statement of the basis for the initial determination or determination on the request for reconsideration to which the accountholder objects and the alleged error in such determination, including citations to applicable statutes and regulations;

(3) any other evidence relied upon by the accountholder which was not previously provided to the Liquidating Agent.

(c) *Procedures for review of request.*

(1) Within 60 days of the date of the Board's receipt of an appeal, the Board may request in writing that the accountholder submit additional facts and records in support of its request. The account-holder shall have 45 days from the date of issuance of such written request to provide such additional information. Failure by the accountholder to provide additional information may, as determined solely by the Board, result in denial of the accountholder's appeal.

(2) Within 60 days from the date of the Board's receipt of an appeal, the accountholder may amend or supplement the request in writing. In the event that the accountholder does amend or supplement the request, the provisions of paragraph (c)(1) of this section with respect to requests for additional information and responses to such requests shall apply with equal force to any such amendment or supplement to a request.

(d) *Determination on appeal.*

(1) Within 180 days from the date of the receipt of an appeal by the Board, the Board shall issue a decision determining the extent of the accountholder's insurance pursuant to the rules of this Part.

(2) The determination by the Board on appeal shall be provided to the accountholder in writing, stating the reason(s) for the determination, and shall constitute a final Agency order regarding the accountholder's claim for insurance.

(3) If the Board determines that the account-holder is entitled to the amount of insurance claimed or portion thereof, upon payment of such insurance the accountholder shall promptly surrender to the Board the certificate of claim in liquidation provided in connection with the initial determination. In the event that the Board determines that the accountholder is only entitled to a portion of the amount of insurance claimed, upon the accountholder's surrender of such certificate a new certificate of claim in liquidation will be provided which reflects the revised amount of the uninsured account.

(4) Failure by the Board to issue a determination on appeal of the accountholder's claim for insurance within the 180-day period provided for under this paragraph (d)(1) shall be deemed to be a denial of such claim for purposes of Section 745.203 of this subpart.

§ 745.203 Judicial Review.

(a) For purposes of seeking judicial review of actions taken pursuant to this subpart, only a determination on appeal issued by the Board pursuant to Section 745.202 of this subpart shall constitute a final determination regarding an accountholder's claim for insurance.

(b) Failure to file an appeal with regard to an initial determination, or a decision rendered on a request for reconsideration within the applicable time periods shall constitute a failure by the accountholder to exhaust available administrative remedies and, due to such failure, any objections to the initial determination or request for reconsideration shall be deemed to be waived and such determination shall be deemed to have been accepted by, and binding upon, the accountholder.

(c) Final determination by the Board is reviewable in accordance with the provisions of Chapter 7, Title 5, United States Code, by the United States Court of Appeals for the District of Columbia or the court of appeals for the Federal judicial circuit where the credit union's principal place of business is located. Such action must be filed not later than 60 days after such final determination is ordered.

Part 747

Administrative Actions, Adjudicative Hearings, Rules of Practice and Procedure, and Investigations

§ 747.0 Scope.

(a) This Part describes the various formal and informal adjudicative actions and non-adjudicative proceedings available to the National Credit Union Administration Board ("NCUA Board"), the grounds for those actions and proceedings, and the procedures used in formal and informal hearings related to each available action. As mandated by Section 916 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA") (12 U.S.C. § 1818 note), this Part incorporates uniform rules of practice and procedure governing formal adjudications generally, as well as proceedings involving cease-and-desist actions, assessment of civil money penalties, and removal, prohibition and suspension actions. In addition, the Uniform Rules are incorporated in other subparts of this Part which provide for formal adjudications. The administrative actions and proceedings described herein, as well as the grounds and hearing procedures for each, are controlled by Sections 120(b) (except where the Federal credit union is closed due to insolvency), 202(a)(3) and 206 of the Act (12 U.S.C. §§ 1766(b), 1782(a)(3), 1786). Should any provision of this Part be inconsistent with these or any other provisions of the Act, as amended, the Act shall control. Judicial enforcement of any action or order described in this Part, as well as judicial review thereof, shall be as prescribed under the Act (12 U.S.C. § 1751 *et seq.*) and the Administrative Procedure Act (5 U.S.C. § 500 *et seq.*).

(b) As used in this Part, the term insured credit union means any Federal credit union or any state-chartered credit union insured under Subchapter II of the Act unless the context indicates otherwise.

Subpart A—Uniform Rules of Practice and Procedure

§ 747.1 Scope.

This Subpart prescribes uniform rules of practice and procedure applicable to adjudicatory proceedings required to be conducted on the record after opportunity for a hearing under the following statutory provisions:

(a) Cease-and-desist proceedings under Section 206(e) of the Act (12 U.S.C. 1786(e));

(b) Removal and prohibition proceedings under Section 206(g) of the Act (12 U.S.C. 1786(g));

(c) Assessment of civil money penalties by the NCUA Board against institutions and institution-affiliated parties for any violation of:

(1) Section 202 of the Act, pursuant to 12 U.S.C. 1782(a);

(2) Section 1120 of FIRREA (12 U.S.C. 3349), or any order or regulation issued thereunder;

(3) The terms of any final or temporary order issued under section 206 of the Act or any written agreement executed by the National Credit Union Administration ("NCUA"), any condition imposed in writing by the NCUA in connection with the grant of an application or request, certain unsafe or unsound practices or breaches of fiduciary duty, or any law or regulation not otherwise provided herein, pursuant to 12 U.S.C. 1786(k); and

(4) Any provision of law referenced in section 102(f) of the Flood Disaster Protection Act of 1973 (42 U.S.C. 4012a(f)) or any order or regulation issued thereunder;

(d) Remedial action under section 102(g) of the Flood Disaster Protection Act of 1973 (42 U.S.C. 4012a(g)); and

(e) This subpart also applies to all other adjudications required by statute to be determined on the record after opportunity for an agency hearing, unless otherwise specifically provided for in Subparts B through J of this Part.

§ 747.2 Rules of Construction.

For purposes of this Subpart:

(a) Any term in the singular includes the plural, and the plural includes the singular, if such use would be appropriate;

(b) Any use of a masculine, feminine, or neuter gender encompasses all three, if such use would be appropriate;

(c) The term *counsel* includes a non-attorney representative; and

(d) Unless the context requires otherwise, a party's counsel of record, if any, may, on behalf of that party, take any action required to be taken by the party.

§ 747.3 Definitions.

For purposes of this Subpart, unless explicitly stated to the contrary:

(a) *Administrative law judge* means one who presides at an administrative hearing under authority set forth at 5 U.S.C. 556.

(b) *Adjudicatory proceeding* means a proceeding conducted pursuant to these rules and leading to the formulation of a final order other than a regulation.

(c) *Decisional employee* means any member of the NCUA's or administrative law judge's staff who has not engaged in an investigative or prosecutorial role in a proceeding and who may assist the Agency or the administrative law judge, respectively, in preparing orders, recommended decisions, decisions, and other documents under the Uniform Rules.

(d) *Enforcement Counsel* means any individual who files a notice of appearance as counsel on behalf of the NCUA in an adjudicatory proceeding.

(e) *Final order* means an order issued by the NCUA with or without the consent of the affected institution or the institution-affiliated party, that has become final, without regard to the pendency of any petition for reconsideration or review.

(f) *Institution* includes:

(1) Any Federal credit union as that term is defined in Section 101(1) of the Act (12 U.S.C. 1752(1)); and

(2) Any insured state credit union as that term is defined in Section 101(7) of the Act (12 U.S.C. 1752(7)).

(g) *Institution-affiliated party* means any institution-affiliated party as that term is defined in Section 206(r) of the Act (12 U.S.C. 1786(r)).

(h) *Local rules* means those rules promulgated by the NCUA in the Subparts of this Part other than Subpart A of this Part.

(i) *OFIA* means the Office of Financial Institution Adjudication, which is the executive body charged with overseeing the administration of administrative enforcement proceedings for the NCUA, the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS).

(j) *Party* means the NCUA and any person named as a party in any notice.

(k) *Person* means an individual, sole proprietor, partnership, corporation, unincorporated association, trust, joint venture, pool, syndicate, agency, or other entity or organization, including an institution as defined in paragraph (f) of this section.

(l) *Respondent* means any party other than the NCUA.

(m) *Uniform Rules* means those rules in Subpart A of this Part that are common to the NCUA, the OCC, the Board, the FDIC, and the OTS.

(n) *Violation* includes any action (alone or with another or others) for or toward causing, bringing about, participating in, counseling, or aiding or abetting a violation.

§ 747.4 Authority of the NCUA Board.

The NCUA Board may, at any time during the pendency of a proceeding, perform, direct the performance of, or waive performance of, any act which could be done or ordered by the administrative law judge.

§ 747.5 Authority of the Administrative Law Judge.

(a) *General rule.* All proceedings governed by this Part shall be conducted in accordance with the provisions of Chapter 5 of Title 5 of the United States Code. The administrative law judge shall have all powers necessary to conduct a proceeding in a fair and impartial manner and to avoid unnecessary delay.

(b) *Powers.* The administrative law judge shall have all powers necessary to conduct the proceeding in accordance with paragraph (a) of this Section, including the following powers:

(1) To administer oaths and affirmations;

(2) To issue subpoenas, subpoenas duces tecum, and protective orders, as authorized by this Part, and to quash or modify any such subpoenas and orders;

(3) To receive relevant evidence and to rule upon the admission of evidence and offers of proof;

(4) To take or cause depositions to be taken as authorized by this Subpart;

(5) To regulate the course of the hearing and the conduct of the parties and their counsel;

(6) To hold scheduling and/or pre-hearing conferences as set forth in § 747.31;

(7) To consider and rule upon all procedural and other motions appropriate in an adjudicatory proceeding, provided that only the NCUA Board shall have the power to grant any motion to dismiss the proceeding or to decide any other motion that results in a final determination of the merits of the proceeding;

(8) To prepare and present to the NCUA Board a recommended decision as provided herein;

(9) To recuse himself or herself by motion made by a party or on his or her own motion;

(10) To establish time, place and manner limitations on the attendance of the public and the media for any public hearing; and

(11) To do all other things necessary and appropriate to discharge the duties of a presiding officer.

§ 747.6 Appearance and Practice in Adjudicatory Proceedings.

(a) *Appearance before the NCUA or an administrative law judge.* (1) *By attorneys.* Any member in good standing of the bar of the highest court of any state, commonwealth, possession, territory of the United States, or the District of Columbia may represent others before the NCUA if such attorney is not currently suspended or debarred from practice before the NCUA.

(2) *By non-attorneys.* An individual may appear on his or her own behalf; a member of a partnership may represent the partnership; a duly authorized officer, director, or employee of any government unit, agency, institution, corporation, or authority may represent that unit, agency, institution, corporation, or authority if such officer, director, or employee is not currently suspended or debarred from practice before the NCUA.

(3) *Notice of appearance.* Any individual acting as counsel on behalf of a party, including the NCUA Board, shall file a notice of appearance with OFIA at or before the time that the individual submits papers or otherwise appears on behalf of a party in the adjudicatory proceeding. The notice of appearance must include a written declaration that the individual is currently qualified as provided in paragraph (a)(1) or (a)(2) of this section and is authorized to represent the particular party. By filing a notice of appearance on behalf of a party in an adjudicatory proceeding, the counsel agrees and represents that he or she is authorized to accept service on behalf of the represented party and that, in the event of withdrawal from representation, he or she will, if required by the administrative law judge, continue to accept service until new counsel has filed a notice of appearance or until the represented party indicates that he or she will proceed on a *pro se* basis.

(b) *Sanctions.* Dilatory, obstructionist, egregious, contemptuous, or contumacious conduct at any phase of any adjudicatory proceeding may be grounds for exclusion or suspension of counsel from the proceeding.

§ 747.7 Good Faith Certification.

(a) *General requirement.* Every filing or submission of record following the issuance of a notice shall be signed by at least one counsel of record in his or her individual name and shall state that counsel's address and telephone number. A party who acts as his or her own counsel shall sign his or her individual name and state his or her address and telephone number on every filing or submission of record.

(b) *Effect of signature.* (1) The signature of counsel or a party shall constitute a certification that: the counsel or party has read the filing or submission of record; to the best of his or her knowledge, information, and belief formed after reasonable inquiry, the filing or submission of record is well-grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law; and the filing or submission of record is not made for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation.

(2) If a filing or submission of record is not signed, the administrative law judge shall strike the filing or submission of record, unless it is signed promptly after the omission is called to the attention of the pleader or movant.

(c) *Effect of making oral motion or argument.* The act of making any oral motion or oral argument by any counsel or party constitutes a certification that to the best of his or her knowledge, information, and belief formed after reasonable inquiry, his or her statements are well-grounded in fact and are warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and are not made

for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation.

§ 747.8 Conflicts of Interest.

(a) *Conflict of interest in representation.* No person shall appear as counsel for another person in an adjudicatory proceeding if it reasonably appears that such representation may be materially limited by that counsel's responsibilities to a third person or by the counsel's own interests. The administrative law judge may take corrective measures at any stage of a proceeding to cure a conflict of interest in representation, including the issuance of an order limiting the scope of representation or disqualifying an individual from appearing in a representative capacity for the duration of the proceeding.

(b) *Certification and waiver.* If any person appearing as counsel represents two or more parties to an adjudicatory proceeding or also represents a non-party on a matter relevant to an issue in the proceeding, counsel must certify in writing at the time of filing the notice of appearance required by § 747.6(a):

(1) That the counsel has personally and fully discussed the possibility of conflicts of interest with each such party and non-party; and

(2) That each such party and non-party waives any right it might otherwise have had to assert any known conflicts of interest or to assert any non-material conflicts of interest during the course of the proceeding.

§ 747.9 Ex Parte Communications.

(a) *Definition.* (1) *Ex parte communication* means any material oral or written communication relevant to the merits of an adjudicatory proceeding that was neither on the record nor on reasonable prior notice to all parties that takes place between—

(i) An interested person outside the NCUA (including such person's counsel); and

(ii) The administrative law judge handling that proceeding, the NCUA Board, or a decisional employee.

(2) *Exception.* A request for status of the proceeding does not constitute an ex parte communication.

(b) *Prohibition of ex parte communications.* From the time the notice is issued by the NCUA Board until the date that the NCUA Board issues its final decision pursuant to § 747.40(c):

(1) No interested person outside the NCUA shall make or knowingly cause to be made an ex parte communication to any member of the NCUA Board, the administrative law judge, or a decisional employee; and

(2) No member of the NCUA Board, administrative law judge, or decisional employee shall make or knowingly cause to be made to any interested person outside the NCUA any ex parte communication.

(c) *Procedure upon occurrence of ex parte communication.* If an ex parte communication is received by the administrative law judge, a member of the NCUA Board or any other person identified in paragraph (a) of this Section, that person shall cause all such written communications (or, if the communication is oral, a memorandum stating the substance of the communication) to be placed on the record of the proceeding and served on all parties. All other parties to the proceeding shall have an opportunity, within ten days of receipt of service of the ex parte communication, to file responses thereto and to recommend any sanctions, in accordance with paragraph (d) of this Section, that they believe to be appropriate under the circumstances.

(d) *Sanctions.* Any party or his or her counsel who makes a prohibited ex parte communication, or who encourages or solicits another to make any such communication, may be subject to any appropriate sanction or sanctions imposed by the NCUA Board or the administrative law judge, including, but not limited to, exclusion from the proceedings and an adverse ruling on the issue which is the subject of the prohibited communication.

(e) *Separation of functions.* Except to the extent required for the disposition of ex parte matters as authorized by law, the administrative law judge may not consult a person or party on any matter relevant to the merits of the adjudication, unless on notice and opportunity for all parties to participate. An employee or agent engaged in the performance of investigative or prosecuting functions for the NCUA in a case may not, in that or a factually related case, participate or advise in the decision, recommended decision, or agency review of the recommended decision under section 747.40, except as witness or counsel in public proceedings.

§ 747.10 Filing of Papers.

(a) *Filing.* Any papers required to be filed, excluding documents produced in response to a discovery request pursuant to §§ 747.25 and 747.26, shall be filed with the OFIA, except as otherwise provided.

(b) *Manner of filing.* Unless otherwise specified by the NCUA Board or the administrative law judge, filing may be accomplished by:

(1) Personal service;

(2) Delivering the papers to a reliable commercial courier service, overnight delivery service, or to the U.S. Post Office for Express Mail delivery;

(3) Mailing the papers by first class, registered, or certified mail; or

(4) Transmission by electronic media, only if expressly authorized, and upon any conditions specified by the NCUA Board or the administrative law judge. All papers filed by electronic media shall also concurrently be filed in accordance with paragraph (c) of this Section.

(c) *Formal requirements as to papers filed.* (1) *Form.* All papers filed must set forth the name, address, and telephone number of the counsel or party making the filing and must be accompanied by a certification setting forth when and how service has been made on all other parties. All papers filed must be double spaced and printed or typewritten on 8 1/2 x 11 inch paper, and must be clear and legible.

(2) *Signature.* All papers must be dated and signed as provided in § 747.7.

(3) *Caption.* All papers filed must include at the head thereof, or on a title page, the name of the NCUA and of the filing party, the title and docket number of the proceeding, and the subject of the particular paper.

(4) *Number of copies.* Unless otherwise specified by the NCUA Board, or the administrative law judge, an original and one copy of all documents and papers shall be filed, except that only one copy of transcripts of testimony and exhibits shall be filed.

§ 747.11 Service of Papers.

(a) *By the parties.* Except as otherwise provided, a party filing papers shall serve a copy upon the counsel of record for all other parties to the proceeding so represented, and upon any party not so represented.

(b) *Method of service.* Except as provided in paragraphs (c)(2) and (d) of this Section, a serving party shall use one or more of the following methods of service:

(1) Personal service;

(2) Delivering the papers to a reliable commercial courier service, overnight delivery service, or to the U.S. Post Office for Express Mail delivery;

(3) Mailing the papers by first class, registered, or certified mail; or

(4) Transmission by electronic media, only if the parties mutually agree. Any papers served by electronic media shall also concurrently be served in accordance with the requirements of § 747.10(c).

(c) *By the NCUA Board or the administrative law judge.* (1) All papers required to be served by the NCUA Board or the administrative law judge upon a party who has appeared in the proceeding in accordance with § 747.6, shall be served by any means specified in paragraph (b) of this section.

(2) If a party has not appeared in the proceeding in accordance with § 747.6, the NCUA Board or the administrative law judge shall make service by any of the following methods:

(i) By personal service;

(ii) If the person to be served is an individual, by delivery to a person of suitable age and discretion at the physical location where the individual resides or works;

(iii) If the person to be served is a corporation or other association, by delivery to an officer, managing or general agent, or to any other agent authorized by appointment or by law to receive service and, if the agent is one authorized by statute to receive service and the statute so requires, by also mailing a copy to the party;

(iv) By registered or certified mail addressed to the person's last known address; or

(v) By any other method reasonably calculated to give actual notice.

(d) *Subpoenas.* Service of a subpoena may be made:

(1) By personal service;

(2) If the person to be served is an individual, by delivery to a person of suitable age and discretion at the physical location where the individual resides or works;

(3) By delivery to an agent, which, in the case of a corporation or other association, is delivery to an officer, managing or general agent, or to any other agent authorized by

appointment or by law to receive service and, if the agent is one authorized by statute to receive service and the statute so requires, by also mailing a copy to the party;

(4) By registered or certified mail addressed to the person's last known address; or

(5) By any other method reasonably calculated to give actual notice.

(e) *Area of service.* Service in any state, territory, possession of the United States, or the District of Columbia, on any person or company doing business in any state, territory, possession of the United States, or the District of Columbia, or on any person as otherwise provided by law, is effective without regard to the place where the hearing is held, provided that if service is made on a foreign bank in connection with an action or proceeding involving one or more of its branches or agencies located in any state, territory, possession of the United States, or the District of Columbia, service shall be made on at least one branch or agency so involved.

§ 747.12 Construction of Time Limits.

(a) *General rule.* In computing any period of time prescribed by this subpart, the date of the act or event that commences the designated period of time is not included. The last day so computed is included unless it is a Saturday, Sunday, or Federal holiday. When the last day is a Saturday, Sunday, or Federal holiday, the period runs until the end of the next day that is not a Saturday, Sunday, or Federal holiday. Intermediate Saturdays, Sundays, and Federal holidays are included in the computation of time. However, when the time period within which an act is to be performed is ten days or less, not including any additional time allowed for in § 747.12(c), intermediate Saturdays, Sundays, and Federal holidays are not included.

(b) *When papers are deemed to be filed or served.*

(1) Filing and service are deemed to be effective:

(i) In the case of personal service or same day commercial courier delivery, upon actual service;

(ii) In the case of overnight commercial delivery service, U.S. Express Mail delivery, or first class, registered, or certified mail, upon deposit in or delivery to an appropriate point of collection;

(iii) In the case of transmission by electronic media, as specified by the authority receiving the filing, in the case of filing, and as agreed among the parties, in the case of service.

(2) The effective filing and service dates specified in paragraph (b)(1) of this Section may be modified by the NCUA Board or administrative law judge in the case of filing or by agreement of the parties in the case of service.

(c) *Calculation of time for service and filing of responsive papers.* Whenever a time limit is measured by a prescribed period from the service of any notice or paper, the applicable time limits are calculated as follows:

(1) If service is made by first class, registered, or certified mail, add three calendar days to the prescribed period;

(2) If service is made by express mail or overnight delivery service, add one calendar day to the prescribed period; or

(3) If service is made by electronic media transmission, add one calendar day to the prescribed period, unless otherwise determined by the NCUA Board or the administrative law judge in the case of filing, or by agreement among the parties in the case of service.

§ 747.13 Change of Time Limits.

Except as otherwise provided by law, the administrative law judge may, for good cause shown, extend the time limits prescribed by the Uniform Rules or by any notice or order issued in the proceedings. After the referral of the case to the NCUA Board pursuant to § 747.38, the NCUA Board may grant extensions of the time limits for good cause shown. Extensions may be granted upon the motion of a party after notice and opportunity to respond is afforded all non-moving parties, or upon the NCUA Board's or the administrative law judge's own motion.

§ 747.14 Witness Fees and Expenses.

Witnesses subpoenaed for testimony or depositions shall be paid the same fees for attendance and mileage as are paid in the United States district courts in proceedings in which the United States is a party, provided that, in the case of a discovery subpoena addressed to a party, no witness fees or mileage need be paid. Fees for witnesses shall be tendered in advance by the party requesting the subpoena, except that fees and

mileage need not be tendered in advance where the NCUA is the party requesting the subpoena. The NCUA shall not be required to pay any fees to, or expenses of, any witness not subpoenaed by the NCUA.

§ 747.15 Opportunity for Informal Settlement.

Any respondent may, at any time in the proceeding, unilaterally submit to Enforcement Counsel written offers or proposals for settlement of a proceeding, without prejudice to the rights of any of the parties. No such offer or proposal shall be made to any NCUA representative other than Enforcement Counsel. Submission of a written settlement offer does not provide a basis for adjourning or otherwise delaying all or any portion of a proceeding under this Part. No settlement offer or proposal, or any subsequent negotiation or resolution, is admissible as evidence in any proceeding.

§ 747.16 NCUA's Right to Conduct Examination.

Nothing contained in this Subpart limits in any manner the right of the NCUA to conduct any examination, inspection, or visitation of any institution or institution-affiliated party, or the right of the NCUA to conduct or continue any form of investigation authorized by law.

§ 747.17 Collateral Attacks on Adjudicatory Proceeding.

If an interlocutory appeal or collateral attack is brought in any court concerning all or any part of an adjudicatory proceeding, the challenged adjudicatory proceeding shall continue without regard to the pendency of that court proceeding. No default or other failure to act as directed in the adjudicatory proceeding within the times prescribed in this Subpart shall be excused based on the pendency before any court of any interlocutory appeal or collateral attack.

§ 747.18 Commencement of Proceeding and Contents of Notice.

(a) *Commencement of proceeding.* (1) A proceeding governed by this Subpart is commenced by issuance of a notice by the NCUA Board.

(2) The notice must be served by the NCUA Board upon the respondent and given to any other appropriate financial institution supervisory authority where required by law.

(3) The notice must be filed with the OFIA.

(b) *Contents of notice.* The notice must set forth:

(1) The legal authority for the proceeding and for the NCUA's jurisdiction over the proceeding;

(2) A statement of the matters of fact or law showing that the NCUA is entitled to relief;

(3) A proposed order or prayer for an order granting the requested relief;

(4) The time, place, and nature of the hearing as required by law or regulation;

(5) The time within which to file an answer as required by law or regulation;

(6) The time within which to request a hearing as required by law or regulation; and

(7) That the answer and/or request for a hearing shall be filed with OFIA.

§ 747.19 Answer.

(a) *When.* Within 20 days of service of the notice, respondent shall file an answer as designated in the notice. In a civil money penalty proceeding, respondent shall also file a request for a hearing within 20 days of service of the notice.

(b) *Content of answer.* An answer must specifically respond to each paragraph or allegation of fact contained in the notice and must admit, deny, or state that the party lacks sufficient information to admit or deny each allegation of fact. A statement of lack of information has the effect of a denial. Denials must fairly meet the substance of each allegation of fact denied; general denials are not permitted. When a respondent denies part of an allegation, that part must be denied and the remainder specifically admitted. Any allegation of fact in the notice which is not denied in the answer must be deemed admitted for purposes of the proceeding. A respondent is not required to respond to the portion of a notice that constitutes the prayer for relief or proposed order. The answer must set forth affirmative defenses, if any, asserted by the respondent.

(c) *Default.* (1) *Effect of failure to answer.* Failure of a respondent to file an answer required by this Section within the time provided constitutes a waiver of his or her right to appear and contest the allegations in the notice. If no timely answer is filed, the administrative law judge, upon motion of the Enforcement Counsel, shall file with the NCUA Board a recommended decision containing the findings and the relief sought in the notice. Any final order issued by the NCUA Board based upon a respondent's failure to answer is deemed to be an order issued upon consent.

(2) *Effect of failure to request a hearing in civil money penalty proceedings.* If respondent

fails to request a hearing as required by law within the time provided, the notice of assessment constitutes a final and unappealable order.

§ 747.20 Amended Pleadings.

(a) *Amendments.* The notice or answer may be amended or supplemented at any stage of the proceeding. The respondent must answer an amended notice within the time remaining for the respondent's answer to the original notice, or within ten days after service of the amended notice, whichever period is longer, unless the NCUA Board or administrative law judge orders otherwise for good cause.

(b) *Amendments to conform to the evidence.* When issues not raised in the notice or answer are tried at the hearing by express or implied consent of the parties, they will be treated in all respects as if they had been raised in the notice or answer, and no formal amendments are required. If evidence is objected to at the hearing on the ground that it is not within the issues raised by the notice or answer, the administrative law judge may admit the evidence when admission is likely to assist in adjudicating the merits of the action and the objecting party fails to satisfy the administrative law judge that the admission of such evidence would unfairly prejudice that party's action or defense upon the merits. The administrative law judge may grant a continuance to enable the objecting party to meet such evidence.

§ 747.21 Failure to Appear.

Failure of a respondent to appear in person at the hearing or by a duly authorized counsel constitutes a waiver of respondent's right to a hearing and is deemed an admission of the facts as alleged and consent to the relief sought in the notice. Without further proceedings or notice to the respondent, the administrative law judge shall file with the NCUA Board a recommended decision containing the findings and the relief sought in the notice.

§ 747.22 Consolidation and Severance of Actions.

(a) *Consolidation.* (1) On the motion of any party, or on the administrative law judge's own motion, the administrative law judge may consolidate, for some or all purposes, any two or more proceedings, if each such proceeding involves or arises out of the same transaction, occurrence or series of transactions or occurrences, or involves at least one common respondent or a material common question of law or fact, unless such consolidation would cause unreasonable delay or injustice.

(2) In the event of consolidation under paragraph (a)(1) of this Section, appropriate adjustment to the prehearing schedule must be made to avoid unnecessary expense, inconvenience, or delay.

(b) *Severance.* The administrative law judge may, upon the motion of any party, sever the proceeding for separate resolution of the matter as to any respondent only if the administrative law judge finds that:

(1) Undue prejudice or injustice to the moving party would result from not severing the proceeding; and

(2) Such undue prejudice or injustice would outweigh the interests of judicial economy and expedition in the complete and final resolution of the proceeding.

§ 747.23 Motions.

(a) *In writing.* (1) Except as otherwise provided herein, an application or request for an order or ruling must be made by written motion.

(2) All written motions must state with particularity the relief sought and must be accompanied by a proposed order.

(3) No oral argument may be held on written motions except as otherwise directed by the administrative law judge. Written memoranda, briefs, affidavits, or other relevant material or documents may be filed in support of or in opposition to a motion.

(b) *Oral motions.* A motion may be made orally on the record unless the administrative law judge directs that such motion be reduced to writing.

(c) *Filing of motions.* Motions must be filed with the administrative law judge, except that upon the filing of the recommended decision, motions must be filed with the NCUA Board.

(d) *Responses.* (1) Except as otherwise provided herein, within ten days after service of any written motion, or within such other period of time as may be established by the administrative law judge or the NCUA Board, any party may file a written response to a motion. The administrative law judge shall not rule on any oral or written

motion before each party has had an opportunity to file a response.

(2) The failure of a party to oppose a written motion or an oral motion made on the record is deemed a consent by that party to the entry of an order substantially in the form of the order accompanying the motion.

(e) *Dilatory motions.* Frivolous, dilatory or repetitive motions are prohibited. The filing of such motions may form the basis for sanctions.

(f) *Dispositive motions.* Dispositive motions are governed by §§ 747.29 and 747.30.

§ 747.24 Scope of Document Discovery.

(a) *Limits on discovery.* (1) Subject to the limitations set out in paragraphs (b), (c), and (d) of this section, a party to a proceeding under this subpart may obtain document discovery by serving a written request to produce documents. For purposes of a request to produce documents, the term "documents" may be defined to include drawings, graphs, charts, photographs, recordings, data stored in electronic form, and other data compilations from which information can be obtained, or translated, if necessary, by the parties through detection devices into reasonably usable form, as well as written material of all kinds.

(2) Discovery by use of deposition is governed by subpart I of this part.

(3) Discovery by use of interrogatories is not permitted.

(b) *Relevance.* A party may obtain document discovery regarding any matter, not privileged, that has material relevance to the merits of the pending action. Any request to produce documents that calls for irrelevant material, that is unreasonable, oppressive, excessive in scope, unduly burdensome, or repetitive of previous requests, or that seeks to obtain privileged documents will be denied or modified. A request is unreasonable, oppressive, excessive in scope, or unduly burdensome if, among other things, it fails to include justifiable limitations on the time period covered and the geographic locations to be searched, the time provided to respond in the request is inadequate, or the request calls for copies of documents to be delivered to the requesting party and fails to include the requester's written agreement to pay in advance for the copying, in accordance with § 747.25.

(c) *Privileged matter.* Privileged documents are not discoverable. Privileges include the attorney-client privilege, work-product privilege, any government's or government agency's deliberative-process privilege, and any other privileges the Constitution, any applicable act of Congress, or the principles of common law provide.

(d) *Time limits.* All discovery, including all responses to discovery requests, shall be completed at least 20 days prior to the date scheduled for the commencement of the hearing, except as provided in the Local Rules. No exceptions to this time limit shall be permitted, unless the administrative law judge finds on the record that good cause exists for waiving the requirements of this paragraph.

§ 747.25 Request for Document Discovery from Parties.

(a) *General rule.* Any party may serve on any other party a request to produce for inspection any discoverable documents that are in the possession, custody, or control of the party upon whom the request is served. The request must identify the documents to be produced either by individual item or by category, and must describe each item and category with reasonable particularity. Documents must be produced as they are kept in the usual course of business or must be organized to correspond with the categories in the request.

(b) *Production or copying.* The request must specify a reasonable time, place, and manner for production and performing any related acts. In lieu of inspecting the documents, the requesting party may specify that all or some of the responsive documents be copied and the copies delivered to the requesting party. If copying of fewer than 250 pages is requested, the party to whom the request is addressed shall bear the cost of copying and shipping charges. If a party requests 250 pages or more of copying, the requesting party shall pay for the copying and shipping charges. Copying charges are the current per-page copying rate imposed by 12 CFR § 792.5 implementing the Freedom of Information Act (5 U.S.C. 552). The party to whom the request is addressed may require payment in advance before producing the documents.

(c) *Obligation to update responses.* A party who has responded to a discovery request with a response that was complete when made is not required to supplement the response to include documents thereafter acquired, unless the responding party learns that:

(1) The response was materially incorrect when made; or

(2) The response, though correct when made, is no longer true and a failure to amend the response is, in substance, a knowing concealment.

(d) *Motions to limit discovery.* (1) Any party that objects to a discovery request may, within ten days of being served with such request, file a motion in accordance with the provisions of § 747.23 to strike or otherwise limit the request. If an objection is made to only a portion of an item or category in a request, the portion objected to shall be specified. Any objections not made in accordance with this paragraph and § 747.23 are waived.

(2) The party who served the request that is the subject of a motion to strike or limit may file a written response within five days of service of the motion. No other party may file a response.

(e) *Privilege.* At the time other documents are produced, the producing party must reasonably identify all documents withheld on the grounds of privilege and must produce a statement of the basis for the assertion of privilege. When similar documents that are protected by deliberative process, attorney work-product, or attorney-client privilege are voluminous, these documents may be identified by category instead of by individual document. The administrative law judge retains discretion to determine when the identification by category is insufficient.

(f) *Motions to compel production.* (1) If a party withholds any documents as privileged or fails to comply fully with a discovery request, the requesting party may, within ten days of the assertion of privilege or of the time the failure to comply becomes known to the requesting party, file a motion in accordance with the provisions of § 747.23 for the issuance of a subpoena compelling production.

(2) The party who asserted the privilege or failed to comply with the request may file a written response to a motion to compel within five days of service of the motion. No other party may file a response.

(g) *Ruling on motions.* After the time for filing responses pursuant to this section has expired, the administrative law judge shall rule promptly on all motions filed pursuant to this section. If the administrative law judge determines that a discovery request, or any of its terms, calls for irrelevant material, is unreasonable, oppressive, excessive in scope, unduly burdensome, or repetitive of previous requests, or seeks to obtain privileged documents, he or she may deny or modify the request, and may issue appropriate protective orders, upon such conditions as justice may require. The pendency of a motion to strike or limit discovery or to compel production is not a basis for staying or continuing the proceeding, unless otherwise ordered by the administrative law judge. Notwithstanding any other provision in this part, the administrative law judge may not release, or order a party to produce, documents withheld on grounds of privilege if the party has stated to the administrative law judge its intention to file a timely motion for interlocutory review of the administrative law judge's order to produce the documents, and until the motion for interlocutory review has been decided.

(h) *Enforcing discovery subpoenas.* If the administrative law judge issues a subpoena compelling production of documents by a party, the subpoenaing party may, in the event of noncompliance and to the extent authorized by applicable law, apply to any appropriate United States district court for an order requiring compliance with the subpoena. A party's right to seek court enforcement of a subpoena shall not in any manner limit the sanctions that may be imposed by the administrative law judge against a party who fails to produce subpoenaed documents.

§ 747.26 Document Subpoenas to Nonparties.

(a) *General rules.* (1) Any party may apply to the administrative law judge for the issuance of a document discovery subpoena addressed to any person who is not a party to the proceeding. The application must contain a proposed document subpoena and a brief statement showing the general relevance and reasonableness of the scope of documents sought. The subpoenaing party shall specify a reasonable time, place, and manner for making production in response to the document subpoena.

(2) A party shall only apply for a document subpoena under this Section within the time period during which such party could serve a discovery request under § 747.24(d). The party obtaining the document subpoena is responsible for serving it on the subpoenaed person and for serving copies on all parties. Document subpoenas may be served in any state, territory, or possession of the United States, the District of Columbia, or as otherwise provided by law.

(3) The administrative law judge shall promptly issue any document subpoena requested pursuant to this Section. If the administrative law judge determines that the application does not set forth a valid basis for the issuance of the subpoena, or that any of its terms are unreasonable, oppressive, excessive in scope, or unduly burdensome, he or she may refuse to issue the subpoena or may issue it in a modified form upon such conditions as may be consistent with the Uniform Rules.

(b) *Motion to quash or modify.* (1) Any person to whom a document subpoena is directed may file a motion to quash or modify such subpoena, accompanied by a statement of the basis for quashing or modifying the subpoena. The movant shall serve the motion on all parties, and any party may respond to such motion within ten days of service of the motion.

(2) Any motion to quash or modify a document subpoena must be filed on the same basis, including the assertion of privilege, upon which a party could object to a discovery request under § 747.25(d), and during the same time limits during which such an objection could be filed.

(c) *Enforcing document subpoenas.* If a subpoenaed person fails to comply with any subpoena issued pursuant to this Section or any order of the administrative law judge which directs compliance with all or any portion of a document subpoena, the subpoenaing party or any other aggrieved party may, to the extent authorized by applicable law, apply to an appropriate United States district court for an order requiring compliance with so much of the document subpoena as the administrative law judge has not quashed or modified. A party's right to seek court enforcement of a document subpoena shall in no way limit the sanctions that may be imposed by the administrative law judge on a party who induces a failure to comply with subpoenas issued under this Section.

§ 747.27 Deposition of Witness Unavailable for Hearing.

(a) *General rules.* (1) If a witness will not be available for the hearing, a party desiring that witness's testimony for the record may apply in accordance with the procedures set forth in paragraph (a)(2) of this Section, to the administrative law judge for the issuance of a subpoena, including a subpoena duces tecum, requiring the attendance of the witness at a deposition. The administrative law judge may issue a deposition subpoena under this Section upon showing that:

(i) The witness will be unable to attend or may be prevented from attending the hearing because of age, sickness or infirmity, or will otherwise be unavailable;

(ii) The witness's unavailability was not procured or caused by the subpoenaing party;

(iii) The testimony is reasonably expected to be material; and

(iv) Taking the deposition will not result in any undue burden to any other party and will not cause undue delay of the proceeding.

(2) The application must contain a proposed deposition subpoena and a brief statement of the reasons for the issuance of the subpoena. The subpoena must name the witness whose deposition is to be taken and specify the time and place for taking the deposition. A deposition subpoena may require the witness to be deposed at any place within the country in which that witness resides or has a regular place of employment or such other convenient place as the administrative law judge shall fix.

(3) Any requested subpoena that sets forth a valid basis for its issuance must be promptly issued, unless the administrative law judge on his or her own motion, requires a written response or requires attendance at a conference concern ing whether the requested subpoena should be issued.

(4) The party obtaining a deposition subpoena is responsible for serving it on the witness and for serving copies on all parties. Unless the administrative law judge orders otherwise, no deposition under this Section shall be taken on fewer than ten days' notice to the witness and all parties. Deposition subpoenas may be served in any state, territory, or possession of the United States, or the District of Columbia, on any person or company doing business in any state, territory, or possession of the United States, or the District of Columbia, or as otherwise permitted by law.

(b) *Objections to deposition subpoenas.* (1) The witness and any party who has not had an opportunity to oppose a deposition subpoena issued under this Section may file a motion with the administrative law judge to quash or modify the subpoena prior to the time for compliance specified in the subpoena, but not more than ten days after service of the subpoena.

(2) A statement of the basis for the motion to quash or modify a subpoena issued under this

Section must accompany the motion. The motion must be served on all parties.

(c) *Procedure upon deposition.* (1) Each witness testifying pursuant to a deposition subpoena must be duly sworn, and each party shall have the right to examine the witness. Objections to questions or documents must be in short form, stating the grounds for the objection. Failure to object to questions or documents is not deemed a waiver except where the ground for the objection might have been avoided if the objection had been timely presented. All questions, answers, and objections must be recorded.

(2) Any party may move before the administrative law judge for an order compelling the witness to answer any questions the witness has refused to answer or submit any evidence the witness has refused to submit during the deposition.

(3) The deposition must be subscribed by the witness, unless the parties and the witness, by stipulation, have waived the signing, or the witness is ill, cannot be found, or has refused to sign. If the deposition is not subscribed by the witness, the court reporter taking the deposition shall certify that the transcript is a true and complete transcript of the deposition.

(d) *Enforcing subpoenas.* If a subpoenaed person fails to comply with any order of the administrative law judge which directs compliance with all or any portion of a deposition subpoena under paragraph (b) or (c)(3) of this Section, the subpoenaing party or other aggrieved party may, to the extent authorized by applicable law, apply to an appropriate United States district court for an order requiring compliance with the portions of the subpoena that the administrative law judge has ordered enforced. A party's right to seek court enforcement of a deposition subpoena in no way limits the sanctions that may be imposed by the administrative law judge on a party who fails to comply with, or procures a failure to comply with, a subpoena issued under this Section.

§ 747.28 Interlocutory Review.

(a) *General rule.* The NCUA Board may review a ruling of the administrative law judge prior to the certification of the record to the NCUA Board only in accordance with the procedures set forth in this Section and § 747.23.

(b) *Scope of review.* The NCUA Board may exercise interlocutory review of a ruling of the administrative law judge if the NCUA Board finds that:

(1) The ruling involves a controlling question of law or policy as to which substantial grounds exist for a difference of opinion;

(2) Immediate review of the ruling may materially advance the ultimate termination of the proceeding;

(3) Subsequent modification of the ruling at the conclusion of the proceeding would be an inadequate remedy; or

(4) Subsequent modification of the ruling would cause unusual delay or expense.

(c) *Procedure.* Any request for interlocutory review shall be filed by a party with the administrative law judge within ten days of his or her ruling and shall otherwise comply with § 747.23. Any party may file a response to a request for interlocutory review in accordance with § 747.23(d). Upon the expiration of the time for filing all responses, the administrative law judge shall refer the matter to the NCUA Board for final disposition.

(d) *Suspension of proceeding.* Neither a request for interlocutory review nor any disposition of such a request by the NCUA Board under this Section suspends or stays the proceeding unless other wise ordered by the administrative law judge or the NCUA Board.

§ 747.29 Summary Disposition.

(a) *In general.* The administrative law judge shall recommend that the NCUA Board issue a final order granting a motion for summary disposition if the undisputed pleaded facts, admissions, affidavits, stipulations, documentary evidence, matters as to which official notice may be taken, and any other evidentiary materials properly submitted in connection with a motion for summary disposition show that:

(1) There is no genuine issue as to any material fact; and

(2) The moving party is entitled to a decision in its favor as a matter of law.

(b) *Filing of motions and responses.* (1) Any party who believes that there is no genuine issue of material fact to be determined and that he or she is entitled to a decision as a matter of law may move at any time for summary disposition in its favor of all or any part of the proceeding. Any party, within 20 days after service of such a motion, or within such time period as allowed by the administrative law judge, may file a response to such motion.

(2) A motion for summary disposition must be accompanied by a statement of the material

facts as to which the moving party contends there is no genuine issue. Such motion must be supported by documentary evidence, which may take the form of admissions in pleadings, stipulations, depositions, investigatory depositions, transcripts, affidavits and any other evidentiary materials that the moving party contends support his or her position. The motion must also be accompanied by a brief containing the points and authorities in support of the contention of the moving party. Any party opposing a motion for summary disposition must file a statement setting forth those material facts as to which he or she contends a genuine dispute exists. Such opposition must be supported by evidence of the same type as that submitted with the motion for summary disposition and a brief containing the points and authorities in support of the contention that summary disposition would be inappropriate.

(c) *Hearing on motion.* At the request of any party or on his or her own motion, the administrative law judge may hear oral argument on the motion for summary disposition.

(d) *Decision on motion.* Following receipt of a motion for summary disposition and all responses thereto, the administrative law judge shall determine whether the moving party is entitled to summary disposition. If the administrative law judge determines that summary disposition is warranted, the administrative law judge shall submit a recommended decision to that effect to the NCUA Board. If the administrative law judge finds that no party is entitled to summary disposition, he or she shall make a ruling denying the motion.

§ 747.30 Partial Summary Disposition.

If the administrative law judge determines that a party is entitled to summary disposition as to certain claims only, he or she shall defer submitting a recommended decision as to those claims. A hearing on the remaining issues must be ordered. Those claims for which the administrative law judge has determined that summary disposition is warranted will be addressed in the recommended decision filed at the conclusion of the hearing.

§ 747.31 Scheduling and Prehearing Conferences.

(a) *Scheduling conference.* Within 30 days of service of the notice or order commencing a proceeding or such other time as parties may agree, the administrative law judge shall direct counsel for all parties to meet with him or her in person at a specified time and place prior to the hearing or to confer by telephone for the purpose of scheduling the course and conduct of the proceeding. This meeting or telephone conference is called a "scheduling conference." The identification of potential witnesses, the time for and manner of discovery, and the exchange of any prehearing materials including witness lists, statements of issues, stipulations, exhibits and any other materials may also be determined at the scheduling conference.

(b) *Prehearing conferences.* The administrative law judge may, in addition to the scheduling conference, on his or her own motion or at the request of any party, direct counsel for the parties to meet with him or her (in person or by telephone) at a prehearing conference to address any or all of the following:

(1) Simplification and clarification of the issues;

(2) Stipulations, admissions of fact, and the contents, authenticity and admissibility into evidence of documents;

(3) Matters of which official notice may be taken;

(4) Limitation of the number of witnesses;

(5) Summary disposition of any or all issues;

(6) Resolution of discovery issues or disputes;

(7) Amendments to pleadings; and

(8) Such other matters as may aid in the orderly disposition of the proceeding.

(c) *Transcript.* The administrative law judge, in his or her discretion, may require that a scheduling or prehearing conference be recorded by a court reporter. A transcript of the conference and any materials filed, including orders, becomes part of the record of the proceeding. A party may obtain a copy of the transcript at its expense.

(d) *Scheduling or prehearing orders.* At or within a reasonable time following the conclusion of the scheduling conference or any prehearing conference, the administrative law judge shall serve on each party an order setting forth any agreements reached and any procedural determinations made.

§ 747.32 Prehearing Submissions.

(a) Within the time set by the administrative law judge, but in no case later than 14 days before the start of the hearing, each party shall serve on every other party, his or her:

(1) Prehearing statement;

(2) Final list of witnesses to be called to testify at the hearing, including name and address of each witness and a short summary of the expected testimony of each witness;

(3) List of the exhibits to be introduced at the hearing along with a copy of each exhibit; and

(4) Stipulations of fact, if any.

(b) *Effect of failure to comply.* No witness may testify and no exhibits may be introduced at the hearing if such witness or exhibit is not listed in the prehearing submissions pursuant to paragraph (a) of this Section, except for good cause shown.

§ 747.33 Public Hearings.

(a) *General rule.* All hearings shall be open to the public, unless the NCUA Board, in its discretion, determines that holding an open hearing would be contrary to the public interest. Within 20 days of service of the notice, any respondent may file with the NCUA Board a request for a private hearing, and any party may file a reply to such a request. A party must serve on the administrative law judge a copy of any request or reply the party files with the NCUA Board. The form of, and procedure for, these requests and replies are governed by § 747.23. A party's failure to file a request or a reply constitutes a waiver of any objections regarding whether the hearing will be public or private.

(b) *Filing document under seal.* Enforcement Counsel, in his or her discretion, may file any document or part of a document under seal if disclosure of the document would be contrary to the public interest. The administrative law judge shall take all appropriate steps to preserve the confidentiality of such documents or parts thereof, including closing portions of the hearing to the public.

§ 747.34 Hearing Subpoenas.

(a) *Issuance.* (1) Upon application of a party showing general relevance and reasonableness of scope of the testimony or other evidence sought, the administrative law judge may issue a subpoena or a subpoena *duces tecum* requiring the attendance of a witness at the hearing or the production of documentary or physical evidence at the hearing. The application for a hearing subpoena must also contain a proposed subpoena specifying the attendance of a witness or the production of evidence from any state, territory, or possession of the United States, the District of Columbia, or as otherwise provided by law at any designated place where the hearing is being conducted. The party making the application shall serve a copy of the application and the proposed subpoena on every other party.

(2) A party may apply for a hearing subpoena at any time before the commencement of a hearing. During a hearing, a party may make an application for a subpoena orally on the record before the administrative law judge.

(3) The administrative law judge shall promptly issue any hearing subpoena requested pursuant to this section. If the administrative law judge determines that the application does not set forth a valid basis for the issuance of the subpoena, or that any of its terms are unreasonable, oppressive, excessive in scope, or unduly burdensome, he or she may refuse to issue the subpoena or may issue it in a modified form upon any conditions consistent with this subpart. Upon issuance by the administrative law judge, the party making the application shall serve the subpoena on the person named in the subpoena and on each party.

(b) *Motion to quash or modify.* (1) Any person to whom a hearing subpoena is directed or any party may file a motion to quash or modify the subpoena, accompanied by a statement of the basis for quashing or modifying the subpoena. The movant must serve the motion on each party and on the person named in the subpoena. Any party may respond to the motion within ten days of service of the motion.

(2) Any motion to quash or modify a hearing subpoena must be filed prior to the time specified in the subpoena for compliance, but not more than ten days after the date of service of the subpoena upon the movant.

(c) *Enforcing subpoenas.* If a subpoenaed person fails to comply with any subpoena issued pursuant to this Section or any order of the administrative law judge which directs compliance with all or any portion of a document subpoena, the subpoenaing party or any other aggrieved party may seek enforcement of the subpoena pursuant to § 747.26(c).

§ 747.35 Conduct of Hearings.

(a) *General rules.* (1) Hearings shall be conducted so as to provide a fair and expeditious presentation of the relevant disputed issues. Each party has the right to present its case or defense by oral and documentary evidence and to conduct such cross examination as may be required for full disclosure of the facts.

(2) *Order of hearing.* Enforcement Counsel shall present its case-in-chief first, unless otherwise ordered by the administrative law judge, or unless otherwise expressly specified by law or regulation. Enforcement Counsel shall be the first party to present an opening statement and a closing statement, and may make a rebuttal statement after the respondent's closing statement. If there are multiple respondents, respondents may agree among themselves as to their order of presentation of their cases, but if they do not agree the administrative law judge shall fix the order.

(3) Examination of witnesses. Only one counsel for each party may conduct an examination of a witness, except that in the case of extensive direct examination, the administrative law judge may permit more than one counsel for the party presenting the witness to conduct the examination. A party may have one counsel conduct the direct examination and another counsel conduct re-direct examination of a witness, or may have one counsel conduct the cross examination of a witness and another counsel conduct the re-cross examination of a witness.

(4) *Stipulations.* Unless the administrative law judge directs otherwise, all stipulations of fact and law previously agreed upon by the parties, and all documents, the admissibility of which have been previously stipulated, will be admitted into evidence upon commencement of the hearing.

(b) *Transcript.* The hearing must be recorded and transcribed. The reporter will make the transcript available to any party upon payment by that party to the reporter of the cost of the transcript. The administrative law judge may order the record corrected, either upon motion to correct, upon stipulation of the parties, or following notice to the parties upon the administrative law judge's own motion.

§ 747.36 Evidence.

(a) *Admissibility.* (1) Except as is otherwise set forth in this Section, relevant, material, and reliable evidence that is not unduly repetitive is admissible to the fullest extent authorized by the Administrative Procedure Act and other applicable law.

(2) Evidence that would be admissible under the Federal Rules of Evidence is admissible in a proceeding conducted pursuant to this Subpart.

(3) Evidence that would be inadmissible under the Federal Rules of Evidence may not be deemed or ruled to be inadmissible in a proceeding conducted pursuant to this Subpart if such evidence is relevant, material, reliable and not unduly repetitive.

(b) *Official notice.* (1) Official notice may be taken of any material fact which may be judicially noticed by a United States district court and any material information in the official public records of any Federal or state government agency.

(2) All matters officially noticed by the administrative law judge or NCUA Board shall appear on the record.

(3) If official notice is requested or taken of any material fact, the parties, upon timely request, shall be afforded an opportunity to object.

(c) *Documents.* (1) A duplicate copy of a document is admissible to the same extent as the original, unless a genuine issue is raised as to whether the copy is in some material respect not a true and legible copy of the original.

(2) Subject to the requirements of paragraph (a) of this Section, any document, including a report of examination, supervisory activity, inspection or visitation, prepared by an appropriate Federal financial institution regulatory agency or by a state regulatory agency, is admissible either with or without a sponsoring witness.

(3) Witnesses may use existing or newly created charts, exhibits, calendars, calculations, outlines or other graphic material to summarize, illustrate, or simplify the presentation of testimony. Such materials may, subject to the administrative law judge's discretion, be used with or without being admitted into evidence.

(d) *Objections.* (1) Objections to the admissibility of evidence must be timely made and rulings on all objections must appear on the record.

(2) When an objection to a question or line of questioning propounded to a witness is sustained, the examining counsel may make a specific proffer on the record of what he or she expected to prove by the expected testimony of the witness, either by representation of counsel or by direct interrogation of the witness.

(3) The administrative law judge shall retain rejected exhibits, adequately marked for identification, for the record, and transmit such exhibits to the NCUA Board.

(4) Failure to object to admission of evidence or to any ruling constitutes a waiver of the objection.

(e) *Stipulations.* The parties may stipulate as to any relevant matters of fact or the authentication of any relevant documents. Such stipulations must be received in evidence at a hearing, and are binding on the parties with respect to the matters therein stipulated.

(f) *Depositions of unavailable witnesses.* (1) If a witness is unavailable to testify at a hearing, and that witness has testified in a deposition to which all parties in a proceeding had notice and an opportunity to participate, a party may offer as evidence all or any part of the transcript of the deposition, including deposition exhibits, if any.

(2) Such deposition transcript is admissible to the same extent that testimony would have been admissible had that person testified at the hearing, provided that if a witness refused to answer proper questions during the deposition, the administrative law judge may, on that basis, limit the admissibility of the deposition in any manner that justice requires.

(3) Only those portions of a deposition received in evidence at the hearing constitute a part of the record.

§ 747.37 Post-hearing Filings.

(a) *Proposed findings and conclusions and supporting briefs.* (1) Using the same method of service for each party, the administrative law judge shall serve notice upon each party that the certified transcript, together with all hearing exhibits and exhibits introduced but not admitted into evidence at the hearing, has been filed. Any party may file with the administrative law judge proposed findings of fact, proposed conclusions of law, and a proposed order within 30 days following service of this notice by the administrative law judge or within such longer period as may be ordered by the administrative law judge.

(2) Proposed findings and conclusions must be supported by citation to any relevant authorities and by page references to any relevant portions of the record. A post-hearing brief may be filed in support of proposed findings and conclusions, either as part of the same document or in a separate document. Any party who fails to file timely with the administrative law judge any proposed finding or conclusion is deemed to have waived the right to raise in any subsequent filing or submission any issue not addressed in such party's proposed finding or conclusion.

(b) *Reply briefs.* Reply briefs may be filed within 15 days after the date on which the parties' proposed findings, conclusions, and order are due. Reply briefs must be strictly limited to responding to new matters, issues, or arguments raised in another party's papers. A party who has not filed proposed findings of fact and conclusions of law or a post-hearing brief may not file a reply brief.

(c) *Simultaneous filing required.* The administrative law judge shall not order the filing by any party of any brief or reply brief in advance of the other party's filing of its brief.

§ 747.38 Recommended Decision and Filing of Record.

(a) *Filing of recommended decision and record.* Within 45 days after expiration of the time allowed for filing reply briefs under § 747.37(b), the administrative law judge shall file with and certify to the NCUA Board, for decision, the record of the proceeding. The record must include the administrative law judge's recommended decision, recommended findings of fact, recommended conclusions of law, and proposed order; all prehearing and hearing transcripts, exhibits, and rulings; and the motions, briefs, memoranda, and other supporting papers filed in connection with the hearing. The administrative law judge shall serve upon each party the recommended decision, findings, conclusions, and proposed order.

(b) *Filing of index.* At the same time the administrative law judge files with and certifies to the NCUA Board for final determination the record of the proceeding, the administrative law judge shall furnish to the NCUA Board a certified index of the entire record of the proceeding. The certified index shall include, at a minimum, an entry for each paper, document or motion filed with the ad-

ministrative law judge in the proceeding, the date of the filing, and the identity of the filer. The certified index shall also include an exhibit index containing, at a minimum, an entry consisting of exhibit number and title or description for: Each exhibit introduced and admitted into evidence at the hearing; each exhibit introduced but not admitted into evidence at the hearing; each exhibit introduced and admitted into evidence after the completion of the hearing; and each exhibit introduced but not admitted into evidence after the completion of the hearing.

§ 747.39 Exceptions to Recommended Decision.

(a) *Filing exceptions.* Within 30 days after service of the recommended decision, findings, conclusions, and proposed order under § 747.38, a party may file with the NCUA Board written exceptions to the administrative law judge's recommended decision, findings, conclusions or proposed order, to the admission or exclusion of evidence, or to the failure of the administrative law judge to make a ruling proposed by a party. A supporting brief may be filed at the time the exceptions are filed, either as part of the same document or in a separate document.

(b) *Effect of failure to file or raise exceptions.* (1) Failure of a party to file exceptions to those matters specified in paragraph (a) of this Section within the time prescribed is deemed a waiver of objection thereto.

(2) No exception need be considered by the NCUA Board if the party taking exception had an opportunity to raise the same objection, issue, or argument before the administrative law judge and failed to do so.

(c) *Contents.* (1) All exceptions and briefs in support of such exceptions must be confined to the particular matters in, or omissions from, the administrative law judge's recommendations to which that party takes exception.

(2) All exceptions and briefs in support of exceptions must set forth page or paragraph references to the specific parts of the administrative law judge's recommendations to which exception is taken, the page or paragraph references to those portions of the record relied upon to support each exception, and the legal authority relied upon to support each exception.

§ 747.40 Review by the NCUA Board.

(a) *Notice of submission to NCUA Board.* When the NCUA Board determines that the record in the proceeding is complete, the NCUA Board shall serve notice upon the parties that the proceeding has been submitted to the NCUA Board for final decision.

(b) *Oral argument before NCUA Board.* Upon the initiative of the NCUA Board or on the written request of any party filed with the NCUA Board within the time for filing exceptions, the NCUA Board may order and hear oral argument on the recommended findings, conclusions, decision, and order of the administrative law judge. A written request by a party must show good cause for oral argument and state reasons why arguments cannot be presented adequately in writing. A denial of a request for oral argument may be set forth in the NCUA Board's final decision. Oral argument before the NCUA Board must be on the record.

(c) *Final Decision of NCUA Board.* (1) Decisional employees may advise and assist the NCUA Board in the consideration and disposition of the case. The final decision of the NCUA Board will be based upon review of the entire record of the proceeding, except that the NCUA Board may limit the issues to be reviewed to those findings and conclusions to which opposing arguments or exceptions have been filed by the parties.

(2) The NCUA Board shall render a final decision within 90 days after notification of the parties that the case has been submitted for final decision, or 90 days after oral argument, whichever is later, unless the NCUA Board orders that the action or any aspect thereof be remanded to the administrative law judge for further proceedings. Copies of the final decision and order of the NCUA Board shall be served upon each party to the proceeding, upon other persons required by statute, and, if directed by the NCUA Board or required by statute, upon any appropriate state or Federal supervisory authority.

§ 747.41 Stays Pending Judicial Review.

The commencement of proceedings for judicial review of a final decision and order of the NCUA Board may not, unless specifically ordered by the NCUA Board or a reviewing court, operate as a stay of any order issued by the NCUA Board. The NCUA Board may, in its discretion, and on such terms as it finds just, stay the effectiveness of all or any part of its order pending a final decision on a petition for review of that order.

Subpart B—Local Rules of Practice and Procedure

§ 747.100 Discovery Limitations.

(a) Parties to a proceeding set forth either at § 747.1 of Subpart A or in Subparts C, E or G of this Part may obtain discovery only through the production of documents. No other form of discovery shall be allowed.

(b) In the event that a person producing documents pursuant to a document subpoena is permitted to be deposed, all questioning shall be strictly limited to the identification of documents produced by that person and a reasonable examination to determine whether the subpoenaed person made an adequate search for, and has produced, all subpoenaed documents.

Subpart C—Local Rules and Procedures Applicable to Proceedings for the Involuntary Termination of Insured Status

§ 747.201 Scope.

Under the authority of Section 206(b) of the Act (12 U.S.C. § 1786(b)), the NCUA Board may terminate the insured status of an insured credit union upon the grounds set forth therein and enumerated in § 747.202. The procedure for terminating the insured status of an insured credit union as therein prescribed will be followed and hearings required thereunder will be conducted in accordance with the rules and procedures set forth in this Subpart and Subpart A of this Part. To the extent any rule or procedure of Subpart A is inconsistent with a rule or procedure prescribed in this Subpart C, Subpart C shall control.

§ 747.202 Grounds for Termination of Insurance.

The NCUA Board may institute proceedings to terminate the insured status of an insured credit union whenever it determines that an insured credit union is:

(a) Engaging or has engaged in unsafe or unsound practices in conducting its business;

(b) In an unsafe or unsound condition to continue as an insured credit union; or

(c) Violating or has violated any applicable law, rule, regulation, order, written condition imposed by the NCUA Board in response to any application or request of the credit union, or any written agreement entered into with the NCUA Board.

§ 747.203 Notice of Charges.

(a) Whenever the NCUA Board determines that grounds for termination of insured status exist, it will, for the purpose of securing correction of errant or illegal conditions, serve a Notice of Charges upon the concerned credit union. This Notice will contain a statement describing the unsafe or unsound practices, condition or the relevant violations.

(b) In the case of an insured state-chartered credit union, the NCUA Board shall send a copy of the Notice of Charges to the appropriate state authority, if any, having supervision over the credit union.

§ 747.204 Notice of Intention to Terminate Insured Status.

Unless correction of the practices, condition, or violations set forth in the Notice of Charges is made within 120 days after service of such statement, or within a shorter period of not less than 20 days after such service as the NCUA Board may require in any case where it determines that the insurance risk with respect to such credit union could be unduly jeopardized by further delay or as the appropriate state supervisory authority shall require in the case of an insured state-chartered credit union, the Board, if it determines to proceed further, shall give to the credit union not less than 30 days written notice of its intent to terminate the status of the credit union as an insured credit union. The notice shall contain a statement of the facts constituting the alleged unsafe or unsound practices or condition or violations on which a hearing will be held. Such hearing shall commence not earlier than 30 days nor later than 60 days after the date of service of such notice

upon the credit union, unless an earlier or later date is set by the NCUA Board at the request of the credit union.

§ 747.205 Order Terminating Insured Status.

If, upon the record of the hearing held pursuant to § 747.204, the NCUA Board finds that any unsafe or unsound practice or condition or violation specified in the notice has been established and has not been corrected within the time prescribed under § 747.204, the NCUA Board may issue and serve upon the credit union an order terminating its status as an insured credit union on a date subsequent to the date of such finding and subsequent to the expiration of the time specified in the notice.

§ 747.206 Consent to Termination of Insured Status.

Unless the credit union appears at the hearing designated in the notice of hearing by a duly authorized representative, it will be deemed to have consented to the termination of its status as an insured credit union. In the event the credit union fails to so appear at such hearing, the administrative law judge shall forthwith report the matter to the NCUA Board and the NCUA Board may thereupon issue an order terminating the credit union's insured status.

§ 747.207 Notice of Termination of Insured Status.

Prior to the effective date of the termination of the insured status of an insured credit union under Section 206(b) of the Act (12 U.S.C. § 1786(b)) and at such time as the Board shall specify, the credit union shall mail to each member at his or her last address of record on the books of the credit union, and publish in not less than two issues of a local newspaper of general circulation, notices of the termination of its insured status, and the credit union shall furnish the NCUA Board with proof of publication of such notice. The notice shall be as follows:

NOTICE

(Date)

1. The status of the _____ as an insured credit union under the provision of the Federal Credit Union Act, will terminate as of the close of business on the _____ day of _____ ;

2. Any deposits made by you after that date, either new deposits or additions to existing accounts, will not be insured by the National Credit Union Administration;

3. Accounts in the credit union on the _____ day of _____ , _____ , up to a maximum of $100,000 for each member, will continue to be insured, as provided by the Federal Credit Union Act, for one (1) year after the close of business on the _____ day of _____ , _____ ; Provided, however, that any withdrawals after the close of business on the _____ day of _____ , _____ , will reduce the insurance coverage by the amount of such withdrawals.

(Name of Credit Union)

(Address)

§ 747.208 Duties after Termination.

(a) After the termination of the insured status of any credit union under Section 206(b) of the Act (12 U.S.C. § 1786(b)), insurance of its member accounts to the extent they were insured on the effective date of such termination, less any amounts thereafter withdrawn which reduce the accounts below the amount covered by insurance on the effective date of such termination, shall continue for a period of one year, but no shares issued by the credit union or deposits made after

the date of such termination shall be insured by the NCUA Board.

(b) The credit union shall continue to pay premiums to the NCUA Board during such period and the Board shall have the right to examine the credit union from time to time during the period. The credit union shall, in all other respects, be subject to the duties and obligations of an insured credit union during the one year period. If the credit union is closed for liquidation within this period, the Board shall have the same powers and rights with respect to such credit union as in the case of an insured credit union.

Subpart D—Local Rules and Procedures Applicable to Suspensions and Prohibitions Where Felony Charged

§ 747.301 Scope.

The rules and procedures set forth in this Subpart are applicable to informal proceedings conducted by the NCUA Board, or a Presiding Officer designated by the Board, pursuant to Section 206(i) of the Act (12 U.S.C. § 1786(i)), to suspend, remove and/or prohibit from office or from further participation any institution-affiliated party of an insured credit union who:

(a) is charged in a state, Federal or territorial information or indictment or complaint with committing or participating in a crime involving dishonesty or breach of trust, which crime is punishable by imprisonment for a term exceeding one year under state or Federal law; or

(b) enters a pretrial diversion or other similar program as result of being charged in such information or indictment or complaint with participating or committing such crime; or

(c) is convicted of such crime.

Subpart A of this Part does not apply to proceedings under this Subpart.

§ 747.302 Rules of Practice; Remainder of Board of Directors.

Except as otherwise specifically provided in this Subpart, the following provisions shall apply to proceedings conducted under this Subpart:

(a)(1) *Power of attorney and notice of appearance.* Any person who is a member in good standing of the bar of the highest court of any state, possession, territory, commonwealth, or the District of Columbia may represent others before the NCUA Board or Presiding Officer designated by the NCUA Board upon filing with the NCUA Board a written declaration that he or she is currently qualified as provided by this paragraph, and is authorized to represent the particular party on whose behalf he acts. Any other person desiring to appear before or transact business with the NCUA Board in a representative capacity may be required to file with the NCUA Board a power of attorney showing his or her authority to act in such capacity, and he or she may be required to show to the satisfaction of the NCUA Board that he or she has the requisite qualifications. Attorneys and representatives of parties to proceedings shall file a written notice of appearance with the NCUA Board or with the Presiding Officer designated by the NCUA Board.

(2) *Summary suspension.* Contemptuous conduct by any person at an argument before the NCUA Board or at the hearing before a Presiding Officer shall be grounds for exclusion therefrom and suspension for the duration of the argument or hearing.

(b)(1) *Notice of hearing.* Whenever a hearing within the scope of this Subpart is ordered by the NCUA Board, a notice of hearing shall be given by the NCUA Board to the party afforded the hearing and to any appropriate state supervisory authority. The notice shall state the time, place, and nature of the hearing and the legal authority and jurisdiction under which the hearing is to be held, and shall contain a statement of the matters of fact or law constituting the grounds for the hearing. It shall be delivered by personal service, by registered or certified mail to the last known address, or by other appropriate means, not later than 30 nor earlier than 60 days before the hearing.

(2) *Party.* The term "party" means a person or agency named or admitted as a party, or any person or agency who has filed a written request and is entitled as of right to be admitted as a party; but a person or agency may be admitted for a limited purpose.

(c)(1) *Computation of time.* In computing any period of time prescribed or allowed by this Subpart, the date of the act, event or default from which the designated period of time begins to run is not to be included. The last day so computed shall be included, unless it is a Saturday, Sunday or legal holiday in the District of Columbia, in which event the period shall run until the end of the next day which is neither a Saturday, Sunday, nor such legal holiday. Intermediate Saturdays, Sundays, and legal holidays shall be in-

cluded in the computation unless the time within which the act is to be performed is ten days or less in which event Saturdays, Sundays, and legal holidays shall not be included.

(2) *Service by mail.* Whenever any party has the right or is required to do some act or take some proceeding, within a period of time prescribed in this Subpart, after the service upon him of any document or other paper of any kind, and such service is made by mail, three days shall be added to the prescribed period from the date when the matter served is deposited in the U.S. mail.

(d) *Nonpublication of submissions.* Unless and until otherwise ordered by the NCUA Board, the notice of hearing, the transcript, written materials submitted during the hearing, the Presiding Officer's recommendation to the NCUA Board and any other papers filed in connection with a hearing under this Subpart, shall not be made public, and shall be for the confidential use only of the NCUA Board, the Presiding Officer, the parties and appropriate authorities.

(e) *Remainder of board of directors.* (1) If at any time, because of the suspension of one or more directors pursuant to this Subpart, there shall be on the board of directors of an insured credit union less than a quorum of directors not so suspended, all powers and functions vested in or exercisable by such board shall vest in and be exercisable by the director or directors on the board not so suspended, until such time as there shall be a quorum on the board of directors.

(2) In the event all of the directors of an insured credit union are suspended pursuant to this Subpart, the NCUA Board shall appoint persons to serve temporarily as directors in their place pending the termination of such suspensions, or until such time as those who have been suspended cease to be directors of the credit union and their respective successors have been elected by the members at an annual or special meeting and have taken office.

(3) Directors appointed temporarily by the NCUA Board pursuant to paragraph (e)(2) of this section, shall, within 30 days following their appointment, call a special meeting for the elec tion of new directors, unless during such 30-day period—

(i) the regular annual meeting is convened; or

(ii) the suspensions giving rise to the appointment of temporary directors are terminated.

§ 747.303 Notice of Suspension or Prohibition.

Whenever an institution-affiliated party of an insured credit union is charged in any state, Federal or territorial information or indictment or complaint with the commission of or participation in a crime involving dishonesty or breach of trust, which crime is punishable by imprisonment for a term exceeding one year under state or Federal law, the NCUA Board may, if continued service or participation by the concerned party may pose a threat to the interests of the credit union's members or may threaten to impair public confidence in the credit union, by written notice served upon such party, suspend him or her from office, or prohibit him or her from further participation in any manner in the affairs of the credit union, or both. A copy of the notice of suspension or prohibition shall also be served upon the credit union. This suspension or prohibition shall remain in effect until such information, indictment, or complaint is finally disposed of, or until such suspension or prohibition is terminated by the NCUA Board.

§ 747.304 Removal or Permanent Prohibition.

In the event that a judgment of conviction or an agreement to enter a pretrial diversion or other similar program is entered against the institution-affiliated party, and at such time as the judgment, if any, is not subject to further appellate review, the NCUA Board may, if continued service or participation by such party may pose a threat to the interests of the credit union's members or may threaten to impair public confidence in the credit union, issue and serve upon the individual an order removing him or her from office or prohibiting him or her from further participation in any manner in the conduct of the affairs of the credit union except with the consent of the NCUA Board. A copy of such order will also be served upon such credit union. A finding of not guilty or other disposition of the charge will not preclude the NCUA Board from thereafter instituting proceedings, pursuant to the provisions of Section 206(g) of the Act (12 U.S.C. 1786(g)) and Subpart A of this Part, to remove such director, committee member, officer, or other person from office or to prohibit his

or her further participation in the affairs of the credit union.

§ 747.305 Effectiveness of Suspension or Removal until Completion of Hearing.

Any notice of suspension or prohibition issued under § 747.303 and any order of removal or prohibition issued under § 747.304 will be effective upon service on the concerned party and will remain effective and outstanding until the completion of any hearing or appeal authorized under Section 206(i) of the Act (12 U.S.C. § 1786(i)) and this Subpart, unless such notice of suspension or order of removal is terminated by the NCUA Board.

§ 747.306 Notice of Opportunity for Hearing.

(a) Any notice of suspension or prohibition issued pursuant to § 747.303, and any order of removal or prohibition issued pursuant to § 747.404, shall be accompanied by a further notice to the concerned individual that he or she may, within 30 days of service of such notice, request in writing an informal hearing at which he or she may present evidence and argument that his or her continued service to or participation in the conduct of the affairs of the credit union does not, or is not likely to, pose a threat to the interests of the credit union's members or threaten to impair confidence in the credit union. Any notice of the opportunity for such a hearing shall be accompanied by a description of the hearing procedure and the criteria to be considered.

(b) A request for a hearing filed pursuant to paragraph (a) of this Section shall state with particularity the relief desired, the grounds therefor, and shall include, when available, supporting evidence. The request and supporting evidence shall be filed in writing with the Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

§ 747.307 Hearing.

(a) Upon receipt of a request for a hearing which complies with § 747.306, the NCUA Board will order an informal hearing to commence within the following 30 days in Washington, D.C. metropolitan area, or at such other place as the NCUA Board designates, before a Presiding Officer designated by the NCUA Board to conduct the hearing. At the request of the concerned party, the NCUA Board may order the hearing to commence at a time more than 30 days after the receipt of the request for such hearing.

(b) The notice of hearing shall be served by the NCUA Board upon the party or parties afforded the hearing and shall set forth the time and place of the hearing and the name and address of the Presiding Officer.

(c) The subject individual may appear at the hearing personally, through counsel, or personally with counsel. The individual shall have the right to introduce relevant and material written materials (or, at the discretion of the NCUA Board, oral testimony), and to present an oral argument before the Presiding Officer. A member of the enforcement staff of the Office of General Counsel of the NCUA may attend the hearing and may participate as a party. Neither the formal rules of evidence nor the adjudicative procedures of the Administrative Procedure Act (5 U.S.C. 554–557), nor Subpart A of this Part shall apply to the hearing. The proceedings shall be recorded and a transcript furnished to the individual upon request and after the payment of the cost thereof. The NCUA Board shall have the discretion to permit the presentation of witnesses, within specified time limits, so long as a list of such witnesses is furnished to the Presiding Officer at least ten days prior to the hearing. Witnesses shall not be sworn, unless specifically requested by either party or directed by the Presiding Officer. The Presiding Officer may examine any witness and each party shall have the opportunity to cross-examine any witness presented by an opposing party. Upon the request of either the subject individual or the representative of the Office of General Counsel, the record shall remain open for a period of five business days following the hearing, during which time the parties may make any additional submissions to the record. Thereafter, the record shall be closed.

(d) In the course of or in connection with any proceeding under this Subpart, the NCUA Board and the Presiding Officer will have the power to administer oaths and affirmations, to take or cause depositions to be taken, and to issue, revoke, quash, or modify subpoenas and subpoenas duces tecum. If the NCUA Board permits the presentation of witnesses, the NCUA Board or the Presiding Officer may require the attendance of witnesses from any place in any state or in any territory or other place subject to the jurisdiction of the United States at any designated place where

such proceeding is being conducted. Witnesses subpoenaed shall be paid the same fees and mileage as are paid witnesses in the District Courts of the United States. The NCUA Board or the Presiding Officer may require the production of documents from any place in any such state, territory, or other place.

(e) The Presiding Officer will make his or her recommendations to the Board, where possible, within ten business days following the close of the record.

§ 747.308 Waiver of Hearing; Failure to Request Hearing or Review Based on Written Submissions; Failure to Appear.

(a) The subject individual may, in writing, waive an oral hearing and instead elect to have the matter determined by the NCUA Board on the basis of written submissions alone.

(b) Should any concerned party fail to request in writing an oral hearing or consideration based on written submissions alone within 30 days of service of the notice described in § 747.306, he or she will be deemed to have consented to the NCUA Board's action.

(c) Unless the concerned party appears at the hearing personally or by duly appointed representative, he or she will be deemed to have consented to the NCUA Board's action.

§ 747.309 Decision of the NCUA Board.

Within 60 days following the hearing, or receipt of the subject individual's written submissions where hearing has been waived pursuant to § 747.308, the NCUA Board shall notify the institution-affiliated party whether the suspension or prohibition will be continued, terminated, or otherwise modified, or whether the order of removal or prohibition will be rescinded or otherwise modified. Such notification shall contain a statement of the basis for the decision of the NCUA Board, if that decision is adverse to the respondent party. In the case of a decision favorable to the respondent on the subject of a prior order of removal or prohibition, the NCUA Board shall take prompt action to rescind or otherwise modify the order of removal or prohibition.

§ 747.310 Reconsideration by the NCUA Board.

(a) The subject individual shall have ten business days following receipt of the decision of the NCUA Board in which to petition the NCUA Board for initial reconsideration.

(b) The subject individual also shall be entitled to petition the NCUA Board for reconsideration of its decision any time after the expiration of a 12-month period from the date of the NCUA Board's decision, but no petition for reconsideration may be made within 12 months of a previous petition.

(c) Any petition shall state with particularity the basis for reconsideration, the relief sought, and any exceptions the individual has to the NCUA Board's findings. An individual's petition may be accompanied by a memorandum of points and authorities in support of his or her petition and any supporting documentation the individual may wish to have considered.

(d) No hearing need be granted on such petition for reconsideration. Promptly following receipt of the petition, the Board shall render its decision.

§ 747.311 Relevant Considerations.

In deciding the question of suspension, prohibition, or removal under this Subpart, the NCUA Board will consider the following:

(a) Whether the alleged offense is a crime which is punishable by imprisonment for a term exceeding one year under state or Federal law, and which involves dishonesty or breach of trust;

(b) Whether the continued presence of the subject individual in his or her position may pose a threat to the interests of the credit union's members because of the nature and extent of the individual's participation in the affairs of the insured credit union and/or the nature of the offense with the commission of or participation in which the individual has been charged;

(c) Whether there is cause to believe that there may be an erosion of public confidence in the integrity, safety, or soundness of a particular credit union (either generally or in the particular locality in which the credit union is situated) if the subject individual is permitted to remain in his or her position in an insured credit union;

(d) Whether the individual is covered by the credit union's fidelity bond and, if so, whether the bond is likely to be revoked, or whether coverage under the bond will be affected adversely as a result of the information, indictment, complaint, judgment of conviction or entry into a pretrial diversion or other similar program; and

(e) The NCUA Board may consider any other factors which, in the specific case, appear relevant to the decision to continue in effect, rescind, terminate, or modify a suspension, prohibition, or removal order, except that it shall not consider the ultimate question of the guilt or innocence of the subject individual with regard to the crime with which he or she has been charged.

Subpart E—Local Rules and Procedures Applicable to Proceedings Relating to the Suspension or Revocation of Charters and to Involuntary Liquidations

§ 747.401 Scope.

The rules and procedures set forth in this subpart and Subpart A of this part are applicable to proceedings by the NCUA Board pursuant to section 120(b)(1) of the Act (12 U.S.C. § 1766(b)(1)) to suspend or revoke the charter of a solvent Federal credit union, and to place a solvent Federal credit union into involuntary liquidation. To the extent a rule or procedure set forth in Subpart A of this Part is inconsistent with a rule or procedure set forth in this Subpart E, Subpart E shall control.

§ 747.402 Grounds for Suspension or Revocation of Charter and for Involuntary Liquidation.

(a) *Grounds in general.* The NCUA Board may suspend or revoke the charter of any Federal credit union, and place such credit union into involuntary liquidation and appoint a liquidating agent therefor, upon its finding that the credit union has violated any provision of its charter or bylaws or of the Act or regulations issued thereunder.

(b) *Immediate suspension.* In any case where the Board determines that the grounds set forth in paragraph (a) of this section exist and that immediate action is necessary in order to prevent further dissipation of credit union assets or earnings, or further weakening of the credit union's condition, or to otherwise protect the interest of the credit union's insured members or the National Credit Union Share Insurance Fund, it may order without prior notice the immediate suspension of the charter of such credit union, and if the circumstances so warrant, may take possession of all books, records, assets, and property of every description of such credit union.

§ 747.403 Notice of Intent to Suspend or Revoke Charter; Notice of Suspension.

(a) Upon its determination that one or more of the grounds listed in § 747.402(a) exists, or that because of conditions described in § 747.402(b) immediate suspension of charter is necessary, the NCUA Board shall cause to be served upon that credit union a notice of intent to suspend or revoke charter and of intent to place into involuntary liquidation, or a notice of suspension. Such notice shall contain a statement of the facts which constitute the grounds for the action, a recitation of the options available to the credit union under paragraph (b) of this section, and an explanation of the results that will occur if the credit union fails to exercise said options.

(b) Not later than 40 days after the receipt of the notice provided for in paragraph (a) of this section, the Federal credit union may file with the NCUA Board a statement in writing setting forth the grounds and reasons why its charter should not be suspended or revoked and why it should not be placed into involuntary liquidation; or in lieu of a written statement, request an oral hearing which shall be conducted in accordance with the procedures set forth in this subpart. This statement or request shall be accompanied by a certified copy of a resolution of the board of directors of the Federal credit union concerned authorizing such statement or request, such certification to be made by the president and secretary of the board of directors.

(c) If the Federal credit union concerned does not exercise either alternative available in paragraph (b) of this section within the time required, it shall be deemed to have admitted the facts alleged in the notice and may be deemed to have consented to the relief sought.

§ 747.404 Notice of Hearing.

(a) Upon receipt of a request for hearing which complies with § 747.403(b), the NCUA Board shall transmit the request to the Office of Financial Institution Adjudication ("OFIA"). Such hearing shall commence no earlier than 30 days nor later than 60 days after the date the OFIA receives the request for a hearing, unless an earlier or later date is requested by the Federal credit union concerned and is granted by the NCUA Board in its discretion.

(b) Except as provided in § 747.405(b), the procedures of the Administrative Procedure Act (5 U.S.C. §§ 554–557) and Subpart A of this Part will apply to the hearing.

(c) Unless the Federal credit union shall appear at such hearing by a duly authorized representative, it shall be deemed to have consented to the suspension or revocation of its charter and to the placing of said credit union into involuntary liquidation.

§ 747.405 Issuance of Order.

(a) In the event of such consent as referred to in §§ 747.403(c) or 747.404(c), or if upon the record made at any such hearing as referred to in § 747.403(b), the NCUA Board finds that the charter of the Federal credit union concerned should be suspended or revoked and the credit union closed and placed into involuntary liquidation, it shall cause to be served on such credit union an order directing the suspension or revocation of its charter and directing that it be closed and placed into involuntary liquidation. Such order shall contain a statement of the findings upon which the order is based. Additionally, the NCUA Board shall appoint a liquidating agent or agents.

(b) The NCUA Board shall render its decision and cause such order to be served not later than 45 days after receipt either of consent or of written submissions, as the case may be, or in the case of a formal hearing, after service or the notice of submission referred to in § 747.40(a).

(c) Upon the receipt of a copy of the order which provides that the Federal credit union concerned be placed into involuntary liquidation, the officers and directors of that Federal credit union shall immediately deliver to the agent for the liquidating agent possession and control of all books, records, assets, and property of every description of the Federal credit union, and the agent for the liquidating agent shall proceed to convert said assets to cash, collect all debts due to said Federal credit union and to wind up its affairs in accordance with the provisions of the Act.

§ 747.406 Cancellation of Charter.

Upon the completion of the liquidation and certification by the agent for the liquidating agent that the distribution of the assets of the Federal credit union has been completed, the NCUA Board shall cancel the charter of the Federal credit union concerned.

Subpart F—Local Rules and Procedures Applicable to Proceedings Relating to the Termination of Membership in the Central Liquidity Facility [RESERVED]

Subpart G—Local Rules and Procedures Applicable to Recovery of Attorneys Fees and Other Expenses Under the Equal Access to Justice Act in NCUA Board Adjudications

§ 747.601 Purpose and Scope.

This Subpart contains the regulations of the NCUA implementing the Equal Access to Justice Act (5 U.S.C. § 504), as amended ("EAJA"). The EAJA provides for the award of attorneys fees and other expenses to eligible individuals and entities who are parties to proceedings conducted under this part. An eligible party may receive an award when it prevails over NCUA in a proceeding, or in a significant and discrete substantive portion of the proceeding, unless the position of the NCUA was substantially justified or special circumstances make an award unjust. The rules in this subpart describe the parties eligible for fee awards, explain how to apply for awards and the procedures and standards that NCUA will use to make them. To the extent a rule or procedure set forth in Subpart A of this part is inconsistent with a rule or procedure set forth in this Subpart G, Subpart G will control.

§ 747.602 Eligibility of Applicants.

(a) To be eligible for an award of attorneys fees and expenses, an applicant must be a prevailing party in the proceeding for which it seeks an award and must be:

(1) An individual with a net worth of not more than $2 million;

(2) The sole owner of an unincorporated business who has a net worth of not more than $7 million, including both personal and business interests and not more than 500 employees at the time the proceeding was commenced (an applicant who owns an unincorporated business will be considered as an "individual" rather than a "sole owner of an unincorporated business" if the issues on which the applicant prevails are related primarily to personal interests rather than to business interests);

(3) A charitable or other tax-exempt organization described in Section 501(c)(3) of the Internal Revenue Code (26 U.S.C. § 501(c)(3)) with not more than 500 employees;

(4) A cooperative association as defined in section 15(a) of the Agricultural Marketing Act (12 U.S.C. § 1141j(a)) with not more than 500 employees; or

(5) Any other partnership, corporation, association, or public or private organization with a net worth of not more than $7 million and not more than 500 employees.

(b) For the purpose of determining eligibility, the net worth of an applicant and the number of employees of an applicant shall be determined as of the date the proceeding was initiated.

(c) The applicant's net worth includes the value of any assets disposed of for the purpose of meeting an eligibility standard and excludes any obligations incurred for this purpose. Transfers of assets or obligations incurred for less than reasonably equivalent value will be presumed to have been made for this purpose.

(d) The employees of an applicant include all persons who regularly perform services for remuneration for the applicant, under the applicant's direction and control; part-time employees shall be included on a proportional basis.

(e) The net worth and number of employees of the applicant and all of its affiliates shall be aggregated to determine eligibility. Any individual, corporation or other entity that directly or indirectly controls or owns a majority of the voting shares or other interest of the applicant, or any corporation or other entity of which the applicant directly or indirectly owns or controls a majority of the voting shares or other interest, will be considered an affiliate for purposes of this subpart, unless the NCUA Board determines that such treatment would be unjust and contrary to the purposes of the EAJA in light of the actual relationship between the affiliated entities. In addition, the NCUA Board may determine that financial relationships of the applicant other than those described in this paragraph constitute special circumstances that would make an award unjust.

(f) An applicant that participates in a proceeding primarily on behalf of one or more other persons or entities that would be ineligible is not itself eligible for an award.

§ 747.603 Prevailing Party.

An eligible applicant may be a "prevailing party" if the applicant wins an action after a full hearing or trial on the merits, if a settlement of the proceeding was effected on terms favorable to it, or if the proceeding against it has been dismissed. In appropriate situations an applicant may also have prevailed if the outcome of the proceeding has substantially vindicated the applicant's position on the significant, substantive matters at issue, even though the applicant has not totally avoided adverse final action.

§ 747.604 Standards for Award.

(a) A prevailing party may receive an award for fees and expenses incurred in connection with a proceeding, or in a significant and discrete substantive portion of the proceeding, by or against NCUA unless the position of NCUA during the proceeding was substantially justified. The burden of proving that an award should not be made is on counsel for NCUA. To avoid an award, counsel for NCUA must show that its position was reasonable in law and in fact.

(b) An award will be reduced or denied if the applicant has unduly or unreasonably protracted the proceeding or if special circumstances make the award sought unjust.

(c) Where an applicant has prevailed on one or more discrete substantive issues in a proceeding, even though all the issues were not resolved in its favor, any award shall be based on the fees and expenses incurred in connection with the discrete significant, substantive issue or issues on which the applicant's position has been upheld. If such segregation of costs is not practicable, the

award may be based on a fair proration of those fees and expenses incurred in the entire proceeding which would be recoverable under this section if proration were not performed.

(d) Whether separate or prorated treatment under the preceding paragraph, including the applicable proration percentage, is appropriate shall be determined on the facts of the particular case. Attention shall be given to the significance and nature of the respective issues and their separability and interrelationship.

§ 747.605 Allowable Fees and Expenses.

(a) Except as provided by § 747.604(b), awards will be based on rates customarily charged by persons engaged in the business of acting as attorneys, agents and expert witnesses, even if the services were made available without charge or at a reduced rate.

(b) No award under this subpart for the fee of an attorney or agent may exceed $75.00 per hour. No award to compensate an expert witness may exceed the highest rate at which NCUA is permitted to pay expert witnesses. However, an award may also include the reasonable expenses of the attorney, agent or witness as a separate item, if the attorney, agent or witness ordinarily charges clients separately for such expenses.

(c) In determining the reasonableness of the fee sought for an attorney, agent, or expert witness, the NCUA Board shall consider the following:

(1) If the attorney, agent, or expert witness is in private practice, his or her customary fee for like services, or, if he or she is an employee of the applicant, the fully allocated cost of the services;

(2) The prevailing rate for similar services in the community in which the attorney, agent, or expert witness ordinarily performs services;

(3) The time actually spent in the representation of the applicant; and

(4) Such other factors as may bear on the value of the services provided.

(d) The reasonable cost of any study, analysis, report, test, project, or similar matter prepared on behalf of the party may be awarded to the extent that the charge for the service does not exceed the prevailing rate for similar services, and the study or other matter was necessary for preparation of the applicant's case.

§ 747.606 Contents of Application.

(a) A prevailing eligible party, as defined in §§ 747.602, 747.603, and 747.604, seeking an award under this section, must file an application for an award of fees and expenses with the Secretary of the NCUA Board. The application shall include the following information:

(1) The identity of the applicant and the proceeding for which an award is sought;

(2) A showing that the applicant has prevailed and an identification of the issues in the proceeding on which the applicant believes that the position of NCUA was not substantially justified;

(3) A statement, with supporting documentation, that the applicant is an eligible party, as defined by § 747.602. If the applicant is an individual, he or she must state that his or her net worth does not exceed $2 million. If the applicant is not an individual, it shall state the number of its employees and that its net worth does not exceed $7 million as of the date the proceeding was initiated. However, an applicant may omit a statement of net worth if:

(i) It attaches a copy of a ruling by the Internal Revenue Service that it qualifies as an organization described in Section 501(c)(3) of the Internal Revenue Code (26 U.S.C. § 501(c)(3)) or, in the case of a tax-exempt organization not required to obtain a ruling from the Internal Revenue Service on its exempt status, a statement that describes the basis for the applicant's belief that it qualifies under such section; or

(ii) It states that it is a cooperative association as defined in section 15(a) of the Agricultural Marketing Act (12 U.S.C. § 1141j(a)).

(4) A statement of the amount of fees and expenses for which an award is sought; and

(5) Any other matters that the applicant believes may assist or wishes the NCUA Board to consider in determining whether and in what amount an award should be made.

(b) The application shall be signed by the applicant or an authorized officer or attorney of the applicant. It shall also contain or be accompanied by a written verification under oath or under penalty of perjury that the information provided in the application is true and correct.

(c) The application and documentation requirements of this subpart are required by law as a

prerequisite to obtaining a benefit under the Equal Access to Justice Act and this subpart.

§ 747.607 Statement of Net Worth.

(a) Each applicant (other than a qualified tax-exempt organization or cooperative association) must provide a detailed statement showing the net worth of the applicant and any affiliates, as defined in § 747.602(a), when the proceeding was initiated. The exhibit may be in any form convenient to the applicant that provides full disclosure of the applicant's and its affiliates' assets and liabilities and is sufficient to determine whether the applicant is an eligible party. The administrative law judge or the NCUA Board may require additional information from the applicant to determine eligibility. Unless otherwise ordered by the Board or required by law, the statement shall be kept confidential and used by the NCUA Board only in making its determination of an award.

(b) If the applicant or any of its affiliates is a Federal credit union, the portion of the statement of net worth which relates to the Federal credit union shall consist of a copy of the Federal credit union's last Statement of Financial Condition filed before the initiation of the underlying proceeding.

(c) All statements of net worth shall describe any transfers of assets from or obligations incurred by the applicant or any affiliate, occurring in the six-month period prior to the date on which the proceeding was initiated, which reduced the net worth of the applicant and its affiliates below the applicable net worth ceiling. If there were none, the applicant shall so state.

§ 747.608 Documentation of Fees and Expenses.

The application shall be accompanied by full documentation of the fees and expenses, including the cost of any study, analysis, audit, test, project or similar matter, for which an award is sought. A separate, itemized statement shall be submitted for each professional firm or individual whose services are covered by the application, showing hours spent in connection with the proceeding by each individual, a description of the specific services performed, the rate at which each fee has been computed, any expenses for which reimbursement is sought, the total amount claimed, and the total amount paid or payable by the applicant or by any other person or entity for the services provided. The administrative law judge or the NCUA Board may require the applicant to provide vouchers, receipts, or other substantiation for any expenses claimed.

§ 747.609 Filing and Service of Applications.

(a) An application may be filed whenever the applicant has prevailed in the proceeding or in a significant and discrete substantive portion of the proceeding, but in no case later than 30 days after the Board's final disposition of the proceeding.

(b) If review or reconsideration is sought or taken of a decision on which an applicant believes it has prevailed, proceedings for the award of fees shall be stayed pending final disposition of the underlying controversy.

(c) As used in this subpart, final disposition means the issuance of a final order or any other final resolution of a proceeding, such as a settlement or voluntary dismissal.

(d) Any application for an award of fees and expenses shall be filed with the Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428. Any application for an award and any other pleading or document related to an application, shall be filed and served on all parties to the proceeding in the same manner as other pleadings in the proceeding, except as provided in § 747.607(a) for statements of net worth.

§ 747.610 Answer to Application.

(a) Within 30 days after service of an application, counsel for NCUA may file an answer to the application. Unless counsel for NCUA requests and is granted an extension of time for filing or files a statement of intent to negotiate under paragraph (b) of this section, failure to file an answer within the 30-day period will be treated as a consent to the award requested.

(b) If counsel for NCUA and the applicant believe that the issues in the fee application can be settled, they may jointly file a statement of their intent to negotiate a settlement. The filing of this statement shall extend the time for filing an answer for an additional 30 days, and further extensions may be granted by the NCUA Board upon the joint request of counsel for NCUA and the applicant.

(c) The answer shall explain in detail any objections to the award requested and identify the facts

relied on in support of counsel's position. If the answer is based on any alleged facts not already in the record of the proceeding, counsel shall include with the answer a request for further proceedings under § 747.613.

(d)(1) The applicant may file a reply if counsel for NCUA has addressed in his or her answer any of the following issues:

(i) That the position of NCUA in the proceeding was substantially justified;

(ii) That the applicant unduly protracted the proceedings; or

(iii) That special circumstances make an award unjust.

(2) The reply shall be filed within 15 days after service of the answer. If the reply is based on any alleged facts not already in the record of the proceeding, the applicant shall include with the reply a request for further proceedings under § 747.613.

§ 747.611 Comments by Other Parties.

Any party to a proceeding, other than the applicant and counsel for NCUA, may file comments on an application within 30 days after service of the application or on an answer within 15 days after service of the answer. A commenting party may not participate further in proceedings on the application unless the administrative law judge or the NCUA Board determines that the public interest requires such participation in order to permit full exploration of matters raised in the comments.

§ 747.612 Settlement.

The applicant and counsel for NCUA may agree on a proposed settlement of the award before final action on the application, either in connection with a settlement of the underlying proceeding, or after the underlying proceeding has been concluded, in accordance with NCUA's standard settlement procedure. If a prevailing party and counsel for NCUA agree on a proposed settlement of an award before an application has been filed, the application shall be filed with the proposed settlement.

§ 747.613 Further Proceedings.

(a) After the expiration of the time allowed for the filing of all documents necessary for the determination of a recommended fee award, the NCUA Board shall transmit the entire record to the administrative law judge who presided at the underlying proceeding. Ordinarily, the determination of an award will be made on the basis of the written record. However, on request of either the applicant or counsel for NCUA, or on its own initiative, the administrative law judge or the NCUA Board may order further proceedings, such as an informal conference, oral argument, additional written submissions or an evidentiary hearing. Such further proceedings shall be held only when necessary for full and fair resolution of the issues arising from the application, and shall be conducted as promptly as possible.

(b) A request that the administrative law judge or the NCUA Board order further proceedings under this section shall specifically identify the information sought or the disputed issues and shall explain why the additional proceedings are necessary to resolve the issues.

§ 747.614 Recommended Decision.

The administrative law judge shall file a recommended decision on the application with the NCUA Board within 60 days after completion of the proceedings on the application. The recommended decision shall include written findings and conclusions on the applicant's eligibility and status as a prevailing party, and an explanation of the reasons for any difference between the amount requested and the amount awarded. The recommended decision shall also include, if at issue, findings on whether NCUA's position was substantially justified, whether the applicant unduly protracted the proceedings, or whether special circumstances make an award unjust. If the applicant has sought an award against more than one agency, the recommended decision shall allocate responsibility for payment of any award made among the agencies, and shall explain the reasons for the allocation made. The administrative law judge shall file with and certify to the NCUA Board the record of the proceeding on the fee application, the recommended decision and proposed order. Promptly upon such filing, the NCUA Board shall serve upon each party to the proceeding a copy of the administrative law judge's recommended decision, findings, conclusions and proposed order. The provisions of this section and § 747.613 shall not apply, however, in any case where the hearing was held before the NCUA Board.

§ 747.615 Decision of the NCUA Board.

Within 15 days after service of the recommended decision, findings, conclusions, and proposed order, the applicant or counsel for NCUA may file with the NCUA Board written exceptions thereto. A supporting brief may also be filed. The NCUA Board shall render its decision within 60 days

after the matter is submitted to it. The NCUA Board shall furnish copies of its decision and order to the parties. Judicial review of the NCUA Board's final decision and order may be obtained as provided in 5 U.S.C. § 504(c)(2).

§ 747.616 Payment of Award.

An applicant seeking payment of an award granted by the NCUA Board shall submit to the NCUA's Office of the Controller a copy of the NCUA Board's Final Decision and Order granting the award, accompanied by a statement that it will not seek review of the decision and order in the United States court. All submissions shall be addressed to the Office of the Controller, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428. The NCUA will pay the amount awarded within 60 days after receiving the applicant's statement, unless judicial review of the award or of the underlying decision of the adversary adjudication has been sought by the applicant or any other party to the proceeding.

Subpart H—Local Rules and Procedures Applicable to Investigations

§ 747.701 Applicability.

The rules in this Subpart apply only to informal and formal investigations conducted by the NCUA Board itself or its delegates. They do not apply to adjudicative or rulemaking proceedings or to routine, periodic or special examinations conducted by the NCUA Board's staff.

§ 747.702 Information Obtained in Investigations.

Information and documents obtained by the Board in the course of any investigation, unless made a matter of public record by the NCUA Board, shall be deemed non-public, but the NCUA Board approves the practice whereby the General Counsel may engage in, and may authorize any person acting on his or her behalf or at his or her direction to engage in, discussions with representatives of domestic or foreign governmental authorities, self-regulatory organizations, and with receivers, trustees, masters and special counsels or special agents appointed by and subject to the supervision of the courts of the United States, concerning information obtained in individual investigations, including investigations conducted pursuant to any order entered by the NCUA Board or its General Counsel pursuant to delegated authority.

§ 747.703 Authority to Conduct Investigations.

(a) The General Counsel and persons acting on his or her behalf and at his or her direction may conduct such investigations into the affairs of any insured credit union or institution-affiliated parties as deemed appropriate to determine whether such credit union or party has violated, is violating or is about to violate any provision of the Act, the NCUA Board's regulations or other relevant statutes or regulations that may bear on a party's fitness to participate in the affairs of a credit union. The General Counsel and persons acting on his or her behalf may investigate whether any party is unfit to participate in the affairs of a credit union, whether formal enforcement proceedings are warranted, or such other matters as the General Counsel or his or her designee, in his or her discretion, shall deem appropriate. Such investigations may be conducted either informally or formally.

(b) Formal investigations involve the exercise of the NCUA Board's subpoena power and are referred to here as formal investigative proceedings. In formal investigative proceedings, the General Counsel and those to whom he or she delegates authority to act on his or her behalf and at his or her direction have augmented investigatory powers and need not rely on the powers available to them in informal investigations, and they may gather evidence through the issuance of subpoenas compelling the production of documents or testimony as well. In informal investigations evidence may be gathered ordinarily through the use of investigatory procedures or credit union examinations and through voluntary statements and submissions.

(c) The NCUA Board has delegated authority to the General Counsel, or designee thereof, to institute formal investigative proceedings by the entry of an order indicating the purpose of the investigation and the designation of persons to conduct that investigation on his or her behalf and at his or her direction. This delegation also extends to the NCUA Board's role as liquidator and conservator of insured credit unions. The power to issue a subpoena may not be delegated outside the agency. The General Counsel may amend such order as he deems appropriate.

Subpart I—Local Rules Applicable to Formal Investigative Proceedings

§ 747.801 Applicability.

The rules in this Subpart are applicable to a witness who is sworn in a formal investigative proceeding. Formal investigative proceedings may be held before the NCUA Board, before one or more of its members, or before any officer designated by the NCUA Board or its General Counsel, as described in Subpart H of this Part, and with or without the assistance of such other counsel as the NCUA Board deems appropriate, for the purpose of taking testimony of witnesses, conducting an investigation and receiving other evidence. The term "officer conducting the investigation" shall mean any of the foregoing.

§ 747.802 Non-public Formal Investigative Proceedings.

Unless otherwise ordered by the NCUA Board, all formal investigative proceedings shall be non-public.

§ 747.803 Subpoenas.

(a) Issuance. In the course of a formal investigative proceeding the officer conducting the investigation may issue a subpoena directing the party named therein to appear before the officer conducting the investigation at a specified time and place to testify or to produce documentary evidence, or both, relating to any matter under investigation.

(b) Service. Service of subpoenas shall be effected in the following manner:

(1) Service upon a natural party. Delivery of a copy of a subpoena to a natural person may be effected by—

(i) handing it to the person;

(ii) leaving it at his or her office with the person in charge thereof or, if there is no one in charge, by leaving it at a conspicuous place there;

(iii) leaving it at his or her dwelling place or usual place of abode with some person of suitable age and discretion who is found there; or

(iv) mailing it by registered or certified mail to him or her at his or her last known address. In the event that personal service as described in this paragraph is impracticable, any other method whereby actual notice is given to the respondent may be employed.

(2) Service upon other persons. When the person to be served is not a natural person, delivery of a copy of the subpoena may be effected by—

(i) handing it to a registered agent for service, or to any officer, director, or agent in charge of any office of such person;

(ii) mailing it by registered or certified mail to any such representative at his or her last known address; or

(iii) any other method whereby actual notice is given to any such representative.

(c) Witness fees and mileage. Witnesses appearing pursuant to subpoena shall be paid the same fees and mileage that are paid to witnesses in the United States district courts. Any such fees and mileage payments need be paid only upon submission of a properly completed application for reimbursement and in no event need they be paid sooner than 30 days after the appearance of the witness pursuant to subpoena.

(d) Enforcement. Whenever it appears to the General Counsel that any person upon whom a subpoena was properly served pursuant to these Rules is refusing to fully comply with the terms of that subpoena, then the General Counsel, in his or her discretion, may apply to the courts of the United States for enforcement of such subpoena.

§ 747.804 Oath; False Statements.

At the discretion of the officer conducting the investigation, testimony of a witness may be taken under oath and administered by the officer. Any person making false statements under oath during the course of a formal investigative proceeding is subject to the criminal penalties for perjury in 18 U.S.C. 1621. Any person who knowingly and willfully makes false and fraudulent statements, whether under oath or otherwise, or who falsifies, conceals or covers up any material fact, or submits any false, fictitious or fraudulent information in connection with such a proceeding, is subject to the criminal penalties set forth in 18 U.S.C. 1001.

§ 747.805 Self-incrimination; Immunity.

(a) Self-incrimination. Except as provided in paragraph (b) of this section, a witness testifying or otherwise giving information in a formal investigative proceeding may refuse to answer questions on the basis of his or her right against self-incrimination granted by the Fifth Amendment of the Constitution of the United States.

(b) Immunity.

(1) No officer conducting any formal investigative proceeding (or any other informal investigation or examination) shall have the power to grant or promise any party any immunity from criminal prosecution under the laws of the United States or of any other jurisdiction.

(2) If the NCUA Board believes that the testimony or other information sought to be obtained from any party may be necessary to the public interest and that party has refused or is likely to refuse to testify or provide other information on the basis of his or her privilege against self-incrimination, the NCUA Board, with the approval of the Attorney General, may issue an order requiring the party to give testimony or provide other information that he or she has previously refused to provide on the basis of self-incrimination.

(3) Whenever a witness refuses, on the basis of his privilege against self-incrimination, to testify or provide other information in a formal investigative proceeding, and the officer conducting the investigation communicates to that person an order of the NCUA Board requiring him or her to testify or provide other information, the witness may not refuse to comply with the order on the basis of his or her privilege against self-incrimination; but no testimony or other information compelled under the order (or any information directly or indirectly derived from such testimony or other information) may be used against the witness in any criminal case, except a prosecution for perjury, giving a false statement, or otherwise failing to comply with the order.

§ 747.806 Transcripts.

Transcripts, if any, of formal investigative proceedings shall be recorded solely by the official reporter, or by any other person or means designated by the officer conducting the investigation. A party who has submitted documentary evidence or testimony in a formal investigative proceeding shall be entitled, upon written request, to procure a copy of his or her documentary evidence or a transcript of his or her testimony on payment of the appropriate fees; provided, however, that in a non-public formal investigative proceeding the NCUA Board may for good cause deny such request or the NCUA Board may place reasonable limitations upon the use of the documentary evidence and transcript. In any event, any witness, upon proper identification, shall have the right to inspect the official transcript of the witness's own testimony.

§ 747.807 Rights of Witnesses.

(a) In the event that a formal investigative proceeding is conducted pursuant to a specific order entered by the NCUA Board or by its General Counsel, then any party who is compelled or requested to provide documentary evidence or testimony as part of such proceeding shall, upon request, be shown a copy of the NCUA Board's or its delegate's order. Copies of such orders shall not be provided for their retention to such persons requesting same except in the sole discretion of the General Counsel or his designee.

(b) Any party compelled to appear, or who appears by request or permission of the officer conducting the investigation, in person at a formal investigative proceeding may be accompanied, represented and advised by counsel who is a member of the bar of the highest court of any state; provided however, that all witnesses in such proceeding shall be sequestered, and unless permitted in the discretion of the officer conducting the investigation, no witness or the counsel accompanying any such witness shall be permitted to be present during the examination of any other witness called in such proceeding.

(c)(1) The right of a witness to be accompanied, represented and advised by counsel shall mean the right to have an attorney present during any formal investigative proceeding and to have the attorney—

(i) advise such person before, during and after such testimony;

(ii) question such person briefly at the conclusion of his testimony to clarify any answers such person has given; and

(iii) make summary notes during such testimony solely for the use of such person.

(2) From time to time, in the discretion of the officer, it shall be necessary for persons other than the witness and his or her counsel to attend nonpublic investigative proceedings. For example, the officer may deem it appropriate that outside counsel to the NCUA Board attend and advise him or her concerning the proceeding including the examination of a particular witness. In these circumstances, outside counsel would not be an officer as that term is used. In other circumstances, it may be appropriate that a technical expert (such as an accountant) accompany the witness and his or

her counsel in order to assist counsel in understanding technical issues. These latter circumstances should be rare, are left to the discretion of the officer conducting the investigation, and shall not in any event be allowed to serve as a ruse to coordinate testimony between witnesses, to oversee or supervise the testimony of any witness, or otherwise defeat the beneficial effects of the witness sequestration rule.

(d) The officer conducting the investigation may report to the NCUA Board any instances where any witness or counsel has been guilty of dilatory, obstructionist or contumacious conduct during the course of a formal investigative proceeding or any other instance of violations of these rules. The NCUA Board will thereupon take such further action as the circumstance may warrant including barring the offending person from further participation in the particular formal investigative proceeding or even from further practice before the Board.

Subpart J—Local Procedures and Standards Applicable to a Notice of Change in Senior Executive Officers, Directors or Committee Members Pursuant to Section 212 of the Act

§ 747.901 Scope.

The rules and procedures set forth in this Subpart shall apply to the notice filed by a credit union pursuant to Section 212 of the Act (12 U.S.C. 1790a) and § 701.14 of this Chapter, for the consent of the NCUA to add to or replace an individual on the board of directors or supervisory or credit committee, or to employ any individual as a senior executive officer or change the responsibilities of any individual to a position of senior executive officer where the credit union either has been chartered less than 2 years; or is in "troubled condition," as defined in § 701.14 of this Chapter. Subpart A of this Part shall not apply to any proceeding under this Subpart.

§ 747.902 Grounds for Disapproval of Notice.

The NCUA Board or its designee may issue a notice of disapproval with respect to a notice submitted by a credit union pursuant to Section 212 of the Act (12 U.S.C. 1790a) and § 701.14 of this Chapter, where the competence, experience, character, or integrity of the individual with respect to whom such notice is submitted indicates that it would not be in the best interest of the members of the credit union or the public to permit the individual to be employed by or associated with, such credit union.

§ 747.903 Procedures Where Notice of Disapproval Issued; Reconsideration.

(a) The notice of disapproval shall be served upon the federally insured credit union and the candidate for director, committee member or senior executive officer. The notice of disapproval shall:

(1) Summarize or cite the relevant consideration specified in § 747.902;

(2) Inform the individual and the credit union that, within 15 days of receipt of the notice of disapproval, they can request reconsideration by the Regional Director of the initial determination, or can appeal the determination directly to the NCUA Board;

(3) Specify what additional information, if any, must be considered in the reconsideration.

(b) The request for reconsideration by the Regional Director must be filed at the appropriate Regional Office.

(c) The Regional Director shall act on a request for reconsideration within 30 days of its receipt.

§ 747.904 Appeal.

(a) Time for filing. Within 15 days after issuance of a Notice of Disapproval or a determination on a request for reconsideration by the Regional Director, the individual or credit union (henceforth petitioner) may appeal by filing with the NCUA Board a written request for appeal.

(b) Contents of request. Any appeal must be in writing and include:

(1) The reasons why the NCUA Board should review the disapproval; and

(2) Relevant, substantive and material facts that for good cause were not previously set forth in the notice required to be filed pursuant to Section 212 of the Act (12 U.S.C. 1790a) and § 701.14 of this Chapter.

(c) Procedures for review of request. Within 30 days of the NCUA Board's receipt of an appeal, the NCUA Board may request in writing that the petitioner submit additional facts and records to support the appeal. The petitioner shall have 15

days from the date of issuance of such written request to provide such additional information. Failure by the petitioner to provide additional information may, as determined solely by the NCUA Board or its designee, result in denial of the petitioner's appeal.

(d) Determination on appeal by NCUA Board or its designee.

(1) Within 90 days from the date of the receipt of an appeal by the NCUA Board or its designee or of its receipt of additional information requested under paragraph (c) of this Section, the NCUA Board or its designee shall notify the petitioner whether the disapproval will be continued, terminated, or otherwise modified. The NCUA Board or its designee shall promptly rescind or modify the notice of disapproval where the decision is favorable to the petitioner.

(2) The determination by the NCUA Board on the appeal shall be provided to the petitioner in writing, stating the basis for any decision of the NCUA Board or its designee that is adverse to the petitioner, and shall constitute a final order of the NCUA Board.

(3) Failure by the NCUA Board to issue a determination on the petitioner's appeal within the 90-day period prescribed under paragraph (d)(1) of this Section shall be deemed a denial of the appeal for purpose of § 747.905.

§ 747.905 Judicial Review.

(a) Failure to file an appeal within the applicable time periods, either to the initial determination or to the decision on request for reconsideration, shall constitute a failure by the petitioner to exhaust available administrative remedies and, due to such failure, any objections to the initial determination or request for reconsideration shall be deemed to be waived and such determination shall be deemed to have been accepted by, and shall be binding upon, the petitioner.

(b) For purposes of seeking judicial review of actions taken pursuant to this Section, suit may be filed in the United States District Court for the district where the requester resides, for the district where the credit union's principal place of business is located, or for the District of Columbia.

Subpart K—Inflation Adjustment of Civil Monetary Penalties

§ 747.1001 Adjustment of civil money penalties by the rate of inflation.

(a) NCUA is required by the Federal Civil Penalties Inflation Adjustment Act of 1990 (Public Law 101–410, 104 Stat. 890, as amended (28 U.S.C. 2461 note)) to adjust the maximum amount of each civil money penalty within its jurisdiction by the rate of inflation. The following chart displays those adjustments, as calculated pursuant to the statute:

U.S. Code citation	CMP description	New maximum amount
(1) 12 U.S.C. 1782(a)(3)	Inadvertent failure to submit a report or the inadvertent submission of a false or misleading report.	$22,000.
(2) 12 U.S.C. 1782(a)(3)	Non-inadvertent failure to submit a report or the non-inadvertent submission of a false or misleading report.	$22,000.
(3) 12 U.S.C. 1782(a)(3)	Failure to submit a report or the submission of a false or misleading report done knowingly or with reckless disregard.	$1,175,000 or 1 percent of the total assets of the credit union, whichever is less.
(4) 12 U.S.C. 1782(d)(2)(A)	First tier	$2,200.
(5) 12 U.S.C. 1782(d)(2)(B)	Second tier	$22,000.
(6) 12 U.S.C. 1782(d)(2)(C)	Third tier	$1,175,000 or 1 percent of the total assets of the credit union, whichever is less.
(7) 12 U.S.C. 1785(e)(3)	Non-compliance with NCUA security regulations	$110.
(8) 12 U.S.C. 1786(k)(2)(A)	First tier	$6,500.
(9) 12 U.S.C. 1786(k)(2)(B)	Second tier	$32,500.

U.S. Code citation	CMP description	New maximum amount
(10) 12 U.S.C. 1786(k)(2)(C)	Third tier	For a person other than an insured credit union: $1,175,000; For an insured credit union: $1,175,000 or 1 percent of the total assets of the credit union, whichever is less
(11) 42 U.S.C. 4012a(f)	Per violation	$385
	Per calendar year	$110,000

(b) The adjustments displayed in paragraph (a) of this section apply to acts occurring beginning on October 23, 2000.

Subpart L—Issuance, Review and Enforcement of Orders Imposing Prompt Corrective Action

§ 747.2001 Scope.

(a) *Independent review process.* The rules and procedures set forth in this subpart apply to federally-insured credit unions, whether federally- or state-chartered (other than corporate credit unions), which are subject to discretionary supervisory actions under part 702 of this chapter, and to reclassification under §§ 702.102(b) and 702.302(d) of this chapter, to facilitate prompt corrective action under section 216 of the Federal Credit Union Act, 12 U.S.C. 1790d; and to senior executive officers and directors of such credit unions who are dismissed pursuant to a discretionary supervisory action imposed under part 702. NCUA staff decisions to impose discretionary supervisory actions under part 702 shall be considered material supervisory determinations for purposes of 12 U.S.C. 1790d(k). Section 747.2002 of this subpart provides an independent appellate process to challenge such decisions.

(b) *Notice to State officials.* With respect to a federally-insured State-chartered credit union under §§ 747.2002, 747.2003 and 747.2004 of this subpart, notices, directives and decisions on appeal served upon a credit union, or a dismissed director or officer thereof, by the NCUA Board shall also be served upon the appropriate State official. Responses, requests for a hearing and to present witnesses, requests to modify or rescind a discretionary supervisory action and requests for reinstatement served upon the NCUA Board by a credit union, or dismissed director or officer thereof, shall also be served upon the appropriate State official.

§ 747.2002 Review of orders imposing discretionary supervisory action.

(a) *Notice of intent to issue directive.*—

(1) *Generally.* Whenever the NCUA Board intends to issue a directive imposing a discretionary supervisory action under §§ 702.202(b), 702.203(b) and 702.204(b) of this chapter on a credit union classified "undercapitalized" or lower, or under §§ 702.304(b) or 702.305(b) of this chapter on a new credit union classified "moderately capitalized" or lower, it must give the credit union prior notice of the proposed action and an opportunity to respond.

(2) *Immediate issuance of directive without notice.* The NCUA Board may issue a directive to take effect immediately under paragraph (a)(1) of this section without notice to the credit union if the NCUA Board finds it necessary in order to carry out the purposes of part 702 of this chapter. A credit union that is subject to a directive which takes effect immediately may appeal the directive in writing to the NCUA Board. Such an appeal must be received by the NCUA Board within 14 calendar days after the directive was issued, unless the NCUA Board permits a longer period. Unless ordered by the NCUA Board, the directive shall remain in effect pending a decision on the appeal. The NCUA Board shall consider any such appeal, if timely filed, within 60 calendar days of receiving it.

(b) *Contents of notice.* The NCUA Board's notice to a credit union of its intention to issue a directive imposing a discretionary supervisory action must state:

(1) The credit union's net worth ratio and net worth category classification;

(2) The specific restrictions or requirements that the NCUA Board intends to impose, and the reasons therefor;

(3) The proposed date when the discretionary supervisory action would take effect and the proposed date for completing the required action or terminating the action; and

(4) That a credit union must file a written response to a notice within 14 calendar days from the date of the notice, or within such shorter period as the NCUA Board determines is appropriate in light of the financial condition of the credit union or other relevant circumstances.

(c) *Contents of response to notice.* A credit union's response to a notice under paragraph (b) of this section must:

(1) Explain why it contends that the proposed discretionary supervisory action is not an appropriate exercise of discretion under this part;

(2) Request the NCUA Board to modify or to not issue the proposed directive;

(3) Include other relevant information, mitigating circumstances, documentation, or other evidence in support of the credit union's position regarding the proposed directive; and

(4) If desired, request the recommendation of NCUA's ombudsman pursuant to paragraph (g) of this section.

(d) *NCUA Board consideration of response.* The NCUA Board, or an independent person designated by the NCUA Board to act on its behalf, after considering a response under paragraph (c) of this section, may:

(1) Issue the directive as originally proposed or as modified;

(2) Determine not to issue the directive and to so notify the credit union; or

(3) Seek additional information or clarification from the credit union or any other relevant source.

(e) *Failure to file response.* A credit union which fails to file a written response to a notice of the NCUA Board's intention to issue a directive imposing a discretionary supervisory action, within the specified time period, shall be deemed to have waived the opportunity to respond, and to have consented to the issuance of the directive.

(f) *Request to modify or rescind directive.* A credit union that is subject to an existing directive imposing a discretionary supervisory action may request in writing that the NCUA Board reconsider the terms of the directive, or rescind or modify it, due to changed circumstances. Unless otherwise ordered by the NCUA Board, the directive shall remain in effect while such request is pending. A request under this paragraph which remains pending 60 days following receipt by the NCUA Board is deemed granted.

(g) *Ombudsman.* A credit union may request in writing the recommendation of NCUA's ombudsman to modify or to not issue a proposed directive under paragraph (b) of this section, or to modify or rescind an existing directive due to changed circumstances under paragraph (f) of this section. A credit union which fails to request the ombudsman's recommendation in a response under paragraph (c) of this section, or in a request under paragraph (f) of this section, shall be deemed to have waived the opportunity to do so. The ombudsman shall promptly notify the credit union and the NCUA Board of his or her recommendation.

§ 747.2003 Review of order reclassifying a credit union on safety and soundness criteria.

(a) *Notice of proposed reclassification based on unsafe or unsound condition or practice.* When the NCUA Board proposes to reclassify a credit union or subject it to the supervisory actions applicable to the next lower net worth category pursuant to §§ 702.102(b) and 702.302(d) of this chapter (each such action hereinafter referred to as "reclassification"), the NCUA Board shall issue and serve on the credit union reasonable prior notice of the proposed reclassification.

(b) *Contents of notice.* A notice of intention to reclassify a credit union based on unsafe or unsound condition or practice shall state:

(1) The credit union's net worth ratio, current net worth category classification, and the net worth category to which the credit union would be reclassified;

(2) The unsafe or unsound practice(s) and/or condition(s) justifying reasons for reclassification of the credit union;

(3) The date by which the credit union must file a written response to the notice (including a request for a hearing), which date shall be no less than 14 calendar days from the date of service of the notice unless the NCUA Board determines that a shorter period is appropriate in light of the financial condition of the credit union or other relevant circumstances; and

(4) That a credit union which fails to—

(i) File a written response to the notice of reclassification, within the specified time period, shall be deemed to have waived the opportunity to respond, and to have consented to reclassification;

(ii) Request a hearing shall be deemed to have waived any right to a hearing; and

(iii) Request the opportunity to present witness testimony shall be deemed have waived any right to present such testimony.

(c) *Contents of response to notice.* A credit union's response to a notice under paragraph (b) of this section must:

(1) Explain why it contends that the credit union should not be reclassified;

(2) Include any relevant information, mitigating circumstances, documentation, or other evidence in support of the credit union's position;

(3) If desired, request an informal hearing before the NCUA Board under this section; and

(4) If a hearing is requested, identify any witness whose testimony the credit union wishes to present and the general nature of each witness's expected testimony.

(d) *Order to hold informal hearing.* Upon timely receipt of a written response that includes a request for a hearing, the NCUA Board shall issue an order commencing an informal hearing no later than 30 days after receipt of the request, unless the credit union requests a later date. The hearing shall be held in Alexandria, Virginia, or at such other place as may be designated by the NCUA Board, before a presiding officer designated by the NCUA Board to conduct the hearing and to recommend a decision.

(e) *Procedures for informal hearing.*—(1) The credit union may appear at the hearing through a representative or through counsel. The credit union shall have the right to introduce relevant documents and to present oral argument at the hearing. The credit union may introduce witness testimony only if expressly authorized by the NCUA Board or the presiding officer. Neither the provisions of the Administrative Procedure Act (5 U.S.C. 554–557) governing adjudications required by statute to be determined on the record nor the Uniform Rules of Practice and Procedure (12 CFR part 747) shall apply to an informal hearing under this section unless the NCUA Board orders otherwise.

(2) The informal hearing shall be recorded, and a transcript shall be furnished to the credit union upon request and payment of the cost thereof. Witnesses need not be sworn, unless specifically requested by a party or by the presiding officer. The presiding officer may ask questions of any witness.

(3) The presiding officer may order that the hearing be continued for a reasonable period following completion of witness testimony or oral argument to allow additional written submissions to the hearing record.

(4) Within 20 calendar days following the closing of the hearing and the record, the presiding officer shall make a recommendation to the NCUA Board on the proposed reclassification.

(f) *Time for final decision.* Not later than 60 calendar days after the date the record is closed, or the date of receipt of the credit union's response in a case where no hearing was requested, the NCUA Board will decide whether to reclassify the credit union, and will notify the credit union of its decision. The decision of the NCUA Board shall be final.

(g) *Request to rescind reclassification.* Any credit union that has been reclassified under this section may file a written request to the NCUA Board to reconsider or rescind the reclassification, or to modify, rescind or remove any directives issued as a result of the reclassification. Unless otherwise ordered by the NCUA Board, the credit union shall remain reclassified, and subject to any directives issued as a result, while such request is pending.

(h) *Non-delegation*. The NCUA Board may not delegate its authority to reclassify a credit union into a lower net worth category or to treat a credit union as if it were in a lower net worth category pursuant to §§ 702.102(b) or 702.302(d) of this chapter.

§ 747.2004 Review of order to dismiss a director or senior executive officer.

(a) *Service of directive to dismiss and notice.* When the NCUA Board issues and serves a directive on a credit union requiring it to dismiss from office any director or senior executive officer under §§ 702.202(b)(7), 702.203(b)(8), 702.204(b)(8), 702.304(b) or 702.305(b) of this chapter, the NCUA Board shall also serve upon the person the credit union is directed to dismiss (Respondent) a copy of the directive (or the relevant portions, where appropriate) and notice of the Respondent's right to seek reinstatement.

(b) *Contents of notice of right to seek reinstatement.* A notice of a Respondent's right to seek reinstatement shall state:

(1) That a request for reinstatement (including a request for a hearing) shall be filed with the NCUA Board within 14 calendar days after the Respondent receives the directive and notice under paragraph (a) of this section,

unless the NCUA Board grants the Respondent's request for further time;

(2) The reasons for dismissal of the Respondent; and

(3) That the Respondent's failure to—

(i) Request reinstatement shall be deemed a waiver of any right to seek reinstatement;

(ii) Request a hearing shall be deemed a waiver of any right to a hearing; and

(iii) Request the opportunity to present witness testimony shall be deemed a waiver of the right to present such testimony.

(c) *Contents of request for reinstatement.* A request for reinstatement in response to a notice under paragraph (b) of this section must:

(1) Explain why the Respondent should be reinstated;

(2) Include any relevant information, mitigating circumstances, documentation, or other evidence in support of the Respondent's position;

(3) If desired, request an informal hearing before the NCUA Board under this section; and

(4) If a hearing is requested, identify any witness whose testimony the Respondent wishes to present and the general nature of each witness's expected testimony.

(d) *Order to hold informal hearing.* Upon receipt of a timely written request from a Respondent for an informal hearing on the portion of a directive requiring a credit union to dismiss from office any director or senior executive officer, the NCUA Board shall issue an order directing an informal hearing to commence no later than 30 days after receipt of the request, unless the Respondent requests a later date. The hearing shall be held in Alexandria, Virginia, or at such other place as may be designated by the NCUA Board, before a presiding officer designated by the NCUA Board to conduct the hearing and recommend a decision.

(e) *Procedures for informal hearing.*— (1) A Respondent may appear at the hearing personally or through counsel. A Respondent shall have the right to introduce relevant documents and to present oral argument at the hearing. A Respondent may introduce witness testimony only if expressly authorized by the NCUA Board or by the presiding officer. Neither the provisions of the Administrative Procedure Act (5 U.S.C. 554–557) governing adjudications required by statute to be determined on the record nor the Uniform Rules of Practice and Procedure (12 CFR part 747) apply to an informal hearing under this section unless the NCUA Board orders otherwise.

(2) The informal hearing shall be recorded, and a transcript shall be furnished to the Respondent upon request and payment of the cost thereof. Witnesses need not be sworn, unless specifically requested by a party or the presiding officer. The presiding officer may ask questions of any witness.

(3) The presiding officer may order that the hearing be continued for a reasonable period following completion of witness testimony or oral argument to allow additional written submissions to the hearing record.

(4) A Respondent shall bear the burden of demonstrating that his or her continued employment by or service with the credit union would materially strengthen the credit union's ability to—

(i) Become "adequately capitalized," to the extent that the directive was issued as a result of the credit union's net worth category classification or its failure to submit or implement a net worth restoration plan or revised business plan; and

(ii) Correct the unsafe or unsound condition or unsafe or unsound practice, to the extent that the directive was issued as a result of reclassification of the credit union pursuant to §§702.102(b) and 702.302(d) of this chapter.

(5) Within 20 calendar days following the date of closing of the hearing and the record, the presiding officer shall make a recommendation to the NCUA Board concerning the Respondent's request for reinstatement with the credit union.

(f) *Time for final decision.* Not later than 60 calendar days after the date the record is closed, or the date of the response in a case where no hearing was requested, the NCUA Board shall grant or deny the request for reinstatement and shall notify the Respondent of its decision. If the NCUA Board denies the request for reinstatement, it shall set forth in the notification the reasons for its decision. The decision of the NCUA Board shall be final.

(g) *Effective date.* Unless otherwise ordered by the NCUA Board, the Respondent's dismissal shall take and remain in effect pending a final decision on the request for reinstatement.

§ 747.2005 Enforcement of orders.

(a) *Judicial remedies.* Whenever a credit union fails to comply with a directive imposing a discretionary supervisory action, or enforcing a manda-

tory supervisory action under part 702 of this chapter, the NCUA Board may seek enforcement of the directive in the appropriate United States District Court pursuant to 12 U.S.C. 1786(k)(1).

(b) *Administrative remedies*—(1) *Failure to comply with directive.* Pursuant to 12 U.S.C. 1786(k)(2)(A), the NCUA Board may assess a civil money penalty against any credit union that violates or otherwise fails to comply with any final directive issued under part 702 of this chapter, or against any institution-affiliated party of a credit union (per 12 U.S.C. 1786(r)) who participates in such violation or noncompliance.

(2) *Failure to implement plan.* Pursuant to 12 U.S.C. 1786(k)(2)(A), the NCUA Board may assess a civil money penalty against a credit union which fails to implement a net worth restoration plan under subpart B of part 702 of this chapter or a revised business plan under subpart C of part 702, regardless whether the plan was published.

(c) *Other enforcement action.* In addition to the actions described in paragraphs (a) and (b) of this section, the NCUA Board may seek enforcement of the directives issued under part 702 of this chapter through any other judicial or administrative proceeding authorized by law.

Part 748

Security Program, Report of Crime and Catastrophic Act and Bank Secrecy Act Compliance

§ 748.0 Security program.

(a) Each federally-insured credit union will develop a written security program within 90 days of the effective date of insurance.

(b) The security program will be designed to:

(1) Protect each credit union office from robberies, burglaries, larcenies, and embezzlement;

(2) Ensure the security and confidentiality of member records, protect against the anticipated threats or hazards to the security or integrity of such records, and protect against unauthorized access to or use of such records that could result in substantial harm or serious inconvenience to a member;

(3) Respond to incidents of unauthorized access to or use of member information that could result in substantial harm or serious inconvenience to a member;

(4) Assist in the identification of persons who commit or attempt such actions and crimes, and

(5) Prevent destruction of vital records, as defined in 12 CFR part 749.

(c) Each Federal credit union, as part of its information security program, must properly dispose of any consumer information the Federal credit union maintains or otherwise possesses, as required under § 717.83 of this chapter.

§ 748.1 Filing of reports.

(a) *Compliance Report.* Each federally-insured credit union shall file with the regional director an annual statement certifying its compliance with the requirements of this Part. The statement shall be dated and signed by the president or other managing officer of the credit union. The statement is contained on the Report of Officials which is submitted annually by federally-insured credit unions after the election of officials. In the case of federally-insured state-chartered credit unions, this statement can be mailed to the regional director via the state supervisory authority, if desired. In any event, a copy of the statement shall always be sent to the appropriate state supervisory authority.

(b) *Catastrophic Act Report.* Each federally-insured credit union will notify the regional director within 5 business days of any catastrophic act that occurs at its office(s). A catastrophic act is any natural disaster such as a flood, tornado, earthquake, etc., or major fire or other disaster resulting in some physical destruction or damage to the credit union. Within a reasonable time after a catastrophic act occurs, the credit union shall ensure that a record of the incident is prepared and filed at its main office. In the preparation of such record, the credit union should include information sufficient to indicate the office where the catastrophic act occurred; when it took place; the amount of the loss, if any; whether any operational or mechanical deficiency(ies) might have contributed to the catastrophic act; and what has been done or is planned to be done to correct the deficiency(ies).

(c) *Suspicious Activity Report.* (1) Each federally-insured credit union will report any crime or suspected crime that occurs at its office(s), utilizing NCUA Form 2362, Suspicious Activity Report (SAR), within thirty calendar days after discovery. Each federally-insured credit union must follow the instructions and reporting requirements accompanying the SAR. Copies of the SAR may be obtained from the appropriate NCUA Regional Office.

(2) Each federally-insured credit union shall maintain a copy of any SAR that it files and the original of all attachments to the report for a period of five years from the date of the report, unless the credit union is informed in writing by the National Credit Union Administration that the materials may be discarded sooner.

(3) Failure to file a SAR in accordance with the instructions accompanying the report may subject the federally-insured credit union, its officers, directors, agents or other institution-affiliated parties to the assessment of civil money penalties or other administrative actions.

(4) Filing of Suspicious Activity Reports will ensure that law enforcement agencies and NCUA are promptly notified of actual or suspected crimes. Information contained on SARs will be entered into an interagency database and will assist the federal government in taking appropriate action.

§ 748.2 Procedures for monitoring Bank Secrecy Act (BSA) compliance.

(a) *Purpose.* This Section is issued to ensure that all federally-insured credit unions establish and maintain procedures reasonably designed to assure and monitor compliance with the requirements of Subchapter II of Chapter 53 of Title 31, United States Code, the Financial Recordkeeping and Reporting of Currency and Foreign Transactions Act, and the implementing regulations promulgated thereunder by the Department of Treasury, 31 C.F.R. Part 103.

(b) *Establishment of a BSA compliance program.* (1) *Program requirement.* Each federally-insured credit union shall develop and provide for the continued administration of a program reasonably designed to assure and monitor compliance with the recordkeeping and recording requirements set forth in subchapter II of chapter 53 of title 31, United States Code and the implementing regulations issued by the Department of the Treasury at 31 CFR part 103. The compliance program must be written, approved by the credit union's board of directors, and reflected in the minutes of the credit union.

(2) *Customer identification program.* Each federally-insured credit union is subject to the requirements of 31 U.S.C. 5318(l) and the implementing regulation jointly promulgated by the NCUA and the Department of the Treasury at 31 CFR 103.121, which require a customer identification program to be implemented as part of the BSA compliance program required under this section.

(c) *Contents of Compliance Program.* Such compliance program shall at a minimum—

(1) Provide for a system of internal controls to assure ongoing compliance;

(2) Provide for independent testing for compliance to be conducted by credit union personnel or outside parties;

(3) Designate an individual responsible for coordinating and monitoring day-to-day compliance; and

(4) Provide training for appropriate personnel.

Appendix A to Part 748—Guidelines for Safeguarding Member Information

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I. Introduction

The Guidelines for Safeguarding Member Information (Guidelines) set forth standards pursuant to sections 501 and 505(b), codified at 15 U.S.C. 6801 and 6805(b), of the Gramm-Leach-Bliley Act. These Guidelines provide guidance standards for developing and implementing administrative, technical, and physical safeguards to protect the security, confidentiality, and integrity of member information. These Guidelines also address standards with respect to the proper disposal of consumer information pursuant to sections 621(b) and 628 of the Fair Credit Reporting Act (15 U.S.C. 1681s(b) and 1681w).

A. *Scope.* The Guidelines apply to member information maintained by or on behalf of federally-insured credit unions. Such entities are referred to in this appendix as "the credit union." These Guidelines also apply to the proper disposal of consumer information by such entities.

B. *Definitions.* 1. *In general.* Except as modified in the Guidelines or unless the context otherwise requires, the terms used in these Guidelines have the same meanings as set forth in 12 CFR part 716.

2. For purposes of the Guidelines, the following definitions apply:

a. *Consumer information* means any record about an individual, whether in paper, electronic, or other form, that is a consumer report or is derived from a consumer report and that is maintained or otherwise possessed by or on behalf of the credit union for a business purpose. Consumer information also means a compilation of such records. The term does not include any record that does not identify an individual.

b. *Consumer report* has the same meaning as set forth in the Fair Credit Reporting Act, 15 U.S.C. 1681a(d). The meaning of consumer report is broad and subject to various definitions, conditions and exceptions in the Fair Credit Reporting Act. It includes written or oral communications from a consumer reporting agency to a third party of information used or collected for use in establishing eligibility for credit or insurance used primarily for personal, family or household purposes, and eligibility for employment purposes. Examples include credit reports, bad check lists, and tenant screening reports.

c. *Member* means any member of the credit union as defined in 12 CFR 716.3(n).

d. *Member information* means any records containing nonpublic personal information, as defined in 12 CFR 716.3(q), about a member, whether in paper, electronic, or other form, that is maintained by or on behalf of the credit union.

e. *Member information system* means any method used to access, collect, store, use, transmit, protect, or dispose of member information.

f. *Service provider* means any person or entity that maintains, processes, or otherwise is permitted access to member information through its provision of services directly to the credit union.

II. Standards for Safeguarding Member Information

A. *Information Security Program.* A comprehensive written information security program includes administrative, technical, and physical safeguards appropriate to the size and complexity of the credit union and the nature and scope of its activities. While all parts of the credit union are not required to implement a uniform set of policies, all elements of the information security program must be coordinated.

B. *Objectives.* A credit union's information security program should be designed to: ensure the security and confidentiality of member information; protect against any anticipated threats

or hazards to the security or integrity of such information; and protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any member; and ensure the proper disposal of member information and consumer information. Protecting confidentiality includes honoring members' requests to opt out of disclosures to nonaffiliated third parties, as described in 12 CFR 716.1(a)(3).

III. Development and Implementation of Member Information Security Program

A. *Involve the Board of Directors.* The board of directors or an appropriate committee of the board of each credit union should:

1. Approve the credit union's written information security policy and program; and

2. Oversee the development, implementation, and maintenance of the credit union's information security program, including assigning specific responsibility for its implementation and reviewing reports from management.

B. *Assess Risk.* Each credit union should:

1. Identify reasonably foreseeable internal and external threats that could result in unauthorized disclosure, misuse, alteration, or destruction of member information or member information systems;

2. Assess the likelihood and potential damage of these threats, taking into consideration the sensitivity of member information; and

3. Assess the sufficiency of policies, procedures, member information systems, and other arrangements in place to control risks.

C. *Manage and Control Risk.* Each credit union should:

1. Design its information security program to control the identified risks, commensurate with the sensitivity of the information as well as the complexity and scope of the credit union's activities. Each credit union must consider whether the following security measures are appropriate for the credit union and, if so, adopt those measures the credit union concludes are appropriate:

a. Access controls on member information systems, including controls to authenticate and permit access only to authorized individuals and controls to prevent employees from providing member information to unauthorized individuals who may seek to obtain this information through fraudulent means;

b. Access restrictions at physical locations containing member information, such as buildings, computer facilities, and records storage facilities to permit access only to authorized individuals;

c. Encryption of electronic member information, including while in transit or in storage on networks or systems to which unauthorized individuals may have access;

d. Procedures designed to ensure that member information system modifications are consistent with the credit union's information security program;

e. Dual controls procedures, segregation of duties, and employee background checks for employees with responsibilities for or access to member information;

f. Monitoring systems and procedures to detect actual and attempted attacks on or intrusions into member information systems;

g. Response programs that specify actions to be taken when the credit union suspects or detects that unauthorized individuals have gained access to member information systems, including appropriate reports to regulatory and law enforcement agencies; and

h. Measures to protect against destruction, loss, or damage of member information due to potential environmental hazards, such as fire and water damage or technical failures.

2. Train staff to implement the credit union's information security program.

3. Regularly test the key controls, systems and procedures of the information security program. The frequency and nature of such tests should be determined by the credit union's risk assessment. Tests should be conducted or reviewed by independent third parties or staff independent of those that develop or maintain the security programs.

4. Develop, implement, and maintain, as part of its information security program, appropriate measures to properly dispose of member information and consumer information in accordance with the provisions in paragraph III.

D. *Oversee Service Provider Arrangements.* Each credit union should:

1. Exercise appropriate due diligence in selecting its service providers;

2. Require its service providers by contract to implement appropriate measures designed to meet the objectives of these guidelines; and

3. Where indicated by the credit union's risk assessment, monitor its service providers to confirm that they have satisfied their obliga-

tions as required by paragraph D.2. As part of this monitoring, a credit union should review audits, summaries of test results, or other equivalent evaluations of its service providers.

E. *Adjust the Program.* Each credit union should monitor, evaluate, and adjust, as appropriate, the information security program in light of any relevant changes in technology, the sensitivity of its member information, internal or external threats to information, and the credit union's own changing business arrangements, such as mergers and acquisitions, alliances and joint ventures, outsourcing arrangements, and changes to member information systems.

F. *Report to the Board.* Each credit union should report to its board or an appropriate committee of the board at least annually. This report should describe the overall status of the information security program and the credit union's compliance with these guidelines. The report should discuss material matters related to its program, addressing issues such as: risk assessment; risk management and control decisions; service provider arrangements; results of testing; security breaches or violations and management's responses; and recommendations for changes in the information security program.

G. *Implement the Standards.*

1. *Effective date.* Each credit union must implement an information security program pursuant to the objectives of these Guidelines by July 1, 2001.

2. *Two-year grandfathering of agreements with service providers.* Until July 1, 2003, a contract that a credit union has entered into with a service provider to perform services for it or functions on its behalf satisfies the provisions of paragraph III.D., even if the contract does not include a requirement that the servicer maintain the security and confidentiality of member information, as long as the credit union entered into the contract on or before March 1, 2001.

3. *Effective date for measures relating to the disposal of consumer information.* Each Federal credit union must properly dispose of consumer information in a manner consistent with these Guidelines by July 1, 2005.

4. *Exception for existing agreements with service providers relating to the disposal of consumer information.* Notwithstanding the requirement in paragraph III.G.3., a Federal credit union's existing contracts with its service providers with regard to any service involving the disposal of consumer information should implement the objectives of these Guidelines by July 1, 2006.

Appendix B to Part 748—Guidance on Response Programs for Unauthorized Access to Member Information and Member Notice

I. Background

This Guidance in the form of Appendix B to NCUA's Security Program, Report of Crime and Catastrophic Act and Bank Secrecy Act Compliance regulation,[29] interprets section 501(b) of the Gramm-Leach-Bliley Act ("GLBA") and describes response programs, including member notification procedures, that a federally insured credit union should develop and implement to address unauthorized access to or use of member information that could result in substantial harm or inconvenience to a member. The scope of, and definitions of terms used in, this Guidance are identical to those of Appendix A to Part 748 (Appendix A). For example, the term "member information" is the same term used in Appendix A, and means any record containing nonpublic personal information about a member, whether in paper, electronic, or other form, maintained by or on behalf of the credit union.

A. Security Guidelines

Section 501(b) of the GLBA required the NCUA to establish appropriate standards for credit unions subject to its jurisdiction that include administrative, technical, and physical safeguards to protect the security and confidentiality of member information. Accordingly, the NCUA amended Part 748 of its rules to require credit unions to develop appropriate security programs, and issued Appendix A, reflecting its expectation that every federally insured credit union would develop an information security program designed to:

1. Ensure the security and confidentiality of member information;
2. Protect against any anticipated threats or hazards to the security or integrity of such information; and
3. Protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any member.

B. Risk Assessment and Controls

1. Appendix A directs every credit union to assess the following risks, among others, when developing its information security program:

a. Reasonably foreseeable internal and external threats that could result in unauthorized disclosure, misuse, alteration, or destruction of member information or member information systems;

b. The likelihood and potential damage of threats, taking into consideration the sensitivity of member information; and

c. The sufficiency of policies, procedures, member information systems, and other arrangements in place to control risks.[30]

2. Following the assessment of these risks, Appendix A directs a credit union to design a program to address the identified risks. The particular security measures a credit union should adopt will depend upon the risks presented by the complexity and scope of its business. At a minimum, the credit union should consider the specific security measures enumerated in Appendix A,[31] and adopt those that are appropriate for the credit union, including:

a. Access controls on member information systems, including controls to authenticate and permit access only to authorized individuals and controls to prevent employees from providing member information to unauthorized individuals who may seek to obtain this information through fraudulent means;

b. Background checks for employees with responsibilities for access to member information; and

c. Response programs that specify actions to be taken when the credit union suspects or detects that unauthorized individuals have gained access to member information systems, including appropriate reports to regulatory and law enforcement agencies.[32]

C. Service Providers

Appendix A advises every credit union to require its service providers by contract to implement appropriate measures designed to protect against unauthorized access to or use of member information that could result in substantial harm or inconvenience to any member.[33]

[29] 12 CFR Part 748.

[30] *See* 12 CFR Part 748, Appendix A, Paragraph III.B.

[31] *See* Appendix A, paragraph III.C.

[32] *See* Appendix A, Paragraph III.C.

[33] *See* Appendix A, Paragraph III.B. and III.D. Further, the NCUA notes that, in addition to contractual obligations

II. Response Program

i. Millions of Americans, throughout the country, have been victims of identity theft.[34] Identity thieves misuse personal information they obtain from a number of sources, including credit unions, to perpetrate identity theft. Therefore, credit unions should take preventative measures to safeguard member information against such attempts to gain unauthorized access to the information. For example, credit unions should place access controls on member information systems and conduct background checks for employees who are authorized to access member information.[35] However, every credit union should also develop and implement a risk-based response program to address incidents of unauthorized access to member information in member information systems that occur nonetheless.[36] A response program should be a key part of a credit union's information security program.[37] The program should be appropriate to the size and complexity of the credit union and the nature and scope of its activities.

ii. In addition, each credit union should be able to address incidents of unauthorized access to member information in member information systems maintained by its domestic and foreign service providers. Therefore, consistent with the obligations in this Guidance that relate to these arrangements, and with existing guidance on this topic issued by the NCUA,[38] a credit union's contract with its service provider should require the service provider to take appropriate actions to address incidents of unauthorized access to or use of the credit union's member information, including notification of the credit union as soon as possible of any such incident, to enable the institution to expeditiously implement its response program.

A. Components of a Response Program

1. At a minimum, a credit union's response program should contain procedures for the following:

a. Assessing the nature and scope of an incident, and identifying what member information systems and types of member information have been accessed or misused;

b. Notifying the appropriate NCUA Regional Director, and, in the case of state-chartered credit unions, its applicable state supervisory authority, as soon as possible when the credit union becomes aware of an incident involving unauthorized access to or use of sensitive member information as defined below.

c. Consistent with the NCUA's Suspicious Activity Report ("SAR") regulations,[39] notifying appropriate law enforcement authorities, in addition to filing a timely SAR in situations involving Federal criminal violations requiring immediate attention, such as when a reportable violation is ongoing;

d. Taking appropriate steps to contain and control the incident to prevent further unauthorized access to or use of member information, for example, by monitoring, freezing, or closing affected accounts, while preserving records and other evidence; [40] and

e. Notifying members when warranted.

2. Where an incident of unauthorized access to member information involves member infor-

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to a credit union, a service provider may be required to implement its own comprehensive information security program in accordance with the Safeguards Rule promulgated by the Federal Trade Commission ("FTC"), 12 CFR Part 314.

[34] The FTC estimates that nearly 10 million Americans discovered they were victims of some form of identify theft in 2002. *See* The Federal Trade Commission, *Identity Theft Survey Report,* (September 2003), available at *http://www.ftc.gov/os/2003/09synovatereport.pdf.*

[35] Credit unions should also conduct background checks of employees to ensure that the credit union does not violate 12 U.S.C. 1785(d), which prohibits a credit union from hiring an individual convicted of certain criminal offenses or who is subject to a prohibition order under 12 U.S.C. 1786(g).

[36] Under 12 CFR Part 748, Appendix A, a credit union's *member information systems* consists of all of the methods used to access, collect, store, use, transmit, protect, or dispose of member information, including the systems maintained by its service providers. *See* 12 CFR Part 748, Appendix A, Paragraph I.C.2.d.

[37] *See* FFIEC Information Technology Examination Handbook, Information Security Booklet, (December, 2002), available at *http://www.ffiec.gov/ffiecinfobase/html—pages/it—01.htm1#infosec,* for additional guidance on preventing, detecting, and responding to intrusions into financial institution computer systems.

[38] *See* FFIEC Information Technology Examination Handbook, Outsourcing Technology Services Booklet, (June 2004), available at *http://www.ffiec.gov/ffiecinfobase/html—pages/it—01.htm1#outscouring* for additional guidance on managing outsourced relationships.

[39] A credit union's obligation to file a SAR is set out in the NCUA's SAR regulations and guidance. *See* 12 CFR Part 748.1(c); NCUA Letter to Credit Unions No. 04–CU–03, Suspiciouis Activity Reports, March 2004; NCUA Regulatory Alert No. 04–RA–01, The Suspicious Activity Report (SAR) Activity Review—Trends, Tips, & Isues, Issue 6, November 2003, February 2004.

[40] *See* FFIEC Information Technology Examination Handbook, Information Security Booklet, (December 2002), pp. 68–74.

mation systems maintained by a credit union's service providers, it is the responsibility of the credit union to notify the credit union's members and regulator. However, a credit union may authorize or contract with its service provider to notify the credit union's members or regulators on its behalf.

III. Member Notice

i. Credit unions have an affirmative duty to protect their members' information against unauthorized access or use. Notifying members of a security incident involving the unauthorized access or use of the member's information in accordance with the standard set forth below is a key part of that duty.

ii. Timely notification of members is important to manage a credit union's reputation risk. Effective notice also may reduce a credit union's legal risk, assist in maintaining good member relations, and enable the credit union's members to take steps to protect themselves against the consequences of identity theft. When member notification is warranted, a credit union may not forgo notifying its customers of an incident because the credit union believes that it may be potentially embarrassed or inconvenienced by doing so.

A. Standard for Providing Notice

When a credit union becomes aware of an incident of unauthorized access to sensitive member information, the credit union should conduct a reasonable investigation to promptly determine the likelihood that the information has been or will be misused. If the credit union determines that misuse of its information about a member has occurred or is reasonably possible, it should notify the affected member as soon as possible. Member notice may be delayed if an appropriate law enforcement agency determines that notification will interfere with a criminal investigation and provides the credit union with a written request for the delay. However, the credit union should notify its members as soon as notification will no longer interfere with the investigation.

1. Sensitive Member Information

Under Part 748.0, a credit union must protect against unauthorized access to or use of member information that could result in substantial harm or inconvenience to any member. Substantial harm or inconvenience is most likely to result from improper access to *sensitive member information* because this type of information is most likely to be misused, as in the commission of identity theft.

For purposes of this Guidance, sensitive member information means a member's name, address, or telephone number, in conjunction with the member's social security number, driver's license number, account number, credit or debit card number, or a personal identification number or password that would permit access to the member's account. *Sensitive member information* also includes any combination of components of member information that would allow someone to log onto or access the member's account, such as user name and password or password and account number.

2. Affected Members

If a credit union, based upon its investigation, can determine from its logs or other data precisely which members' information has been improperly accessed, it may limit notification to those members with regard to whom the credit union determines that misuse of their information has occurred or is reasonably possible. However, there may be situations where the credit union determines that a group of files has been accessed improperly, but is unable to identify which specific member's information has been accessed. If the circumstances of the unauthorized access lead the credit union to determine that misuse of the information is reasonably possible, it should notify all members in the group.

B. Content of Member Notice

1. Member notice should be given in a clear and conspicuous manner. The notice should describe the incident in general terms and the type of member information that was the subject of unauthorized access or use. It also should generally describe what the credit union has done to protect the members' information from further unauthorized access. In addition, it should include a telephone number that members can call for further information and assistance.[41] The notice also should remind members of the need to remain vigilant over the next twelve to twenty-four months, and to promptly

[41] The credit union should, therefore, ensure that it has reasonable policies and procedures in place, including trained personnel, to respond appropriately to member inquiries and requests for assistance.

report incidents of suspected identity theft to the credit union. The notice should include the following additional items, when appropriate:

a. A recommendation that the member review account statements and immediately report any suspicious activity to the credit union;

b. A description of fraud alerts and an explanation of how the member may place a fraud alert in the member's consumer reports to put the member's creditors on notice that the member may be a victim of fraud;

c. A recommendation that the member periodically obtain credit reports from each nationwide credit reporting agency and have information relating to fraudulent transactions deleted;

d. An explanation of how the member may obtain a credit report free of charge; and

e. Information about the availability of the FTC's online guidance regarding steps a consumer can take to protect against identity theft. The notice should encourage the member to report any incidents of identity theft to the FTC, and should provide the FTC's Web site address and toll-free telephone number that members may use to obtain the identity theft guidance and report suspected incidents of identity theft.[42]

2. NCUA encourages credit unions to notify the nationwide consumer reporting agencies prior to sending notices to a large number of members that include contact information for the reporting agencies.

C. Delivery of Member Notice

Member notice should be delivered in any manner designed to ensure that a member can reasonably be expected to receive it. For example, the credit union may choose to contact all members affected by telephone or by mail, or by electronic mail for those members for whom it has a valid e-mail address and who have agreed to receive communications electronically.

[42] Currently, the FTC Web site for the ID Theft brochure and the FTC Hotline phone number are *http://www.ftc.gov/idtheft* and 1–877–IDTHEFT. The credit union may also refer members to any materials developed pursuant to section 15(1)(b) of the FACT Act (educational materials developed by the FTC to teach the public how to prevent identity theft).

Part 749

Records Preservation Program and Record Retention Appendix

§ 749.0 What is covered in this part?

This part describes the obligations of all federally insured credit unions to maintain a records preservation program to identify, store and reconstruct vital records in the event that the credit union's records are destroyed. It establishes flexibility in the format credit unions may use for maintaining writings, records or information required by other NCUA regulations. The appendix also provides guidance concerning the appropriate length of time credit unions should retain various types of operational records.

§ 749.1 What are vital records?

Vital records include at least the following records, as of the most recent month-end:

(a) A list of share, deposit, and loan balances for each member's account which:

(1) Shows each balance individually identified by a name or number;

(2) Lists multiple loans of one account separately; and

(3) Contains information sufficient to enable the credit union to locate each member, such as address and telephone number, unless the board of directors determines that the information is readily available from another source.

(b) A financial report, which lists all of the credit union's asset and liability accounts and bank reconcilements.

(c) A list of the credit union's financial institutions, insurance policies, and investments. This information may be marked "permanent" and stored separately, to be updated only when changes are made.

§ 749.2 What must a credit union do with vital records?

The board of directors of a credit union is responsible for establishing a vital records preservation program within 6 months after its insurance certificate is issued. The vital records preservation program must contain procedures for storing duplicate vital records at a vital records center and must designate the staff member responsible for carrying out the vital records duties. Records must be stored every 3 months, within 30 days after the end of the 3-month period. Previously stored records may be destroyed when the current records are stored. The credit union must also maintain a records preservation log showing what records were stored, where the records were stored, when the records were stored, and who sent the records for storage. Credit unions, which have some or all of their records maintained by an off-site data processor, are considered to be in compliance for the storage of those records.

§ 749.3 What is a vital records center?

A vital records center is defined as a storage facility at any location far enough from the credit union's offices to avoid the simultaneous loss of both sets of records in the event of disaster.

§ 749.4 What format may the credit union use for preserving records?

Preserved records may be in any format that can be used to reconstruct the credit union's records. Formats include paper originals, machine copies, micro-film or fiche, magnetic tape, or any electronic format that accurately reflects the information in the record, remains accessible to all persons who are entitled to access by statute, regulation or rule of law, and is capable of being reproduced by transmission, printing or otherwise.

§ 749.5 What format may credit unions use for maintaining writings, records or information required by other NCUA regulations?

Various NCUA regulations require credit unions to maintain certain writings, records or information. Credit unions may use any format, electronic or other, for maintaining the writings, records or information that accurately reflects the

information, remains accessible to all persons who are entitled to access by statute, regulation or rule of law, and is capable of being reproduced by transmission, printing or otherwise. The credit union must maintain the necessary equipment or software to permit an examiner access to the records during the examination process.

Appendix A to Part 749—Record Retention Guidelines

Credit unions often look to NCUA for guidance on the appropriate length of time to retain various types of operational records. NCUA does not regulate in this area, but as an aid to credit unions it is publishing this appendix of suggested guidelines for record retention. NCUA recognizes that credit unions must strike a balance between the competing demands of space, resource allocation and the desire to retain all the records that they may need to conduct their business successfully. Efficiency requires that all records that are no longer useful be discarded, just as both efficiency and safety require that useful records be preserved and kept readily available.

A. What Format Should the Credit Union Use for Retaining Records?

NCUA does not recommend a particular format for record retention. If the credit union stores records on microfilm, microfiche, or in an electronic format, the stored records must be accurate, reproducible and accessible to an NCUA examiner. If records are stored on the credit union premises, they should be immediately accessible upon the examiner's request; if records are stored by a third party or off-site, then they should be made available to the examiner within a reasonable time after the examiner's request. The credit union must maintain the necessary equipment or software to permit an examiner to review and reproduce stored records upon request. The credit union should also ensure that the reproduction is acceptable for submission as evidence in a legal proceeding.

B. Who Is Responsible for Establishing a System for Record Disposal?

The credit union's board of directors may approve a schedule authorizing the disposal of certain records on a continuing basis upon expiration of specified retention periods. A schedule provides a system for disposal of records and eliminates the need for board approval each time the credit union wants to dispose of the same types of records created at different times.

C. What Procedures Should a Credit Union Follow When Destroying Records?

The credit union should prepare an index of any records destroyed and retain the index permanently. Destruction of records should ordinarily be carried out by at least two persons whose signatures, attesting to the fact that records were actually destroyed, should be affixed to the listing.

D. What Are the Recommended Minimum Retention Times?

Record destruction may impact the credit union's legal standing to collect on loans or defend itself in court. Since each state can impose its own rules, it is prudent for a credit union to consider consulting with local counsel when setting minimum retention periods. A record pertaining to a member's account that is not considered a vital record may be destroyed once it is verified by the supervisory committee. Individual Share and Loan Ledgers should be retained permanently. Records, for a particular period, should not be destroyed until both a comprehensive annual audit by the supervisory committee and a supervisory examination by the NCUA have been made for that period.

E. What Records Should Be Retained Permanently?

1. Official records of the credit union that should be retained permanently are:

(a) Charter, bylaws, and amendments.

(b) Certificates or licenses to operate under programs of various government agencies, such as a certificate to act as issuing agent for the sale of U.S. savings bonds.

(c) Current manuals, circular letters and other official instructions of a permanent character received from the NCUA and other governmental agencies.

2. Key operational records that should be retained permanently are:

(a) Minutes of meetings of the membership, board of directors, credit committee, and supervisory committee.

(b) One copy of each NCUA 5300 financial report or its equivalent.

(c) One copy of each supervisory committee comprehensive annual audit report and attachments.

(d) Supervisory committee records of account verification.

(e) Applications for membership and joint share account agreements.

(f) Journal and cash record.

(g) General ledger.

(h) Copies of the periodic statements of members, or the individual share and loan ledger. (A complete record of the account should be kept permanently.)

(i) Bank reconcilements.

(j) Listing of records destroyed.

F. What Records Should a Credit Union Designate for Periodic Destruction?

Any record not described above is appropriate for periodic destruction unless it must be retained to comply with the requirements of consumer protection regulations. Periodic destruction should be scheduled so that the most recent of the following records are available for the annual supervisory committee audit and the NCUA examination. Records that may be periodically destroyed include:

(a) Applications of paid off loans.

(b) Paid notes.

(c) Various consumer disclosure forms, unless retention is required by law.

(d) Cash received vouchers.

(e) Journal vouchers.

(f) Canceled checks.

(g) Bank statements.

(h) Outdated manuals, canceled instructions, and nonpayment correspondence from the NCUA and other governmental agencies.

Part 760

Loans in Areas Having Special Flood Hazards

§ 760.1 Authority, purpose, and scope.

(a) *Authority.* This part is issued pursuant to 12 U.S.C. 1757, 1789 and 42 U.S.C. 4012a, 4104a, 4104b, 4106, 4128.

(b) *Purpose.* The purpose of this part is to implement the requirements of the National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973, as amended (42 U.S.C. 4001–4129).

(c) *Scope.* This part, except for §§ 760.6 and 760.8, applies to loans secured by buildings or mobile homes located or to be located in areas determined by the Director of the Federal Emergency Management Agency to have special flood hazards. Sections 760.6 and 760.8 apply to loans secured by buildings or mobile homes, regardless of location.

§ 760.2 Definitions.

(a) *Act* means the National Flood Insurance Act of 1968, as amended (42 U.S.C. 4001–4129).

(b) *Credit union* means a Federal or State-chartered credit union that is insured by the National Credit Union Share Insurance Fund.

(c) *Building* means a walled and roofed structure, other than a gas or liquid storage tank, that is principally above ground and affixed to a permanent site, and a walled and roofed structure while in the course of construction, alteration, or repair.

(d) *Community* means a State or a political subdivision of a State that has zoning and building code jurisdiction over a particular area having special flood hazards.

(e) *Designated loan* means a loan secured by a building or mobile home that is located or to be located in a special flood hazard area in which flood insurance is available under the Act.

(f) *Director of FEMA* means the Director of the Federal Emergency Management Agency.

(g) *Mobile home* means a structure, transportable in one or more sections, that is built on a permanent chassis and designed for use with or without a permanent foundation when attached to the required utilities. The term *mobile home* does not include a recreational vehicle. For purposes of this part, the term *mobile home* means a mobile home on a permanent foundation. The term *mobile home* means a manufactured home as that term is used in the NFIP.

(h) *NFIP* means the National Flood Insurance Program authorized under the Act.

(i) *Residential improved real estate* means real estate upon which a home or other residential building is located or to be located.

(j) *Servicer* means the person responsible for:

(1) Receiving any scheduled, periodic payments from a borrower under the terms of a loan, including amounts for taxes, insurance premiums, and other charges with respect to the property securing the loan; and

(2) Making payments of principal and interest and any other payments from the amounts received from the borrower as may be required under the terms of the loan.

(k) *Special flood hazard area* means the land in the flood plain within a community having at least a one percent chance of flooding in any given year, as designated by the Director of FEMA.

(l) *Table funding* means a settlement at which a loan is funded by a contemporaneous advance of loan funds and an assignment of the loan to the person advancing the funds.

§ 760.3 Requirement to purchase flood insurance where available.

(a) *In general.* A credit union shall not make, increase, extend, or renew any designated loan unless the building or mobile home and any personal property securing the loan is covered by flood insurance for the term of the loan. The amount of insurance must be at least equal to the lesser of the outstanding principal balance of the designated loan or the maximum limit of coverage available for the particular type of property under the Act. Flood insurance coverage under the Act is limited to the overall value of the property securing the designated loan minus the value of the land on which the property is located.

(b) *Table funded loan.* A credit union that acquires a loan from a mortgage broker or other entity through table funding shall be considered to be making a loan for the purposes of this part.

§ 760.4 Exemptions.

The flood insurance requirement prescribed by § 760.3 does not apply with respect to:

(a) Any State-owned property covered under a policy of self-insurance satisfactory to the Director of FEMA, who publishes and periodically revises the list of States falling within this exemption; or

(b) Property securing any loan with an original principal balance of $5,000 or less and a repayment term of one year or less.

§ 760.5 Escrow requirement.

If a credit union requires the escrow of taxes, insurance premiums, fees, or any other charges for a loan secured by *residential* improved real estate or a mobile home that is made, increased, extended, or renewed on or after November 1, 1996, the credit union shall also require the escrow of all premiums and fees for any flood insurance required under § 760.3. The credit union, or a servicer acting on behalf of the credit union, shall deposit the flood insurance premiums on behalf of the borrower in an escrow account. This escrow account will be subject to escrow requirements adopted pursuant to section 10 of the Real Estate Settlement Procedures Act of 1974 (12 U.S.C. 2609) (RESPA), which generally limits the amount that may be maintained in escrow accounts for certain types of loans and requires escrow account statements for those accounts, only if the loan is otherwise subject to RESPA. Following receipt of a notice from the Director of FEMA or other provider of flood insurance that premiums are due, the credit union, or a servicer acting on behalf of the credit union, shall pay the amount owed to the insurance provider from the escrow account by the date when such premiums are due.

§ 760.6 Required use of standard flood hazard determination form.

(a) Use of form. A credit union shall use the standard flood hazard determination form developed by the Director when determining whether the building or mobile home offered as collateral security for a loan is or will be located in a special flood hazard area in which flood insurance is available under the Act. The standard flood hazard determination form may be used in a printed, computerized, or electronic manner. A credit union may obtain the standard flood hazard determination form from FEMA, P.O. Box 2012, Jessup, MD 20794–2012.

(b) *Retention of form.* A credit union shall retain a copy of the completed standard flood hazard determination form, in either hard copy or electronic form, for the period of time the credit union owns the loan.

§ 760.7 Forced placement of flood insurance.

If a credit union, or a servicer acting on behalf of the credit union, determines, at any time during the term of a designated loan that the building or mobile home and any personal property securing the designated loan is not covered by flood insurance or is covered by flood insurance in an amount less than the amount required under § 760.3, then the credit union or its servicer shall notify the borrower that the borrower should obtain flood insurance, at the borrower's expense, in an amount at least equal to the amount required under § 760.3, for the remaining term of the loan. If the borrower fails to obtain flood insurance within 45 days after notification, then the credit union or its servicer shall purchase insurance on the borrower's behalf. The credit union or its servicer may charge the borrower for the cost of premiums and fees incurred in purchasing the insurance.

§ 760.8 Determination fees.

(a) *General.* Notwithstanding any Federal or State law other than the Flood Disaster Protection Act of 1973, as amended (42 U.S.C. 4001–4129), any credit union, or a servicer acting on behalf of the credit union, may charge a reasonable fee for determining whether the building or mobile home securing the loan is located or will be located in a special flood hazard area. A determination fee may also include, but is not limited to, a fee for life-of-loan monitoring.

(b) *Borrower fee.* The determination fee authorized by paragraph (a) of this section may be charged to the borrower if the determination:

(1) Is made in connection with a making, increasing, extending, or renewing of the loan that is initiated by the borrower;

(2) Reflects the Director of FEMA's revision or updating of floodplain areas or flood-risk zones;

(3) Reflects the Director of FEMA's publication of a notice or compendium that:

(i) Affects the area in which the building or mobile home securing the loan is located; or

(ii) By determination of the Director of FEMA, may reasonably require a determination whether the building or mobile home securing the loan is located in a special flood hazard area; or

(4) Results in the purchase of flood insurance coverage by the credit union or its servicer on behalf of the borrower under § 760.7.

(c) *Purchaser or transferee fee.* The determination fee authorized by paragraph (a) of this section may be charged to the purchaser or transferee of a loan in the case of the sale or transfer of the loan.

§ 760.9 Notice of special flood hazards and availability of Federal disaster relief assistance.

(a) *Notice requirement.* When a credit union makes, increases, extends, or renews a loan secured by a building or a mobile home located or to be located in a special flood hazard area, the credit union shall mail or deliver a written notice to the borrower and to the servicer in all cases whether or not flood insurance is available under the Act for the collateral securing the loan.

(b) *Contents of notice.* The written notice must include the following information:

(1) A warning, in a form approved by the Director of FEMA, that the building or the mobile home is or will be located in a special flood hazard area;

(2) A description of the flood insurance purchase requirements set forth in section 102(b) of the Flood Disaster Protection Act of 1973, as amended (42 U.S.C. 4012a(b));

(3) A statement, where applicable, that flood insurance coverage is available under the NFIP and may also be available from private insurers; and

(4) A statement whether Federal disaster relief assistance may be available in the event of damage to the building or mobile home caused by flooding in a Federally-declared disaster.

(c) *Timing of notice.* The credit union shall provide the notice required by paragraph (a) of this section to the borrower within a reasonable time before the completion of the transaction and to the servicer as promptly as practicable after the credit union provides notice to the borrower and in any event no later than the time the credit union provides other similar notices to the servicer concerning hazard insurance and taxes. Notice to the servicer may be made electronically or may take the form of a copy of the notice to the borrower.

(d) *Record of receipt.* The credit union shall retain a record of the receipt of the notices by the borrower and the servicer for the period of time the credit union owns the loan.

(e) *Alternate method of notice.* Instead of providing the notice to the borrower required by paragraph (a) of this section, a credit union may obtain satisfactory written assurance from a seller or lessor that, within a reasonable time before the completion of the sale or lease transaction, the seller or lessor has provided such notice to the purchaser or lessee. The credit union shall retain a record of the written assurance from the seller or lessor for the period of time the credit union owns the loan.

(f) *Use of prescribed form of notice.* A credit union will be considered to be in compliance with the requirement for notice to the borrower of this section providing written notice to the borrower containing the language presented in the appendix to this part within a reasonable time before the completion of the transaction. The notice presented in the appendix to this part satisfies the borrower notice requirements of the Act.

§ 760.10 Notice of servicer's identity.

(a) *Notice requirement.* When a credit union makes, increases, extends, renews, sells, or transfers a loan secured by a building or mobile home located or to be located in a special flood hazard area, the credit union shall notify the Director of FEMA (or the Director's designee) in writing of the identity of the servicer of the loan. The Director of FEMA has designated the insurance provider to receive the credit union's notice of the servicer's identity. This notice may be provided electronically if electronic transmission is satisfactory to the Director of FEMA's designee.

(b) *Transfer of servicing rights.* The credit union shall notify the Director of FEMA (or the Director's designee) of any change in the servicer of a loan described in paragraph (a) of this section within 60 days after the effective date of the change. This notice may be provided electronically if electronic transmission is satisfactory to the Director of FEMA's designee. Upon any change in the servicing of a loan described in paragraph (a) of this section, the duty to provide notice under this paragraph (b) shall transfer to the transferee servicer.

Appendix to Part 760—Sample Form of Notice of Special Flood Hazards and Availability of Federal Disaster Relief Assistance

We are giving you this notice to inform you that:

The building or mobile home securing the loan for which you have applied is or will be located in an area with special flood hazards.

The area has been identified by the Director of the Federal Emergency Management Agency (FEMA) as a special flood hazard area using FEMA's *Flood Insurance Rate Map* or the *Flood Hazard Boundary Map* for the following community: _____. This area has at least a one percent (1%) chance of a flood equal to or exceeding the base flood elevation (a 100-year flood) in any given year. During the life of a 30-year mortgage loan, the risk of a 100-year flood in a special flood hazard area is 26 percent (26%).

Federal law allows a lender and borrower jointly to request the Director of FEMA to review the determination of whether the property securing the loan is located in a special flood hazard area. If you would like to make such a request, please contact us for further information.

_____ The community in which the property securing the loan is located participates in the National Flood Insurance Program (NFIP). Federal law will not allow us to make you the loan that you have applied for if you do not purchase flood insurance. The flood insurance must be maintained for the life of the loan. If you fail to purchase or renew flood insurance on the property, Federal law authorizes and requires us to purchase the flood insurance for you at your expense.

- Flood insurance coverage under the NFIP may be purchased through an insurance agent who will obtain the policy either directly through the NFIP or through an insurance company that participates in the NFIP. Flood insurance also may be available from private insurers that do not participate in the NFIP.
- At a minimum, flood insurance purchased must cover *the lesser of*:

(1) the outstanding principal balance of the loan; *or*

(2) the maximum amount of coverage allowed for the type of property under the NFIP.

Flood insurance coverage under the NFIP is limited to the overall value of the property securing the loan minus the value of the land on which the property is located.

- Federal disaster relief assistance (usually in the form of a low-interest loan) may be available for damages incurred in excess of your flood insurance if your community's participation in the NFIP is in accordance with NFIP requirements.

_____ Flood insurance coverage under the NFIP is not available for the property securing the loan because the community in which the property is located does not participate in the NFIP. In addition, if the non-participating community has been identified for at least one year as containing a special flood hazard area, properties located in the community will not be eligible for Federal disaster relief assistance in the event of a Federally-declared flood disaster.

Part 790

Description of NCUA; Requests for Agency Action.

§ 790.1 Scope.

This Part contains a description of NCUA's organization and the procedures for public requests for action by the Board. Part 790 pertains to the practices of the National Credit Union Administration (NCUA) only and does not apply to credit union operations.

§ 790.2 Central and Regional Office Organization.

(a) *General organization.* NCUA is composed of the Board with a Central Office in Alexandria, Virginia, five Regional Offices, the Asset Management and Assistance Center, the Community Development Revolving Loan Program, and the NCUA Central Liquidity Facility (CLF).

(b) *Central Office.* The Central Office address is NCUA, 1775 Duke St., Alexandria, Virginia 22314–3428.

(1) *The NCUA Board.* NCUA is managed by its Board. The Board consists of three members appointed by the President, with the advice and consent of the Senate, for six-year terms. One Board member is designated by the President to be Chairman of the Board. A second member is designated by the Board to be Vice-Chairman. The Board is also responsible for management of the National Credit Union Share Insurance Fund (NCUSIF) and serves as the Board of Directors of the CLF. The Chairman shall be the spokesman for the Board and shall represent the Board and the NCUA in its official relations with other branches of the government.

(2) *Secretary of the Board.* The Secretary of the Board is responsible for the secretarial functions of the Board. The Secretary's responsibilities include preparing agendas for meetings of the Board, preparing and maintaining the minutes for all official actions taken by the Board, and executing and maintaining all documents adopted by the Board or under its direction. The Secretary also serves as the Secretary of the CLF.

(3) *Asset Management and Assistance Center.* The President of the Asset Management and Assistance Center (AMAC) is responsible for monitoring, evaluating, disposing, and/or managing major assets acquired by NCUA; responsible for managing involuntary liquidations for all federally insured credit unions placed into involuntary liquidation including the orderly processing of payments of share insurance, sale and/or collection of loan portfolios, liquidation of other assets and achieving other recoveries, payments to creditors, and distributions to any uninsured shareholders. The President, AMAC, serves as a primary consultant with the regional offices on asset sales or purchases to restructure problem case credit unions, as technical expert to evaluate specific areas of credit union operations, and as instructor in training classes; responsible to prepare and negotiate bond claims; responsible to manage or assist in the management of conservatorships. The address of AMAC is 4807 Spicewood Springs Road, Suite 5100, Austin, Texas 78759–8490.

(4) *Office of Chief Financial Officer.* NCUA's chief financial officer is in charge of budgetary, accounting and financial matters for the NCUA, including responsibility for submitting annual budget and staffing requests for approval by the Board and, as required, by the Office of Management and Budget; for managing NCUA's budgetary resources; for managing the operations of the National Credit Union Share Insurance Fund (NCUSIF) to include accounting, financial reporting and the collection and payment of capitalization deposits, insurance premiums and insurance dividends; for collecting annual operating fees from federal credit unions, for maintaining NCUA's accounting system and accounting records; for processing payroll, travel, and accounts payable disbursements; and for preparing internal and external financial reports. The Director is also responsible for providing NCUA's executive offices and Regional Directors with administrative services, including: agency security; contracting and procurement; management of equipment and supplies; acquisition; printing; and warehousing and distribution.

(5) *Office of Examination and Insurance.*

(i) The Director of the Office of Examination and Insurance: Formulates standards and procedures for examination and supervision of the community of federally insured credit unions, and reports to the Board on the performance of the examination program; manages the risk to the NCUSIF, to include overseeing the NCUSIF Investment Committee, monitoring the adequacy of NCUSIF reserves, analyzing the reasons for NCUSIF losses, formulating policies and procedures regarding the supervision of financially troubled credit unions, and evaluating certain requests for special assistance pursuant to Section 208 of the Federal Credit Union Act and for certain proposed administrative actions regarding federally-insured credit unions; serves as the Board expert on accounting principles and standards and on auditing standards; represents NCUA at meetings with the American Institute of Certified Public Accountants (AICPA), Federal Financial Institutions Examination Council (FFIEC) and General Accounting Office (GAO); and collects data and provides statistical reports. The Director is also responsible for developing and conducting research in support of NCUA programs, and for preparing reports on research activities for the information and use of agency staff, credit union officials, state credit union supervisory authorities, and other governmental and private groups.

(ii) *NCUA Central Liquidity Facility (CLF).* The CLF was created to improve general financial stability by providing funds to meet the liquidity needs of credit unions. It is a mixed-ownership government corporation under the Government Corporation Control Act (31 U.S.C. 9101 *et seq.*). The CLF is managed by the President, under the general supervision of the NCUA Board which serves as the CLF Board of Directors. The Chairman of the NCUA Board serves as the Chairman of the CLF Board of Directors. The Secretary of the NCUA Board serves as the Secretary of the CLF Board of Directors. The NCUA Board shall appoint the CLF President and Vice President.

(6) *Office of the Executive Director.* The Executive Director reports to the entire NCUA Board. The Executive Director translates NCUA Board policy decisions into workable programs, delegates responsibility for these programs to appropriate staff members, and coordinates the activities of the senior executive staff, which includes: the General Counsel; the Regional Directors; and the Office Directors for Administration, Chief Financial Officer, Examination and Insurance, Human Resources, Chief Information Officer, and Public and Congressional Affairs. Because of the nature of the attorney/client relationship between the Board and General Counsel, the General Counsel may be directed by the Board not to disclose discussions and/or assignments with anyone, including the Executive Director. The Executive Director is otherwise to be privy to all matters within senior executive staff's responsibility. The Executive Director also serves as the agency's Director of Equal Employment Opportunity (EEO).

(7) *Office of General Counsel.* The General Counsel reports to the entire NCUA Board. The General Counsel has overall responsibility for all legal matters affecting NCUA and for liaison with the Department of Justice. The General Counsel represents NCUA in all litigation and administrative hearings when such direct representation is permitted by law and, in other instances, assists the attorneys responsible for the conduct of such litigation. The General Counsel also provides NCUA with legal advice and opinions on all matters of law, and the public with interpretations of the Federal Credit Union Act, the NCUA Rules and Regulations, and other NCUA Board directives. The General Counsel has responsibility for the drafting, reviewing, and publication of all items which appear in the **Federal Register**, including rules, regulations, and notices required by law. The office has responsibility for processing Freedom of Information requests and appeals and carrying out the Board's responsibilities under the Privacy Act.

(8) *The Office of Human Resources.* The Office of Human Resources provides a comprehensive program for the management of NCUA's human resources. This is done in support of NCUA's goal to recruit, develop, and retain a quality and representative workforce. The Director is responsible for managing NCUA's compensation program, for facilitating good organization design, for staffing positions through recruitment and merit promotion programs, and for maintaining an automated personnel records system. The Director is also responsible for the Board's performance management, incentive awards, employee assistance, and benefit programs. These programs are geared to foster healthy employee/management relations and to provide employees

with good working conditions. The Director is also responsible for providing a comprehensive program for the training and development of NCUA's staff, including developing policy consistent with the Government Employees Training Act; providing training opportunities equitably so that all employees have the skills necessary to help meet the agency's mission; evaluating the agency's training and development efforts; and ensuring that the agencies training monies are spent in a cost efficient manner and in accordance with the law.

(9) *Office of Chief Information Officer.* The Chief Information Officer has responsibility for the management and administration of NCUA's information resources. This includes the development, maintenance, operation, and support of information systems which directly support the Agency's mission, maintaining and operating the Agency's information processing infrastructure, responding to requests for releaseable Agency information, and insuring all related material security and integrity risks are recognized and controlled as much as possible. The Chief Information Officer is also responsible for carrying out the Board's responsibilities under the Paperwork Reduction Act and in directing NCUA responses to reporting requirements.

(10) *Office of the Inspector General.* The Inspector General reports directly to the Board and provides semiannual reports regarding audit and investigation activities to the Board and the Congress. The Inspector General is responsible for: (a) conducting independent audits and investigations of all NCUA programs and functions to promote efficiency; (b) reviewing policies and procedures to evaluate controls to prevent fraud, waste, and abuse; and (c) reviewing existing and proposed legislation and regulations to evaluate their impact on the economic and efficient administration of the Agency.

(11) *Office of Public and Congressional Affairs.* The Director of the Office of Public and Congressional Affairs is responsible for maintaining NCUA's relationship with the public and the media; for liaison with the U.S. Congress, and with other Executive Branch agencies concerning legislative matters; and for the analysis and development of legislative proposals and public affairs programs. The Director is also responsible for providing NCUA's executive offices and Regional Directors with graphics.

(12) *Office of Credit Union Development.* This Office is responsible for coordinating NCUA policy as it relates to community development credit unions, including those credit unions designated as "low-income." The Office administers the Community Development Revolving Loan Program for Credit Unions (Program). This Program was funded from a congressional appropriation and serves as a loan and technical assistance vehicle for low-income credit unions. The Office Director serves as Program Chairman and authorizes loans and technical assistance to participating credit unions. The Program is governed by part 705 of subchapter A of this chapter.

(13) *Office of Strategic Program Support and Planning.* This office is responsible for providing interest rate risk assessment, investment expertise and advice to the Board and agency staff and conducting research and development to assess risk areas of emerging products, delivery systems, infrastructure issues, and investments. The office provides leadership, vision and focus on the internal and external environment related to the development of the agency's long range planning and implementation of the Government Performance Act of 1993. The office provides a macro view of the industry in a way that can be integrated into the day-to-day program functions. A working relationship is maintained with the financial marketplace to develop resources available to the NCUA and keep abreast of product initiatives. The NCUA Investment Hotline housed in this office is a toll-free number that is available to examiners, credit unions and financial product vendors to ask investment related questions. The Hotline provides NCUA an opportunity to be aware of current investment issues as they arise in credit unions and has permitted NCUA to become proactive, rather than reactive, to such issues. In addition, investment officers advise agency management on the purchase of authorized investments for the NCUSIF and the CLF.

(14) *Office of Corporate Credit Unions.* The Director, Office of Corporate Credit Unions, manages NCUA's corporate credit union program in accordance with established policies and the corporate regulation. The Director's duties include directing chartering, examination and supervision programs to promote and assure safety and soundness; managing NCUA's corporate resources to meet program objectives in the most economical and practical manner;

and maintaining good public relations with public, private and governmental organizations, corporate credit union officials, credit union organizations, and other groups which have an interest in corporate credit union matters.

(c) *Regional Offices.*

(1) NCUA's programs are conducted through five Regional Offices:

(2) A Regional Director is in charge of each Regional Office. The Regional Director manages NCUA's programs in the Region assigned in accordance with established policies. This person's duties include: directing chartering, insurance, examination, and supervision programs to promote and assure safety and soundness; managing regional resources to meet program objectives in the most economical and practical manner; and maintaining good public relations with public, private, and governmental organizations, Federal credit union officials, credit union organizations, and other groups which have an interest in credit union matters in the assigned Region. The Director maintains liaison and cooperation with other regional offices of Federal departments and agencies, state agencies, city and county officials, and other governmental units that affect credit unions. The Regional Director is aided by an Associate Regional Director for Operations and Associate Regional Director for Programs. Staff working in the Regional Office report to the Associate Regional Director for Operations. Each region is divided into examiner districts, each assigned to a Supervisory Credit Union Examiner; groups of examiners are directed by a Supervisory Credit Union Examiner, each of whom in turn reports directly to the Associate Regional Director for Programs.

Region No.	Area Within Region	Office Address
I	Connecticut, Maine, Massachusetts, Michigan, New Hampshire, New York, Rhode Island, Vermont	9 Washington Square Washington Avenue Extension Albany, NY 12205–5512
II	Delaware, District of Columbia, Maryland, New Jersey, Pennsylvania, Virginia, West Virginia	1775 Duke Street Suite 4206 Alexandria, VA 22314–3437
III	Alabama, Florida, Georgia, Indiana, Kentucky, Mississippi, North Carolina, Ohio, Puerto Rico, South Carolina, Tennessee, Virgin Islands	7000 Central Parkway Suite 1600 Atlanta, GA 30328–4598
IV	Arkansas, Illinois, Iowa, Kansas, Louisiana, Minnesota, Missouri, Nebraska, North Dakota, Oklahoma, South Dakota, Texas, Wisconsin	4807 Spicewood Springs Road Suite 5200 Austin, TX 78759–8490
V	Alaska, Arizona, American Samoa, California, Colorado, Guam, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, Wyoming	1230 W. Washington Street Suite 301 Tempe, AZ 85281

§ 790.3 Requests for Action.

Except as otherwise provided by NCUA regulation, all applications, requests, and submittals for action by the NCUA shall be in writing and addressed to the appropriate office described in § 790.2. This will usually be one of the Regional Offices. In instances where the appropriate office cannot be determined, requests should be sent to the Office of Public and Congressional Affairs.

Part 791

Rules of NCUA Board Procedure; Promulgation of NCUA Rules and Regulations; Public Observation of NCUA Board Meetings

Subpart A—Rules of NCUA Board Procedure

§ 791.1 Scope.

The rules contained in this Subpart are the rules of procedure governing how the Board conducts its business. These rules concern the Board's exercise of its authority to act on behalf of NCUA; the conduct, scheduling and subject matter of Board meetings; and the recording of Board action.

§ 791.2 Number of Votes Required for Board Action.

The agreement of at least two of the three Board members is required for any action by the Board.

§ 791.3 Voting by Proxy.

Proxy voting shall not be allowed for any action by the Board.

§ 791.4 Methods of Acting.

(a) *Board Meeting.*

(1) *Applicability of the Sunshine Act.* The Government in the Sunshine Act (5 U.S.C. 552b, "Sunshine Act") requires that joint deliberations of the Board be held in accordance with its open meetings provisions (5 U.S.C. 552b(b)–(f)). (Subpart C of this Part contains NCUA's regulations implementing the Sunshine Act.)

(2) *Presiding officer.* The Chairman is the presiding officer, and in the Chairman's absence, the designated Vice Chairman shall preside. The presiding officer shall make procedural rulings. Any Board member may appeal a ruling made by the presiding officer. The appeal of a procedural ruling by the presiding officer shall be immediately considered by the Board, and a majority decision by the Board shall decide the procedural ruling.

(b) *Notation voting.* Notation voting is the circulation of written memoranda and voting sheets to the office of each Board member simultaneously and the tabulation of responses.

(1) *Matters that may be Decided by Notation Voting.* Notation voting may be used only for routine matters.

(2) *Notation Vote Sheets.* Notation vote sheets will be used to record the vote tally on a notation vote. The Secretary of the Board has administrative responsibility over notation voting, including the authority to establish deadlines for voting, receive notation vote sheets, count votes, and determine whether further action is required.

(3) *Veto of notation voting.* In view of public policy for openness reflected in the Sunshine Act, each Board member is authorized to veto the use of notation voting for the consideration of any particular matter, and thus require that the matter be placed on the agenda of the next regularly scheduled Board meeting that is held at least ten days after the date of the veto.

(4) *Disclosure of Result.* A record is to be maintained of Board transactions by use of the notation voting procedure. Public disclosure of this record is determined by the provisions of the Freedom of Information Act (5 U.S.C. § 552).

§ 791.5 Scheduling of Board Meetings.

(a) *Meeting Calls.*

(1) *Regular Meetings.* The Board will hold regular meetings each month unless there is no business or a quorum is not available. The Secretary of the Board will coordinate the dates for meetings.

(2) *Special meetings.* The Chairman shall call special meetings either on the Chairman's own initiative or within fourteen days of a request from two Board members that is accompanied by an NCUA B–1 form and a Board Action Memorandum that states the specific issue(s) or action(s) to be considered by the Board.

(b) *Notice of Meetings.*

(1) *Notifying the Public.* The Sunshine Act and Subpart C set forth the procedures for notifying the public of Board meetings.

(2) *Notifying Board Members.*

(i) *Special Meetings.* Except in cases of emergency as determined by a majority of the Board, each Board member is entitled to receive notice of any special meeting at least twenty-

four hours in advance of such meeting. The notice shall set forth the place, day, hour, and nature of business to be transacted at the meeting. In cases of emergency, a record of the vote, including a statement explaining the decision that an emergency exists, will be maintained.

(ii) *Regular Meetings.* Each Board member entitled to receive notice of the agenda and/or notice of any changes in the subject matter of such meetings concurrent with the public release of such notices under the Sunshine Act. Each Board member shall be entitled to at least twenty-four hours advance notice of the consideration of a particular subject matter, except in cases of emergency as determined by a majority of the Board. In cases of emergency, a record of the vote, including a statement explaining the decision that an emergency exists, will be maintained.

§ 791.6 Subject Matter of a Meeting.

(a) *Agenda.* The Chairman is responsible for the final order of each meeting agenda. Items shall be placed on the agenda by determination of the Chairman or, at the request of any Board Member, an item will be placed on the agenda of the next regularly scheduled meeting provided that the request is submitted at least ten days in advance of the next regularly scheduled meeting and is accompanied by an NCUA B–1 form and a Board Action Memorandum that states the specific issue(s) or action(s) to be considered by the Board.

(b) *Submission of Recommended Agenda Items.* Recommended agenda items may be submitted to the Secretary of the Board by Board members, the Executive Staff (which includes all Office Directors and President of the Central Liquidity Facility), and Regional Directors.

Subpart B—Promulgation of NCUA Rules and Regulations

§ 791.7 Scope.

The rules contained in this Subpart B pertain to the promulgation of NCUA Rules and Regulations.

§ 791.8 Promulgation of NCUA rules and regulations.

(a) NCUA's procedures for developing regulations are governed by the Administrative Procedure Act (5 U.S.C. 551 *et seq.*), the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), and NCUA's policies for the promulgation of rules and regulations as set forth in its Interpretive Ruling and Policy Statement 87–2 as amended by Interpretive Ruling and Policy Statement 03–2.

(b) *Proposed Rulemaking.* Notices of proposed rulemaking are published in the Federal Register except as specified in paragraph (d) or as otherwise provided by law. A notice of proposed rulemaking may also be identified as a "request for comments" or as a "proposed rule." The notice will include:

(1) a statement of the nature of the rulemaking proceedings;

(2) reference to the authority under which the rule is proposed;

(3) either the terms or substance of the proposed rule or a description of the subjects and issues involved; and

(4) a statement of the effect of the proposed rule on state-chartered federally-insured credit unions.

(c) *Public Participation.* After publication of notice of proposed rulemaking, interested persons will be afforded the opportunity to participate in the making of the rule through the submission of written data, views, or arguments, delivered within the time prescribed in the notice of proposed rulemaking, to the Secretary, NCUA Board, 1775 Duke Street, Alexandria, VA 22314–3428. Interested persons may also petition the Board for the issuance, amendment, or repeal of any rule by mailing such petition to the Secretary of the Board at the address given in this section.

(d) *Exceptions to Notice.* The following are not subject to the notice requirement contained in paragraph (b) of this section:

(1) matters relating to agency management or personnel or to public property, loans, grants, benefits, or contracts;

(2) when persons subject to the proposed rule are named and either personally served or otherwise have actual notice thereof in accordance with law;

(3) interpretive rules, general statements of policy, or rules of agency organization, procedure or practice, unless notice or hearing is required by statute; and

(4) if the Board, for good cause, finds (and incorporates the finding and a brief statement therefor in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest, unless notice or hearing is required by statute.

(e) *Effective Dates.* No substantive rule issued by NCUA shall be effective less than 30 days after its publication in the Federal Register, except that this requirement may not apply to:

(1) rules which grant or recognize an exemption or relieve a restriction;

(2) interpretive rules and statements of policy; or

(3) any substantive rule which the Board makes effective at an earlier date upon good cause found and published with such rule.

Subpart C—Public Observation of NCUA Board Meetings Under the Sunshine Act

§ 791.9 Scope.

This subpart contains regulations implementing subsections (b) through (f) of the "Government in the Sunshine Act" [5 U.S.C. § 552b]. The primary purpose of these regulations is to provide the public with the fullest access authorized by law to the deliberations and decisions of the Board, while protecting the rights of individuals and preserving the ability of the agency to carry out its responsibilities.

§ 791.10 Definitions.

For the purpose of this subpart:

(a) "agency" means the National Credit Union Administration;

(b) "Board" means the National Credit Union Administration Board, whose members were appointed by the President with the advice and consent of the Senate;

(c) "subdivision of the Board" means a group composed of two Board members authorized by the Board to act on behalf of the agency;

(d) "meeting" means any deliberations by two or more members of the Board or any subdivision of the Board that determine or result in the joint conduct or disposition of official agency business with the exception of:

(1) deliberations to determine whether a meeting or a portion thereof will be open or closed to public observation and whether information regarding closed meetings will be withheld from public disclosure;

(2) deliberations to determine whether or when to schedule a meeting; and

(3) infrequent dispositions of official agency business by sequential circulation of written recommendations to individual Board members ("notation voting procedure"), provided the votes of each Board member and the action taken are recorded for each matter and are publicly available, unless exempted from disclosure pursuant to 5 U.S.C. § 552 (the Freedom of Information Act);

(e) "public observation" means that a member or group of the public may listen to and observe any open meeting and may record in an unobtrusive manner any portion of that meeting by use of a camera or any other electronic device, but shall not participate in any meeting unless authorized by the Board;

(f) "public announcement" or "publicly announce" means reasonable efforts under the particular circumstances to fully inform the public, especially those individuals who have expressed interest in the subject matters to be discussed or the decisions of the agency;

(g) "Sunshine Act" means the open meeting provisions of the "Government in the Sunshine Act" (5 U.S.C. § 552b).

§ 791.11 Open Meetings.

Except as provided in Section 791.12(a), any portion of any meeting of the Board shall be open to public observation. The Board, and any subdivision of the Board, shall jointly conduct official agency business only in accordance with this subpart.

§ 791.12 Exemptions.

(a) Under the procedures specified in Section 791.14, the Board may close a meeting or any portion of a meeting from public observation or may withhold information pertaining to such meetings provided the Board has properly determined that the public interest does not require otherwise and that the meeting (or any portion thereof) or the disclosure of meeting information is likely to:

(1) disclose matters that are (i) specifically authorized under criteria established by an Executive Order to be kept secret in the interests of national defense or foreign policy, and (ii) in fact properly classified pursuant to such Executive Order;

(2) relate solely to internal personnel rules and practices;

(3) disclose matters specifically exempted from disclosure by statute (other than Section 552 of Title 5 of the United States Code, the Freedom of Information Act), provided that such statute (i) requires that the matters be withheld from the public in such a manner as to leave no discretion on the issue, or (ii) establishes par-

ticular criteria for withholding or refers to particular types of matters to be withheld;

(4) disclose trade secrets and commercial or financial information obtained from a person and privileged or confidential;

(5) involve accusing any person of a crime, or formally censuring any person;

(6) disclose information of a personal nature where disclosure would constitute a clearly unwarranted invasion of personal privacy;

(7) disclose investigatory records compiled for enforcement purposes, or information which if written would be contained in such records, but only to the extent that the production of such records or information would (i) interfere with enforcement proceedings, (ii) deprive a person of a right to a fair trial or an impartial adjudication, (iii) constitute an unwarranted invasion of personal privacy, (iv) disclose the identity of a confidential source and, in the case of a record compiled by a criminal law enforcement authority in the course of a criminal investigation, or by a Federal agency conducting a lawful national security intelligence investigation, confidential information furnished only by the confidential source, (v) disclose investigation techniques and procedures, or (vi) endanger the life or physical safety of law enforcement personnel;

(8) disclose information contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of Federal agencies responsible for the regulation or supervision of financial institutions;

(9) disclose information the premature disclosure of which would be likely to (A)(i) lead to significant speculation in currencies, securities, or commodities, or (ii) significantly endanger the stability of any financial institution, or (B) be likely to significantly frustrate implementation of a proposed action, except that this subparagraph shall not apply in any instance where the Board has already disclosed to the public the content or nature of its proposed action, or where the Board is required by law to make such disclosure on its own initiative prior to taking final action on such proposal; or

(10) specifically concern the issuance of a subpoena, participation in a civil action or proceeding, an action in a foreign court or international tribunal, or an arbitration, or the initiation, conduct or disposition of a particular case of formal agency adjudication pursuant to the procedures in Section 554 of Title 5 of the United States Code or otherwise involving a determination on the record after opportunity for a hearing.

(b) Prior to closing a meeting whose discussions are likely to fall within the exemptions stated in paragraph (a) of this Section, the Board will balance the public interest in observing the deliberations of an exemptible matter and the agency need for confidentiality of the exemptible matter. In weighing these interests, the Board is assisted by the General Counsel as provided in Section 791.16, by expressions of the public interest set forth in requests for open meetings as provided by Section 791.15(b), and by the brief staff analysis of public interest which will accompany each staff recommendation that an agenda item be considered in a closed meeting.

§ 791.13 Public Announcement of Meetings.

(a) Except as otherwise provided in this Section, the Board shall, for each meeting, make a public announcement, at least one week in advance of the meeting, of the time, place and subject matter of the meeting, whether it will be open or closed to public observation, and the name and telephone number of the Secretary of the Board or the person designated by the Board to respond to requests for information about the meeting.

(b) Advance notice is required unless a majority of the members of the Board determine by a recorded vote that agency business requires that a meeting be called at an earlier date, in which case, the information to be announced in paragraph (a) of this Section shall be publicly announced at the earliest practicable time.

(c) A change, including a postponement or a cancellation, in the time or place of a meeting after a published announcement may be made only if announced at the earliest practicable time.

(d) A change in or deletion of the subject matter of a meeting or any portion of a meeting or a redetermination to open or close a meeting or any portion of a meeting after a published announcement may be made only if (1) a majority of the Board determines by recorded vote that agency business so requires and that no earlier announcement of the change was possible and (2) public announcement of the change and of the vote of each member on such change shall be made at the earliest practicable time.

(e) Each meeting announcement or amendment thereof shall be posted on the Public Notice Bulletin Board in the reception area of the agency

headquarters and may be made available by other means deemed desirable by the Board. Immediately following each public announcement required by this Section, the stated information shall be submitted to the Federal Register for publication.

(f) No announcement shall contain information which is determined to be exempt from disclosure under Section 791.12(a).

(g) The agency shall maintain a mailing list of names and addresses of all persons who wish to receive copies of agency announcements of meetings open to public observation and amendments to such announcements. Requests to be placed on the mailing list should be made by telephoning or by writing to the Secretary of the Board.

§ 791.14 Regular Procedure for Closing Meeting Discussions or Limiting the Disclosure of Information.

(a) A decision to close any portion of a meeting and to withhold information about any portion of a meeting closed pursuant to Section 791.12(a) will be taken only when a majority of the entire Board votes to take such action. In deciding whether to close a meeting or any portion of a meeting or to withhold information, the Board shall independently consider whether the public interest requires an open meeting. A separate vote of the Board will be taken and recorded for each portion of a meeting to be closed to public observation pursuant to Section 791.12(a) or to withhold information from the public pursuant to Section 791.12(a). A single vote may be taken and recorded with respect to a series of meetings, or any portions of meetings which are proposed to be closed to the public, or with respect to any information concerning the series of meetings, so long as each meeting in the series involves the same particular matters and is scheduled to be held no more than thirty days after the initial meeting in such series. No proxies shall be allowed.

(b) Any person whose interests may be directly affected by any portion of a meeting for any of the reasons stated in subparagraphs (5), (6) or (7) of Section 791.12(a) may request that the Board close such portion of the meeting. After receiving notice of a person's desire for any specified portion of a meeting to be closed, the Board, upon a request by one member, will decide by recorded vote whether to close the relevant portion or portions of the meeting. This procedure applies to requests received either prior or subsequent to the announcement of a decision to hold an open meeting.

(c) Within one day after any vote is taken pursuant to paragraphs (a) or (b) of this Section, the Board shall make publicly available a written copy of the vote taken indicating the vote of each Board member. Except to the extent that such information is withheld and exempt from disclosure, for each meeting or any portion of a meeting closed to the public, the Board shall make publicly available within one day after the required vote, a written explanation of its action, together with a list of all persons expected to attend the closed meeting and their affiliation. The list of persons to attend need not include the names of individual staff, but shall state the offices of the agency expected to participate in the meeting discussions.

§ 791.15 Requests for Open Meeting.

(a) Following any announcement that the Board intends to close a meeting or any portion of any meeting, any person may make a written request to the Secretary of the Board that the meeting or a portion of the meeting be open. The request shall be circulated to the members of the Board, and the Board, upon the request of one member, shall reconsider its action under Section 791.14 before the meeting or before discussion of the matter at the meeting. If the Board decides to open a portion of a meeting proposed to be closed, the Board shall publicly announce its decision in accordance with Section 791.13(e). If no request is received from a Board member to reconsider the decision to close a meeting or portion thereof prior to the meeting discussion, the Chairman of the Board shall certify that the Board did not receive a request to reconsider its decision to close the discussion of the matter.

(b) The request to open a portion of a meeting shall be submitted to the Secretary of the Board in advance of the meeting in question. The request shall set forth the requestor's interest in the matter to be discussed and the reasons why the requestor believes that the public interest requires that the meeting or portions thereof be open to public observation.

(c) The submission of a request to open a portion of a meeting shall not act to stay the effectiveness of Board action or to postpone or delay the meeting unless the Board decides otherwise.

(d) The Secretary of the Board shall advise the requestor of the Board's consideration of the re-

quest to open a portion of the meeting as soon as practicable.

§ 791.16 General Counsel Certification.

For each meeting or any portion of a meeting closed to public observation under Section 791.14, the General Counsel shall publicly certify, whether in his or her opinion, the meeting or portion thereof may be closed to public observation and shall state each relevant exemption provision of law. A copy of the certification, together with a statement from the presiding officer of the meeting setting forth the time and place of the meeting and the persons present, shall be retained as a part of the permanent meeting records. As part of the certification, the General Counsel shall recommend to the Board whether the public interest requires that the meeting or portions thereof proposed to be closed to public observation be held in the open.

§ 791.17 Maintenance of Meeting Records.

(a) Except in those circumstances which are beyond the control of the agency, the Board shall maintain a complete transcript or electronic recording adequate to record fully the proceedings of each meeting, or any portion thereof, closed to public observation. However, for meetings closed under subparagraphs (8), (9)(A) or (10) of Section 791.12(a), the Board shall maintain either a transcript, a recording or a set of minutes. The Board shall maintain a complete electronic recording for each open meeting or any portion thereof. All records shall clearly identify each speaker.

(b) A set of minutes shall fully and clearly describe all matters discussed and shall provide a full and accurate summary of any actions taken, and the reasons for taking such action. Minutes shall also include a description of each of the views expressed by each person in attendance on any item and the record of any roll call vote, reflecting the vote of each member. All documents considered in connection with any action shall be identified in the minutes.

(c) The agency shall maintain a complete verbatim copy of the transcript, a complete copy of the minutes or a complete electronic recording of each meeting, or any portion of a meeting, closed to public observation, for at least two years after such meeting or for one year after the conclusion of any agency proceeding with respect to which the meeting or any portion was held, whichever occurs later. The agency shall maintain a complete electronic recording of each open meeting for at least three months after the meeting date. A complete set of minutes shall be maintained on a permanent basis for all meetings.

§ 791.18 Public Availability of Meeting Records and Other Documents.

(a) The agency shall make promptly available to the public, in the Public Reference Room, the transcript, electronic recording, or minutes of any meeting, deleting any agenda item or any item of the testimony of a witness received at a closed meeting which the Board determined, pursuant to paragraph (c) of this Section, was exempt from disclosure under Section 791.12(a). The exemption or exemptions relied upon for any deleted information shall be reflected on any record or recording.

(b) Copies of any transcript, minutes or transcription of a recording, disclosing the identity of each speaker, shall be furnished to any person requesting such information in the form specified in paragraph (a) of this Section. Copies shall be furnished at the actual cost of duplication or transcription unless waived by the Secretary of the Board.

(c) Following each meeting or any portion of a meeting closed pursuant to § 791.12(a), the General Counsel or his designee, after consultation with the Secretary of the Board, shall determine which, if any, portions of the meeting transcript, electronic recording or minutes not otherwise available under 5 U.S.C. 552a (the Privacy Act) contain information which should be withheld pursuant to § 791.12(a). If, at a later time, the Board determines that there is no further justification for withholding any meeting record or other item of information from the public which has previously been withheld, then such information shall be made available to the public.

(d) Except for information determined by the Board to be exempt from disclosure pursuant to paragraph (c) of this Section, meeting records shall be promptly available to the public in the Public Reference Room. Meeting records include but are not limited to: the transcript, electronic recording or minutes of each meeting, as required by Section 791.17(a); the notice requirements of Section 791.13 and 791.14(c); and the General Counsel Certification along with the presiding officer's statement, as required by Section 791.16.

(e) These provisions do not affect the procedures set forth in Part 792, Subpart A, governing the inspection and copying of agency records, except that the exemptions set forth in Section 791.12(a) of this subpart and in 5 U.S.C. § 552b(c) shall govern in the case of a request made pursuant to Part 792, Subpart A, to copy or inspect the meeting records described in this Section. Any documents considered or mentioned at Board meetings may be obtained subject to the procedures set forth in Part 792, Subpart A.

Part 792

Requests for Information Under the Freedom of Information Act and Privacy Act, and by Subpoena; Security Procedures for Classified Information

Subpart A—The Freedom of Information Act

General Purpose

§ 792.01 What is the purpose of this subpart?

This subpart describes the procedures you must follow to obtain records from NCUA under the Freedom of Information Act (FOIA), (5 U.S.C. 552).

Records Publicly Available

§ 792.02 What records does NCUA make available to the public for inspection and copying?

Except for records that are exempt from public disclosure under FOIA as amended (5 U.S.C. 552) or are promptly published and copies are available for purchase, NCUA routinely makes the following five types of records available for you to inspect and copy:

(a) Final opinions, including concurring and dissenting opinions, and orders made in the adjudication of cases;

(b) Statements of policy and interpretations which have been adopted by the agency but not published in the FEDERAL REGISTER;

(c) Administrative staff manuals and instructions to staff that affect a member of the public;

(d) Copies of all records, regardless of form or format, which have been released after March 31, 1997, in response to a FOIA request and which, because of the nature of their subject matter, NCUA determines have been or are likely to become the subject of subsequent requests; and

(e) Indices of the documents referred to in this paragraph.

§ 792.03 How will I know which records to request?

NCUA maintains current indices providing identifying information for the public for any matter referred to in § 792.02, issued, adopted, or promulgated after July 4, 1967. The listing of material in an index is for the convenience of possible users and does not constitute a determination that all of the items listed will be disclosed. NCUA has determined that publication of the indices is unnecessary and impractical. You may obtain copies of indices by making a request to the Office of Administration, at NCUA, 1775 Duke Street, Alexandria, VA 22314–2387 or, as indicated, on the NCUA web site. The indices are available for public inspection and copying and are provided at their duplication cost. The indices are:

(a) NCUA Publications List: Manuals relating to general and technical information, booklets published by NCUA, and the Credit Union Directory. The NCUA Publications list is available on the NCUA web site.

(b) Directives Control Index: A list of statements of policy, NCUA Instructions, Bulletins, Letters to Credit Unions, and certain internal manuals.

(c) Popular FOIA Index: Records released in response to a FOIA request, that NCUA determines are likely to be the subject of subsequent requests because of the nature of their subject matter. The Popular FOIA Index will be available on the NCUA web site on or before December 31, 1999.

§ 792.04 How can I obtain these records?

You may obtain these types of records or information in the following ways:

(a) You may obtain copies of the records referenced in § 792.02 by obtaining the index referred to in § 792.03 and following the ordering instructions it contains, or by making a request to the FOIA Officer, NCUA, Office of General Counsel at 1775 Duke Street, Alexandria, Virginia 22314–3428.

(b) If they were created by NCUA on or after November 1, 1996, records referenced in § 792.02

are available on the NCUA web site, found at http://www.ncua.gov.

§ 792.05 What is the significance of records made available and indexed?

The records referred to in § 792.02 may be relied on, used, or cited as precedent by NCUA against a party, provided:

(a) The materials have been indexed and either made available or published; or

(b) The party has actual and timely notice of the materials' contents.

Records Available Upon Request

§ 792.06 Can I obtain other records?

Except with respect to records routinely made available under § 792.02 or published in the FEDERAL REGISTER, or to the extent that records are exempt under the FOIA, if you make a request for records in accordance with this subpart, NCUA will make such records available to you, including records maintained in electronic format, as long as you agree to pay the actual, direct costs.

§ 792.07 Where do I send my request?

(a) You must send your request to one of NCUA's Information Centers. The Central Office and Office of Inspector General are designated as Information Centers for the NCUA. The Freedom of Information Officer of the Office of General Counsel is responsible for the operation of the Information Center maintained at the Central Office. The Inspector General is responsible for the operation of the Inspector General Information Center.

(b) If you are seeking any NCUA record, other than those maintained by the Office of Inspector General, you should send your request to the Freedom of Information Officer at NCUA, Office of the General Counsel, 1775 Duke Street, Alexandria, Virginia 22314–3428. You may also send your request by electronic mail to *FOIA@NCUA.gov*.

(c) If you are seeking a record you think may be maintained by the NCUA Office of Inspector General, then you should send your request to the Inspector General, NCUA, 1775 Duke Street, Alexandria, Virginia 22314–3428.

§ 792.08 What must I include in my request?

(a) Your name, address and telephone number where you can be reached during normal business hours. If you would like us to respond to your FOIA request by electronic mail (e-mail), you should include your e-mail address.

(b) A reasonable description of the records you seek. A reasonable description is one that enables an NCUA employee, who is familiar with the subject area of the request, to locate the record with a reasonable amount of effort.

(c) A statement agreeing to pay all applicable fees or to pay fees up to a certain maximum amount, or requesting a fee reduction or waiver in accordance with § 792.27. If the actual fees are expected to exceed the maximum amount you indicate in your request, NCUA will contact you to see if you are willing to pay the estimated fees. If you do not want to pay the estimated fees, your request will be closed and no bill will be sent.

(d) If other than paper copy, you must identify the form and format of responsive information you are requesting.

§ 792.09 What if my request does not meet the requirements of this subpart?

NCUA need not accept or process your request if it does not comply with the requirements of this subpart. NCUA may return such a request to you with an explanation of the deficiency. You may then submit a corrected request, which will be treated as a new request.

§ 792.10 What will NCUA do with my request?

(a) On receipt of any request, the Information Center assigns it to the appropriate processing schedule, pursuant to paragraph (b) of this section. The date of receipt for any request, including one that is addressed incorrectly or that is referred to NCUA by another agency, is the date the appropriate Information Center actually receives the request.

(b) NCUA has a multi-track processing system. Requests for records that are readily identifiable by the Information Center and have already been cleared for public release may qualify for fast track processing. Requests which meets the requirements of § 792.18 will be processed on the expedited track. All other requests will be handled under normal processing procedures.

(c) The Information Center will make the determination whether a request qualifies for fast track processing or expedited track processing. You may contact the Information Center to learn to which track your request has been assigned. If your request has not qualified for fast track processing, you will have an opportunity to limit the scope of material requested to qualify for fast track processing. Limitations of requests must be in writing. If your request for expedited processing is not granted, you will be advised of your right to appeal.

(d) The Information Center will normally process requests in the order they are received in the separate processing tracks. However, in NCUA's discretion, a particular request may be processed out of turn.

(e) Upon a determination by the appropriate Information Center to comply with your initial request for records, the records will be made promptly available to you. If we notify you of a denial of your request, we will include the names and titles or positions of each person responsible for the denial.

(f) The Information Center will search for records responsive to your request and will generally include all records in existence at the time the search begins. If we use a different search cut-off date, we will inform you of that date.

§ 792.11 What kind of records are exempt from public disclosure?

(a) All records of NCUA or any officer, employee, or agent thereof, are confidential, privileged and exempt from disclosure, except as otherwise provided in this subpart, if they are:

(1) Records specifically authorized under criteria established by an Executive Order to be kept secret in the interest of national defense or foreign policy and are in fact properly classified pursuant to an Executive Order.

(2) Records related solely to NCUA internal personnel rules and practices. This exemption applies to internal rules or instructions which must be kept confidential in order to assure effective performance of the functions and activities for which NCUA is responsible and which do not materially affect members of the public. This exemption also applies to manuals and instructions to the extent that release of the information would permit circumvention of laws or regulations.

(3) Specifically exempted from disclosure by statute, where the statute either makes nondisclosure mandatory or establishes particular criteria for withholding information.

(4) Records which contain trade secrets and commercial or financial information which relate to the business, personal or financial affairs of any person or organization, are furnished to NCUA, and are confidential or privileged. This exemption includes, but is not limited to, various types of confidential sales and cost statistics, trade secrets, and names of key customers and personnel. Assurances of confidentiality given by staff are not binding on NCUA.

(5) Inter-agency or intra-agency memoranda or letters which would not be available by law to a private party in litigation with NCUA. This exemption preserves the existing freedom of NCUA officials and employees to engage in full and frank written or taped communications with each other and with officials and employees of other agencies. It includes, but is not limited to, inter-agency and intra-agency reports, memoranda, letters, correspondence, work papers, and minutes of meetings, as well as staff papers prepared for use within NCUA or in concert with other governmental agencies.

(6) Personnel, medical, and similar files (including financial files), the disclosure of which without written permission would constitute a clearly unwarranted invasion of personal privacy. Files exempt from disclosure include, but are not limited to:

(i) The personnel records of the NCUA;

(ii) The personnel records voluntarily submitted by private parties in response to NCUA's requests for proposals; and

(iii) Files containing reports, records or other material pertaining to individual cases in which disciplinary or other administrative action has been or may be taken.

(7) Records or information compiled for law enforcement purposes, but only to the extent that the production of such law enforcement records or information:

(i) Could reasonably be expected to interfere with enforcement proceedings;

(ii) Would deprive a person of a right to a fair trial or an impartial adjudication;

(iii) Could reasonably be expected to constitute an unwarranted invasion of personal privacy;

(iv) Could reasonably be expected to disclose the identity of a confidential source, including a state, local, or foreign agency or authority or any private institution which fur-

nished information on a confidential basis, and, in the case of a record or information compiled by a criminal law enforcement authority in the course of a criminal investigation on or by an agency conducting a lawful national security intelligence investigation, information furnished by the confidential source;

(v) Would disclose techniques and procedures for law enforcement investigation or prosecutions, or would disclose guidelines for law enforcement investigations or prosecutions if such disclosure could reasonably be expected to risk circumvention of the law; or

(vi) Could reasonably be expected to endanger the life or physical safety of any individual. This includes, but is not limited to, information relating to enforcement proceedings upon which NCUA has acted or will act in the future.

(8) Contained in or related to examination, operating or condition reports prepared by, or on behalf of, or for the use of NCUA or any agency responsible for the regulation or supervision of financial institutions. This includes all information, whether in formal or informal report form, the disclosure of which would harm the financial security of credit unions or would interfere with the relationship between NCUA and credit unions.

(b) We will provide any reasonably segregable portion of a requested record after deleting those portions that are exempt from disclosure under this section.

§ 792.12 How will I know what records NCUA has determined to be exempt?

As long as it is technically feasible and does not threaten an interest protected by the FOIA, we will:

(a) Mark the place where we redacted information from documents released to you and note the exemption that protects the information from public disclosure; or

(b) Make reasonable efforts to include with our response to you an estimate of the volume of information withheld.

§ 792.13 Can I get the records in different forms or formats?

NCUA will provide a copy of the record in any form or format requested, such as computer disk, if the record is readily reproducible by us in that form or format, but we will not provide more than one copy of any record.

§ 792.14 Who is responsible for responding to my request?

The Freedom of Information Officer or designee is responsible for making the initial determination whether to grant or deny a request for information submitted to the Central Office Information Center. The Inspector General or designee is responsible for making the initial determination whether to grant or deny a request for information submitted to the Inspector General Information Center. This official may refer a request to an NCUA employee who is familiar with the subject area of the request. Other NCUA staff members may aid the official by providing information, advice, recommending a decision, or implementing a decision, but no NCUA employee other than an authorized official may make the initial determination. Referral of a request by the official to an employee will not affect the time limitation imposed in § 792.15 unless the request involves an unusual circumstance as provided in § 792.16.

§ 792.15 How long will it take to process my request?

NCUA will respond to requests within 20 working days, except:

(a) Where the running of such time is suspended for payment of fees pursuant to § 792.26;

(b) In unusual circumstances, as defined in 5 U.S.C. 552(a)(6)(B) and § 792.16, the time limit may be extended for:

(1) An additional 10 working days as provided by written notice to you, stating the reasons for the extension and the date on which a determination will be sent; or

(2) Such alternative time period as mutually agreed by you and the Information Office,

when NCUA notifies you that the request cannot be processed in the specified time limit.

§ 792.16 What unusual circumstances can delay NCUA's response?

(a) In unusual circumstances, the time limits for responding to your request (or your appeal) may be extended by NCUA. If NCUA extends the time it will provide you with written notice, setting forth the reasons for such extension and the date on which a determination is expected to be dispatched. Our notice will not specify a date that would result in an extension for more than 10 working days, except as set forth in paragraph (c) of this section. The unusual circumstances that can delay NCUA's response to your request are:

(1) The need to search for, and collect the requested records from field facilities or other establishments that are separate from the office processing the request;

(2) The need to search for, collect, and appropriately examine a voluminous amount of separate and distinct records which are demanded in a single request; or

(3) The need for consultation, which will be conducted with all practicable speed, with another agency having substantial interest in the determination of the request or among two or more components of NCUA having a substantial interest in the subject matter.

(b) If you, or you and a group of others acting in concert, submit multiple requests that NCUA believes actually constitute a single request, which would otherwise satisfy the unusual circumstances criteria specified in this section, and the requests involve related matters, then NCUA may aggregate those requests and the provisions of § 792.15(b) will apply.

(c) If NCUA sends you an extension notice, it will also advise you that you can either limit the scope of your request so that it can be processed within the statutory time limit or agree to an alternative time frame for processing your request.

§ 792.17 What can I do if the time limit passes and I still have not received a response?

You can file suit against NCUA because you will be deemed to have exhausted your administrative remedies if NCUA fails to comply with the time limit provisions of this subpart. If NCUA can show that exceptional circumstances exist and that it is exercising due diligence in responding to your request, the court may retain jurisdiction and allow NCUA to complete its review of the records. In determining whether exceptional circumstances exist, the court may consider your refusal to modify the scope of your request or arrange an alternative time frame for processing after being given the opportunity to do so by NCUA, when it notifies you of the existence of unusual circumstances as set forth in § 792.16.

Expedited Processing

§ 792.18 What if my request is urgent and I cannot wait for the records?

You may request expedited processing of your request if you can show a compelling need for the records. In cases where your request for expedited processing is granted or if NCUA has determined to expedite the response, it will be processed as soon as practicable.

(a) To demonstrate a compelling need for expedited processing, you must provide a certified statement. The statement, certified by you to be true and correct to the best of your knowledge and belief, must demonstrate that:

(1) The failure to obtain the records on an expedited basis could reasonably be expected to pose an imminent threat to the life or physical safety of an individual; or

(2) The requester is a representative of the news media, as defined in § 792.20, and there is urgency to inform the public concerning actual or alleged NCUA activity.

(b) In response to a request for expedited processing, the Information Center will notify you of the determination within ten days of receipt of the request. If the Information Center denies your request for expedited processing, you may file an appeal pursuant to the procedures set forth in § 792.28, and NCUA will expeditiously respond to the appeal.

(c) The Information Center will normally process requests in the order they are received in the separate processing tracks. However, in NCUA's discretion, a particular request may be processed out of turn.

Fees

§ 792.19 How does NCUA calculate the fees for processing my request?

We will charge you our allowable direct costs, unless they are less than the cost of billing you. Direct costs means those expenditures that NCUA actually incurs in searching for, duplicating and reviewing documents to respond to a FOIA request. Search means all time spent looking for material that is responsive to a request, including page-by-page or line-by-line identification of material within documents. Searches may be done manually or by computer. Search does not include modification of an existing program or system that would significantly interfere with the operation of an automated information system. Review means examining documents to determine whether any portion should be withheld and preparing documents for disclosure. Fees are subject to change as costs increase. The current rate schedule is available on our web site at http://www.ncua.gov. We may contract with the private sector to locate, reproduce or disseminate records. NCUA will not contract out responsibilities that FOIA requires it to discharge, such as determining the applicability of an exemption, or determining whether to waive or reduce fees. The following labor and duplication rate calculations apply:

(a) NCUA will charge fees at the following rates for manual searches for and review of records:

(1) If search/review is done by clerical staff, the hourly rate for CU–5, plus 16% of that rate to cover benefits;

(2) If search/review is done by professional staff, the hourly rate for CU–13, plus 16% of that rate to cover benefits.

(b) NCUA will charge fees at the hourly rate for CU–13, plus 16% of that rate to cover benefits, plus the hourly cost of operating the computer for computer searches for records.

(c) NCUA will charge the following duplication fees:

(1) The per-page fee for paper copy reproduction of a document is $.05;

(2) The fee for documents generated by computer is the hourly fee for the computer operator, plus the cost of materials (computer paper, tapes, labels, etc.);

(3) If any other method of duplication is used, NCUA will charge the actual direct cost of duplication.

§ 792.20 What are the charges for each fee category?

The fee category definitions are:

(a) *Commercial use request* means a request from or on behalf of one who seeks information for a use or purpose that furthers the commercial, trade, or profit interests of the requester or the person on whose behalf the request is made.

(b) *Educational institution* means a preschool, an elementary or secondary school, an institution of undergraduate higher education, an institution of graduate higher education, an institution of professional education, and an institution of vocational education operating a program or programs of scholarly research.

(c) *Noncommercial scientific institution* means an institution that is not operated for a "commercial" purpose as that term is used in paragraph (a) of this section and is operated solely for the purpose of conducting scientific research, the results of which are not intended to promote any particular product or industry.

(d) *Representative of the news media* means any person actively gathering news for an entity that is organized and operated to publish or broadcast news to the public. Included within the meaning of public is the credit union community. The term news means information that is about current events or that would be of current interest to the public.

You may consult the following chart to find the fees applicable to your request:

If your fee category is	You'll receive	And you'll be charged
Commercial use	0 hours free search	search time
	0 hours free review	review time
	0 free pages	duplication
Educational institution, noncommercial scientific institution, newsmedia.	Unlimited free search hours	duplication
	Unlimited free review hours	
	100 free pages	
All others	2 hours free search	search time
	Unlimited free review hours.	

If your fee category is	You'll receive	And you'll be charged
	100 free pages	duplication

§ 792.21 Will NCUA provide a fee estimate?

NCUA will notify you of the estimated amount if fees are likely to exceed $25, unless you have indicated in advance a willingness to pay fees as high as those anticipated. You will then have the opportunity to confer with NCUA personnel to reformulate the request to meet your needs at a lower cost.

§ 792.22 What will NCUA charge for other services?

Complying with requests for special services is entirely at the discretion of NCUA. NCUA will recover the full costs of providing such services to the extent it elects to provide them.

§ 792.23 Can I avoid charges by sending multiple, small requests?

You may not file multiple requests, each seeking portions of a document or similar documents, solely to avoid payment of fees. If this is done, NCUA may aggregate any such requests and charge you accordingly.

§ 792.24 Can NCUA charge me interest if I fail to pay my bill?

NCUA can assess interest charges on an unpaid bill starting on the 31st day following the date of the bill. If you fail to pay your bill within 30 days, interest will be at the rate prescribed in 31 U.S.C. 3717, and will accrue from the date of the billing.

§ 792.25 Will NCUA charge me if the records are not found or are determined to be exempt?

NCUA may assess fees for time spent searching and reviewing, even if it fails to locate the records or if records located are determined to be exempt from disclosure.

§ 792.26 Will I be asked to pay fees in advance?

NCUA will require you to give an assurance of payment or an advance payment only when:

(a) NCUA estimates or determines that allowable charges that you may be required to pay are likely to exceed $250. NCUA will notify you of the likely cost and obtain satisfactory assurance of full payment where you have a history of prompt payment of FOIA fees, or require an advance payment of an amount up to the full estimated charges in the case where you have no history of payment; or

(b) You have previously failed to pay a fee charged in a timely fashion. NCUA may require you to pay the full amount owed, plus any applicable interest, or demonstrate that you have, in fact, paid the fee, and to make an advance payment of the full amount of the estimated fee before we begin to process a new request or a pending request from you.

(c) If you are required to make an advance payment of fees, then the administrative time limits prescribed in § 792.16 will begin only after NCUA has received the fee payments described.

Fee Waiver or Reduction

§ 792.27 Can fees be reduced or waived?

You may request that NCUA waive or reduce fees if disclosure of the information you request is in the public interest because it is likely to contribute significantly to public understanding of the operations or activities of the government, and is not primarily in your commercial interest.

(a) NCUA will make a determination of whether the public interest requirement above is met based on the following factors:

(1) Whether the subject of the requested records concerns the operations or activities of the government;

(2) Whether the disclosure is likely to contribute to an understanding of government operations or activities;

(3) Whether disclosure of the requested information will contribute to public understanding; and

(4) Whether the disclosure is likely to contribute significantly to public understanding of government operations or activities,

(b) If the public interest requirement is met, NCUA will make a determination on the commer-

cial interest requirement based upon the following factors:

(1) Whether you have a commercial interest that would be furthered by the requested disclosure; and if so

(2) Whether the magnitude of your commercial interest is sufficiently large in comparison with the public interest in disclosure, that disclosure is primarily in your commercial interest.

(c) If the required public interest exists and your commercial interest is not primary in comparison, NCUA will waive or reduce fees.

(d) If you are not satisfied with our determination on your fee waiver or reduction request, you may submit an appeal to the General Counsel in accordance with § 792.28.

Appeals

§ 792.28 What if I am not satisfied with the response I receive?

If you are not satisfied with NCUA's response to your request, you can file an administrative appeal. Your appeal must be in writing and must be filed within 30 days from receipt of the initial determination (in cases of denials of an entire request, or denial of a request for fee waiver or reduction), or from receipt of any records being made available pursuant to the initial determination (in cases of partial denials.) In its response to your initial request, the Freedom of Information Act Officer or the Inspector General (or designee), will notify you that you may appeal any adverse determination to the Office of General Counsel. The General Counsel, or designee, as set forth in this paragraph, will:

(a) Make a determination with respect to any appeal within 20 days (excepting Saturdays, Sundays, and legal public holidays) after the receipt of such appeal. If, on appeal, the denial of the request for records is, in whole or in part, upheld, the Office of General Counsel will notify you of the provisions for judicial review of that determination under FOIA. Where you do not address your request or appeal to the proper official, the time limitations stated above will be computed from the receipt of the request or appeal by the proper official.

(b) The General Counsel is the official responsible for determining all appeals from initial determinations. In case of this person's absence, the appropriate officer acting in the General Counsel's stead will make the appellate determination, unless such officer was responsible for the initial determination, in which case the Vice-Chairman of the NCUA Board will make the appellate determination.

(c) All appeals should be addressed to the General Counsel in the Central Office and should be clearly identified as such on the envelope and in the letter of appeal by using the indicator "FOIA–APPEAL." Failure to address an appeal properly may delay commencement of the time limitation stated in paragraph (a)(1) of this section, to take account of the time reasonably required to forward the appeal to the Office of General Counsel.

§ 792.29 If I send NCUA confidential commercial information, can it be disclosed under FOIA?

(a) If you submit confidential commercial information to NCUA, it may be disclosed in response to a FOIA request in accordance with this section.

(b) For purposes of this section:

(1) *Confidential commercial information* means commercial or financial information provided to NCUA by a submitter that arguably is protected from disclosure under § 792.11(a)(4) because disclosure could reasonably be expected to cause substantial competitive harm.

(2) *Submitter* means any person or entity who provides business information, directly or indirectly, to NCUA.

(c) Submitters of business information must use good faith efforts to designate, by appropriate markings, either at the time of submission or at a reasonable time thereafter, those portions of their submissions deemed to be protected from disclosure under § 792.11(a)(4). Such a designation shall expire ten years after the date of submission.

(d) We will provide a submitter with written notice of a FOIA request or administrative appeal encompassing designated business information when:

(1) The information has been designated in good faith by the submitter as confidential commercial information deemed protected from disclosure under § 792.11(a)(4); or

(2) NCUA has reason to believe that the information may be protected from disclosure under § 792.11(a)(4).

(e) A copy of the notice to the submitter will also be provided to the FOIA requester.

(f) Through the notice described in paragraph (d) of this section, NCUA will afford the submitter a reasonable period of time within which to provide a detailed written statement of any objection to disclosure. The statement must describe why the information is confidential commercial information and why it should not be disclosed.

(g) Whenever we decide that we must disclose confidential commercial information over the objection of the submitter, we will send both the submitter and the FOIA requester, within a reasonable number of days prior to the specified disclosure date, a written notice which will include:

(1) A statement of the reasons for which the submitter's disclosure objection was not sustained; and

(2) A description of the information to be disclosed; and

(3) A specified disclosure date.

(h) If a requester brings suit to compel disclosure of confidential commercial information, we will promptly notify the submitter.

(i) The notice requirements of paragraph (d) of this section do not apply if:

(1) We determine that the information should not be disclosed;

(2) The information has been lawfully published or has been officially made available to the public;

(3) Disclosure of the information is required by law; or

(4) The designation made by the submitter in accordance with paragraph (c) of this section appears obviously frivolous; except that in such case, NCUA will provide the submitter with written notice of any final administrative decision to disclose the information within a reasonable number of days prior to the specified disclosure date.

Release of Exempt Information

§ 792.30 Is there a prohibition against disclosure of exempt records?

Except those authorized officials listed in § 792.14, or as provided in §§ 792.31–792.32, and subpart C of this part, no officer, employee, or agent of NCUA or of any federally-insured credit union shall disclose or permit the disclosure of any exempt records of NCUA to any person other than those NCUA or credit union officers, employees, or agents properly entitled to such information for the performance of their official duties.

§ 792.31 Can exempt records be disclosed to credit unions, financial institutions and state or federal agencies?

The NCUA Board, in its sole discretion, or any person designated by it in writing, may make available to certain governmental agencies and insured financial institutions copies of reports of examination and other documents, papers or information for their use, when necessary, in the performance of their official duties or functions. All reports, documents and papers made available pursuant to this paragraph shall remain the property of NCUA. No person, agency or employee shall disclose the reports or exempt records without NCUA's express written authorization.

§ 792.32 Can exempt records be disclosed to investigatory agencies?

The NCUA Board, or any person designated by it in writing, in its discretion and in appropriate circumstances, may disclose to proper federal or state authorities copies of exempt records pertaining to irregularities discovered in credit unions which may constitute either unsafe or unsound practices or violations of federal or state, civil or criminal law.

Subpart B—Reserved

Subpart C—Production of Nonpublic Records and Testimony of NCUA Employees in Legal Proceedings

§ 792.40 What does this subpart prohibit?

This subpart prohibits the release of nonpublic records or the appearance of an NCUA employee to testify in legal proceedings except as provided in this subpart. Any person possessing nonpublic records may release them or permit their disclosure only as provided in this subpart.

(a) *Duty of NCUA employees.* (1) If an NCUA employee is served with a subpoena requiring him or her to appear as a witness or produce records, the employee must promptly notify the Office of

General Counsel. The General Counsel has the authority to instruct NCUA employees to refuse appearing as a witness or to withhold nonpublic records. The General Counsel may let an NCUA employee provide testimony, including expert or opinion testimony, if the General Counsel determines that the need for the testimony clearly outweighs contrary considerations.

(2) If a court or other appropriate authority orders or demands expert or opinion testimony or testimony beyond authorized subjects contrary to the General Counsel's instructions, an NCUA employee must immediately notify the General Counsel of the order and respectfully decline to comply. An NCUA employee must decline to answer questions on the grounds that this subpart forbids such disclosure and should produce a copy of this subpart, request an opportunity to consult with the Office of General Counsel, and explain that providing such testimony without approval may expose him or her to disciplinary or other adverse action.

(b) *Duty of persons who are not NCUA employees.* (1) If you are not an NCUA employee but have custody of nonpublic records and are served with a subpoena requiring you to appear as a witness or produce records, you must promptly notify the NCUA about the subpoena. Also, you must notify the issuing court or authority and the person or entity for whom the subpoena was issued of the contents of this subpart. Notice to the NCUA is made by sending a copy of the subpoena to the General Counsel of the NCUA, Office of General Counsel, 1775 Duke Street, Alexandria, Virginia 22314–3428. After receiving notice, the NCUA may advise the issuing court or authority and the person or entity for whom the subpoena was issued that this subpart applies and, in addition, may intervene, attempt to have the subpoena quashed or withdrawn, or register appropriate objections.

(2) After notifying the Office of General Counsel, you should respond to a subpoena by appearing at the time and place stated in the subpoena. Unless authorized by the General Counsel, you should decline to produce any records or give any testimony, basing your refusal on this subpart. If the issuing court or authority orders the disclosure of records or orders you to testify, you should continue to decline to produce records or testify and should advise the Office of General Counsel.

(c) *Penalties.* Anyone who discloses nonpublic records or gives testimony related to those records, except as expressly authorized by the NCUA or as ordered by a federal court after NCUA has had the opportunity to be heard, may face the penalties provided in 18 U.S.C. 641 and other applicable laws. Also, former NCUA employees, in addition to the prohibition contained in this subpart, are subject to the restrictions and penalties of 18 U.S.C. 207.

§ 792.41 When does this subpart apply?

This subpart applies if you want to obtain nonpublic records or testimony of an NCUA employee for legal proceedings. It doesn't apply to the release of records under the Freedom of Information Act (FOIA), 5 U.S.C. 552, or the Privacy Act, 5 U.S.C. 552a, or the release of records to federal or state investigatory agencies under § 792.32.

§ 792.42 How do I request nonpublic records or testimony?

(a) To request nonpublic records or the testimony of an NCUA employee, you must submit a written request to the General Counsel of the NCUA. If you serve a subpoena on the NCUA or an NCUA employee before submitting a written request and receiving a final determination, the NCUA will oppose the subpoena on the grounds that you failed to follow the requirements of this subpart. You may serve a subpoena as long as it is accompanied by a written request that complies with this subpart.

(b) To request nonpublic records that are part of the records of the Office of the Inspector General or the testimony of an NCUA employee on matters within the knowledge of the NCUA employee as a result of his or her employment with the Office of the Inspector General, you must submit a written request to the Office of the Inspector General. Your request will be handled in accordance with the provisions of this subpart except that the Inspector General will be responsible for those determinations that would otherwise be made by the General Counsel.

§ 792.43 What must my written request contain?

Your written request for records or testimony must include:

(a) The caption of the legal proceeding, docket number, and name of the court or other authority involved.

(b) A copy of the complaint or equivalent document setting forth the assertions in the case and any other pleading or document necessary to show relevance.

(c) A list of categories of records sought, a detailed description of how the information sought is relevant to the issues in the legal proceeding, and a specific description of the substance of the testimony or records sought.

(d) A statement as to how the need for the information outweighs the need to maintain the confidentiality of the information and outweighs the burden on the NCUA to produce the records or provide testimony.

(e) A statement indicating that the information sought is not available from another source, such as a credit union's own books and records, other persons or entities, or the testimony of someone other than an NCUA employee, for example, retained experts.

(f) A description of all prior decisions, orders, or pending motions in the case that bear upon the relevance of the records or testimony you want.

(g) The name, address, and telephone number of counsel to each party in the case.

(h) An estimate of the amount of time you anticipate that you and other parties will need with each NCUA employee for interviews, depositions, or testifying.

§ 792.44 When should I make a request?

You should submit your request at least 45 days before the date that you need the records or testimony. If you want to have your request processed in less time, you must explain why you couldn't submit the request earlier and why you need expedited processing. If you are requesting the testimony of an NCUA employee, the NCUA expects you to anticipate your need for the testimony in sufficient time to obtain it by a deposition. The General Counsel may deny a request for testimony at a legal proceeding unless you explain why you could not use deposition testimony. The General Counsel will determine the location of a deposition taking into consideration the NCUA's interest in minimizing the disruption for an NCUA employee's work schedule and the costs and convenience of other persons attending the deposition.

§ 792.45 Where do I send my request?

You must send your request or subpoena for records or testimony to the attention of the General Counsel for the NCUA, Office of General Counsel, 1775 Duke Street, Alexandria, Virginia 22314–3428. You must send your request or subpoena for records or testimony from the Office of the Inspector General to the attention of the NCUA Inspector General, 1775 Duke Street, Alexandria, Virginia 22314–3428.

§ 792.46 What will the NCUA do with my request?

(a) *Factors the NCUA will consider.* The NCUA may consider various factors in reviewing a request for nonpublic records or testimony of NCUA employees, including:

(1) Whether disclosure would assist or hinder the NCUA in performing its statutory duties or use NCUA resources unreasonably, including whether responding to the request will interfere with NCUA employees' ability to do their work.

(2) Whether disclosure is necessary to prevent the perpetration of a fraud or other injustice in the matter or if you can get the records or testimony you want from sources other than the NCUA.

(3) Whether the request is unduly burdensome.

(4) Whether disclosure would violate a statute, executive order, or regulation, for example, the Privacy Act, 5 U.S.C. 552a.

(5) Whether disclosure would reveal confidential, sensitive or privileged information, trade secrets or similar, confidential commercial or financial information, or would otherwise be inappropriate for release and, if so, whether a confidentiality agreement or protective order as provided in § 792.48(a) can adequately limit the disclosure.

(6) Whether the disclosure would interfere with law enforcement proceedings, compromise constitutional rights, or hamper NCUA research or investigatory activities.

(7) Whether the disclosure could result in NCUA appearing to favor one litigant over another.

(8) Any other factors the NCUA determines to be relevant to the interests of the NCUA.

(b) *Review of your request.* The NCUA will process your request in the order it is received. The NCUA will try to respond to your request within 45 days, but this may vary depending on the scope of your request.

(c) *Final determination.* The General Counsel makes the final determination on requests for nonpublic records or NCUA employee testimony. All final determinations are in the sole discretion of the General Counsel. The General Counsel will notify you and the court or other authority of the final determination of your request. In considering your request, the General Counsel may contact you to inform you of the requirements of this subpart, ask that the request or subpoena be modified or withdrawn, or may try to resolve the request or subpoena informally without issuing a final determination. You may seek judicial review of the final determination under the Administrative Procedure Act. 5 U.S.C. 702.

§ 792.47 If my request is granted, what fees apply?

(a) *Generally.* You must pay any fees associated with complying with your request, including copying fees for records and witness fees for testimony. The General Counsel may condition the production of records or appearance for testimony upon advance payment of a reasonable estimate of the fees.

(b) *Fees for records.* You must pay all fees for searching, reviewing and duplicating records produced in response to your request. The fees will be the same as those charged by the NCUA under its Freedom of Information Act regulations, § 792.19.

(c) *Witness fees.* You must pay the fees, expenses, and allowances prescribed by the court's rules for attendance by a witness. If no such fees are prescribed, the local federal district court rule concerning witness fees, for the federal district court closest to where the witness appears, will apply. For testimony by current NCUA employees, you must pay witness fees, allowances, and expenses to the General Counsel by check made payable to the "National Credit Union Administration" within 30 days from receipt of NCUA's billing statement. For the testimony of a former NCUA employee, you must pay witness fees, allowances, and expenses directly to the former employee, in accordance with 28 U.S.C. 1821 or other applicable statutes.

(d) *Certification of records.* The NCUA may authenticate or certify records to facilitate their use as evidence. If you require authenticated records, you must request certified copies at least 45 days before the date they will be needed. The request should be sent to the General Counsel. You will be charged a certification fee of $5.00 per document.

(e) *Waiver of fees.* A waiver or reduction of any fees in connection with the testimony, production, or certification or authentication of records may be granted in the discretion of the General Counsel. Waivers will not be granted routinely. If you request a waiver, your request for records or testimony must state the reasons why a waiver should be granted.

§ 792.48 If my request is granted, what restrictions apply?

(a) *Records.* The General Counsel may impose conditions or restrictions on the release of nonpublic records, including a requirement that you obtain a protective order or execute a confidentiality agreement with the other parties in the legal proceeding that limits access to and any further disclosure of the nonpublic records. The terms of a confidentiality agreement or protective order must be acceptable to the General Counsel. In cases where protective orders or confidentiality agreements have already been executed, the NCUA may condition the release of nonpublic records on an amendment to the existing protective order or confidentiality agreement.

(b) *Testimony.* The General Counsel may impose conditions or restrictions on the testimony of NCUA employees, including, for example, limiting the areas of testimony or requiring you and the other parties to the legal proceeding to agree that the transcript of the testimony will be kept under seal or will only be used or made available in the particular legal proceeding for which you requested the testimony. The General Counsel may also require you to provide a copy of the transcript of the testimony to the NCUA at your expense.

§ 792.49 Definitions.

Legal proceedings means any matter before any federal, state or foreign administrative or judicial authority, including courts, agencies, commissions, boards or other tribunals, involving such proceedings as lawsuits, licensing matters, hearings, trials, discovery, investigations, mediation or arbitration. When the NCUA is a party to a legal proceeding, it will be subject to the applicable

rules of civil procedure governing production of documents and witnesses, however, this subpart will still apply to the testimony of former NCUA employees.

NCUA employee means current and former officials, members of the Board, officers, directors, employees and agents of the National Credit Union Administration, including contract employees and consultants and their employees. This definition does not include persons who are no longer employed by the NCUA and are retained or hired as expert witnesses or agree to testify about general matters, matters available to the public, or matters with which they had no specific involvement or responsibility during their employment.

Nonpublic records means any NCUA records that are exempt from disclosure under § 792.11, the NCUA regulations implementing the provisions of the Freedom of Information Act. For example, this means records created in connection with NCUA's examination and supervision of insured credit unions, including examination reports, internal memoranda, and correspondence, and, also, records created in connection with NCUA's enforcement and investigatory responsibilities.

Subpoena means any order, subpoena for records or other tangible things or for testimony, summons, notice or legal process issued in a legal proceeding.

Testimony means any written or oral statements made by an individual in connection with a legal proceeding including personal appearances in court or at depositions, interviews in person or by telephone, responses to written interrogatories or other written statements such as reports, declarations, affidavits, or certifications or any response involving more than the delivery of records.

Subpart D—Security Procedures for Classified Information

§ 792.50 Program.

(a) The NCUA's Chief Financial Officer is designated as the person responsible for implementation and oversight of NCUA's program for maintaining the security of confidential information regarding national defense and foreign relations. The Chief Financial Officer receives questions, suggestions and complaints regarding all elements of this program. The Chief Financial Officer is solely responsible for changes to the program and assures that the program is consistent with legal requirements.

(b) The Chief Financial Officer is the Agency's official contact for declassification requests regardless of the point of origin of such requests.

§ 792.51 Procedures.

(a) *Mandatory review.* All declassification requests made by a member of the public, by a government employee or by an agency shall be handled by the Chief Financial Officer or the Chief Financial Officer's designee. Under no circumstances shall the Chief Financial Officer refuse to confirm the existence or nonexistence of a document under the Freedom of Information Act or the mandatory review provisions of other applicable law, unless the fact of its existence or nonexistence would itself be classifiable under applicable law. Although NCUA has no authority to classify or declassify information, it occasionally handles information classified by another agency. The Chief Financial Officer shall refer all declassification requests to the agency that originally classified the information. The Chief Financial Officer or the Chief Financial Officer's designee shall notify the requesting person or agency that the request has been referred to the originating agency and that all further inquiries and appeals must be made directly to the other agency.

(b) *Handling and safeguarding national security information.* All information classified "Top Secret," "Secret," and "Confidential" shall be delivered to the Chief Financial Officer or the Chief Financial Officer's designee immediately upon receipt. The Chief Financial Officer shall advise those who may come into possession of such information of the name of the current designee. If the Chief Financial Officer is unavailable, the designee shall lock the documents, unopened, in the combination safe located in the Office of the Chief Financial Officer. If the Chief Financial Officer or the Chief Financial Officer's designee is unavailable to receive such documents, the documents shall be delivered to the Director of the Personnel Office who shall lock them, unopened, in the combination safe in the Personnel Office. Under no circumstances shall classified materials that cannot be delivered to the Chief Financial Officer be stored other than in the two designated safes.

(c) *Storage.* All classified documents shall be stored in the combination safe located in the Chief Financial Officer's Office, except as provided in paragraph (b) of this Section. The combination shall be known only to the Chief Financial Officer

and the Chief Financial Officer's designee holding the proper security clearance.

(d) *Employee Education.* The Chief Financial Officer shall send a memo to every NCUA employee who (1) has a security clearance and (2) may handle classified materials. This memo shall describe NCUA procedures for handling, reproducing and storing classified documents. The Chief Financial Officer shall require each such employee to review Executive Order 12356.

(e) *Agency Terminology.* The National Credit Union Administration's Central Office shall use the terms "Top Secret," "Secret" or "Confidential" only in relation to materials classified for national security purposes.

Subpart E—The Privacy Act

§ 792.52 Scope.

This Subpart governs requests made of NCUA under the Privacy Act (5 U.S.C. § 552a). The regulation applies to all records maintained by NCUA which contain personal information about an individual and some means of identifying the individual, and which are contained in a system of records from which information may be retrieved by use of an identifying particular; sets forth procedures whereby individuals may seek and gain access to records concerning themselves and request amendments of those records; and sets forth requirements applicable to NCUA employees' maintaining, collecting, using, or disseminating such records.

§ 792.53 Definitions.

For purposes of this Subpart:

(a) "Individual" means a citizen of the United States or an alien lawfully admitted for permanent residence.

(b) "Maintain" includes maintain, collect, use, or disseminate.

(c) "Record" means any item, collection, or grouping of information about an individual that is maintained by NCUA, and that contains the name, or an identifying number, symbol, or other identifying particular assigned to the individual.

(d) "System of records" means a group of any records under NCUA's control from which information is retrieved by the name of the individual or by some identifying number, symbol, or other identifying particular assigned to the individual.

(e) "Routine use" means, with respect to the disclosure of a record, the use of such record for a purpose which is compatible with the purpose for which it was collected.

(f) "Statistical record" means a record in a system of records maintained for statistical research or reporting purposes only and not used in whole or in part in making any determination about an identifiable individual, except as provided by Section 8 of Title 13 of the United States Code.

§ 792.54 Procedures for requests pertaining to individual records in a system of records.

(a) An individual seeking notification of whether a system of records contains a record pertaining to that individual, or an individual seeking access to information or records pertaining to that individual which are available under the Privacy Act shall present a request to the NCUA official identified in the access procedure section of the "Notice of Systems of Records" published in the *FEDERAL REGISTER* which describes the system of records to which the individual's request relates. An individual who does not have access to the *FEDERAL REGISTER* and who is unable to determine the appropriate official to whom a request should be submitted may submit a request to the Privacy Officer, Office of General Counsel, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428, in which case the request will then be referred to the appropriate NCUA official and the date of receipt of the request will be determined as the date of receipt by the official.

(b) In addition to meeting the identification requirements set forth in § 792.55, an individual seeking notification or access, either in person or by mail, shall describe the nature of the record sought, the approximate dates covered by the record, and the system in which it is thought to be included, as described in the "Notice of Systems of Records" published in the *FEDERAL REGISTER.*

§ 792.55 Times, places, and requirements for identification of individuals making requests and identification of records requested.

(a) The following standards are applicable to an individual submitting requests either in person or by mail under § 792.54:

(1) If not personally known to the NCUA official responding to the request, an individual seeking access to records about that individual in person shall establish identity by the presentation of a single document bearing a photograph (such as a passport or identification

badge) or by the presentation of two items of identification which do not bear a photograph but do bear both a name and address (such as a driver's license or credit card);

(2) An individual seeking access to records about that individual by mail may establish identity by a signature, address, date of birth, employee identification number if any, and one other identifier such as a photocopy of driver's license or other document. If less than all of this requisite identifying information is provided, the NCUA official responding to the request may require further identifying information prior to any notification or responsive disclosure.

(3) An individual seeking access to records about himself by mail or in person, who cannot provide the required documentation or identification, may provide an unsworn declaration subscribed to as true under penalty of perjury.

(b) The parent or guardian of a minor or a person judicially determined to be incompetent shall, in addition to establishing identity of the minor or other person as required in paragraph (a) of this section, furnish a copy of a birth certificate showing parentage or a court order establishing guardianship.

(c) An individual may request by telephone notification of the existence of and access to records about that individual and contained in a system of records. In such a case, the NCUA official responding to the request shall require, for the purpose of comparison and verification of identity, at least two items of identifying information (such as date of birth, home address, social security number) already possessed by the NCUA. If the requisite identifying information is not provided, or otherwise at the discretion of the responsible NCUA official, an individual may be required to submit the request by mail or in person in accordance with paragraph (a) of this Section.

(d) An individual seeking to review records about that individual may be accompanied by another person of their own choosing. In such cases, the individual seeking access shall be required to furnish a written statement authorizing discussion of that individual's records in the accompanying person's presence.

(e) In addition to the requirements set forth in paragraphs (a), (b) and (c) of this Section, the published "Notice of Systems of Records" for individual systems may include further requirements of identification where necessary to retrieve the individual records from the system.

§ 792.56 Notice of existence of records, access decisions and disclosure of requested information; time limits.

(a) The NCUA official identified in the record access procedure section of the "Notice of Systems of Records" and identified in accordance with § 792.54(a), by an individual seeking notification of, or access to, a record, shall be responsible: (1) for determining whether access is available under the Privacy Act; (2) for notifying the requesting individual of that determination; and (3) for providing access to information determined to be available. In the case of an individual access request made in person, information determined to be available shall be provided by allowing a personal review of the record or portion of a record containing the information requested and determined to be available, and the individual shall be allowed to have a copy of all or any portion of available information made in a form comprehensible to him. In the case of an individual access request made by mail, information determined to be available shall be provided by mail, unless the individual has requested otherwise.

(b) The following time limits shall be applicable to the required determinations, notification and provisions of access set forth in paragraph (a) of this Section:

(1) A request concerning a single system of records which does not require consultation with or requisition of records from another agency will be responded to within 20 working days after receipt of the request.

(2) A request requiring requisition of records from or consultation with another agency will be responded to within 30 working days of receipt of the request.

(3) If a request under paragraphs (b)(1) or (2) of this section presents unusual difficulties in determining whether the records involved are exempt from disclosure, the Privacy Act Officer, in the Office of General Counsel, may extend the time period established by the regulations by 10 working days.

(c) Nothing in this Section shall be construed to allow an individual access to any information

compiled in reasonable anticipation of a civil action or proceeding, or any information exempted from the access provisions of the Privacy Act.

§ 792.57 Special procedures: Information furnished by other agencies; medical records.

(a) When a request for records or information from NCUA includes information furnished by other Federal agencies, the NCUA official responsible for action on the request shall consult with the appropriate agency prior to making a decision to disclose or refuse access to the record, but the decision whether to disclose the record shall be made in the first instance by the NCUA official.

(b) When an individual requests medical records concerning himself, the NCUA official responsible for action on the request may advise the individual that the records to be released will be provided first to a physician designated in writing by the individual. The physician will provide the records to the individual.

§ 792.58 Requests for correction or amendment to a record; administrative review of requests.

(a) An individual may request amendment of a record concerning that individual by addressing a request, either in person or by mail, to the NCUA official identified in the "contesting record procedures" section of the "Notice of Systems of Records" published in the *FEDERAL REGISTER* and describing the system of records which contains the record sought to be amended. The request must indicate the particular record involved, the nature of the correction sought, and the justification for the correction or amendment. Requests made by mail should be addressed to the responsible NCUA official at the address specified in the "Notice of Systems of Records" describing the system of records which contains the contested record. An individual who does not have access to NCUA's "Notice of Systems of Records," and to whom the appropriate address is otherwise unavailable, may submit a request to the Privacy Act Officer, Office of General Counsel, National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia, 22314–3428, in which case the request will then be referred to the appropriate NCUA official. The date of receipt of the request will be determined as of the date of receipt by that official.

(b) Within 10 working days of receipt of the request, the appropriate NCUA official shall advise the individual that the request has been received. The appropriate NCUA official shall then promptly (under normal circumstances, not later than 30 working days after receipt of the request) advise the individual that the record is to be amended or corrected, or inform the individual of rejection of the request to amend the record, the reason for the rejection, and the procedures established by § 792.27 for the individual to request a review of that rejection.

§ 792.59 Appeal of initial determination.

(a) A rejection, in whole or in part, of a request to amend or correct a record may be appealed to the General Counsel within 30 working days of receipt of notice of the rejection. Appeals shall be in writing, and shall set forth the specific item of information sought to be corrected and the documentation justifying the correction. Appeals shall be addressed to the Office of General Counsel, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428. Appeals shall be decided within 30 working days of receipt unless the General Counsel, for good cause, extends such period for an additional 30 working days.

(b) Within the time limits set forth in paragraph (a) of this Section, the General Counsel shall either advise the individual of a decision to amend or correct the record, or advise the individual of a determination that an amendment or correction is not warranted on the facts, in which case the individual shall be advised of the right to provide for the record a "Statement of Disagreement" and of the right to further appeal pursuant to the Privacy Act. For records under the jurisdiction of the Office of Personnel Management, appeals will be made pursuant to that agency's regulations.

(c) A statement of disagreement may be furnished by the individual. The statement must be sent, within 30 days of the date of receipt of the notice of General Counsel refusal to authorize correction, to the General Counsel, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428. Upon receipt of a statement of disagreement in accordance with this Section, the General Counsel shall take steps to ensure that the statement is included in the system of

records containing the disputed item and that the original item is so marked to indicate that there is a statement of dispute and where, within the system of records, that statement may be found.

(d) When a record has been amended or corrected or a statement of disagreement has been furnished, the system manager for the system of records containing the record shall, within 30 days thereof, advise all prior recipients of information to which the amendment or statement of disagreement relates whose identity can be determined by an accounting made as required by the Privacy Act of 1974 or any other accounting previously made, of the amendment or statement of disagreement. When a statement of disagreement has been furnished, the system manager shall also provide any subsequent recipient of a disclosure containing information to which the statement relates with a copy of the statement and note the disputed portion of the information disclosed. A concise statement of the reasons for not making the requested amendment may also be provided if deemed appropriate.

(e) If access is denied because of an exemption, the individual will be notified of the right to appeal that determination to the General Counsel within 30 days after receipt. Appeals will be determined within 20 working days.

§ 792.60 Disclosure of record to person other than the individual to whom it pertains.

No record or item of information concerning an individual which is contained in a system of records maintained by NCUA shall be disclosed by any means of communication to any person, or to another agency, without the prior written consent of the individual to whom the record or item of information pertains, unless the disclosure would be—

(a) To an employee of the NCUA who has need for the record in the performance of duty;

(b) Required by the Freedom of Information Act;

(c) For a routine use as described in the "Notice of Systems of Records," published in the *FEDERAL REGISTER*, which describes the system of records in which the record or item of information is contained;

(d) To the Bureau of the Census for purposes of planning or carrying out a census or survey or related activity pursuant to the provisions of Title 13 of the United States Code;

(e) To a recipient who has provided the NCUA with advance adequate written assurance that the record or item will be used solely as a statistical research or reporting record, and the record is to be transferred in a form that is not individually identifiable;

(f) To the National Archives and Records Administration as a record or item which has sufficient historical or other value to warrant its continued preservation by the United States Government, or for evaluation by the Archivist of the United States or the designee of the Archivist to determine whether the record has such value;

(g) To another agency or to an instrumentality of any governmental jurisdiction within or under the control of the United States for a civil or criminal law enforcement activity if the activity is authorized by law, and if the head of the agency or instrumentality has made a written request to NCUA specifying the particular portion desired and the law enforcement activity for which the record or item is sought;

(h) To a person pursuant to a showing of compelling circumstances affecting the health or safety of an individual if, upon such disclosure, notification is transmitted to the last known address of such individual;

(i) To either House of Congress, or, to the extent of matter within its jurisdiction, any committee or subcommittee thereof, any joint committee of Congress or subcommittee of any such joint committee;

(j) To the Comptroller General, or any of his authorized representatives, in the course of the performance of the duties of the General Accounting Office; or

(k) Pursuant to the order of a court of competent jurisdiction; or

(l) To a consumer reporting agency in accordance with Section 3711(f) of Title 31 of the United States Code (31 U.S.C. § 3711(f)).

§ 792.61 Accounting for disclosures.

(a) Each system manager identified in the "Notice of Systems of Records" as published in the *FEDERAL REGISTER* for each system of records maintained by the NCUA, shall establish a system of accounting for all disclosures of information or records concerning individuals and contained in the system of records, made outside NCUA. Accounting procedures may be established in the least expensive and most convenient form that

will permit the system manager to advise individuals, promptly upon request, of the persons or agencies to which records concerning them have been disclosed.

(b) Accounting records, at a minimum, shall include the information disclosed, the name and address of the person or agency to whom disclosure was made, and the date of disclosure. When records are transferred to the National Archives and Records Administration for storage in records centers, the accounting pertaining to those records shall be transferred with the records themselves.

(c) Any accounting made under this Section shall be retained for at least five years or the life of the record, whichever is longer, after the disclosure for which the accounting is made.

§ 792.62 Requests for accounting for disclosures.

At the time of the request for access or correction or at any other time, an individual may request an accounting of disclosures made of the individual's record outside the NCUA. Request for accounting shall be directed to the system manager. Any available accounting, whether kept in accordance with the requirements of the Privacy Act or under procedures established prior to September 27, 1975, shall be made available to the individual, except that an accounting need not be made available if it relates to: (a) a disclosure made pursuant to the Freedom of Information Act (5 U.S.C. 552); (b) a disclosure made within the NCUA; (c) a disclosure made to a law enforcement agency pursuant to 5 U.S.C. 552a(b)(7); (d) a disclosure which has been exempted from the provisions of 5 U.S.C. 552a(c)(3) pursuant to 5 U.S.C. 552a(j) or (k).

§ 792.63 Collection of information from individuals: information forms.

(a) The system manager, as identified in the "Notice of Systems of Records" published in the *FEDERAL REGISTER* for each system of records maintained by the Administration, shall be responsible for reviewing all forms developed and used to collect information from or about individuals for incorporation into the system of records.

(b) The purpose of the review shall be to eliminate any requirement for information that is not relevant and necessary to carry out an NCUA function and to accomplish the following objectives:

(1) To ensure that no information concerning religion, political beliefs or activities, association memberships (other than those required for a professional license), or the exercise of other First Amendment rights is required to be disclosed unless such requirement of disclosure is expressly authorized by statute or is pertinent to and within the scope of any authorized law enforcement activity;

(2) To ensure that the form or accompanying statement makes clear to the individual which information by law must be disclosed and the authority for that requirement, and which information is voluntary;

(3) To ensure that the form or accompanying statement makes clear the principal purpose or purposes for which the information is being collected, and states concisely the routine uses that will be made of the information;

(4) To ensure that the form or accompanying statement clearly indicates to the individual the existing rights, benefits or privileges not to provide all or part of the requested information; and

(5) To ensure that any form requesting disclosure of a social security number, or an accompanying statement, clearly advises the individual of the statute or regulation requiring disclosure of the number, or clearly advises the individual that disclosure is voluntary and that no consequence will flow from a refusal to disclose it, and the uses that will be made of the number whether disclosed mandatorily or voluntarily.

(c) Any form which does not meet the objectives specified in the Privacy Act and this Section shall be revised to conform thereto.

§ 792.64 Contracting for the operation of a system of records.

(a) No NCUA component shall contract for the operation of a system of records by or on behalf of the Agency without the express approval of the NCUA Board.

(b) Any contract which is approved shall continue to ensure compliance with the requirements of the Privacy Act. The contracting component shall have the responsibility for ensuring that the contractor complies with the contract requirements relating to the Privacy Act.

§ 792.65 Fees.

(a) Fees pursuant to 5 U.S.C. 552a(f)(5) shall be assessed for actual copies of records provided to individuals on the following basis, unless the NCUA official determining access waives the fee because of the inability of the individual to pay or the cost of collecting the fee exceeds the fee:

(1) For copies of documents provided, copy fees as stated in NCUA's current FOIA fee schedule; and

(2) For copying information, if any, maintained in nondocument form, the direct cost to NCUA may be assessed.

(b) If it is determined that access fees chargeable under this Section will amount to more than $25, and the individual has not indicated in advance willingness to pay fees as high as are anticipated, the individual shall be notified of the amount of the anticipated fees before copies are made, and the individual's access request shall not be considered to have been received until receipt by NCUA of written agreement to pay.

§ 792.66 Exemptions.

(a) NCUA maintains four systems of records that are exempted from some provisions of the Privacy Act. In paragraph (b) of this Section, those systems of records are identified by System Name and System Number, as stated in the NCUA's "Notice of Systems of Records," published in the *FEDERAL REGISTER*. The provisions from which each system is exempted and the reasons therefor are also set forth.

(b)(1) System NCUA–1, entitled "Employee Suitability Security Investigations Containing Adverse Information," consists of adverse information about NCUA employees that had been obtained as a result of routine U.S. Office of Personnel Management (OPM) security Investigations. To the extent that NCUA maintains records in this system pursuant to OPM guidelines that may require retrieval of information by use of individual identifiers, those records are encompassed by and included in the OPM Central system of records number Central-9 entitled, "Personnel Investigations Records," and thus are subject to the exemptions promulgated by OPM. Additionally, in order to ensure the protection of properly confidential sources, particularly as to those records which are not maintained pursuant to such Office of Personnel Management requirements, the records in these systems of records are exempted, pursuant to Section (k)(5) of the Privacy Act (5 U.S.C. 552a(k)(5)), from Section (d) of the Act (5 U.S.C. 552a(d)). To the extent that disclosure of a record would reveal the identity of a confidential source, NCUA need not grant access to that record by its subject. Information which would reveal a confidential source shall, however, whenever possible, be extracted or summarized in a manner which protects the source and the summary or extract shall be provided to the requesting individual.

(2) System NCUA–8, entitled, "Investigative Reports Involving Any Crime or Suspicious Activity Against a Credit Union, NCUA," consists of investigatory or enforcement records about individuals suspected of involvement in violations of laws or regulations, whether criminal or administrative. These records are maintained in an overall context of general investigative information concerning crimes against credit unions. To the extent that individually identifiable information is maintained, however, for purposes of protecting the security of any investigations by appropriate law enforcement authorities and promoting the successful prosecution of all actual criminal activity, the records in this system are exempted, pursuant to Section k(2) of the Privacy Act (5 U.S.C. 552a (k)(2)), from Sections (c)(3), and (d)). NCUA need not make an accounting of previous disclosures of a record in this system of records available to its subject, and NCUA need not grant access to any records in this system of records by their subject. Further, whenever individuals request records about themselves and maintained in this system of records, the NCUA shall, to the extent necessary to realize the above-stated purposes, neither confirm nor deny the existence of the records but shall advise the individuals only that no records available to them pursuant to the Privacy Act of 1974 have been identified. However, should review of the record reveal that the information contained therein has been used or is being used to deny the individuals any right, privilege or benefit for which they are eligible or to which they would otherwise be entitled under Federal law, the individuals shall be advised of the existence of the information and shall be provided the information, except to the extent disclosure would identify a confidential source. Information which would identify a confidential source shall, if possible, be extracted or summarized in a manner which protects the source and the summary or extract shall be provided to the requesting individual.

(3) System NCUA–11, entitled, "Office of Inspector General (OIG) Investigative Records," consists of OIG records of closed and pending investigations of individuals alleged to have been involved in criminal violations. The records in this system are exempted pursuant to Sections (k)(2) of the Privacy Act, 5 U.S.C. 552a(k)(2), from sections (c)(3); (d); (e)(1); (e)(4)(G); (e)(4)(H); (e)(4)(I); and (f). The records in this system are also exempted pursuant to Section (j)(2) of the Privacy Act, 5 U.S.C. 552a(j)(2), from sections (c)(3); (c)(4); (d); (e)(1); (e)(2); (e)(3); and (g).

(4) System NCUA–13, entitled, "Litigation Case Files," consists of investigatory materials compiled for law enforcement purposes. Records in the Litigation Case Files system are used in connection with the execution of NCUA's legal and enforcement responsibilities. Because the system covers investigatory materials compiled for law enforcement purposes, it is eligible for exemption under subsection (k)(2) of the Privacy Act. 5 U.S.C. 552a(k)(2). The Litigation Case Files system is exempt from subsections (c)(3), (d), (e)(1), (e)(4)(G), (H), (I) and (f) of the Privacy Act. 5 U.S.C. 552a (c)(3), (d), (e)(1), (e)(4)(G), (H), (I) and (f). However, if an individual is denied any right, privilege, or benefit to which he would otherwise be entitled by federal law, or for which he otherwise would be eligible, as a result of the maintenance of such records, the records or information will be made available to him, provided the identity of a confidential source is not disclosed.

(c) For purposes of this Section, a "confidential source" means a source who furnished information to the Government under an express promise that the identity of the source would remain confidential, or, prior to September 27, 1976, under an implied promise that the identity of the source would be held in confidence.

§ 792.67 Security of systems of records.

(a) Each system manager, with the approval of the head of that Office, shall establish administrative and physical controls to ensure the protection of a system of records from unauthorized access or disclosure and from physical damage or destruction. The controls instituted shall be proportional to the degree of sensitivity of the records, but at a minimum must ensure: that records are enclosed in a manner to protect them from public view; that the area in which the records are stored is supervised during all business hours to prevent unauthorized personnel from entering the area or obtaining access to the records; and that the records are inaccessible during nonbusiness hours.

(b) Each system manager, with the approval of the head of that Office, shall adopt access restriction to insure that only those individuals within the agency who have a need to have access to the records for the performance of duty have access. Procedures shall also be adopted to prevent accidental access to or dissemination of records.

§ 792.68 Use and collection of Social Security numbers.

The head of each NCUA Office shall take such measures as are necessary to ensure that employees authorized to collect information from individuals are advised that individuals may not be required without statutory or regulatory authorization to furnish Social Security numbers, and that individuals who are requested to provide Social Security numbers voluntarily must be advised that furnishing the number is not required and that no penalty or denial of benefits will flow from the refusal to provide it.

§ 792.69 Training and employee standards of conduct with regard to privacy.

(a) The Director of the Office of Human Resources, with advice from the General Counsel, is responsible for training NCUA employees in the obligations imposed by the Privacy Act and this subpart.

(b) The head of each NCUA Office shall be responsible for assuring that employees subject to that person's supervision are advised of the provisions of the Privacy Act, including the criminal penalties and civil liabilities provided therein, and that such employees are made aware of their responsibilities to protect the security of personal information, to assure its accuracy, relevance, timeliness, and completeness, to avoid unauthorized disclosure either orally or in writing, and to ensure that no information system concerning individuals, no matter how small or specialized, is maintained without public notice.

(c) With respect to each system of records maintained by NCUA, Agency employees shall:

(1) Collect no information of a personal nature from individuals unless authorized to collect it to achieve a function or carry out an NCUA responsibility;

(2) Collect from individuals only that information which is necessary to NCUA functions or responsibilities;

(3) Collect information, wherever possible, directly from the individual to whom it relates;

(4) Inform individuals from whom information is collected of the authority for collection, the purposes thereof, the routine uses that will be made of the information, and the effects, both legal and practical, of not furnishing the information;

(5) Not collect, maintain, use, or disseminate information concerning an individual's religious or political beliefs or activities or his membership in associations or organizations, unless (i) the individual has volunteered such information for his own benefit; (ii) the information is expressly authorized by statute to be collected, maintained, used, or disseminated; or (iii) activities involved are pertinent to and within the scope of an authorized investigation or adjudication;

(6) Advise their supervisors of the existence or contemplated development of any record system which retrieves information about individuals by individual identifier;

(7) Maintain an accounting, in the prescribed form, of all dissemination of personal information outside NCUA, whether made orally or in writing;

(8) Disseminate no information concerning individuals outside NCUA except when authorized by 5 U.S.C. 552a or pursuant to a routine use as set forth in the "routine use" section of the "Notice of Systems of Records" published in the *FEDERAL REGISTER*;

(9) Maintain and process information concerning individuals with care in order to ensure that no inadvertent disclosure of the information is made either within or outside NCUA; and

(10) Call to the attention of the proper NCUA authorities any information in a system maintained by NCUA which is not authorized to be maintained under the provisions of the Privacy Act, including information on First Amendment activities, information that is inaccurate, irrelevant or so incomplete as to risk unfairness to the individuals concerned.

(d) Heads of offices within NCUA shall, at least annually, review the record systems subject to their supervision to ensure compliance with the provisions of the Privacy Act.

Part 793

Tort Claims Against The Government

Subpart A—General

§ 793.1 Scope of regulations.

The regulations in this Part shall apply only to claims asserted under the Federal Tort Claims Act, as amended, 28 U.S.C. Sections 2671–2680, accruing on or after January 18, 1967, for money damages against the United States for damage to or loss of property or personal injury or death caused by the negligent or wrongful act or omission of any employee of the National Credit Union Administration while acting within the scope of his office of employment.

Subpart B—Procedures

§ 793.2 Administrative claim; when presented; place of filing.

(a) For purposes of the regulations in this Part, a claim shall be deemed to have been presented when the National Credit Union Administration receives, at a place designated in paragraph (c) of this Section, an executed Standard Form 95 or other written notification of an incident accompanied by a claim for money damages in a sum certain for damage to or loss of property, for personal injury, or for death, alleged to have occurred by reason of the incident. A claim which should have been presented to the National Credit Union Administration but which was mistakenly addressed to or filed with another Federal agency, shall be deemed to be presented to the National Credit Union Administration as of the date that the claim is received by the National Credit Union Administration. A claim mistakenly addressed to or filed with the National Credit Union Administration shall forthwith be transferred to the appropriate Federal agency, if ascertainable, or returned to the claimant.

(b) A claim presented in compliance with paragraph (a) of this Section may be amended by the claimant at any time prior to final action by the Office of General Counsel, National Credit Union Administration or prior to the exercise of the claimant's option to bring suit under 28 U.S.C. 2675(a). Amendments shall be submitted in writing and signed by the claimant or his duly authorized agent or legal representative. Upon the timely filing of an amendment to a pending claim, the National Credit Union Administration shall have 6 months in which to make a final disposition of the claim as amended and the claimant's option under 28 U.S.C. 2675(a) shall not accrue until 6 months after the filing of an amendment.

(c) Forms may be obtained and claims may be filed with the regional office of the National Credit Union Administration having jurisdiction over the employee involved in the accident or incident, or with the Office of General Counsel, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

§ 793.3 Administrative claim; who may file.

(a) A claim for injury to or loss of property may be presented by the owner of the property interest which is the subject matter of the claim, his duly authorized agent, or his legal representative.

(b) A claim for personal injury may be presented by the injured person, his duly authorized agent, or his legal representative.

(c) A claim based on death may be presented by the executor or administrator of the decedent's estate or by any other person legally entitled to assert such a claim under applicable state law.

(d) A claim for loss wholly compensated by an insurer with the rights of a subrogee may be presented by the insurer. A claim for loss partially compensated by an insurer with the rights of a subrogee may be presented by the insurer or the insured individually, as their respective interests appear, or jointly. Whenever an insurer presents a claim asserting the rights of a subrogee, he shall present with his claim appropriate evidence that he has the rights of a subrogee.

(e) A claim presented by an agent or legal representative shall be presented in the name of the claimant, be signed by the agent or legal representative, show the title or legal capacity of the person signing, and be accompanied by evidence

of his authority to present a claim on behalf of the claimant as agent, executor, administrator, parent, guardian, or other representative.

§ 793.4 Administrative claim; evidence and information to be submitted.

(a) *Death.* In support of a claim based on death, the claimant may be required to submit the following evidence or information:

(1) An authenticated death certificate or other competent evidence showing the cause of death, date of death, and age of the decedent.

(2) Decedent's employment or occupation at the time of death, including his monthly or yearly salary or earnings (if any), and the duration of his last employment or occupation.

(3) Full names, addresses, birthdates, kinship, and marital status of the decedent's survivors, including those survivors who were dependent for support upon the decedent at the time of his death.

(4) Degree of support afforded by the decedent to each survivor dependent upon him for support at the time of his death.

(5) Decedent's general physical and mental condition before death.

(6) Itemized bills for medical and burial expenses incurred by reason of the incident causing death, or itemized receipts of payments for such expenses.

(7) If damages for pain and suffering before death are claimed, a physician's detailed statement specifying the injuries suffered, duration of pain and suffering, any drugs administered for pain and the decedent's physical condition in the interval between injury and death.

(8) Any other evidence or information which may have a bearing on the responsibility of the United States for the death or the damages claimed.

(b) *Personal injury.* In support of a claim based on personal injury, the claimant may be required to submit the following evidence or information: (1) A written report by his attending physician or dentist setting forth the nature and extent of the injury, nature and extent of the treatment, any degree of temporary or permanent disability, the prognosis, period of hospitalization, and any diminished earning capacity. In addition, the claimant may be required to submit to a physical and/or mental examination by a physician employed or designated by the National Credit Union Administration. A copy or report of the examining physician shall be made available to the claimant upon the claimant's written request provided that claimant has, upon request, furnished the report referred to in the first sentence of this subparagraph and has made or agrees to make available to the National Credit Union Administration any other physician's reports previously or thereafter made of the physical or mental condition which is the subject of his claim.

(2) Itemized bills for medical, dental, and hospital expenses incurred, or itemized receipts of payment for such expenses.

(3) If the prognosis reveals the necessity for future treatment, a statement of expected duration of and expenses for such treatment.

(4) If a claim is made for loss of time from employment, a written statement from his employer showing actual time lost from his employment, whether he is a full or part time employee, and wages or salary actually lost.

(5) If a claim is made for loss of income and the claimant is self-employed, documentary evidence showing the amount of earnings actually lost.

(6) Any other evidence or information which may have a bearing on the responsibility of the United States for the personal injury or the damages claimed.

(c) *Property damage.* In support of a claim for damages to or loss of property, real or personal, the claimant may be required to submit the following information or evidence:

(1) Proof of ownership.

(2) A detailed statement of the amount claimed with respect to each item of property.

(3) An itemized receipt of payment for necessary repairs or itemized written estimates of the cost of such repairs.

(4) A statement listing date of purchase, purchase price, market value of the property as of date of damage, and salvage value, where repair is not economical.

(5) Any other evidence or information which may have a bearing on the responsibility of the United States for the injury to or loss of property or the damages claimed.

(d) *Time limit.* All evidence required to be submitted by this Section shall be furnished by the claimant within a reasonable time. Failure of a claimant to furnish evidence necessary for a determination of his claim within 3 months after a request therefor has been mailed to his last known

address may be deemed an abandonment of the claim. The claim may be thereupon disallowed.

§ 793.5 Investigation, examination, and determination of claims.

When a claim is received, the constituent agency out of whose activities the claim arose shall make such investigation as may be necessary or appropriate for a determination of the validity of the claim and thereafter shall forward the claim, together with all pertinent material, and a recommendation based on the merits of the case, with regard to the allowance or disallowance of the claim, to the Office of General Counsel, National Credit Union Administration to whom authority has been delegated to adjust, determine, compromise and settle all claims hereunder.

§ 793.6 Final denial of claim.

(a) Final denial of an administrative claim shall be in writing and sent to the claimant, his attorney, or legal representative by certified or registered mail. The notification of final denial may include a statement of the reasons for the denial and shall include a statement that, if the claimant is dissatisfied with the action of the National Credit Union Administration, he may file suit in an appropriate U.S. District Court not later than 6 months after the date of mailing the notification.

(b) Prior to the commencement of suit and prior to the expiration of the 6-month period after the date of mailing, by certified or registered mail of notice of final denial of the claim as provided in 28 U.S.C. 2401(b), a claimant, his duly authorized agent, or legal representative, may file a written request with the National Credit Union Administration for reconsideration of a final denial of a claim under paragraph (a) of this Section. Upon the timely filing of a request for reconsideration the National Credit Union Administration shall have 6 months from the date of filing in which to make a final disposition of the claim and the claimant's option under 28 U.S.C. 2675(a) to bring suit shall not accrue until 6 months after the filing of a request for reconsideration. Final National Credit Union Administration action on a request for reconsideration shall be effected in accordance with the provisions of paragraph (a) of this Section.

§ 793.7 Payment of approved claims.

(a) Upon allowance of his claim, claimant or his duly authorized agent shall sign the voucher for payment, Standard Form 1145, before payment is made.

(b) When the claimant is represented by an attorney, the voucher for payment (S.F. 1145) shall designate both the claimant and his attorney as "payees." The check shall be delivered to the attorney whose address shall appear on the voucher.

§ 793.8 Release.

Acceptance by the claimant, his agent or legal representative, of any award, compromise or settlement made hereunder, shall be final and conclusive on the claimant, his agent or legal representative and any other person on whose behalf or for whose benefit the claim has been presented, and shall constitute a complete release of any claim against the United States and any employee of the Government whose act or omission gave rise to the claim, by reason of the same subject matter.

§ 793.9 Penalties.

A person who files a false claim or makes a false or fraudulent statement in a claim against the United States may be liable to a fine of not more than $10,000 or to imprisonment of not more than 5 years, or both (18 U.S.C. 287–1001), and, in addition, to a forfeiture of $2,000 and a penalty of double the loss or damage sustained by the United States (31 U.S.C. 231).

§ 793.10 Limitation on National Credit Union Administration's authority.

(a) An award, compromise or settlement of a claim hereunder in excess of $25,000 shall be effected only with the prior written approval of the Attorney General or his designee. For purposes of this paragraph, a principal claim and any derivative or subrogated claim shall be treated as a single claim.

(b) An administrative claim may be adjusted, determined, compromised or settled hereunder only after consultation with the Department of Justice when, in the opinion of the National Credit Union Administration:

(1) A new precedent or a new point of law is involved; or

(2) A question of policy is or may be involved; or

(3) The United States is or may be entitled to indemnity or contribution from a third party and the National Credit Union Administration is unable to adjust the third party claim; or

(4) The compromise of a particular claim, as a practical matter, will or may control the disposition of a related claim in which the amount to be paid may exceed $25,000.

(c) An administrative claim may be adjusted, determined, compromised or settled only after consultation with the Department of Justice when it is learned that the United States or any employee, agent or cost-plus contractor of the United States is involved in litigation based on a claim arising out of the same incident or transaction.

This regulation requires the NCUA operate all of its programs and activities to ensure nondiscrimination against qualified handicapped persons. It sets forth standards for what constitutes discrimination on the basis of mental or physical handicap, provides a definition for handicapped person and qualified handicapped person, and establishes a complaint mechanism for resolving allegations of discrimination. This regulation is issued under the authority of Section 504 of the Rehabilitation Act of 1973, as amended, which prohibits discrimination on the basis of handicap in programs or activities conducted by Federal executive agencies.

The regulation will not be reprinted here because of its length and the fact that it is not applicable to credit unions. If a copy is desired, it may be obtained by writing to: Office of the Chief Financial Officer, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

Part 794

Enforcement of Nondiscrimination on the Basis of Handicap in Federally Conducted Programs

Part 795

OMB Control Numbers Assigned Pursuant to The Paperwork Reduction Act

§ 795.1 OMB control numbers.

(a) *Purpose.* This subpart collects and displays the control numbers assigned to NCUA's information collection requirements by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995, 44 U.S.C. Chapter 35. NCUA intends to comply with the requirement that agencies display a current OMB control number upon the collection of information. 44 U.S.C. 3507(a)(3). The table does not include the currently valid OMB control numbers already on display in NCUA's forms, questionnaires, instructions, and other written collections of information. 5 CFR 1320.3(f).

(b) *Display.*

12 CFR part or section where identified and described	Current OMB control No.
701.1	3133–0015
701.14	3133–0121
701.21	3133–0139
	3133–0058
701.22	3133–0141
701.23	3133–0127
701.26	3133–0149
701.31	3133–0068
701.32	3133–0114
	3133–0117
701.33	3133–0130
701.34	3133–0140
701.36	3133–0040
702	3133–0154
703	3133–0133
704	3133–0129
706	3133–0165
707	3133–0134
708a	3133–0153
708b	3133–0024
	3133–0099
711	3133–0152
712	3133–0149
714	3133–0151
716	3133–0163
722	3133–0125
723	3133–0101
740.2	3133–0098
740.3	3133–0149
741	3133–0099
	3133–0142
	3133–0163
748	3133–0033
	3133–0108
749	3133–0032
	3133–0057
	3133–0058
	3133–0059
	3133–0080
760	3133–0143
792	3133–0146

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NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 745

Share Insurance and Appendix

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is amending its share insurance rules to simplify and clarify them and provide parity with the deposit insurance rules of the Federal Deposit Insurance Corporation (FDIC). Specifically, the amendments: Provide continuation of coverage following the death of a member and for separate coverage after the merger of insured credit unions for limited periods of time; clarify that the interests of nonqualifying beneficiaries of a revocable trust account are treated as the individually owned funds of the owner even where the owner has not actually opened an individual account; and clarify that there is coverage for Coverdell Education Savings Accounts, formerly Education IRAs.

DATES: This final rule is effective January 29, 2004.

FOR FURTHER INFORMATION CONTACT: Frank Kressman, Staff Attorney, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

NCUA staff identified part 745 as a regulation in need of updating, clarification and simplification. To that end, NCUA issued a proposed rule on June 26, 2003 to improve part 745 and maintain parity between the separate federal insurance programs administered by NCUA and FDIC. 68 FR 39868 (July 3, 2003).

NCUA proposed to provide a six-month grace period for members to restructure their insured accounts to maximize insurance coverage in each of two separate occurrences. Specifically, NCUA proposed the grace periods would take effect upon the death of a member and the merger of insured credit unions.

NCUA explained that the death of a member results in an immediate change in the ownership of the member's share accounts. This change in ownership could significantly change the amount of share insurance coverage available for those accounts, most likely reducing coverage.[1]

NCUA recognizes the practical difficulties a member's survivors might encounter in attempting to restructure the member's share accounts immediately after the member's death, and that these difficulties are worsened as they would occur at a time of grief when dealing with financial matters may be particularly difficult for the member's survivors. Accordingly, NCUA proposed to grant a six-month grace period after a member's death for his or her survivors to restructure the accounts. During this grace period, the insurance coverage of the deceased member's accounts would not change from that available immediately before the member's death, unless the accounts are restructured during the grace period by those authorized to do so. Because the intent of the proposal is to avoid reduced insurance coverage, the grace period would not be applied if doing so would result in decreased share insurance coverage.

NCUA also proposed a six-month grace period for members to restructure their insured accounts after the merger of insured credit unions. NCUA explained that a member's share accounts at an insured credit union are insured separately from that member's share accounts at any other separately chartered, insured credit union. When a member has accounts at more than one insured credit union, a merger of those credit unions could reduce the amount of share insurance coverage the member had before the merger.[2]

NCUA does not believe members should immediately have reduced share insurance coverage as a result of credit union mergers. Accordingly, NCUA proposed to provide members with a six-month grace period following the merger of insured credit unions, during which members will receive separate insurance of their accounts as though no merger had occurred. NCUA also proposed a methodology for extending insurance coverage for share certificates that mature at varying times in relation to the merger.[3]

NCUA believes insured credit unions should help their members benefit from these grace periods wherever possible and reasonable. We believe this can be done in a number of ways. For example, insured credit unions should make reasonable efforts to explain to their members how the grace periods operate. Merging credit unions are encouraged to make their members aware of the pending merger as soon as possible so members can evaluate their existing accounts and begin to plan how to restructure their accounts to maximize their coverage after the merger. Once a merger is completed, the surviving credit union should make reasonable efforts to notify members with uninsured funds as a result of the merger that the grace period has begun to run and assist members to restructure their accounts to maximize coverage. NCUA encourages insured credit unions to do all of these things as a service to their members and to minimize the potential for confusion regarding the coverage of their accounts.

In May 2000, Education IRAs were specified as insurable under NCUA's share insurance rules as irrevocable trust accounts. 65 FR 34921 (June 1, 2000). Since that time, Education IRAs have been replaced with Coverdell Education Savings Accounts. NCUA proposed to revise the share insurance rules to reflect that change.

NCUA also proposed to revise its revocable trust account insurance rule to address the frequent inquiries NCUA receives regarding how: (1) Revocable trusts are created; (2) an owner

[1] For example, a husband and wife may hold a joint account, a joint revocable trust account for the benefit of their two children, and two individual accounts in their own names. Assuming these accounts satisfy all applicable requirements, these four accounts would be insured up to a maximum of $800,000. The $800,000 is broken down as follows: $200,000 for the joint account; $400,000 for the joint revocable trust account; and $100,000 for each of the two individual accounts. Upon the death of either the husband or wife, however, the surviving spouse would become the sole owner of the joint account and the joint revocable trust account. Under NCUA share insurance rules, the joint account would be transformed into an individual account subject to aggregation with the surviving spouse's other individual account and insured up to a maximum of $100,000. The single ownership (individual) account in the name of the deceased spouse would continue to be insured separately from the other accounts. The maximum coverage of the joint revocable trust account would be reduced from $400,000 to $200,000, because coverage for this type of account is calculated as $100,000 for each combination of settlors and qualifying beneficiaries. In sum, the maximum coverage of the four accounts would be reduced immediately upon the death of the husband or wife from $800,000 to $400,000.

[2] For example, member X has a $75,000 individual account at insured credit union A and a $50,000 individual account at insured credit union B. Both accounts are fully insured because a member is entitled to $100,000 of coverage in the aggregate for all individual accounts in each insured credit union. 12 CFR 745.1; 12 CFR 745.3. If the credit unions merge, then X would have individual accounts in the surviving insured credit union totaling $125,000. X's individual accounts would be uninsured for $25,000.

[3] A share certificate that matures after the six-month grace period will receive the separate insurance treatment until the first maturity date following the grace period. One that matures during the six-month grace period and is renewed for the same term and amount will receive the separate insurance treatment until the first maturity date after the grace period under the terms of the renewed certificate. One that matures during the grace period that is not renewed, or is renewed on any basis other than for the same term and amount as the original certificate, is separately insured only for the six-month grace period.

demonstrates testamentary intent; and (3) the interests of nonqualifying beneficiaries are treated. In brief, NCUA explained that simple revocable trusts can be created at the credit union without the need for a formal written trust. NCUA proposed that the member's intent to create a revocable trust be noted in the title to the account. NCUA explained that common terms used in the account title to create a revocable trust and indicate the owner's intent include ''payable on death,'' ''in trust for,'' and ''as trustee for,'' or acronyms for these phrases, respectively, POD, ITF and ATF. NCUA explained that the account title ''John Smith POD'' is sufficient to create a revocable trust account. NCUA stated in the proposal it believed that naming the beneficiaries in the account *title* is the most effective way of establishing insurance coverage, but made it clear that, to be insurable, the beneficiaries must only be specifically named somewhere in the credit union's account *records*, not necessarily in the account *title*.

Finally, NCUA explained that it treats the interests of nonqualifying beneficiaries, those beneficiaries that are not the owner's spouse, child, grandchild, parent, brother or sister, as the individually owned funds of the owner of the account. In this context, these funds would be aggregated with all other individual accounts of the owner and insured up to $100,000. NCUA acknowledged that the current language of the rule could be read as providing that these nonqualifying beneficiary interests would only be insured as the individually owned funds of the owner if the owner has actually opened an individual account in the insured credit union where the revocable trust account is held. NCUA proposed to revise the rule to clarify that it will treat nonqualifying beneficiary interests as the individually owned funds of the owner even if the owner has not actually opened an individual account at the credit union. This is consistent with FDIC's treatment of these funds.

B. Summary of Comments

NCUA received sixteen comment letters regarding the proposed rule: Six from federal credit unions (FCUs), two from state credit unions, and eight from credit union trade organizations.

The commenters expressed general support for all of the proposed amendments, except for the titling requirement in the revocable trust account provision. Fifteen commenters strongly opposed the titling requirement and expressed the same or similar concerns. The concerns they cited included the great expense of updating their forms and systems. The commenters noted a host of problems the titling requirement would create for their computer-based data processing systems, which they stated presently cannot accommodate the additional titling information required by the proposal. Many of these commenters stated that the information NCUA proposes to be included in the account title could just as easily be captured elsewhere in the account documentation without the need to update forms or data processing systems. Six commenters were concerned that the titling requirement would apply to existing accounts and that it would be expensive and labor intensive to identify those accounts to alter their titles to comply with the proposal.

It appears from the comment letters that a significant number of commenters misread the titling requirement of the proposal and are under the impression it requires that beneficiaries be named in the title. As noted above, that is not the case. NCUA proposed only that a member's intent to create a revocable trust must be demonstrated in the title of the account using commonly accepted terms such as ''in trust for,'' ''as trustee for,'' ''payable on death to,'' or any acronym for these terms. As noted, NCUA stated that, while it prefers the beneficiaries also be listed in the title, it only requires that the beneficiaries be named somewhere in the share account records of the insured credit union.

NCUA's intent in proposing the titling requirement was to make it simpler for credit union members to create revocable trust accounts and to obtain the expanded insurance coverage they seek. NCUA did not anticipate the proposed requirement would create any significant, additional burden for credit unions and, moreover, did not intend to impose the requirement retroactively to existing revocable trust accounts. Nevertheless, as a result of the information provided by the commenters and other interested parties, NCUA has decided not to adopt the proposed titling requirement at this time because of the difficulties commenters identified that some FCUs would have in adapting their data processing systems and account forms. NCUA continues to believe that titling of revocable trust accounts so as to indicate the nature of the account would benefit FCUs in a number of ways, including enabling FCUs to help members better appreciate the nature of their accounts and share insurance coverage. NCUA encourages FCUs to modernize and maximize their data processing systems' capabilities as much as is practicable, given their circumstances, in this regard.

As noted, there was general support for all the other proposed amendments which include: Providing a six-month grace period for members to restructure their insured accounts upon the death of a member and the merger of insured credit unions; clarifying that the interests of nonqualifying beneficiaries of a revocable trust account are treated as the individually owned funds of the owner even where the owner has not actually opened an individual account; and clarifying that there is coverage for Coverdell Education Savings Accounts, formerly Education IRAs. There was little specific comment on these proposals except that two commenters suggested extending the six-month grace periods to one year. NCUA believes six months is a sufficient amount of time to restructure insured accounts and consistent with the FDIC's deposit insurance rules. Accordingly, these proposed amendments are adopted in the final rule without change.

C. Technical Correction

In 2000, NCUA amended Part 724 of its regulations to permit an FCU in a territory, including trust territories, or a possession of the United States, or the Commonwealth of Puerto Rico, to act as a trustee or custodian for certain pension or profit sharing plans. 65 FR 10933 (March 1, 2000). At the same time, NCUA amended § 745.9–2 of the share insurance rules to clarify that these accounts would be entitled to separate share insurance coverage. *Id.*

In a subsequent separate rulemaking, NCUA further amended § 745.9–2 to address coverage of accounts unrelated to the prior amendments to § 745.9–2 providing coverage of trust or custodial accounts. 65 FR 34921 (June 1, 2000). Inadvertently, the subsequent amendments to § 745.9–2 deleted the provision providing coverage for trust or custodial accounts. Accordingly, NCUA is reinstating those provisions as a technical amendment.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a proposed rule may have on a substantial number of small credit unions, defined as those under ten million dollars in assets. This rule only clarifies the share insurance coverage available to credit union members, without imposing any regulatory

burden. The final amendments would not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 745

Credit unions, Share insurance.

By the National Credit Union Administration Board on December 18, 2003.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 701 and 741

Suretyship and Guaranty; Maximum Borrowing Authority

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is revising its rules concerning maximum borrowing authority to permit federally insured, state-chartered credit unions (FISCUs) to apply for a waiver from the maximum borrowing limitation of 50 percent of paid-in and unimpaired capital and surplus (shares and undivided earnings, plus net income or minus net loss). This amendment will provide FISCUs with more flexibility by allowing them to apply for a waiver up to the amount permitted under state law.

NCUA is also adding a provision to its regulations that allows a federal credit union (FCU) to act as surety or guarantor on behalf of its members. The final rule establishes certain requirements to ensure that FCUs, and FISCUs if permitted under state law to act as a surety or guarantor, are not exposed to undue risk.

DATES: This final rule is effective March 26, 2004.

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

SUPPLEMENTARY INFORMATION:

A. Background

On September 24, 2003, the NCUA Board requested comment on proposed changes to §§ 701.20 and 741.2 of its regulations. 68 FR 56586 (October 1, 2003). Proposed § 701.20 created a new provision to recognize that an FCU, as part of its incidental powers, may act as a guarantor or surety on behalf of a member. Section 741.2 sets forth a maximum borrowing limitation of 50 percent of paid-in and unimpaired capital and surplus for all federally insured credit unions. The proposed amendment permitted federally insured, state-chartered credit unions (FISCUs) to apply for a waiver up to the amount permitted by state law.

B. Summary of Comments

The NCUA Board received 10 comments on the proposal: three from credit unions; three from credit union trade groups; two from credit union leagues; and two from bank trade groups. Below is a summary of the comments.

Suretyship and Guaranty

Eight of the ten commenters support allowing a credit union to act as a surety or guarantor. Two of the eight positive commenters suggested allowing FISCUs to apply for a waiver from the safety and soundness limitations placed on the transactions. One of the positive commenters suggested slightly different collateral requirements. The two negative commenters were the bank trade groups.

The positive commenters noted that allowing credit unions to enter into suretyship and guaranty agreements with the safety and soundness requirements in the proposal will give credit unions additional flexibility to meet the needs of their members while ensuring the safety and soundness of the transaction. The commenters noted that this activity could become a valuable service for credit unions. A couple of the commenters suggested, because this activity is so new for credit unions, that NCUA review the rule after it has been in effect for a few years to address any operational issues that may arise. The Board intends to incorporate this suggestion into its regulatory review process.

Two of the positive commenters suggested allowing FISCUs to apply for a waiver that would allow the state regulator or legislature to authorize more flexible guarantor or surety requirements. They suggest that a waiver only be granted if there are no safety and soundness implications. Because, as some of the commenters noted, this activity is new for credit unions, NCUA believes it is premature to adopt a waiver provision. The Board believes the requirements in the rule that would be the subject of a waiver all relate directly to safety and soundness, however, as NCUA and credit unions gain more experience in this area, the Board may reconsider this issue.

One of the commenters suggested that corporate credit unions have a role to play when a natural person credit union is acting as a guarantor for its member. The commenter recommended including deposits at corporate credit unions in the 100% collateral category. Because it is the natural person member that is providing the collateral and natural person members do not have deposits at corporate credit unions, we do not believe it is appropriate to implement this suggestion.

The two bank trade groups believe allowing credit unions to engage in these transactions conflicts with a credit union's mission of serving people of modest means. They also assert that allowing this activity is an expansion of a credit union's commercial lending powers and should not be allowed as long as credit unions are tax exempt. Congress has specifically authorized commercial lending for FCUs. 12 U.S.C. 1757a. Contrary to the bankers' claims, this rule is consistent with Congress' intent for FCUs with respect to serving their members and business lending.

Waiver of Maximum Borrowing Limitations for FISCUs

Eight of the ten commenters supported this proposal. The two negative commenters were the bank trade groups.

Those in support of the proposal contend that: It is inherent in the concept of dual chartering to allow state-chartered credit unions to exercise powers authorized under state law and regulation within the bounds of safety and soundness; the proposal's approach is similar to the approach used by the other banking agencies; and the waiver provision will assist FISCUs in providing service to low income families by allowing FISCUs to borrow from the Federal Home Loan Bank a greater amount than the regulatory limitation currently permits. Finally, a few of the positive commenters suggested NCUA seek similar authority for FCUs through a legislative change.

The two negative bank commenters expressed concern that the waiver provision could negatively impact on the safety and soundness of FISCUs. As noted in the proposal and echoed by many of the commenters, NCUA has incorporated the appropriate safeguards into the rule to ensure these transactions are handled in a safe and sound manner. One of the negative commenters incorrectly characterized the proposal as an ''attempt by the credit union industry to exceed its statutory, maximum borrowing authority.'' As noted in the proposal, the statutory limitation applies only to FCUs.

C. Final Amendments

New Sections 701.20 and 741.221--Suretyship and Guaranty

The final rule is identical to the proposal. Section 701.20 recognizes that an FCU, as part of its incidental powers, may act as a guarantor or surety on behalf of a member. 12 U.S.C. 1757(17). Acting as a guarantor or surety on behalf of an FCU member meets the definition of an incidental power because it: Is convenient or useful to an FCU in extending credit to its members; is a logical extension of an FCU's authority to make loans to its members and to

provide letters of credit on behalf of members; and involves risks that are similar in nature to the risks involved in an FCU's lending activity. 12 CFR 721.2.

The final rule defines suretyship, guaranty agreements, and principal and includes three requirements designed to ensure the safety and soundness of surety and guaranty agreements. The Board has the same safety and soundness concerns for FISCUs authorized under state law to enter into surety and guaranty agreements as it does for FCUs. Accordingly, the requirements will apply to FISCUs as provided in § 741.220. The requirements are modeled after the requirements in the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) rules on guaranty and suretyship. 12 CFR 7.1017 and 560.60.

The first two requirements are substantially similar to the requirements in the OTS rule. The first requires that the obligation under the agreement be limited to a fixed amount and limited in duration. Without a requirement to limit the amount and duration of the agreement, an FCU may take on more risk than it anticipated in the agreement.

The second provision requires that an FCU's performance under the agreement create a loan that is permissible under applicable law because the nature of a surety or guaranty agreement is a loan. The FCU is lending its credit and, in effect, is lending to its member. An FCU may not use a surety or guaranty agreement as a mechanism to avoid the applicable regulatory requirements for loans. These regulatory requirements are in place to ensure the safety and soundness of the transactions. For example, if an FCU will be a surety or guarantor for a member's obligation for a business loan, it must comply with the member business loan requirements. 12 CFR part 723.

This provision also highlights that an FCU must treat its obligation under the agreement as a contractual commitment to advance funds to the principal under the loans-to-one-borrower limits and loans to insider restrictions. 12 CFR 560.60(b)(3), 701.21(c)(5), (d) and 723.8. Again, these requirements are in place to ensure the safety and soundness of the transaction and should not be circumvented through the use of a surety or guaranty agreement.

The third provision addresses collateral requirements and parallels requirements in the OCC and OTS rules. Depending on the nature of the collateral, an FCU must have collateral equal to 100 or 110 percent of the obligation. The 100 percent collateral category includes cash, obligations of the United States or its agencies, obligations fully guaranteed by the United States or its agencies as to principal and interest, and notes, drafts, bills of exchange, and bankers' acceptances that are eligible for rediscount or purchase by a Federal Reserve Bank. Because the value of some of these types of collateral can fluctuate, the proposal requires that the collateral have a market value at the close of each business day equal to 100 percent of the FCU's total potential liability.

The 110 percent collateral category includes real estate and marketable securities. If the collateral is real estate, an FCU must establish the value of the collateral by an evaluation or appraisal of the real estate consistent with NCUA's appraisal regulation. 12 CFR 722.3. If the collateral is marketable securities, an FCU must be authorized to invest in the securities and must ensure that the value of the securities is equal to 110 percent of the obligation at all times. To protect against risk of loss, an FCU must perfect its security interest in the collateral.

Section 741.2--Maximum Borrowing Authority

The final rule is identical to the proposal. It allows an FISCU to apply for a waiver from § 741.2 up to the amount permitted under state law or by the state regulator. Prerequisites for a waiver request include that appropriate safeguards must be in place and that either state law permits the higher limit than that specified in the FCU Act for which the FISCU seeks approval, which is verified by the state regulator, or the state regulator has duly approved a higher limit than that allowed under state law. Instances in which it would seem appropriate to seek a waiver could include a situation where, for example, the borrowing has minimal risk associated with it but the FISCU is unable to enter into the transaction because of the regulatory prohibition. Circumstances presenting minimal risk could be, for example, a transaction where the FISCU is acting as a co-borrower with a member and the member has provided collateral sufficient to cover its obligation if the member defaults on the loan. The waiver process will permit regional directors to take into consideration the circumstances of the FISCU, its community, and members, and provide additional flexibility to address particular needs or benefits on a case-by-case basis. The final regulation contemplates that FISCUs wishing to engage in particular transactions, programs or projects, which would otherwise take their borrowings above the regulatory limitation, will have the opportunity to apply for a waiver, which will include a thorough explanation of the business purposes and strategies the FISCU has in place to mitigate risk, so that regional directors may make an informed determination regarding safety and soundness.

To apply for a waiver, an FISCU must submit its request to the appropriate regional director. The request must include a detailed analysis of the safety and soundness implications of the waiver, a proposed aggregate dollar amount or percentage of paid-in and unimpaired capital and surplus limitation, a letter from the state regulator approving the request, and an explanation demonstrating the need for a higher limit. The regional director will approve the waiver request if he or she determines that the proposed borrowing limit will not adversely affect the safety and soundness of the FISCU.

D. Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) requires NCUA to prepare an analysis to describe any significant economic impact any proposed regulation may have on a substantial number of small credit unions, defined as those under ten million dollars in assets. The rule authorizes FCUs to enter into surety and guaranty agreements and permits FISCUs to request a waiver from the maximum borrowing limitation. It is unlikely that small credit unions will participate in either of these activities. The final rule will not have a significant economic impact on a substantial number of small credit unions, and therefore, a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

The NCUA Board has determined that the final rule that allows FISCUs to file for a waiver from the borrowing limitations in § 741.2 is covered under the Paperwork Reduction Act. NCUA submitted a copy of the proposed rule to the Office of Management and Budget (OMB) for its review and is awaiting approval and issuance of a new OMB control number (3133-——).

Under the Paperwork Reduction Act of 1995, no persons are required to respond to a collection of information unless it has a valid OMB number. The control number will be displayed in the table at 12 CFR part 795.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to

consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule will apply directly to federally insured state-chartered credit unions. NCUA has determined that the final rule will not have a substantial direct effect on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that the final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999--Assessment of Federal Regulations and Policies on Families

NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105-277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1966 (SBREFA) (Pub. L. 104-121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of SBREFA.

E. Agency Regulatory Goal

NCUA's goal is clear, understandable regulations that impose a minimal regulatory burden. The final rule is understandable and imposes minimum regulatory burden.

List of Subjects

12 CFR Part 701

Credit unions.

12 CFR Part 741

Credit unions, Requirements for insurance.

By the National Credit Union Administration Board on February 19, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 708a

Conversion of Insured Credit Unions to Mutual Savings Banks

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is updating its rule regarding conversion of insured credit unions to mutual savings banks. This amendment requires a converting credit union to provide additional information in the notice to members of its intent to convert. Specifically, the credit union must disclose any economic benefit a director or senior management official of a converting credit union may receive in connection with the conversion. A converting credit union must also disclose how conversion to a mutual savings bank will affect members' voting rights, and how any subsequent conversion to a stock institution may affect ownership interests. NCUA believes this amendment enhances a member's ability to make informed decisions about the conversion without increasing the regulatory burden for converting credit unions and helps converting credit unions to more fully understand what NCUA expects to be included in the notice to members.

DATES: This final rule is effective March 26, 2004.

FOR FURTHER INFORMATION CONTACT: Frank Kressman, Staff Attorney, Office of General Counsel, at the above address or telephone: (703) 518-6540.

SUPPLEMENTARY INFORMATION:

A. Background

The Credit Union Membership Access Act (CUMAA) was enacted into law on August 7, 1998. Public Law 105-21. Section 202 of CUMAA amended the provisions of the Federal Credit Union Act (Act) concerning conversion of insured credit unions to mutual savings banks. 12 U.S.C. 1785(b). CUMAA required NCUA to promulgate final rules regarding charter conversions that were: (1) Consistent with CUMAA; (2) consistent with the charter conversion rules promulgated by other financial regulators; and (3) no more or less restrictive than rules applicable to charter conversions of other financial institutions. NCUA issued rules in compliance with this mandate. 63 FR 65532 (November 27, 1998); 64 FR 28733 (May 27, 1999).

In the approximately five years since NCUA first amended Part 708a to comply with CUMAA, NCUA has grown concerned that credit union members may not fully appreciate the effect the conversion may have on their ownership interests in the credit union and voting power in the mutual savings bank. Accordingly, NCUA issued a proposed rule in September 2003 to require a converting credit union to disclose additional information to its members to better educate them regarding the conversion. 68 FR 56589 (October 1, 2003).

B. Discussion

There are increasing indications that a high percentage of credit unions that convert to mutual savings banks have or will undertake a second conversion to become a stock institution. While it is certainly within the rights of the credit union membership to exercise their right to convert and change the structure of the institution, converting credit unions generally do not adequately discuss in the notice to credit union members the likelihood and ramifications of a second conversion to a stock institution.

While state laws may vary, under the Office of Thrift Supervision's regulations, there is no minimum waiting period for a newly chartered federal mutual savings bank to convert to a stock institution. As a result, it is possible for a credit union that converts to a federal mutual savings bank to attempt to convert to a stock institution in as little as two years. In most cases, a conversion from a mutual savings bank to a stock institution will result in a loss of ownership interest for the vast majority of members because they do not purchase stock, while most officers and directors do obtain stock in the newly created stock institution. While members and officials generally have the same opportunity to purchase stock at an initial public offering, officials also obtain stock through other methods such as employee stock ownership plans, restricted stock awards and stock options. These opportunities, which are not available to the general membership, have in the past been little understood and inadequately explained to the members.

While CUMAA provides that an insured credit union may convert to a mutual savings bank without the prior approval of NCUA, it also requires NCUA to administer the member vote on conversion and review the methods and procedures by which the vote is taken. This is reflected in NCUA's conversion rule. The rule requires a converting credit union to provide its members with written notice of its intent to convert. 12 CFR 708a.4. It also specifies that the member notice must adequately describe the purpose and subject matter of the vote on conversion. *Id.* In addition, a converting credit union must notify NCUA of its intent to convert. 12 CFR 708a.5. A credit union must provide for NCUA's review a copy of the member notice, ballot, and all other written materials it has provided or intends to provide to its members in connection with a conversion. *Id.*

A converting credit union has the option of submitting these materials to NCUA before it begins to distribute them to its members. *Id.* This enables a credit union to obtain NCUA's preliminary determination on the methods and procedures of the member vote based on NCUA's review of the written materials. A credit union can then decide whether to move forward with the often expensive, labor intensive conversion process with an understanding of NCUA's position. NCUA believes its review of these materials is a practical and unintrusive way of fulfilling, at least part of, its congressionally mandated responsibility to review the methods and procedures of the vote to ensure that all reasonable measures to accomplish full disclosure and transparency have been taken to inform the credit union membership of the potential consequences of their vote. Prior submission of these materials does not relieve the credit union of its other obligations under Part 708a, nor does it eliminate NCUA's right to disapprove the methods and procedures of the vote if the credit union fails to conduct the vote in a fair and legal manner. 12 CFR 708a.5.

If NCUA disapproves of the methods and procedures of the member vote, after the vote is conducted, then NCUA is authorized to direct a new vote be taken. 12 CFR 708a.7. NCUA interprets its responsibility to review the methods and procedures of the member vote to include determining that the member notice and other materials sent to the members are accurate and not misleading, that all required notices are timely, and that the membership vote is conducted in a fair and legal manner.

NCUA believes that full and proper disclosure to members that they could potentially lose their ownership interest in their credit union if it ultimately became a stock institution is key to describing the purpose and subject matter of the member vote adequately. Failing to discuss this integral risk associated with the conversion adequately is tantamount to providing misleading information. Most of the conversion documentation NCUA has reviewed since CUMAA went into effect has contained some information relating to this issue, but it has become apparent

to NCUA that it has not addressed it sufficiently to make this point clear to members.

A charter conversion is a sophisticated transaction with consequences that might not surface for a number of years and that are often not recognizable at the time of conversion to even the most astute members. As a result, few members can make a truly informed decision about how the conversion will affect their ownership interest in the credit union unless the credit union provides them with this information. Accordingly, for the reasons discussed above and in an effort to achieve full disclosure and transparency, NCUA amends Part 708a to require a converting credit union to disclose that the conversion from a credit union to a mutual savings bank could lead to members losing their ownership interests in the credit union if the mutual savings bank subsequently converted to a stock institution and the members do not become stockholders.

The Act provides that a member of a federal credit union is entitled to only one vote irrespective of the number of shares held by that member. The ''one member one vote'' structure gives an equal voice to all members, even those of modest means. 12 U.S.C. 1760. Most, if not all, state credit unions also are required to follow this approach. This is not usually the case with mutual savings banks. In most instances, mutual savings banks allot votes based on the amount of a member's deposits. Commonly, one vote is granted for each $100 a member has on deposit up to a maximum of 1,000 votes. Also, many issues, such as election of directors, which are subject to a member vote in a credit union, may not be subject to a vote in a mutual savings bank. As noted above, NCUA believes that disclosing that members could have lesser voting power in the mutual savings bank than they do in the credit union is central to describing adequately the purpose and subject matter of the member vote. Accordingly, for the reasons discussed above and in an effort to achieve full disclosure and transparency, NCUA amends Part 708a to require a converting credit union to disclose how the conversion from a credit union to a mutual savings bank will affect members' voting rights. The language of the proposal would have required a disclosure that the members may have lesser voting rights in a mutual savings bank. This final rule requires an actual explanation of how voting rights will change. This is a clearer articulation of the information the proposal intended members to receive and will assist members in casting a better informed vote on the proposed conversion.

NCUA's conversion rule echoes CUMAA by providing that directors and senior management officials of a credit union may not receive any economic benefit from the conversion of their credit union other than compensation and benefits paid to them in the ordinary course of business. 12 CFR 708a.10. This is intended to insure that management's decision to begin the conversion process is based on sound business judgment reflecting the best interests of the members. Consistent with this statutory and regulatory limitation, NCUA believes it is appropriate to require a converting credit union to disclose in the member notice any conversion related benefits a director or senior management official may receive, including compensation not permitted in the credit union context. To be complete, this disclosure must include any stock related benefits associated with a subsequent conversion to a stock institution. Accordingly, for the reasons discussed above and in an effort to achieve full disclosure and transparency, NCUA amends Part 708a to require a converting credit union to disclose any increased compensation or other conversion related benefits, including stock related benefits, that directors or senior management officials may receive. This disclosure must include a comparison of the stock related benefits available to the general membership with those available to officials and employees in the event of conversion to a stock institution. This comparison of stock benefits more clearly articulates the information the proposal intended members to receive and will assist members in casting a better informed vote.

C. Summary of Comments

NCUA received forty-five comment letters regarding the proposed rule: nine from federal credit unions, seven from state credit unions, one from a professional association representing the forty-eight state credit union regulators, sixteen from credit union trade organizations, two from state financial institution regulators, one from a financial services company that has been involved in facilitating the majority of credit union conversions to mutual savings banks, two from law firms that also have been involved in facilitating many credit union conversions to mutual savings banks (together these law firms and the financial services company will be referred to as conversion consultants), one from an attorney who represents credit unions, three from private individuals, and three from banking trade organizations.

Thirty-four of the commenters fully supported the proposal and acknowledged the importance of educating credit union members about the effects and ramifications of the conversion to enable them to cast informed votes. Over two-thirds of those supporters stated that they believe NCUA should impose more disclosures and requirements on converting credit unions than proposed. The kinds of additional disclosures and requirements they suggested include: requiring the member vote be conducted by an independent third party, establishing a voting standard greater than the present simple majority of those who actually vote, disclosing the percentage of credit unions that have converted to mutual savings banks that went on to convert to the stock form of ownership, disclosing the views of a converting credit union's directors who do not favor converting or have specific reservations, permitting members to post comments on the conversion proposal as a part of the conversion process, disclosing that voluntary liquidation of the credit union is an option for members to extract their ownership interests in the credit union if management believes the institution can no longer serve its members' needs as a credit union, increasing the number of members required for a quorum for special meetings to insure that there is sufficient member participation for such a monumental decision, disclosing the estimated cost of the conversion, providing additional financial data to support claims that the conversion will benefit members, and disclosing historical data regarding the percentage of stock management buys as compared to the amount members buy in a stock bank that previously converted from a credit union to a mutual savings bank to the stock form of ownership.

One commenter supported parts of the proposal, but opposed some sections it believes require speculation on the credit union's part. Three commenters stated that the current disclosure requirements are sufficient.

The conversion consultants and the banking trade organizations opposed the proposal. Some of these commenters believe the proposal is inconsistent with CUMAA, duplicates the disclosures required by other regulators like the Securities and Exchange Commission (SEC), the Federal Deposit Insurance Corporation (FDIC) and the Office of Thrift Supervision (OTS), or requires the credit union to determine whether it will *ever* convert to the stock form of ownership. One of these commenters stated that it did not believe that a credit

union disclosing its intent to convert to stock would enhance a member's ability to cast an informed vote. NCUA is aware of the limitations that CUMAA has placed on its authority to approve a conversion but is mindful of its responsibility to oversee the methods and procedures applicable to the member vote on conversion and protect the interests of credit union members. The proposal does not require a converting credit union to speculate about future events, rather it simply provides that the credit union must disclose its present intent regarding its business plans and provide information about how future events might affect members' interests. Although NCUA does not necessarily agree that the proposal duplicates disclosures required by the SEC, FDIC, and OTS, NCUA believes that, even if it did, these disclosures are necessary at the time the credit union's members are deciding how to vote on the conversion to a mutual savings bank. If credit union members wait to receive similar disclosures from the SEC, FDIC, or OTS, then that means the credit union has already converted to a mutual savings bank and may be on its way to converting to the stock form of ownership. Obviously, at that point, the disclosures are too late with respect to enabling a credit union member to make an informed decision on the conversion from a credit union to a mutual savings bank. For the reasons discussed above, NCUA adopts the proposed amendments as final without change.

D. Additional Information

NCUA appreciates the valuable suggestions offered by commenters who believe NCUA should impose more disclosures and requirements on converting credit unions. Many of these suggestions deserve further consideration but are beyond the scope of the proposal and will have to be considered in a separate rule making. Also, over time, NCUA has gained a more in-depth, practical understanding of the nuances of the disclosure and voting processes associated with a conversion. Accordingly, in the near future, NCUA intends to further fine tune the conversion regulation by providing more specific guidelines to help credit unions understand what will satisfy the regulatory standard that the vote be conducted in a fair and legal manner.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a proposed rule may have on a substantial number of small credit unions, defined as those under ten million dollars in assets. This rule provides the procedures an insured credit union must follow to convert to a mutual savings bank. The final amendments will not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999--Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105-277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104-121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 708a

Charter conversions, Credit unions.

By the National Credit Union Administration Board on February 19, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 745

Share Insurance; Living Trust Accounts

AGENCY: National Credit Union Administration (NCUA).

ACTION: Interim final rule with request for comments.

SUMMARY: NCUA is amending its share insurance rules to simplify them and maintain parity with the deposit insurance rules of the Federal Deposit Insurance Corporation (FDIC). Specifically, the amendment changes the existing rules concerning coverage for beneficial interests in living trust accounts. The rules are amended by eliminating the provisions that would limit insurance coverage where the interest of the beneficiary is subject to a defeating contingency in a living trust agreement. With the amendment, share insurance coverage of up to $100,000 is provided per qualifying beneficiary who, as of the date of an insured credit union's failure, would become the owner of assets in the living trust upon the account owner's death. The FDIC recently amended its deposit insurance rules by making a similar change. This amendment is adopted as an interim rule to provide parity between NCUA and FDIC insurance regulations and aid the public and prevent confusion over the amount of Federal account insurance available on those accounts.

DATES: This final rule is effective on April 1, 2004. Comments must be received on or before April 26, 2004.

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. You are encouraged to fax comments to (703) 518–6319 or e-mail comments to *regcomments@ncua.gov* instead of mailing or hand-delivering them. Whatever method you choose, *please send comments by one method only.*

FOR FURTHER INFORMATION CONTACT: Ross Kendall, Staff Attorney, Office of General Counsel, at the above address or telephone: (703) 518–6562.

SUPPLEMENTARY INFORMATION:

A. Background

Living trusts have become an increasingly popular way for individuals to transfer assets outside of probate while retaining control of the funds during their lifetime. Where a grantor establishes a share account with funds that are subject to a separate living trust agreement, share insurance coverage is provided in accordance with NCUA's rules that govern revocable trust accounts. 12 CFR 745.4. The NCUA believes, based on its experience and upon the experience of the FDIC, that many persons who have established living trust accounts do not understand the impact under the current rules of a defeating contingency on the availability of separate insurance coverage for beneficial interests in the account, even for ''qualifying beneficiaries'' (the spouse, child, grandchild, parent or sibling of the grantor).

The rules were designed to cover a straightforward ''payable on death'' account, sometimes simply referred to as a ''POD'' account, that provides for the payment of any balance remaining in an account upon its owner's death to specified beneficiaries. Evidence of the intent of the account owner to pass funds to one or more beneficiaries may be as simple as a designation in the account signature card such as ''POD.'' By contrast, a living trust arrangement involves a separate, often complex trust document that may specify that an identified beneficiary's right to receive some portion of the account balance is dependent upon certain conditions.

Currently, if the interest of a qualifying beneficiary in an account established under the terms of a living trust agreement is contingent upon fulfillment of a specified condition, referred to as a defeating contingency, separate insurance is not available for that beneficial interest. Instead, the beneficial interest would be added to any individual account(s) of the grantor and insured to a maximum of $100,000. Because the coverage for these types of accounts is under the same rules that govern a simple ''payable on death'' account, members and credit unions sometimes mistakenly believe that interests in living trusts are automatically insured up to $100,000 per qualifying beneficiary.

An example of a defeating contingency is where an account owner names his son as a beneficiary but specifies in the living trust document that his son's ability to receive any share of the trust funds is dependent upon him successfully completing college. Another common example is where a grantor's will provides that funds in the living trust account can be used to satisfy a legacy made in the will. A third example is where the interest of one beneficiary is dependent upon another beneficiary's surviving the grantor. In each case, the current rule operates to prevent separate insurance coverage, even for a qualifying beneficiary, because his or her interest is contingent.

Even though the existing rules contain a definition of a defeating contingency and an explanation of how such a contingency can defeat separate insurance coverage, our experience, consistent with that of the FDIC, is that the operation of the rule is not widely understood. NCUA recognizes that the rules governing the insurance of living trust accounts are complex and confusing. The FDIC reports that it has had to deny separate insurance coverage for some beneficiaries of living trusts in cases where it was clear that the grantor was not aware of the impact of language in the trust agreement. NCUA staff have reviewed recent examples of trust agreements that appear to have inadvertently created defeating contingencies that would thwart separate insurance for otherwise qualifying beneficiaries. In addition, the current rules may require a detailed review of the trust documents to determine if a defeating contingency exists. This effort is both difficult and time consuming.

B. Parity With FDIC Deposit Insurance Rules

The changes will minimize confusion about the application of NCUA's insurance rules to these types of accounts and maintain parity with FDIC insurance on similar accounts at banks and savings associations. The policy of the NCUA Board is to maintain parity with the FDIC, since the account insurance funds administered by both agencies are backed by the full faith and credit of the Federal Government. NCUA believes it important that members of the public who use living trust accounts for the future transfer of ownership of family assets without loss of control during the owner's life receive the same protection, whether the accounts are maintained at credit unions or other federally insured institutions.

C. The Interim Rule

NCUA has revised the current living trust account rules to provide for insurance coverage of up to $100,000 per qualifying beneficiary who, as of the date of a credit union's failure, would become entitled to the living trust assets upon the owner's death. While this approach provides insurance coverage for qualifying beneficial interests irrespective of defeating contingencies, a beneficiary's trust interest that is dependent upon the *death* of another trust beneficiary will still not qualify for separate insurance. If a beneficiary's interest is subordinate only to a life

estate of another beneficiary, that interest will be insured. The amended rule allows for separate insurance for both the life estate and the remainder interest for qualified beneficiaries.

An example that illustrates the basic rule is where an account established under a living trust provides that the trust assets go in equal shares to the grantor's three children upon the grantor's death. This account would be eligible for $300,000 of deposit insurance coverage. The coverage would still be $300,000 even if the trust provides that the funds would go to the children only if each graduates from college before the owner's death because defeating contingencies will no longer be relevant for deposit insurance purposes.

Another example would be where a living trust provides that the owner's spouse becomes the owner of the trust assets upon the owner's death but, if the spouse predeceases the owner, the three children then become the owners of the assets. In this case, if the spouse is alive when the credit union fails, the account will be insured up to a maximum of $100,000, because only the spouse is entitled to the assets upon the owner's death. If at the time of the credit union failure, however, the spouse had predeceased the owner, then the account would be eligible for up to $300,000 coverage because there would be three qualifying beneficiaries entitled to the trust assets upon the owner's death.

Consistent with the FDIC's position, the NCUA has also determined not to require a credit union to maintain records disclosing the names of living trust beneficiaries and their respective trust interests. The FDIC solicited comment specifically on this matter and concluded that to do so would be unnecessary and burdensome. The NCUA Board concurs with that judgment, recognizing that a grantor may elect to change the beneficiaries or their interests at any time before his or her death and that requiring a credit union to maintain a current record of this information is impractical and unnecessarily burdensome. The general principles governing share insurance coverage in NCUA's regulations, however, require that the records of the credit union disclose the basis for any claim of separate insurance. 12 CFR 745.2(c). This obligation may be met if the title of the account or other credit union records refer to a living trust. The final rule makes reference to this fact, but specifically disclaims any requirement that the credit union's records must identify beneficiaries or disclose the amount or nature of their interest in the account.

NCUA believes the final rule achieves two important objectives: simplifying the existing rule and providing consistency in how insurance coverage is determined for all types of revocable trust accounts. With the amendment, both living trust accounts and ''payable on death'' accounts will have insurance coverage calculated in the same fashion. In each case, coverage is based upon the interest of the beneficiaries who will receive the account funds when the owner dies, determined as of the date of the credit union's failure, regardless of any contingencies or conditions affecting those interests. In addition, the amendment will provide credit unions and their members with a better understanding of the share insurance coverage rules and will help to eliminate the present confusion surrounding the coverage of living trust accounts.

Non-qualifying beneficiaries

The amendment does not change the way in which non-qualifying beneficiaries are treated for share insurance purposes. As is the case with traditional revocable trust accounts, a beneficiary must be the spouse, child, grandchild, parent or sibling of the grantor in order to qualify for separate insurance coverage. The interest of any non-qualifying beneficiary will be added to any other single-ownership or individual funds of the grantor and insured to a maximum of $100,000.

Life estate and remainder interests

Living trusts sometimes provide for a life estate interest for designated beneficiaries and a remainder interest for other beneficiaries. The final rule addresses this situation by deeming each life estate holder and each remainder beneficiary to have an equal interest in the trust assets and provides up to $100,000 coverage per qualifying beneficiary. For example, assume a grantor creates a living trust providing for a spouse to have a life estate interest in the trust assets with the remaining assets going to their two children upon the spouse's death. The assets in the trust are $300,000 and a living trust account is opened for that full amount. Unless otherwise indicated in the trust, the NCUA would deem each of the beneficiaries to own an equal share of the $300,000, and the full amount would be insured. This result would be the same even if the spouse has the power to invade the principal of the trust, because, under the amended rule, defeating contingencies are no longer relevant for insurance purposes.

Another example would be where the living trust provides for a life estate interest for the grantor's spouse and remainder interests for two nephews. As in the preceding example, each beneficiary would be deemed to have an equal ownership interest in the trust assets, unless there were an indication specifying different ownership interests. Here the life estate holder is a qualifying beneficiary, the grantor's spouse, but the remainder beneficiaries, the grantor's nephews, are not. As such, assuming an account balance of $300,000, the living trust account would be insured for *at least* $100,000 because the grantor's spouse is a qualifying beneficiary. The $200,000 attributable to the grantor's nephews would be insured as the grantor's single-ownership funds. If the grantor has no other single-ownership funds at the same credit union, then only $100,000 would be insured. Thus, the $300,000 in the living trust account would be insured for a total of $200,000 and $100,000 would be uninsured. The NCUA believes this is a simple, balanced approach to insuring living trust accounts where the living trust provides for one or more life estate interests and is also consistent with the FDIC's approach.

Appendix

The interim rule makes a corresponding change to Example 4, under part B of the appendix to part 745, to reflect this amendment. It removes language that had been in that example discussing the need to determine whether a defeating contingency adds an example to illustrate the operation of the rule in cases involving a life estate and remainder interests.

D. Request for Comments

The Administrative Procedure Act requires that an agency must provide an opportunity for public comment before issuing a final rule unless it finds for ''good cause'' that public comment is impracticable, unnecessary, or contrary to the public interest. 5 U.S.C. 553(b)(B). The NCUA Board has determined that public comment is unnecessary and contrary to the public interest because: The rule preserves parity with recently amended account insurance rules administered by the FDIC, 69 FR 2825 (January 21, 2004); the rule benefits credit union members and employees by simplifying how to determine the amount of coverage available on a commonly used account; it increases the amount of coverage that is available for the benefit of credit union members; and it does not prejudice credit union members or credit unions or require

changes to current practices. Nevertheless, this is an interim final rule, and the Board will accept comments for a period of 60 days following the date of publication in the **Federal Register**. All comments will be considered and the rule may be changed in light of the comments received.

E. Effective Date

To avoid confusion and preserve parity with the FDIC, this interim rule will become effective on April 1, 2004, the beginning of the next calendar quarter following publication in the **Federal Register**. Consistent with the FDIC's approach, the rule will apply as of that date to all living trust accounts unless, upon the failure of an insured credit union, a member who established a living trust account prior to April 1, 2004, elects coverage under the previous living trust account rules. If a credit union fails between the date of publication in the **Federal Register** and April 1, 2004, NCUA will apply the final rule if doing so will result in greater coverage for a living trust account.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a proposed rule may have on a substantial number of small credit unions, defined as those under ten million dollars in assets. This rule only clarifies the share insurance coverage available to credit union members, without imposing any regulatory burden. The final amendments would not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the States, on the connection between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999--Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. NCUA has obtained the determination of the Office of Management and Budget that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 745

Credit unions, Share insurance.

By the National Credit Union Administration Board on February 19, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 701 and 790

Organization and Operations of Federal Credit Unions; Description of NCUA

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The National Credit Union Administration (NCUA) Board decided to restructure NCUA's regions, effective January 1, 2004, due to economic and operational factors. The final rule amends the NCUA's regulations to reflect the resulting elimination of one office and the relocation of another office. The final rule also amends the office description of NCUA's Executive Director to include the delegated responsibility of being the NCUA's Director of Equal Employment Opportunity (EEO).

EFFECTIVE DATE: January 1, 2004.

FOR FURTHER INFORMATION CONTACT: Regina Metz, Staff Attorney, Division of Operations, Office of General Counsel, (703) 518–6540, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

SUPPLEMENTARY INFORMATION: The NCUA Board is amending parts 701 and 790 of its regulations, to conform them to the restructuring of NCUA's regional office locations. 12 CFR parts 701, 790. The NCUA is transitioning from six regional offices to five, and relocating its California office to Arizona. The new regional structure is effective January 1, 2004, but we note that the Lisle, Illinois office will remain open until April 3, 2004. In part 701, the office addresses are found in Appendix C to NCUA's Interpretive Ruling and Policy Statement (IRPS) 03–1.

The Board is also amending part 790 to reflect that, while the NCUA Board has ultimate responsibility for all equal employment opportunity programs within NCUA, the Board has delegated responsibility to NCUA's Executive Director to be Director of EEO.

Regulatory Procedures

Final Rule Under the Administrative Procedure Act

The revisions made to this part are not subject to the notice and comment provisions of the Administrative Procedure Act (APA), 5 U.S.C. 551 *et seq.* The final rule revisions relate only to matters relating to agency management and personnel, topics exempt from APA requirements. 5 U.S.C. 553(a)(2).

Effective Date

NCUA also finds good cause to dispense with the 30-day delayed effective date requirement under the APA. 5 U.S.C. 553(d)(3). The rule relates only to internal agency operations. The rule will, therefore, be effective on the day the new regional structure is effective, January 1, 2004.

Regulatory Flexibility Act

An initial regulatory flexibility analysis under the Regulatory Flexibility Act is required only when an agency is required to publish a general notice of proposed rulemaking for any proposed rule. 5 U.S.C. 603. As noted previously, NCUA has determined that it is unnecessary to publish a notice of proposed rulemaking for this rule. Accordingly, an initial regulatory analysis is not required. Moreover, since this final rule imposes no new requirements and makes only housekeeping amendments, NCUA has determined and certifies that this rule will not have any significant economic impact on a substantial number of small credit unions (primarily those under $10 million in assets).

Small Business Regulatory Enforcement Fairness Act

Title II of the Small Business Regulatory Enforcement Fairness Act (SBREFA) of 1996 (Pub. L. 104–121) provides, generally, for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the APA. 5 U.S.C. 551. The Office of Management and Budget has reviewed this rule and has determined that for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996 it is not a major rule.

Paperwork Reduction Act

NCUA has determined that the final rule does not increase paperwork requirements under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*) and regulations of the Office of Management and Budget.

Executive Order 13132 Statement

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their regulatory actions on State and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the Executive Order. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the Executive Order.

The Treasury and General Government Appropriations Act, 1999--Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

List of Subjects in 12 CFR Parts 701 and 790

Credit unions.

By the National Credit Union Administration Board on February 20, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 795

OMB Control Numbers

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is updating its listing of regulations and their corresponding Office of Management and Budget (OMB) control numbers to comply with Paperwork Reduction Act requirements.

DATES: Effective March 16, 2004.

ADDRESSES: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428.

FOR FURTHER INFORMATION CONTACT: Regina M. Metz, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

NCUA is amending its regulation on OMB control numbers to reflect changes in NCUA's information collection requirements and related OMB's control numbers occurring since NCUA last revised the display table. 12 CFR 795.1; 64 FR 49080, Sept. 10, 1999. NCUA displays the control numbers to comply with the Paperwork Reduction Act of 1995, 44 U.S.C. Chapter 35, and OMB's implementing regulation, 5 CFR part 1320.

The regulation conforms with OMB's recommendation that agencies issuing regulations that contain information collections display the related control numbers in a table in the CFR. 5 CFR 1320.3(f)(3) and 1320.5(b)(2)(ii)(C). The table identifies those NCUA regulations with their corresponding OMB control numbers but excludes, as recommended by OMB, OMB control numbers already displayed in NCUA's forms, questionnaires, instructions, and other written collections of information. 12 CFR 795.1(b); 5 CFR 1320.3(f).

B. Final Rule

The NCUA Board is issuing the amendments to § 795.1 as a final rule because the publication of the OMB numbers in a display table provides information to the public in a recommended format. Therefore, public comment and a delayed effective date are both unnecessary. If the rule is effective upon publication, then NCUA can immediately display the updated table. Accordingly, for good cause, the Board finds that, under 5 U.S.C. 553(b)(3)(B), notice and public procedures are impracticable, unnecessary, and contrary to the public interest; and, under 5 U.S.C. 553(d)(3), the rule will be effective immediately and without 30 days advanced notice of publication.

C. Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a rule may have on a substantial number of small entities, primarily those under one million dollars in assets. The final rule will not have a significant economic impact on a substantial number of small credit unions, and therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. This final rule would not have substantial direct effects on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Act. 5 U.S.C. 551. OMB is reviewing this rule to determine whether it is major for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 795

Credit unions, Collection requirements.

By the National Credit Union Administration Board on March 5, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 701, 703, 709, 715, 723, and 725

Technical Corrections

AGENCY: National Credit Union Administration.

ACTION: Final rule.

SUMMARY: The National Credit Union Administration (NCUA) Board is issuing a final technical corrections rule. The rule corrects cross-references, updates references to NCUA publications, and makes minor typographic corrections.

DATES: This rule is effective May 17, 2004.

FOR FURTHER INFORMATION CONTACT: Paul Peterson, Staff Attorney, Division of Operations, Office of General Counsel, at the National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428 or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

The Board has a policy of continually reviewing NCUA regulations to ''update, clarify and simplify existing regulations and eliminate redundant and unnecessary provisions.'' NCUA Interpretive Rulings and Policy Statement (IRPS) 87–2, Developing and Reviewing Government Regulations. The NCUA staff's most recent review of NCUA's regulations revealed the need for several minor updates and corrections.

Section 701.21(i)(4) currently states that Federal credit unions must account for financial options contracts transactions in accordance with the NCUA Accounting Manual for Credit Unions, but the current version of the Accounting Manual does not address financial options contracts accounting. 12 CFR 701.21(i)(4). Accordingly, the Board amends § 701.21(i)(4) to delete the reference to the Accounting Manual.

Section 703.1(b)(6) contains an incorrect reference to § 741.3(a)(3). The correct reference should be to § 741.3(a)(2). The Board amends § 703.1(b)(6) to make this correction.

Sections 709.1(c) and 725.18(c) contain incorrect references to § § 700.1(j) and 700.1(k), respectively. The correct references should both be to § 700.2(e)(1). The Board amends § § 709.1(c) and 725.18(c) to make this correction.

In § 715.3(a), the conjunction ''and'' that should be between the two subparagraphs (1) and (2) is incorrectly placed in the second subparagraph. The Board amends § 715.3(a) to correct this.

In the first sentence of § 723.20(b), the phrase ''members business loan rule'' should be ''member business loan rule.'' In § 723.21, the capitalization of ''Net Member Business Loan Balance'' should be changed to ''Net member business loan balance'' to make it consistent with the format of the other definitions in that section. The Board amends § § 723.20(b) and 723.21 to make these changes.

B. Regulatory Procedures

Final Rule Under the Administrative Procedure Act

The amendments in this rule are technical rather than substantive. NCUA finds good cause that notice and public comment are unnecessary under sec. 553(b)(B) of the Administrative Procedure Act (APA), 5 U.S.C. 553(b)(B). NCUA also finds good cause to dispense with the 30-day delayed effective date requirement under sec. 553(d)(3) of the APA. The rule will, therefore, be effective immediately upon publication of this notice.

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a rule may have on a substantial number of small entities (those credit unions under ten million dollars in assets). This rule will not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that this rule will not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on State and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. This rule will not have substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

List of Subjects

12 CFR Part 701

Credit unions.

12 CFR Part 703

Credit unions, Investments.

12 CFR Part 709

Credit unions, Liquidations.

12 CFR Part 715

Audits, Credit unions, Supervisory committees.

12 CFR Part 723

Credit, Credit unions.

12 CFR Part 725

Credit unions, Liquidity.

By the National Credit Union Administration Board on May 11, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 703 and 704

Investment in Exchangeable Collateralized Mortgage Obligations

AGENCY: National Credit Union Administration.

ACTION: Final rule.

SUMMARY: The National Credit Union Administration (NCUA) is issuing final revisions to its regulations regarding investment in collateralized mortgage obligations (CMOs) to authorize all federal credit unions (FCUs) and corporate credit unions to invest in exchangeable CMOs representing interests in one or more SMBS subject to certain safety and soundness limitations. Currently, NCUA regulations prohibit FCUs and certain corporate credit unions from investing in stripped mortgage backed securities (SMBS) and exchangeable CMOs that represent interests in one or more SMBS. NCUA has safety and soundness concerns with direct investment in SMBS, but recognizes that some exchangeable CMOs representing interests in one or more SMBS may be safe investments for credit unions. This rule will also authorize FCUs and corporate credit unions to accept exchangeable CMOs as assets in a repurchase transaction or as collateral on a securities lending transaction regardless of whether the CMO contains SMBS. Finally, this rule contains miscellaneous technical corrections and minor changes to NCUA's Investment and Deposit Activities rule and Corporate Credit Unions rule.

DATES: This rule is effective August 2, 2004.

FOR FURTHER INFORMATION CONTACT: Steve Sherrod, Senior Investment Officer, Office of Strategic Program Support and Planning (OSPSP) at the above address or telephone (703) 518–6620; Kim Iverson, Senior Investment Officer, Office of Strategic Program Support and Planning, at the above address or telephone (703) 518–6620; George Curtis, Corporate Program Specialist, Office of Corporate Credit Unions at the above address or telephone (703) 518–6640; or Paul Peterson, Staff Attorney, Office of General Counsel, at the above address or telephone (703) 518–6555.

SUPPLEMENTARY INFORMATION:

A. Background

The Federal Credit Union Act permits FCUs and corporate credit unions to purchase mortgage related securities (MRS) subject to such regulations as the NCUA Board may prescribe. 12 U.S.C. 1757(15)(B). NCUA regulations generally permit the purchase of CMOs, a multi-class MRS, but not if the CMO is a stripped mortgage backed security (SMBS). 12 CFR 703.14(d) and 703.16(e); 704.5(c)(5) and (h)(4). SMBS include interest-only CMOs (IOs) and principal-only CMOs (POs).

Currently, many CMO issues contain one or more classes of exchangeable CMOs. An exchangeable CMO represents a beneficial ownership interest in a combination of two or more underlying CMOs, and the owner may pay a fee and take delivery of the underlying CMOs. In many cases, these underlying CMOs include IOs and POs.

Because NCUA regulations prohibit investment in SMBS, the regulations also prohibit investment in an exchangeable CMO that represents an interest in one or more IOs or POs. Certain exchangeable CMOs representing IOs or POs, however, do not carry the risk or raise the same safety and soundness concerns associated with direct investment in an SMBS.

On January 22, 2004, the NCUA Board issued a notice of proposed rulemaking to amend NCUA rules to authorize FCUs and corporate credit unions to invest in an exchangeable CMO representing interests in one or more IOs or POs if the exchangeable CMO meets certain conditions. 69 FR 4886 (February 2, 2004).

The first condition concerned the rate of amortization of the underlying IOs and POs. For an exchangeable CMO representing one or more IOs, the Board proposed that the notional principal of each IO must decline at the same rate as the principal on one or more non-IO CMOs included in the combination. For an exchangeable CMO representing one or more POs, the Board proposed that the principal of each PO must decline at the same rate as the notional principal of one or more IOs included in the combination or at the same rate as the principal on one or more interest-bearing CMOs included in the combination. The Board also proposed a second condition: that, at the time of purchase, the ratio of the market price of the CMO to its remaining principal balance is between .8 and 1.2, meaning that the discount or premium of the market price to par must be less than 20 points. The proposed rule also stated that credit unions may not exercise the right to exchange an exchangeable CMO if it represents an interest in one or more SMBS that would be impermissible for that credit union to hold as a separate investment.

The Board's proposal also contained several definitional changes and other technical corrections to Parts 703 and 704 of NCUA's rules and regulations. In Part 703, the Board proposed to add a definition of ''collateralized mortgage obligation;'' amend the definitions of ''put,'' ''call,'' ''custodial agreement,'' ''derivative,'' and ''european financial options;'' and change the phrase ''nationally recognized statistical rating agency'' to ''nationally recognized statistical rating organization.'' In Part 704, the Board proposed to add a definition of ''derivative,'' amend the definitions of ''small business related security'' and ''weighted average life,'' and change the phrase ''interest rate risk simulation tests'' to ''interest rate sensitivity analysis requirements.''

B. Summary of Changes From the Proposed Rule

In this final rule, the Board generally adopts the rule as proposed with some variations. The Board will permit the purchase of exchangeable CMOs representing interests in SMBS only if the CMOs satisfy the conditions established in the proposed rule. The final rule differs from the proposed rule as follows: First, the Board believes that CMOs are not appropriate for all credit unions, and notes that those with investment authority at a credit union must be qualified by education or experience to assess the risk characteristics of every investment that they make, including CMOs. Since exchangeable CMOs are a more complex investment, the final rule specifically requires that a credit union seeking to invest in exchangeable CMOs must have the expertise to apply the unique price range and amortization conditions in this rule. Second, the final rule relaxes the proposed conditions on exchangeable CMOs containing SMBS, but only for CMOs that are accepted by the credit union as assets associated with repurchase transactions or as collateral associated with securities lending transactions. Third, the rule clarifies that derivatives in the form of interest rate lock commitments and forward sales commitments on loans originated by the credit union are not prohibited. Fourth, the rule changes the NCUA office to which applications for an Investment Pilot Program should be addressed from the Office of Examination and Insurance to the Office of Strategic Program Support and Planning.

C. Public Comments

NCUA received 30 comment letters regarding the proposed rule. Many commenters supported the

exchangeable CMO portion of the proposed rule without reservation, and all but a few of the remaining commenters expressed general support for the Board's intent to allow credit unions to invest in certain exchangeable CMOs containing strips. In addition, the commenters uniformly supported the miscellaneous technical corrections and clarifying amendments.

Comments Requesting Elimination of the Proposed Safety and Soundness Conditions

Several commenters supported authorizing credit unions to purchase exchangeable CMOs representing SMBS without conditions, or with significantly lesser conditions, than those NCUA proposed.

One commenter suggested that NCUA authorize credit unions to buy any exchangeable CMO containing strips, without restriction, so long as the credit union does not exercise the exchange option. This commenter believes a simple statement that the exchange option cannot be exercised is sufficient, and no other conditions are necessary.

Several commenters thought that, for corporate credit unions, NCUA should focus on the interest rate risk associated with the corporate's aggregate portfolio and should not place conditions on particular individual investments such as exchangeable CMOs and strips. These commenters believe that the proposed conditions on the purchase of individual exchangeable CMOs are unnecessary and overly complex in light of the requirement that corporate credit unions conduct a periodic interest rate sensitivity analysis on their investment portfolios and limit their risk exposure as described in § 704.8. 12 CFR 704.8.

Two commenters said NCUA should allow FCUs to invest directly in SMBS, and in exchangeable CMOs containing SMBS, without restriction when used for the purpose of reducing balance sheet risk and earnings volatility.

One commenter suggested that credit unions qualifying under NCUA's Regulatory Flexibility Program, 12 CFR part 742, should be exempt from the Part 703 prohibition on investment in SMBS and any prohibition on exchangeable CMOs representing SMBS.

A few commenters question the need for the proposed rule. One of these commenters stated, ''It appears that the proposed rule is basically seeking to prevent practices that simply do not exist today. Current rules clearly state that investing in IO and PO Strips is not allowed because of the highly volatile nature of theses investments. Exchangeable CMOs are clearly not MBS strips.'' The commenter requests a simple clarification that ''a credit union may not exercise the right to exchange an exchangeable CMO nor undertake any re-engineering of mortgage cash flows that results in the creation of securities that are impermissible under NCUA rules and regulations.''

While the Board appreciates these comments, it is concerned about the volatile and risky nature of SMBS. The Board believes SMBS are generally inappropriate investments for credit unions and are not normally well suited to risk reduction practices such as hedging, even in a well-run credit union or a credit union conducting aggregate portfolio interest rate risk analysis. On the other hand, the Board agrees that very few, if any, of the existing exchangeable CMOs that represent SMBS are overly risky. In fact, the Board believes that all or almost all currently existing exchangeable CMOs satisfy the safety and soundness conditions imposed in the final rule. Nevertheless, the securities market is constantly evolving, and the Board anticipates that, in the future, the market may include exchangeable CMOs representing SMBS that do have the substantive risks of those SMBS. The Board wants to make clear in this rulemaking how federal credit unions and corporate credit unions can determine the permissibility of any exchangeable CMO representing SMBS.

Comments Expressing Concern About the Complexity of Exchangeable CMO Investments

Two commenters remarked on the complexity of the exchangeable CMO investment and thought credit unions that invest in them should demonstrate a complete understanding of how these products work and the risks they entail. Another commenter noted that SMBS are volatile and should only play a limited role, if any, as a core investment. Still another commenter thought NCUA should not authorize credit unions to purchase exchangeable CMOs representing SMBS because of a perceived lack of expertise and sophistication at some credit unions.

The Board appreciates that CMOs may offer a unique risk-reward tradeoff among the various investments permitted for FCUs by the FCU Act, and that CMOs may play an important role in a well-diversified investment portfolio. Still, the Board agrees with these commenters that CMOs are not appropriate investments for all credit unions and notes that NCUA's investment regulation specifically provides that ''those with investment authority [at the FCU] must be qualified by education or experience to assess the risk characteristics of investments and investment transactions.'' 12 CFR 703.3(g). The Board expects FCUs and corporate credit unions to understand each and every investment that they make, including CMOs, and how those investments work. Since exchangeable CMOs are a more complex investment and subject to unique price range and amortization conditions, the final rule specifically requires that a credit union seeking to invest in exchangeable CMOs must have the expertise to apply the price range and amortization conditions.

Comments on the Proposed Price Range Condition for Exchangeable CMOs Representing SMBS

Most commenters thought the .8 to 1.2 range on the ratio of purchase price to par was a reasonable method to separate out those exchangeable CMOs with risk characteristics substantially similar to the underlying SMBS. Some commenters suggested variations on this condition.

A few commenters suggest NCUA should treat exchangeable CMOs containing PO strips differently from those containing IO strips. These commenters believe NCUA should allow the purchase at less than 80% of par of exchangeable CMOs containing PO strips. One commenter states ''A PO that trades at a steep discount (less than 80% of par) is often less risky than one that trades at par, since it can result in significant gains if paid off early, and it does not have more downside risk than a PO CMO purchased at greater than 80% of par.''

One commenter suggests that, to keep an exchangeable CMO from having the substantive risk characteristics of an IO, NCUA should limit the coupon rate of the exchangeable CMO so that it is no higher than the coupon on the underlying collateral. The same commenter suggests that, to keep the exchangeable CMO from having the substantive risk characteristics of a PO, NCUA should require eligible securities to have a coupon at the time of issuance that is above a readily available index. For example, if the security has an expected weighted average life of 3 years at the time of issuance, the coupon for such security can not be below the yield on a 3 year Treasury plus a set spread, such as 50 basis points.

One commenter suggests that a credit union with adequate staff and resources to monitor an exchangeable CMO would be in the best position to determine acceptable risk tolerances and set premium or discount limits.

As stated above, the Board believes some safety and soundness conditions on exchangeable CMOs representing

SMBS are necessary. The conditions in the final rule are simple enough for a credit union to apply but specific enough to ensure that any exchangeable CMO that meets these conditions will not be too risky. Any FCU that wishes to invest in exchangeable CMOs subject to different conditions may always submit an application seeking NCUA approval for an investment pilot program. 12 CFR 703.19.

Comments on the Proposed Amortization Condition for Exchangeable CMOs Representing SMBS

Another commenter asks that NCUA provide more flexibility to allow for underlying IOs to amortize slower than other non-IO portions of exchangeable CMO. The commenter believes this would allow the investing credit union to receive more income over the life of the investment.

The Board notes that if the underlying IO amortized more slowly than the other non-IO portions of the exchangeable CMO, the credit union would eventually hold an exchangeable CMO that represented only an IO and had risk characteristics identical to the underlying IO. This is unacceptable to the Board and demonstrates the need for the amortization condition.

One commenter agreed with the proposed price range restrictions but stated that the amortization limitations do not materially advance NCUA's safety and soundness objectives and may unnecessarily restrict the investment flexibility of FCUs.

Another commenter also supported the ''pre-purchase'' condition, meaning the limit on premium or discount of purchase price to par, but objects to the ''post-purchase'' condition, meaning the amortization requirement. This commenter believes the latter issue is addressed for corporate credit unions by the interest rate modeling of § 704.8, and that ''to require separate risk management requirements specific to exchangeable CMOs is both unnecessary and overly burdensome.''

The Board does not intend that the amortization condition be a ''post-purchase'' condition; that is, that the credit union monitor amortization speeds after purchase. The Board is changing the language of the final rule to clarify that the determination of whether a particular CMO complies with the amortization condition will be made at the time of purchase from estimates of amortization speeds contained in the offering circular or other official information.

Comments on the Proposed Requirement That Credit Unions Not Exercise the Exchange Option if One or More of the Underlying CMOs Is an Impermissible IO or PO

One commenter suggests NCUA allow credit unions that hold otherwise permissible exchangeable CMOs representing IOs or POs to exchange the CMO for the underlying securities if the credit union immediately sells the impermissible IOs or POs resulting from the exchange. This commenter believes this approach will allow the credit union flexibility to make best use of the exchangeable CMO feature.

As stated above, the Board is generally opposed to credit unions holding SMBS. A credit union that invests in exchangeable CMOs representing impermissible SMBS and that would like to exercise the exchange option may, however, submit an investment pilot program for NCUA review and possible approval. 12 CFR 703.19.

Miscellaneous Comments on the Proposed Exchangeable CMO Rule

Several commenters state a final prospectus may not be available for CMOs purchased at time of issue. These commenters ask that, for investments in exchangeable CMOs made before issuance of the final prospectus, NCUA authorize the credit union to rely on a preliminary prospectus to determine if the CMO is exchangeable and, if so, permissible. If the preliminary prospectus does not indicate the CMO will be exchangeable or does not include decrement tables allowing the CU to determine if the underlying investments amortize at the same rate, these commenters want NCUA to allow the credit union to purchase and hold the investment even if the final prospectus indicates the investment is an exchangeable CMO that fails the amortization requirement.

The Board appreciates that credit unions may have difficulty ascertaining if a CMO purchased at or before issuance satisfies the requirements of this final rule. Before committing to purchase, a credit union should use its best efforts to examine the available documentary information to determine if the CMO will satisfy the requirements. If necessary, a credit union may seek assurances of compliance from the issuer. If an FCU uses its best efforts, and then determines after purchase that the CMO fails the requirements of this rule, it should process the investment as specified in its investment policies for investments that fail a requirement of part 703. 12 CFR 703.3(j). Corporate credit unions should process the failed investment under the Investment Action Plan provisions of the corporate rule. 12 CFR 704.10.

Several commenters ask that NCUA provide guidance to credit unions currently holding exchangeable CMOs that fail the requirements in the proposed rule, preferring that NCUA allow credit unions to continue holding these CMOs. One of these commenters also noted that in 1993 NCUA indicated some CMOs created from SMBS might be permissible. *See* 58 FR 34868 (June 30, 1993) (''The NCUA Board notes that recently some CMOs and REMICs have been created from stripped mortgage-backed securities. These instruments are permitted if they can pass the high-risk security tests.'') This 1993 statement has lead the commenter to believe that there is no regulatory prohibition on CMOs containing strips.

As stated above, the Board believes that few, if any, existing exchangeable CMOs will fail the conditions established in this final rule. Any CMOs that do fail the conditions should be processed under the FCU's investment policies or, for corporate credit unions, under an Investment Action Plan. 12 CFR 703.3(j), 704.10. While the NCUA recognized in 1993 that some CMOs had been created from SMBS and that they might be permissible if they passed the high-risk securities test (HRST), any CMO that had substantially the same risk characteristics as the underlying SMBS would likely have failed the HRST. NCUA regulations no longer require HRS testing. To ensure that credit unions do not hold exchangeable CMOs with significant risks from the underlying SMBS, those CMOs must satisfy the conditions provided in this final rule.

One corporate credit union commenter is particularly concerned about the effect of the rule on repurchase transactions. FCUs and corporate credit unions may only accept as repurchase assets those assets in which they can invest directly, and this commenter believes it will be difficult to identify and cull out impermissible exchangeable CMOs. 12 CFR 703.13(c)(1), 704.5(d)(2). The commenter states that, since credit unions are a small portion of the repurchase market, it is improbable that repurchase custodians will restrict repurchase assets to those CMOs qualifying under this proposal. Given the speed and volume of repurchase transactions, the commenter believes it would be onerous for a credit union to review each CMO that is part of the

repurchase transaction to ensure it complies with this proposal.

The Board appreciates the commenter's concerns about the difficulties in separating out impermissible assets and collateral in these transactions. The Board also notes that, in both repurchase transactions and securities lending transactions, a credit union relies primarily on the creditworthiness of the counterparty to get its money back and only secondarily on the repurchase asset or securities lending collateral. The potential for interest rate risk and price volatility associated with CMOs representing interests in SMBS is less significant in these transactions. Accordingly, the Board is amending parts 703 and 704 to indicate that exchangeable CMOs representing interests in SMBS may be used as assets or collateral in investment repurchase transactions or securities lending transactions, and the price range and amortization conditions need not be applied to exchangeable CMOs used in this way.

One commenter seeks clarification that the rule applies to both privately issued and federally issued CMOs. The Board intends that the rule apply to all exchangeable CMOs, regardless of issuer.

Miscellaneous Comments on the Exchangeable CMO Rule

Two commenters suggested that NCUA modify the proposed exchangeable CMO definition, and references to CMOs in the rule text, to reflect that the purchase of a CMO is an investment in a particular class of a CMO structure, not in an instrument that is a multi-class CMO structure. The Board agrees with the commenter and amends the final rule text as suggested.

One commenter states credit unions should set aggregate investment limits, not NCUA. Another commenter states NCUA should amend the call report to obtain additional detail on exchangeable CMOs. These issues are beyond the scope of the proposed rule and are not addressed in the final rule.

Comments on the Proposed Miscellaneous Technical Corrections and Clarifying Amendments

One commenter states that, if NCUA does not intend with its proposed change to the definition of derivative to expand or contract permissible types of investments for credit unions, it should say so.

The Board does not intend, through its changes to the derivative definition and other provisions of parts 703 and 704 that reference that definition, to either expand or contract the universe of investments currently permissible for FCUs and corporate credit unions.

D. Other Changes in the Final Rule

The Board is making additional changes not triggered by specific public comment. The Board proposed to change the definition of derivative so it would track the definition of derivative instrument used under generally accepted accounting principles (GAAP) while excluding those derivatives that, under GAAP, do not have to be recognized as an asset or liability in the statement of financial condition and be valued at fair market value. The Board's intent was to ensure that: (1) The regulatory definition of derivative is consistent with the accounting definition; and (2) embedded options in an otherwise permissible investment that are not significant enough to require separate accounting under GAAP would not cause that investment to be considered a prohibited derivative. The final rule retains the Board's intent but achieves it through different rule text. Instead of excluding embedded options from the regulatory definition of derivative, the final rule recognizes them as derivatives but excludes them from the general prohibition on derivatives.

Recently, the GAAP definition of derivative evolved to include loan commitments that relate to the origination of mortgage loans that will be held for sale. Financial Accounting Standards Board Statement of Financial Accounting Standards No. 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities,* paragraph 6(c). FCUs routinely enter into loan commitments such as interest rate lock commitments and forward sales commitments on mortgage loans they originate for sale, and the Board supports such commitments when used in a prudent manner. Since NCUA will now tie the regulatory definition of derivative to the GAAP definition, the general prohibition on derivatives could be interpreted to prohibit these types of commitments. Accordingly, the final rule clarifies that derivatives in the form of interest rate lock commitments and forward sales commitments on loans FCUs originate are excluded from the general prohibition on derivatives. Similarly, for corporate credit unions, the general prohibition on derivatives excludes forward sales commitments on loans originated by another credit union where the corporate intends to purchase the loan.

Currently, the responsibility for receipt and initial processing of applications under the Investment Pilot Program rests with NCUA's Office of Examination and Insurance. 12 CFR 703.19(c). The final rule transfers that responsibility to NCUA's Office of Strategic Program Support and Planning.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a proposed rule may have on a substantial number of small credit unions (those under $10 million in assets). This rule expands the investment authority granted to FCUs and corporate credit unions. The rule will not have a significant economic impact on a substantial number of small credit unions and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget. NCUA currently has OMB clearance of part 703 and part 704 collection requirements. *See* OMB No. 3133–0133 for 12 CFR part 703, and OMB No. 3133–0129 for 12 CFR part 704.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The executive order states that: ''[n]ational action limiting the policymaking discretion of the states shall be taken only where there is constitutional and statutory authority for the action and the national activity is appropriate in light of the presence of a problem of national significance.'' Portions of the rule apply to all corporates that accept funds from federally insured credit unions, including state chartered corporates. The Board believes that the protection of such credit unions from unwarranted investment in risky investments, and ultimately the National Credit Union Share Insurance Fund (NCUSIF), warrants application of the proposed rule to all corporates, including both state chartered and nonfederally insured. The rule does not impose additional costs or burdens on the states

or affect the states' ability to discharge traditional state government functions. NCUA has determined that this rule may have an occasional direct effect on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. However, the potential risk to the NCUSIF without the final changes justifies them.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget is reviewing whether this rule is a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects

12 CFR Part 703

Credit unions, Investments.

12 CFR Part 704

Corporate Credit unions, Reporting and Recordkeeping Requirements.

By the National Credit Union Administration Board on June 24, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 705

Community Development Revolving Loan Program for Credit Unions

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is amending its regulation pertaining to the Community Development Revolving Loan Program For Credit Unions (CDRLP) to permit student credit unions to participate in the program.

DATES: This final rule is effective August 30, 2004.

FOR FURTHER INFORMATION CONTACT: Frank Kressman, Staff Attorney, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

Part 705 of NCUA's regulations implements the CDRLP. 12 CFR part 705. The purpose of the CDRLP is to support the community development activities of participating credit unions. 12 CFR § 705.2. Participating credit unions are defined as those that are specifically involved in the stimulation of economic development and community revitalization activities in the communities they serve, whose membership consists of predominantly low-income members as reflected by a current low-income designation pursuant to § 701.34, § 741.204, or other applicable standards, and have submitted an application for participation and have been selected. 12 CFR § 705.3(b); 12 CFR § 701.34; 12 CFR § 741.204. The CDRLP achieves its purpose by making low interest loans and providing technical assistance to those credit unions. A credit union that participates in the CDRLP increases economic and employment opportunities for its low-income members.

Previously, NCUA took the position that although student credit unions are designated as low-income credit unions for purposes of receiving nonmember deposits, they did not qualify to participate in the CDRLP because they were not specifically involved in the stimulation of economic development activities and community revitalization. 61 FR 50694 (September 27, 1996); 58 FR 21642 (April 23, 1993). The NCUA believes this historical perspective underestimates the importance of student credit unions and the impact they have on the economic development and revitalization of the communities they serve. Student credit unions not only provide their members with valuable financial services generally not available but also a unique opportunity for financial education. NCUA believes that well run student credit unions would benefit greatly from participation in the CDRLP and, as a result, would be better able to serve their communities. Accordingly, in April 2004, NCUA issued a proposed rule to amend the CDRLP regulation to allow student credit unions to participate in the program. 69 FR 21443 (April 21, 2004).

B. Summary of Comments

NCUA received twenty-six comment letters regarding the proposed rule: eleven from federal credit unions, four from state credit unions, one from a private individual, and ten from credit union and student trade organizations. Twenty-one commenters fully supported the proposal. Four low-income designated credit unions involved in community development activities and one trade organization that represents community development credit unions opposed the proposal. Those opposed took the position that student credit unions do not fulfill the same mission as those credit unions for which the CDRLP was created. As noted above, NCUA believes that viewpoint underestimates the impact the few remaining student credit unions have on the communities they serve. Student credit unions not only provide their members with valuable financial services generally not available but also a unique opportunity for financial education. Also, NCUA believes a small CDRLP loan or technical assistance grant might help a student credit union survive or prosper while having a minor impact on CDRLP funding availability. Accordingly, NCUA adopts the amendments to part 705 as proposed.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a rule may have on a substantial number of small credit unions, defined as those under ten million dollars in assets. This rule permits student credit unions to participate in the CDRLP, without imposing any additional regulatory burden. The final amendments will not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 705

Community development, Credit unions, Loan programs—housing and community development, Reporting and recordkeeping requirements, Technical assistance.

By the National Credit Union Administration Board on July 22, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 721 and 724

Health Savings Accounts

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The NCUA is amending its regulations governing a federal credit union's (FCU) authority to act as trustee or custodian to authorize FCUs to serve as trustee or custodian for Health Savings Accounts (HSA). The NCUA is issuing this final rule so that FCUs and their members can take advantage of the authority granted in the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (Medicare Act). The Medicare Act authorizes the establishment of HSAs by individuals who obtain a qualifying high deductible health plan and specifies that an HSA may be established and maintained at an FCU. The final rule also amends NCUA's incidental powers regulation to include trustee or custodial services for HSAs as a pre-approved activity.

DATES: This rule is effective July 29, 2004.

FOR FURTHER INFORMATION CONTACT: Ross P. Kendall, Staff Attorney, at the above address, or telephone: (703) 518–6562.

SUPPLEMENTARY INFORMATION:

Background

On May 20, 2004, the NCUA Board requested comment on a proposed change to parts 724 and 721 of its regulations to permit federal credit unions (FCUs) to serve as trustee or custodian for health savings accounts (HSAs) established by their members. 69 FR 29907 (May 26, 2004). As authorized by Title XII of the Medicare Act, HSAs are available to anyone with a qualifying high deductible health plan. The NCUA proposed amending Part 724 of its regulations to specifically include HSAs in the listing of the types of accounts for which an FCU may fulfill the role of trustee or custodian on behalf of members. In addition, NCUA proposed to amend Part 724 to clarify that an FCU's authority to fulfill this role is not limited to pension or retirement accounts, but rather includes other specific types of tax advantaged savings accounts, such as Coverdell Education Savings Accounts and HSAs. The amendment also clarifies that HSAs are among the types of accounts for which a member may direct investment decisions. Finally, NCUA proposed to amend Part 721 to include serving as trustee or custodian for member HSAs within the category of activities in which an FCU may engage as a preapproved exercise of its incidental powers.

NCUA received six comments regarding the proposed changes from three federal credit unions, two national credit union trade associations, and one credit union service provider.

Summary of Comments

The commenters uniformly supported all aspects of the proposal. All commenters noted that the proposed amendments would provide FCU members with a viable, tax-advantaged option for obtaining health insurance and health care at a reasonable cost. Three commenters noted the importance of the proposal in assuring that FCUs can maintain parity with banks and thrifts, each of which are able to offer these types of accounts to their customers. Two commenters specifically approved of the proposal to broaden the rules to refer to ''Tax Advantaged Savings Plans,'' which they believe is more accurate and will allow for a more flexible approach toward offering similar types of savings plans that may become available in the future. Three commenters noted their agreement with the NCUA's assessment, as discussed in the preamble to the proposed rule, that FCUs should not have difficulty in handling the administrative duties associated with serving as account trustee or custodian, based on their experience with IRAs.

Additional Guidance

Additional information about HSAs, including important details concerning the type of high deductible health plan an individual must obtain to qualify for an HSA, is available from the Public Affairs Office of the U.S. Department of the Treasury. The Treasury Department has also developed proposed model forms for use in establishing an HSA. The information and the proposed forms are directly accessible from the Treasury Web site, *http://www.ustreas.gov.*

Final Rule

In view of the comments, NCUA is adopting the proposed amendments as a final rule without change.

Regulatory Procedures

Regulatory Flexibility Act

The final rule conforms current regulations to recent changes in the federal tax law and implements authority for FCUs to offer HSAs to their members. The Board has determined and certifies that the rule will not have a significant economic impact on a substantial number of small credit unions. Accordingly, the NCUA Board has determined that a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

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

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects

12 CFR Part 721

Incidental Powers.

12 CFR Part 724

Pensions, Reporting and recordkeeping, Trusts and trustees.

By the National Credit Union Administration Board, this 22nd day of July, 2004.

Becky Baker,

Secretary, NCUA Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 745

Share Insurance; Living Trust Accounts

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is adopting as a final rule without change the interim rule amending Part 745 of its regulations concerning share insurance coverage for beneficial interests in living trust accounts. NCUA published the interim rule with a sixty-day comment period at 69 FR 8798, on February 26, 2004.

DATES: This final rule is effective on July 29, 2004.

FOR FURTHER INFORMATION CONTACT: Ross Kendall, Staff Attorney, Office of General Counsel, at the above address or telephone: (703) 518–6562.

SUPPLEMENTARY INFORMATION: Effective April 1, 2004, NCUA revised its living trust account rules to provide for insurance coverage of up to $100,000 per qualifying beneficiary who, as of the date of a credit union's failure, would become entitled to the living trust assets upon the owner's death, regardless of the existence of a defeating contingency affecting the beneficiary's interest. The NCUA Board determined that elimination of the defeating contingency provisions in the rule was beneficial to credit unions and their members because the operation of the rule was complex and not widely understood. The amendment also clarified that a credit union need not maintain records disclosing the names and interests of beneficiaries of living trusts. In addition, the amendment preserved parity between the NCUA and the Federal Deposit Insurance Corporation (FDIC), which administers the insurance fund that protects bank depositors and which had, in January of 2004, adopted a similar amendment to its rules.

Even though NCUA issued the amendment as an interim final rule, the Board established a sixty-day comment period in which interested members of the public could comment on any aspect of the amendment. We received five comments, all of which were fully supportive of the amendment. The commenters uniformly indicated the changes would result in elimination of confusion by credit unions and their members and an enhanced understanding of the scope and operation of the share insurance rules for beneficial interests in living trust accounts. The commenters also cited the benefit of having uniformity of insurance coverage between living trust accounts and other types of revocable trust accounts, as well as the benefit of parity between the NCUA and the FDIC.

In view of the comments and the benefits described herein and in the preamble to the interim rule, the NCUA Board has determined to adopt the rule as final without change.

List of Subjects in 12 CFR Part 745

Credit unions, Share insurance.

By the National Credit Union Administration Board on July 22, 2004.

Becky Baker,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 701 and 742

Federal Credit Union Ownership of Fixed Assets

AGENCY: National Credit Union Administration.

ACTION: Final rule.

SUMMARY: The National Credit Union Administration (NCUA) Board is issuing final revisions to its fixed asset rule. The fixed asset rule governs Federal credit union (FCU) ownership of fixed assets and, among other things, limits investment in fixed assets to five percent of an FCU's shares and retained earnings. This final rule clarifies and reorganizes the requirements of the current rule to make it easier to understand. The only substantive changes in the final rule are to: Eliminate the requirement that an FCU, when calculating its investment in fixed assets, include its investments in any entity that holds fixed assets used by the FCU; and establish a time frame for submission of requests for waiver of the requirement for partial occupation of premises acquired for future expansion.

DATES: This rule is effective October 29, 2004.

FOR FURTHER INFORMATION CONTACT: Paul Peterson, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

The Federal Credit Union Act authorizes an FCU to purchase, hold, and dispose of property necessary or incidental to its operations. 12 U.S.C. 1757(4). Generally, an FCU may only invest in property it intends to use to transact credit union business, that is, to support its internal operations or serve its members. 12 CFR 721.3(d). NCUA's fixed asset rule limits an FCU's investment in fixed assets and imposes requirements on the planning for, use of, and disposal of real property acquired for future expansion. 12 CFR 701.36.

The NCUA Board has a policy of continually reviewing NCUA regulations to ''update, clarify and simplify existing regulations and eliminate redundant and unnecessary provisions.'' NCUA Interpretive Ruling and Policy Statement (IRPS) 87–2, Developing and Reviewing Government Regulations. As a result of the NCUA's 2003 review, the Board determined that the fixed asset rule should be updated. In April, 2004, the Board published its proposed updates for public comment. 69 FR 21439 (April 21, 2004).

B. Section-by-Section Analysis of the Final Rule

This final rule does not vary significantly from the proposed rule. Like the proposed rule, the only substantive revisions in the final rule from the current rule are to (1) eliminate the requirement that an FCU, when calculating its investment in fixed assets, include its investments in any entity that holds fixed assets used by the FCU, and (2) establish a time frame for submission of requests for waiver of the requirement for partial occupation of premises acquired for future expansion. The final rule also reorganizes the paragraph structure and clarifies the provisions governing an FCU's plans for future expansion into fixed assets. A section-by-section analysis of these revisions follows.

Section 701.36(a)

The final rule renumbers § 701.36(c), Investment in Fixed Assets, as § 701.36(a). The final rule retains the requirement that FCUs with $1,000,000 or more in assets cannot invest in fixed assets if the investment would cause the aggregate of all the FCU's fixed assets to exceed five percent of the FCU's shares and retained earnings. The final rule retains the waiver process that allows FCUs to apply for a waiver of the five percent limitation and reorganizes the waiver provisions to simplify them and make them easier to follow.

Section 701.36(b)

The final rule renumbers § 701.36(d), Premises, to § 701.36(b). This paragraph contains provisions on real property owned by an FCU that is not currently used to transact credit union business.

The final rule changes the title of this paragraph to ''Premises Not Currently Used to Transact Credit Union Business'' to better indicate its scope.

The final rule clarifies that requests for waiver of the partial occupation requirement must be in writing and submitted to NCUA within 30 months of acquisition of the premises. The final rule also clarifies that partial use occurs when FCU staff occupy some part of the space on a full-time basis.

The final clarifies that, after real property acquired for future expansion has been held for one year, a board resolution with definitive plans for full utilization must be available for inspection by an NCUA examiner. The final rule also clarifies that full use occurs when the premises are completely occupied by the FCU, or by some combination of the FCU, credit union service corporations (CUSOs), and credit union vendors, on a full-time basis. CUSO and vendor activities must be primarily to support the operations of the FCU or serve its members.

The final rule clarifies and simplifies the provisions on abandoned premises. The final rule revises the provision that an FCU ''shall endeavor to dispose of ''abandoned premises'' at a price sufficient to reimburse the FCU for its investment and costs of acquisition'' to state that an FCU must seek fair market value for the property.

Section 701.36(c)

The final rule renumbers § 701.36(e), Prohibited Transactions, to § 701.36(c). The rule retains the prohibition on an FCU acquiring or leasing property (without the prior approval of NCUA) from the FCU's insiders, their family members, or corporations and partnerships in which the insider has a significant ownership interest. To ensure that all business forms are covered, the rule adds limited liability companies and ''other entities'' to this list.

Section 701.36(d)

FCUs that qualify for the Regulatory Flexibility (RegFlex) Program are exempt from the five percent limitation on investment in fixed assets. 12 CFR part 742. Accordingly, the final rule adds a new paragraph (d) to § 701.36 with a cross-reference to the RegFlex Program. The rule also reiterates that FCUs that once qualified for the RegFlex Program and its associated exemptions but no longer qualify for RegFlex must comply with all the provisions of the fixed asset rule.

Section 701.36(e)

The final rule renumbers § 701.36(b), Definitions, to § 701.36(e). The rule retains the definition of ''investment in fixed assets'' found in subparagraph (4), but deletes the subparagraph (4)(iv) portion of the definition that includes any investments in, and loans to, a partnership or corporation, including a CUSO, that holds any fixed assets used by the FCU. This portion of the definition is unnecessary and, in some cases, may cause investment in fixed assets to be overstated.

The final rule revises the definition of ''retained earnings'' in subparagraph (7) to mean ''undivided earnings, regular reserve, reserve for contingencies, supplemental reserves, reserve for losses, and other appropriations from undivided earnings as designated by management or the Administration.'' The revision recognizes that reserve

accounts may be created out of undivided earnings consistent with generally accepted accounting principles. The rule also separates the definitions of ''shares'' and ''retained earnings'' and alphabetizes all the definitions to make them easier to locate.

Section 742.4(a)

The final rule includes a technical amendment to the RegFlex Program rule reflecting the restructuring of the fixed asset rule.

C. Public Comments

NCUA received 12 comment letters regarding the proposed rule. Almost all the commenters expressed general agreement with the proposed rule, and, in particular, the clarifications and simplifications. Most of the commenters expressed appreciation for NCUA's policy of reviewing its regulations at least once every three years. Summaries of the comments and the Board's reaction follow.

Amendment to Definition of Fixed Asset

Almost all the commenters agree with the change in the definition of fixed asset to exclude investments in entities that hold fixed assets used by the FCU.

One commenter believes that lease payments for fixed assets should also be excluded from the calculation of the fixed asset limit. The Board does not want to exclude lease payments. The Board's longstanding position is that an FCU can over-invest in fixed assets through binding lease arrangements just as it can over-invest through outright ownership. See, for example, the preamble to the 1989 final fixed asset rule. 54 FR 18466 (May 1, 1989).

Clarification of ''Partially Occupy'' and ''Fully Occupy'' and Associated Time Frames

The proposed rule sought to clarify that premises were considered partially occupied when the credit union is using some part of the space on a full-time basis and fully occupied when the credit union, or a combination of the credit union, CUSOs, or vendors, use the entire space on a full-time basis. Almost all the commenters agreed that the clarifications were helpful.

Most commenters believe it is reasonable that credit unions intending to seek a waiver of the requirement for partial occupation of premises within three years should file the request for waiver within 30 months. One commenter asks that, instead of 30 months, the request for waiver be filed within 35 months, one month before the expiration of the three-year period. One commenter objects to the waiver provision and believes it should be eliminated. This commenter is particularly concerned that a credit union that loses its eligibility for the RegFlex Program should not be granted a waiver.

The final rule retains the 30-month notice requirement. Thirty months seems a reasonable amount of time to prepare a waiver request. The Board also believes that the Regional Director should have flexibility to grant waivers in appropriate cases, and the final rule retains this waiver authority.

Several commenters believe NCUA should reduce or eliminate the rule's requirements for both partial and full occupation, but particularly for full occupation. These commenters contend it is difficult for a credit union to obtain a building or lease space that is a perfect fit for the credit union's current and near term plans and the rule's occupation requirements restrict credit union growth and may be anticompetitive. One commenter cites the perceived difficulty rural and low-income credit unions have in finding appropriate office space, and another cites the perceived difficulty a continuing credit union in a merger has in balancing reduced staffing needs with the buildings it inherits in a merger. Another commenter stated that office construction projects take more than three years from first planning to building occupation and that it is ''impractical to write a regulation that will inevitably require a waiver.'' A few commenters also believe credit unions eligible for the RegFlex program should be exempt from any requirements to fully occupy a building because of the lack of safety and soundness concerns for these credit unions. Two commenters cite with approval the Office of the Comptroller of the Currency's (OCC's) approach to real estate owned by national banks. The OCC requires partial occupation of bank-owned real estate but not always full occupation.

The Board recognizes the difficulties associated with the management of real estate and other fixed assets but believes that the fixed asset rule, as revised by this rulemaking, provides maximum flexibility to FCUs within the bounds of the law and safety and soundness. Federal credit unions are chartered for the purpose of providing financial services to their members and it is not permissible for them to engage in real estate activities that do not support that purpose.

While it may sometimes be difficult for credit unions to find real estate to fit their needs or to downsize real estate holdings following a merger, the Board believes the rule provides enough flexibility to meet various circumstances. The rule allows an FCU to own or lease premises it will not occupy immediately but needs for future expansion and gives FCUs significant leeway on how to achieve both partial and full occupation. For example, there is no set time period within which an FCU must achieve full occupation. While the rule requires an FCU to develop a definitive plan for full occupation, it has an entire year after it acquires property to develop the plan. Further, with regard to partial occupation, the rule permits FCUs to hold real estate for significant periods of time—up to three years—before the FCU has to occupy *any* of the space. If an FCU needs additional time beyond three years to achieve partial occupation, it may request approval for additional time from its Regional Director. The Board believes that it would be unusual, even when an FCU is constructing its own premises, for the FCU not to achieve partial occupation within three years. Still, if the construction process will take more than three years, a waiver is appropriate and the credit union should obtain it before binding itself contractually to the project.

The Board is aware that the Office of the Comptroller of the Currency has a different view of the powers of national banks under the National Bank Act, but the Board has concluded, for both legal and safety and soundness reasons, that FCUs may not lease real estate to unrelated third parties indefinitely. As noted above, the acquisition of real estate and other fixed assets must support the provision of financial services to credit union members and the Board believes the rule provides significant and sufficient flexibility for FCUs in how they address any excess capacity they may have in fixed assets they acquire.

Fixed Asset Limitation

The current rule limits an FCU's fixed assets to five percent of shares and retained earnings. Credit unions eligible for the RegFlex Program are exempt from this limitation and there is a waiver process that other credit unions may use to avoid the five percent limitation.

A few commenters are concerned with the proposed rule's clarification that credit unions that lose their eligibility for the regulatory flexibility program must again comply with the fixed asset rule's five percent limitation. One commenter suggests that a credit union that loses its status have up to five years to dispose of fixed assets,

citing a similar time frame in the rule for disposition of abandoned premises. Another commenter suggests that credit unions with less than 9% net worth should have their RegFlex Program status extended for purposes of compliance with the fixed asset limitation even if they lose their RegFlex status for other purposes. One commenter suggests that NCUA apply the 5% limit on fixed assets to credit unions that have a 7% or less net worth ratio, and that NCUA modify its rule to increase the limit in direct proportion to the amount that the net worth ratio exceeds 7%. Another commenter believes the ratio of fixed assets to a combination of deposits and capital is not a meaningful test of prudent management.

In addressing these comments, the Board first wishes to clarify a statement made in the preamble of the proposed rule. The preamble stated that an FCU eligible for the RegFlex Program with fixed assets exceeding five percent of shares and retained earnings and that subsequently loses its RegFlex eligibility must either reduce its fixed asset holdings below the five percent level or obtain a waiver. The RegFlex Program regulation, however, has a grandfather provision that states:

> Any action by the credit union under the RegFlex authority will be grandfathered. Any actions subsequent to losing the RegFlex authority must meet NCUA's regulatory requirements. This does not diminish NCUA's authority to require a credit union to divest its investments or assets for substantive safety and soundness reasons.

12 CFR 742.8. Accordingly, an FCU that loses its RegFlex eligibility and finds itself with fixed assets exceeding five percent of shares and retained earnings does not have to divest itself of any fixed assets unless NCUA affirmatively orders it to do so for safety and soundness reasons. If the FCU wants to acquire additional fixed assets, the FCU will need a waiver from the Regional Director before the acquisition if, after acquisition, the FCU would exceed the five percent limit. The Board has amended the final rule text to reflect this more clearly.

As stated above, a few commenters request modification of the five percent limit for FCUs that lose their RegFlex eligibility. The Board does not believe these credit unions need any special variance from the five percent limit. A Regional Director has authority to grant waivers and set conditions on those waivers. For FCUs that lose RegFlex eligibility and have or want fixed assets that would put them over the five percent limit, a Regional Director has authority to establish appropriate fixed asset levels on a case-by-case basis.

D. Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a proposed rule may have on a substantial number of small entities (those credit unions under ten million dollars in assets). NCUA believes that, under the current rule, the only burden imposed on small credit unions is the requirement to submit a waiver request if investment in fixed assets exceeds 5% of retained shares and earnings. There are presently about 4,500 small, federally-insured credit unions. Each year, only about ten of these credit unions submit a waiver request, and NCUA estimates each waiver request takes about ten hours to prepare. Accordingly, and as stated in the preamble to the proposed rule, NCUA does not believe the rule imposes a significant economic impact on a substantial number of small entities and no flexibility analysis is required. NCUA received no comments about this conclusion.

Paperwork Reduction Act

The proposed rule requested comment on the information collection requirements contained in the fixed asset rule and advised that NCUA was seeking the reinstatement of Collection of Information, FCU Ownership of Fixed Assets, Control Number 3133–0040. No comments were received. On July 7, 2004, the Office of Management and Budget (OMB) approved the reinstatement of Control Number 3133–0040, with revisions as proposed and an expiration date of July 31, 2007.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. This rule will not have substantial direct effects on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects

12 CFR Part 701

Credit unions.

12 CFR Part 742

Credit unions, Reporting and recordkeeping requirements.

By the National Credit Union Administration Board on September 23, 2004.

Mary Rupp,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 747

Civil Monetary Penalty Inflation Adjustment

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: Congress, in the Federal Civil Penalties Inflation Adjustment Act of 1990, as amended by the Debt Collection Improvement Act of 1996, required all federal agencies with the authority to impose civil monetary penalties (CMPs) to regularly evaluate those CMPs to ensure that they continue to maintain their deterrent value. In order to comply with Congress' mandate to adjust CMPs for inflation at least every four years, NCUA is issuing this final rule to implement the required adjustments to the CMPs authorized by the Federal Credit Union Act and other relevant laws.

DATES: Effective November 1, 2004.

FOR FURTHER INFORMATION CONTACT: Allan Meltzer, Associate General Counsel, or Jon Canerday, Trial Attorney, Office of General Counsel, NCUA, 1775 Duke Street, Alexandria, Virginia 22314, or telephone (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

The Debt Collection Improvement Act of 1996 [1] (DCIA) amended the Federal Civil Penalties Inflation Adjustment Act of 1990 [2] (FCPIA Act) to require every Federal agency to enact regulations that adjust each civil monetary penalty (CMP) [3] provided by law under its jurisdiction by the rate of inflation pursuant to the inflation adjustment formula in section 5(b) of the FCPIA Act. Each Federal agency was required to issue these implementing regulations by October 23, 1996, and at least once every 4 years thereafter. Section 6 of the amended FCPIA Act specifies that inflation-adjusted CMPs will only apply to violations that occur after the effective date of the adjustment. The inflation adjustment is based on the percentage increase in the Consumer Price Index (CPI).[4] Specifically, section 5(b) of the FCPIA Act defines the term ''cost-of-living adjustment'' as ''the percentage (if any) for each civil monetary penalty by which—(1) The Consumer Price Index for the month of June of the calendar year preceding the adjustment, exceeds (2) the Consumer Price Index for the month of June of the calendar year in which the amount of such civil monetary penalty was last set or adjusted pursuant to law.'' Furthermore, each CMP that has been adjusted for inflation must be rounded to a number prescribed by section 5(a) of the FCPIA Act.[5]

The CMPs which NCUA is authorized to impose were last adjusted by NCUA in either 1996 or 2000. For those CMPs that were adjusted in 2000, the current adjustment will be the percentage by which the CPI for the month of June 2003 exceeds the CPI for the month of June 2000. According to the Bureau of Labor Statistics, the CPI for the month of June 2000 was 172.4 and the CPI for the month of June 2003 was 183.7. The percentage by which the 2003 figure exceeds the 2000 figure is 6.55 percent. Thus, the CMPs that were last adjusted in 2000 should be increased by 6.55 percent to arrive at the new adjusted amounts (before required rounding).

For those CMPs that were adjusted in 1996, the current adjustment will be the percentage by which the CPI for the month of June 2003 exceeds the CPI for the month of June 1996. According to the Bureau of Labor Statistics, the CPI for the month of June 1996 was 156.7 and the CPI for the month of June 2003 was 183.7. The percentage by which the 2003 figure exceeds the 1996 figure is 17.23 percent. The CMPs that were last adjusted in 1996 should be increased by 17.23 percent to arrive at the new adjusted amounts (before required rounding).

B. Mathematical Calculations of the Adjustments

1. 12 U.S.C. 1782a(a)(3)

NCUA is authorized to require credit unions to periodically provide reports of condition. The failure to submit a required report or the submission of a false or misleading report subjects a credit union to three levels of CMPs, depending upon the reasons for noncompliance.

Calculation of the Adjustment

The CMPs authorized by 12 U.S.C. 1782a(a)(3) were last adjusted by NCUA in 2000.[6] Therefore, these CMPs should be multiplied by 6.55 percent to arrive at the new adjusted amounts (before required rounding).

The maximum CMP authorized by 12 U.S.C. 1782a(a)(3) for an inadvertent failure to submit a report or the inadvertent submission of a false or misleading report is $2,000 for each day the failure continues or such false or misleading information is not corrected. After the required adjustment for inflation in 2000, the maximum penalty was increased to $2,200 for each day. Multiplying the current penalty of $2,200 by 6.55 percent results in an increase of $144.10. When that number is rounded as required by the FCPIA Act,[7] the inflation-adjusted maximum remains $2,200.

The maximum CMP authorized by 12 U.S.C. 1782a(a)(3) for a non-inadvertent failure to submit a report or the non-inadvertent submission of a false or misleading report is $20,000 for each day the failure continues or such false or misleading information is not corrected. After the required adjustment for inflation in 2000, the maximum penalty was increased to $22,000 for each day. Multiplying the current penalty of $22,000 by 6.55 percent results in an increase of $1,441. When that number is rounded as required by the FCPIA Act,[8] the inflation-adjusted maximum remains $22,000.

The maximum CMP authorized by 12 U.S.C. 1782a(a)(3) for a failure to submit a report or the submission of a false or misleading report done knowingly or with reckless disregard is $1,000,000 or 1 percent of the total assets of the credit union, whichever is less, for each day the failure continues or such false or misleading information is not corrected. After the required adjustment for

[1] Pub. L. 104–134, 31001(s), 110 Stat. 1321–373, (Apr. 26, 1996). The Provision is codified at 28 U.S.C. 2461 note.

[2] Pub. L. 101–410, 104 Stat. 890, (Oct. 5, 1990), also codified at 28 U.S.C. 2461 note.

[3] Section 3(2) of the amended FCPIA Act defines a CMP as any penalty, fine, or other sanction that: (1) Either is for a specific monetary amount as provided by Federal law or has a maximum amount provided for by Federal law; (2) is assessed or enforced by an agency pursuant to Federal law; and (3) is assessed or enforced pursuant to an administrative proceeding or a civil action in the Federal courts.

[4] The CPI is published by the Department of Labor, Bureau of Statistics, and is available at its Web site: *http://data.bls.gov/cgi-bin/surveymost.*

[5] In 2000, NCUA recognized that the rounding provision of the FCPIA Act was capable of differing interpretations. Since then, the Comptroller General has interpreted the rounding requirements of the FCPIA Act the same way as NCUA did in calculating the 2000 inflation adjustments. Comp. Gen. B–290021, 2002 U.S. Comp. Gen. LEXIS 266, July 15, 2002.

[6] The previous inflation adjustments were made to 12 U.S.C. 1782. That provision has been redesignated as 1782a.

[7] ''Any increase determined under this subsection shall be rounded to the nearest– * * * (3) multiple of $1,000 in the case of penalties greater than $1,000 but less than or equal to $10,000.'' Section 5(a), FCPIA Act. Therefore, $144.10 is rounded to the nearest multiple of $1,000 or to $0.

[8] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (4) multiple of $5,000 in the case of penalties greater than $10,000 but less than or equal to $100,000.'' Section 5(a), FCPIA Act. Therefore, $1,441 is rounded to the nearest multiple of $5,000 or to $0.

inflation in 2000, the maximum penalty was increased to $1,100,000 for each day. Multiplying the current penalty of $1,100,000 by 6.55 percent results in an increase of $72,050. When that number is rounded as required by the FCPIA Act,[9] the inflation-adjusted maximum becomes $1,175,000 or 1 percent of the total assets of the credit union, whichever is less, per day.

2. 12 U.S.C. 1782a(d)(2)

In a provision similar to that discussed above, NCUA is authorized to require each credit union to provide periodic certified statements of the amount of insured shares in the credit union, as well as to pay required deposits into the National Credit Union Share Insurance Fund. The failure to submit a required certified statement or the submission of a false or misleading statement subjects a credit union to three levels or tiers of CMPs, depending upon the reasons for noncompliance.

Calculation of the Adjustment

The CMPs authorized by 12 U.S.C. 1782a(d)(2) were last adjusted by NCUA in 2000. Therefore, these CMPs should be multiplied by 6.55 percent to arrive at the new adjusted amounts (before required rounding).

First Tier CMPs

The maximum CMP authorized by 12 U.S.C. 1782a(d)(2)(A) for an inadvertent failure to timely submit a certified statement or an inadvertent submission of a false or misleading certified statement is $2,000 for each day the failure continues or such false or misleading information is not corrected. After the required adjustment for inflation in 2000, the maximum penalty was increased to $2,200 for each day. Multiplying the current penalty of $2,200 by 6.55 percent results in an increase of $144.10. When that number is rounded as required by the FCPIA Act,[10] the inflation-adjusted maximum remains $2,200.

Second Tier CMPs

The maximum CMP authorized by 12 U.S.C. 1782a(d)(2)(B) for a non-inadvertent failure to timely submit a certified statement, or a non-inadvertent submission of a false or misleading certified statement, or the failure or refusal to pay any required deposit or premium for insurance is $20,000 for each day the failure continues or such false or misleading information is not corrected. After the required adjustment for inflation in 2000, the maximum penalty was increased to $22,000 for each day. Multiplying the current penalty of $22,000 by 6.55 percent results in an increase of $1,441. When that number is rounded as required by the FCPIA Act,[11] the inflation-adjusted maximum remains $22,000.

Third Tier CMPs

The maximum CMP authorized by 12 U.S.C. 1782a(d)(2)(C) for a failure to submit a report or the submission of a false or misleading report done knowingly or with reckless disregard is $1,000,000 or 1 percent of the total assets of the credit union, whichever is less, for each day the failure continues or such false or misleading information is not corrected. After the required adjustment for inflation in 2000, the maximum penalty was increased to $1,100,000 for each day. Multiplying the current penalty of $1,100,000 by 6.55 percent results in an increase of $72,050. When that number is rounded as required by the FCPIA Act,[12] the inflation-adjusted maximum becomes $1,175,000 or 1 percent of the total assets of the credit union, whichever is less, per day.

3. 12 U.S.C. 1785(e)(3)

Pursuant to 12 U.S.C. 1785(e)(1), NCUA is authorized to promulgate regulations to provide minimum standards with which each insured credit union must comply with respect to security devices and procedures to discourage robberies, burglaries and larcenies and to assist in the identification and apprehension of persons who commit such acts. A credit union that violates such a regulation is subject to a CMP for each day the violation continues.

Calculation of the Adjustment

The CMPs authorized by 12 U.S.C. 1785(e)(3) were last adjusted by NCUA in 2000. Therefore, these CMPs should be multiplied by 6.55 percent to arrive at the new adjusted amounts (before required rounding).

The maximum CMP authorized by 12 U.S.C. 1785(e)(3) for non-compliance with NCUA security regulations is $100 for each day the violation continues. After the required adjustment for inflation in 2000, the maximum penalty was increased to $110 for each day. Multiplying the current penalty of $110 by 6.55 percent results in an increase of $7.21. When that number is rounded as required by the FCPIA Act,[13] the inflation-adjusted maximum remains $110.

4. 12 U.S.C. 1786(k)(2)

NCUA is authorized to impose three levels or tiers of CMPs upon insured credit unions or institution-affiliated parties for certain conduct. First and second tier CMPs were not increased for inflation in 2000 because the amount of the increase was not large enough as a result of the rounding rules. Because these CMPs were last adjusted for inflation in 1996, they should now be increased by 17.23 percent to arrive at the new adjusted amounts (before required rounding). Third tier CMPs were increased for inflation in 2000 and therefore, should now be increased by 6.55 percent (before required rounding).

First Tier CMPs

First tier CMPs, 12 U.S.C. 1786(k)(2)(A), may be imposed for the violation of any law or regulation, the violation of certain final orders or temporary orders, the violation of conditions imposed in writing by the NCUA Board, or the violation of any written agreement between the credit union and NCUA. The statute provides that first tier CMPs shall not be more than $5,000 for each day the violation continues. After the required adjustment for inflation in 1996, the maximum penalty was increased to $5,500 for each day. Multiplying the current penalty of $5,500 by 17.23 percent results in an increase of $947.65. When that number is rounded as required by the FCPIA Act,[14] the inflation-adjusted maximum for a first tier CMP becomes $6,500.

[9] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (6) multiple of $25,000 in the case of penalties greater than $200,000.'' Section 5(a), FCPIA Act. Therefore, $72,050 is rounded to the nearest multiple of $75,000 or to $75,000.

[10] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (3) multiple of $1,000 in the case of penalties greater than $1,000 but less than or equal to $10,000.'' Section 5(a), FCPIA Act. Therefore, $144.10 is rounded to the nearest multiple of $1,000 or to $0.

[11] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (4) multiple of $5,000 in the case of penalties greater than $10,000 but less than or equal to $100,000.'' Section 5(a), FCPIA Act. Therefore, $1,441 is rounded to the nearest multiple of $5,000 or to $0.

[12] ''Any increase determined under this subsection shall be rounded to the nearest– * * * (6) multiple of $25,000 in the case of penalties greater than $200,000.'' Section 5(a), FCPIA Act. Therefore, $72,050 is rounded to the nearest multiple of $75,000 or to $75,000.

[13] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (2) multiple of $100 in the case of penalties greater than $100 but less than or equal to $1,000.'' Section 5(a), FCPIA Act. Therefore, $7.21 is rounded to the nearest multiple of $100 or to $0.

[14] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (3) multiple of $1,000 in the case of penalties

Second Tier CMPs

Second tier CMPs, 12 U.S.C. 1786(k)(2)(B), are authorized for violations described in first tier CMPs, the reckless engaging in an unsafe or unsound practice in conducting the affairs of a credit union, or the breach of any fiduciary duty, when the violation, practice or breach is part of a pattern of misconduct, or causes or is likely to cause more than a minimal loss to the credit union, or results in pecuniary gain or other benefit. The statute provides a maximum second tier CMP of $25,000 for each day the violation, practice or breach continues. After the required 1996 adjustment for inflation, the maximum penalty was increased to $27,500 per day. Multiplying the current penalty of $27,500 by 17.23 percent results in an increase of $4,738.25. When that number is rounded as required by the FCPIA Act,[15] the inflation-adjusted maximum for a second tier CMP becomes $32,500.

Third Tier CMPs

Third tier CMPs, 12 U.S.C. 1786(k)(2)(C), may be imposed for any of the acts described in second tier CMPs that cause a substantial loss to the credit union or a substantial pecuniary gain or other benefit. The amount of third tier CMPs depends upon the status of the respondent required to pay the CMP, 12 U.S.C. 1786(k)(2)(D). For a person other than an insured credit union, under the statute, the maximum third tier CMP is $1,000,000 for each day the violation, practice or breach continues. For an insured credit union, the statute provides a daily maximum CMP of the lesser of $1,000,000 or 1 percent of the total assets of the credit union. In 2000, the maximum CMP for a person other than an insured credit union was increased for inflation to $1,175,000 per day. At the same time, the maximum CMP for an insured credit union was increased to the lesser of $1,175,000 or 1 percent of the total assets of the credit union. Multiplying the current penalty of $1,175,000 by 6.55 percent results in an increase of $76,962.50. When that number is rounded as required by the FCPIA Act,[16] the new maximum inflation-adjusted third tier CMP becomes $1,250,000.

5. 42 U.S.C. 4012a(f)

Pursuant to 42 U.S.C. 4012a(f), NCUA is authorized to impose CMPs against a credit union that is found to have a pattern or practice of committing certain specified actions in violation of the National Flood Insurance Program.

Calculation of the Adjustment

The CMPs authorized by 42 U.S.C. 4012a(f) were last adjusted by NCUA in 2000. Therefore, these CMPs should be multiplied by 6.55 percent to arrive at the new adjusted amounts (before required rounding).

The maximum CMP authorized by 42 U.S.C. 4012a(f) is $350 for each violation, up to a maximum of $100,000 per calendar year. After the required adjustments for inflation in 2000, the maximum penalty was increased to $385 for each day, up to a maximum of $110,000 per calendar year. Multiplying the current penalty of $385 by 6.55 percent results in an increase of $25.22. When that number is rounded as required by the FCPIA Act,[17] the inflation-adjusted maximum remains $385. Multiplying the current annual maximum of $110,000 by 6.55 percent results in an increase of $7,205. When that number is rounded as required by the FCPIA Act,[18] the inflation-adjusted annual maximum penalty becomes $120,000 per calendar year.

The NCUA Board now adopts this final rule to adjust the forgoing CMPs for the rate of inflation, as required by the FCPIA Act. As provided in the final rule, the revised CMP amounts will only apply to violations that occur after the effective date of the final rule.

C. Regulatory Procedures

Final Rule Under the Administrative Procedures Act

The FCPIA Act requires adjustments of CMPs for inflation to occur at least every four years. Additionally, the FCPIA Act provides federal agencies with no discretion in the adjustment of CMPs for inflation. Thus, NCUA is unable to vary the amount of the adjustments to reflect any views or suggestions provided by commenters. Further, the regulation is ministerial and technical. For all of these reasons, the NCUA Board finds good cause to determine that public notice and comment for this new regulation is unnecessary, impractical and contrary to the public interest, pursuant to the Administrative Procedure Act (APA), 5 U.S.C. 553(b)(3)(B).

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a proposed rule may have on a substantial number of small credit unions (those under ten million dollars in assets). The proposed rule would not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

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

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their regulatory actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the Executive Order. This final rule will apply to all federally-insured credit unions, but it will not have substantial direct effects on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined the final rule does not constitute a policy that has federalism implications for purposes of the Executive Order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

NCUA has determined that this rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

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greater than $1,000 but less than or equal to $10,000.'' Section 5(a), FCPIA Act. Therefore, $947.65 is rounded to the nearest multiple of $1,000 or to $1,000.

[15] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (4) multiple of $5,000 in the case of penalties greater than $10,000 but less than or equal to $100,000.'' Section 5(a), FCPIA Act. Therefore, $4,738.25 is rounded to the nearest multiple of $5,000 or to $5,000.

[16] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (6) multiple of $25,000 in the case of penalties greater than $200,000.'' Section 5(a), FCPIA Act. Therefore, $76,962.50 is rounded to the nearest multiple of $25,000 or to $75,000.

[17] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (2) multiple of $100 in the case of penalties greater than $100 but less than or equal to $1,000.'' Section 5(a), FCPIA Act. Therefore, $25.22 is rounded to the nearest multiple of $100 or to $0.

[18] ''Any increase determined under this subsection shall be rounded to the nearest- * * * (5) multiple of $10,000 in the case of penalties greater than $100,000 but less than or equal to $200,000.'' Section 5(a), FCPIA Act. Therefore, $7,205 is rounded to the nearest multiple of $10,000 or to $10,000.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–21) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Act. 5 U.S.C. 551. The Office of Management and Budget has reviewed this rule and has determined that for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, it is not a major rule.

List of Subjects in 12 CFR Part 747

Credit unions, Civil monetary penalties.

By the National Credit Union Administration Board on September 27, 2004.

Mary Rupp,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Change in Official or Senior Executive Officer in Credit Unions That Are Newly Chartered or Are in Troubled Condition

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is amending its rule concerning the requirement that federally-insured credit unions that are newly chartered or troubled file notice with NCUA before adding or replacing a board or committee member or employing or changing the duties of a senior executive officer. The amendments clarify the relationship between the prior notice provision and the commencement of service provision, so as to eliminate any potential confusion. In addition, the amendments reorganize the requirements in the current rule to make it easier to understand.

DATES: This rule is effective on November 26, 2004.

FOR FURTHER INFORMATION CONTACT: Ross P. Kendall, Staff Attorney, Division of Operations, Office of General Counsel, at telephone: (703) 518–6562.

SUPPLEMENTARY INFORMATION:

Background

On June 24, 2004, the NCUA Board requested comment on proposed changes to § 701.14 of its regulations, clarifying the procedures that newly chartered or troubled federally-insured credit unions must follow to obtain NCUA approval before adding or replacing board or committee members or changing the duties of a senior executive officer. 69 FR 39871 (July 1, 2004). The proposed amendments clarify the relationship between the prior notice provision and the commencement of service provision in the current rule to eliminate confusion and reorganize the requirements to make the rule easier to understand.

NCUA received comments regarding the proposed changes from two federal credit unions, two national credit union trade associations, one state credit union trade association and one state credit union supervisory association, for a total of six comments.

Summary of Comments

The comments were generally favorable and supportive of the amendments, and all but one commenter supported the efforts to clarify and reorganize the provisions of the rule. Two commenters supported the proposal as published without recommending any changes.

One commenter recommended that the revised rule include a specific reference to the role of the state supervisory authority (SSA) in cases involving state-chartered credit unions. The rule, however, implements authority in the Federal Credit Union Act specifically authorizing the NCUA to review and approve of the service of certain senior credit union officials and employees of federally-insured credit unions, including credit unions that are state-chartered. 12 U.S.C. 1790a. While the NCUA is the decision maker in these cases, the current rule does require a state-chartered, federally-insured credit union to provide a copy of the NCUA notice to its SSA. 12 CFR 701.14(d)(1). In addition, the Board notes that another provision of our regulations also requires NCUA to consult with the appropriate SSA and provide it with notice concerning NCUA's decision. 12 CFR 741.205. The Board has not adopted this recommendation to otherwise reference the role of SSAs.

Another commenter suggested that the rule provide that a request for approval of an official's or employee's service to be deemed complete unless the regional office specifically requires additional information within ten days of its receipt of the request.

The current rule provides that the appropriate NCUA regional office will notify the credit union within ten days of its receipt of the request for approval either that the request is complete or that additional information is required and the Board is not aware of any instances of problems with the current procedure. The final rule retains this provision. The rule already calls for the regional office to advise the credit union about whether the request is complete and providing an automatic determination that an application is deemed complete within ten days could create confusion with the provision in the rule providing for automatic approval if a Regional Director fails to issue a written decision within thirty days. In addition, the suggested revision could, in fact, delay processing. A regional office may determine that it wants to provide an applicant with an opportunity to supplement a submission after performing an initial review. A credit union will generally be willing to provide additional information if it is able since failure to do so would likely result in the disapproval of its request.

One commenter suggested that NCUA exclude service by employees from coverage of the rule. This commenter contends that selection and oversight of employees should be the exclusive province of the board of directors, absent some indication that the board has behaved unethically or is responsible for the credit union's unhealthy financial condition. The authority in the FCU Act for this rule specifically addresses senior executive employees as well as board and committee members. 12 U.S.C. 1790a(a). Senior executives are directly involved in and are responsible for the day-to-day operation of a credit union, and the Board believes their competence is as critical as that of the elected officers and board members. Accordingly, the Board has not adopted this recommended change.

One commenter noted its opposition to the proposal, contending that the current rule permits an officer or senior executive employee to commence service on an interim basis until such time as the credit union is notified in writing of NCUA's determination to disapprove such service. The commenter has mistakenly characterized the current rule, which only permits such interim service if NCUA grants a waiver from the otherwise mandatory thirty-day notice. The proposed amendments preserve the ability of a credit union to seek a waiver from the advance notice requirements in those cases in which the circumstances may warrant service to begin immediately. The final rule clarifies any ambiguity in the current rule between the operation of the prior notice and commencement of service provisions in the rule. The final rule retains the waiver provisions that provide sufficient flexibility where circumstances warrant immediate service yet permits the regional offices to conduct the review contemplated by the Federal Credit Union Act.

Final Rule

In view of the comments, NCUA is adopting the proposed amendments as a final rule without change.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) requires NCUA to prepare an analysis to describe any significant economic impact any proposed regulation may have on a substantial number of small entities. NCUA considers credit unions having less than ten million dollars in assets to be small for purposes of RFA. Interpretive Ruling and Policy Statement (IRPS) 87–2 as amended by IRPS 03–2. The amendment clarifies the relationship between the waiver of prior

notice provision and the temporary service provision, so as to eliminate any potential confusion. The NCUA has determined and certifies that this amendment will not have a significant economic impact on a substantial number of small credit unions. Accordingly, the NCUA has determined that a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

NCUA has determined that this amendment would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget (OMB). NCUA currently has OMB clearance for § 701.14's collection requirements (OMB No. 3133–0121).

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The amendment will apply to all federally-insured credit unions. NCUA has determined that the amendment will not have a substantial direct effect on the States, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this amendment does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

NCUA has determined that this amendment will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 701

Credit unions, Senior executive officials.

By the National Credit Union Administration Board on October 21, 2004.

Mary Rupp,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 723

Member Business Loans

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is amending the collateral and security requirements of its member business loans (MBL) rule to enable credit unions subject to the rule to participate more fully in Small Business Administration (SBA) guaranteed loan programs.

DATES: This final rule is effective November 26, 2004.

FOR FURTHER INFORMATION CONTACT: Frank Kressman, Staff Attorney, Office of General Counsel, at (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

In 2003, NCUA amended its MBL rule and other rules related to business lending to enhance credit unions' ability to meet their members' business loans needs. 68 FR 56537 (October 1, 2003). In addition to comments on those amendments, NCUA received other suggestions on how it could improve the MBL rule. Among the most significant of these, commenters suggested NCUA amend the MBL rule ''so that it could be better aligned with lending programs offered by the Small Business Administration,'' such as the SBA's Basic 7(a) Loan Program. *Id.* at 56538. While NCUA recognized the merits of this suggestion, NCUA could not include it in the final rulemaking because it addressed issues outside the scope of the rulemaking. The Administrative Procedure Act generally prohibits Federal Government agencies from adopting rules without affording the opportunity for public comment. 5 U.S.C. 553. NCUA noted in the final rule, however, that it would review this suggestion to determine if it would be appropriate to act on it in a subsequent rulemaking.

As a result of that review, NCUA issued a proposed amendment to its MBL rule in June 2004 to permit credit unions to make SBA guaranteed loans under SBA's less restrictive lending requirements instead of under the more restrictive MBL rule's lending requirements. 69 FR 39873 (July 1, 2004). NCUA reviewed the SBA's loan programs in which credit unions can participate and determined they provide reasonable criteria for credit union participation and compliance within the bounds of safety and soundness. Additionally, these SBA programs are ideally suited to the mission of many credit unions to satisfy their members' business loans needs.

NCUA noted in the proposal that it recognizes NCUA's collateral and security requirements for MBLs, including construction and development loans, are generally more restrictive than those of the SBA's guaranteed loan programs and could hamper a credit union's ability to participate fully in SBA loan programs. As a result, the MBL rule's collateral and security requirements could prevent a credit union from making a particular loan that it could otherwise make under SBA's requirements. NCUA issued the proposal to provide relief from these more restrictive requirements and to help enable credit unions to better serve their members' business loans needs.

B. Clarification of Existing Authority

NCUA discussed in the proposal that its Office of General Counsel in Legal Opinion 03–0911, dated May 20, 2004, clarified that NCUA's general lending rule and the Federal Credit Union Act (Act) permit federal credit unions (FCUs) to make MBLs under the terms of the SBA's guaranteed loan programs to the extent the terms and conditions under which the guarantee is provided are consistent with the requirements and limitations in the MBL rule. 12 CFR 701.21(e); 12 U.S.C. 1757(5)(A)(iii). Specifically, the opinion identified loan maturity limits, usury ceilings and prepayment penalties as terms of the SBA's guaranteed loan programs that an FCU could use in lieu of corresponding terms in NCUA's rules. The opinion stated, however, that a credit union could not rely on the exception for government guaranteed loan programs in NCUA's general lending rule and the Act with regard to collateral requirements for MBLs. 12 CFR 701.21(e); 12 U.S.C. 1757(5)(A)(iii). The opinion explained the MBL rule expressly sets collateral requirements for MBLs in the form of maximum loan-to-value ratios. The collateral requirements of the SBA's guaranteed loan programs are not consistent with those of the current MBL rule and, therefore, cannot be used. The proposed amendments to the MBL rule remove that impediment by exempting SBA guaranteed loans from the MBL rule's collateral requirements.

The proposal also noted that there could be circumstances where a business loan made under an SBA loan program would not be subject to the MBL rule. For example, a $40,000 business loan with an SBA guarantee to a member who has no other loans with the originating credit union would be too small to meet the definition of an MBL. Thus, the credit union in this example can rely on the authority provided by § 701.21(e) of NCUA's rules and make a business loan as part of an SBA loan program under all of the terms and conditions required or permitted by the program.

The MBL rule applies to all FCUs and to most federally-insured state credit unions (FISCUs). The proposal noted that a FISCU is exempt from the MBL rule only if, after August 7, 1998, the enactment of the Credit Union Membership Access Act (CUMAA), Public Law 105–21, its state supervisory authority (SSA) has adopted its own business loan rule, with the approval of the NCUA Board, for use instead of NCUA's MBL rule. The amendments regarding collateral requirements apply to all credit unions subject to the MBL rule, but it is important to note that legal opinion OGC 03–0911 applies only to FCUs, not FISCUs. FISCUs follow state law and regulation with respect to loan maturity, interest rate and prepayment penalties. For those issues, the relationship between any state law limitations and SBA's requirements should be determined by FISCUs in consultation with their state supervisory authority.

Finally, the proposal noted that, while NCUA believes many credit unions would greatly benefit from participating in SBA programs, NCUA also believes that programs of this type can create some additional safety and soundness concerns. For example, the loans being guaranteed are often riskier than other loans made by credit unions, and most credit unions would not make these kinds of loans without the security the SBA guarantees provide. NCUA noted it is aware that SBA guarantee programs generally place stringent requirements on participating lenders to comply with program requirements or face losing the guarantee. Accordingly, the proposal recommended that, before a credit union becomes a participating lender, it makes certain it fully understands the terms of the program and has procedures in place to assure its compliance with all program requirements.

C. Summary of Comments

NCUA received twenty-four comment letters regarding the proposed rule: four from FCUs, three from state credit unions, one from a private individual, seven from credit union trade organizations, one from a credit union service organization, one from a certified development company, one from a certified development company

trade organization, one from a professional association representing state and territorial regulatory agencies, one from a bank, and four from banking trade organizations. All commenters supported the proposal except the bank and banking trade organizations.

Many of the commenters supporting the proposal also offered additional comments. For example, seven commenters asked NCUA to clarify that the proposal applies to SBA's Certified Development Company (504) Loan Program in addition to SBA's Basic 7(a) Loan Program. NCUA confirms the proposal applies to the 504 Loan Program and highlights that the proposal expressly states it applies to MBLs made *as part of* an SBA guaranteed loan program.

Four commenters suggested NCUA expand the scope of the proposal to include other government guaranteed loan programs. Three of them specifically named the Farm Service Agency or United States Department of Agriculture loan programs. Two of them suggested all government guaranteed loan programs be included. As noted in the preamble to the proposal, NCUA is willing to consider other government guaranteed loan programs as it becomes apparent there is demand for the program among credit unions.

Two commenters suggested NCUA reference Part 702 Prompt Corrective Action (PCA) in § 723.4 of the MBL rule to indicate PCA applies to member business lending. These commenters also stated it is burdensome for credit unions to have to track and report MBLs differently for different purposes. Specifically, they noted credit unions must do this when calculating net member business loan balances (NMBLB) under the MBL rule and risk-based net worth (RBNW) requirement under PCA. One of these commenters asked NCUA to explore ways of minimizing this burden. The other suggested using the NMBLB for purposes of calculating the RBNW requirement and permit credit unions to exclude MBLs that have been paid down below $50,000 from the calculation of the RBNW requirement. Part 702 is currently referenced in § 723.1 but not in § 723.4. NCUA is including a reference to part 702 in § 723.4 in the final rule. While NCUA recognizes there is some degree of inconvenience associated with tracking and reporting MBLs differently when calculating NMBLB and RBNW, NCUA believes the risks associated with making MBLs necessitate this form of accounting. Additionally, this system helps preserve the flexibility a credit union has to exclude MBLs from its NMBLB when they have been paid down below $50,000.

Three commenters asked NCUA to clarify how an SBA loan term could be both less restrictive than an NCUA requirement and still consistent with the MBL rule. This is possible when an SBA term is less restrictive than an NCUA requirement that is not specifically addressed in the MBL rule. For example, maturity limits are not specifically addressed in the MBL rule but are in the Act and elsewhere in NCUA's regulations.

The bank and four banking trade organizations opposed the proposal stating, among other things, it contradicts congressional intent to limit credit unions' ability to make MBLs. NCUA disagrees. The proposal does not increase any congressional limits on the kind or amount of MBLs a credit union may make. Moreover, the legal authority allowing credit unions to make MBLs under the terms of an SBA guaranteed loan program is in the Act and, therefore, directly reflecting congressional intent. Finally, congressional representatives have urged NCUA to use its authority, conferred by Congress, to facilitate MBL lending and to refrain from imposing any limitations on credit unions in this context not explicitly called for by Congress in CUMAA. 68 FR 56537, 56538 (October 1, 2003).

Accordingly, except for technical amendments, NCUA adopts the proposed amendments to part 723 as final without change.

D. Net Member Business Loan Balance

The MBL rule uses the phrase ''net member business loan balance'' to describe the outstanding loan balance plus any unfunded commitments reduced by a number of factors. Section 723.10(h) uses the phrase ''outstanding member business loan balance'' instead of ''net member business loan balance.'' This inconsistent use of language was inadvertent and is corrected by amending § 723.10(h) to read ''net member business loan balance.''

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a rule may have on a substantial number of small credit unions (those under ten million dollars in assets). This rule permits credit unions to more fully participate in SBA loan programs, without imposing any additional regulatory burden. The final rule would not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. This final rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 723

Credit, Credit unions, Reporting and recordkeeping requirements.

By the National Credit Union Administration Board on October 21, 2004.

Mary F. Rupp,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 717 and 748

Fair Credit Reporting—Proper Disposal of Consumer Information Under the Fair and Accurate Credit Transactions Act of 2003

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The NCUA Board is adopting a final rule to implement section 216 of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act) by amending security program regulations and NCUA's Guidelines for Safeguarding Member Information and establishing a section in new part 717. The final rule generally requires federal credit unions (FCUs) to develop, implement, and maintain appropriate measures to properly dispose of consumer information derived from consumer reports to address the risks associated with identity theft. FCUs are expected to implement these measures consistent with the provisions in NCUA's Guidelines for Safeguarding Member Information.

DATES: Effective December 29, 2004.

FOR FURTHER INFORMATION CONTACT: Chrisanthy J. Loizos, Staff Attorney, Office of General Counsel, National Credit Union Administration, (703) 518–6540.

SUPPLEMENTARY INFORMATION:

I. Introduction

Section 216 of the FACT Act adds a new section 628 to the Fair Credit Reporting Act (FCRA) that, in general, is designed to protect a consumer against the risks associated with unauthorized access to information about the consumer contained in a consumer report, such as fraud and identity theft. 15 U.S.C. 1681w. Section 216 of the FACT Act requires NCUA to adopt a rule requiring any FCU ''that maintains or otherwise possesses consumer information, or any compilation of consumer information, derived from consumer reports for a business purpose to properly dispose of any such information or compilation.'' Pub. L. 108–159, 117 Stat. 1985–86. The FACT Act mandates that the rule be consistent with the requirements issued pursuant to the Gramm-Leach-Bliley Act (GLBA) (Pub. L. 106–102), as well as other provisions of Federal law. The FACT Act also requires NCUA to consult and coordinate with the Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (FRB), Federal Deposit Insurance Corporation (FDIC), Office of Thrift Supervision (OTS), Federal Trade Commission (FTC), and Securities and Exchange Commission (collectively, the Agencies) so that, to the extent possible, NCUA's rule is consistent and comparable with the regulations issued by each of the other agencies.

II. Background

In 2001, NCUA amended the security program rule to establish standards for federally insured credit unions (FICUs) relating to administrative, technical, and physical safeguards to protect the security and confidentiality of member records and information, pursuant to section 501 of GLBA. 15 U.S.C. 6805(b). NCUA worked with the Agencies and state insurance authorities to develop appropriate standards. 66 FR 8152 (Jan. 30, 2001). The Federal banking agencies issued their standards as guidelines under section 39 of the Federal Deposit Insurance Act. 12 U.S.C. 1831p.[1] NCUA determined it could best meet the congressional directive to prescribe standards by amending the rule governing security programs and by providing guidance in an appendix to the rule. 12 CFR part 748, appendix A; 66 FR 8152 (Jan. 30, 2001).

Section 748.0 requires an FICU to develop a security program that implements safeguards designed to: (1) Ensure the security and confidentiality of member records and information; (2) protect against any anticipated threats or hazards to the security or integrity of such records; and (3) protect against unauthorized access to or use of such records or information that could result in substantial harm or inconvenience to a member. 12 CFR 748.0(b)(2).

Appendix A to part 748 sets forth NCUA's Guidelines for Safeguarding Member Information (Guidelines), which are substantially identical to the guidelines issued by the Agencies. 66 FR 8152 (Jan. 30, 2001). The Guidelines ''are intended to outline industry best practices and assist credit unions to develop meaningful and effective security programs to ensure their compliance with the safeguards contained in the regulation.'' *Id.*

The Guidelines direct FICUs to assess the risks to their member information and member information systems and, in turn, implement appropriate security measures to control those risks. 12 CFR part 748, appendix A. For example, under the risk-assessment framework, FICUs should evaluate whether the controls the FICU has developed sufficiently protect its member information from unauthorized access, misuse, or alteration when the FICU disposes of the information. ''[A] credit union's responsibility to safeguard member information continues through the disposal process.'' 66 FR 8152, 8155.

On May 28, 2004, the NCUA Board published a proposal to add a section to the new fair credit reporting rule and amend the security program rule and Guidelines for Safeguarding Member Information (Guidelines) to require FCUs to implement controls designed to ensure the proper disposal of consumer information within the meaning of section 216. 69 FR 30601 (May 28, 2004). NCUA's proposed regulation and the preamble were substantively similar to a joint notice of proposed rulemaking issued by the FRB, OCC, FDIC and OTS (the Federal banking agencies). 69 FR 31913 (June 8, 2004).

In the proposal, NCUA noted that section 216 of the FACT Act requires NCUA to issue final regulations for entities under its enforcement authority under section 621 of the FCRA. Unlike the current provisions in the security program rule, which apply to all FICUs, the requirements in NCUA's final rule apply solely to FCUs. *See* 15 U.S.C. 1681s(b)(3). Federally insured state-chartered credit unions are subject to the enforcement jurisdiction of the FTC for purposes of the FCRA. *See* 15 U.S.C. 1681s(a). State charters, therefore, should refer to the final rule issued by the FTC regarding the proper disposal of consumer information under section 216.

III. Summary of Comments

NCUA received fourteen comment letters: One from a corporate credit union; four from natural person credit unions; five from credit union trades or leagues; one from a consumer; two from financial services trade organizations; and a joint letter from seven consumer rights organizations. The Agencies also received numerous letters from financial institutions, industry trade organizations, consumer advocacy groups, consumers, and trade associations from the information destruction industry. NCUA and the Agencies considered the comments and suggestions submitted.

Of the letters received by NCUA, twelve commenters generally supported the proposed regulation requiring FCUs to properly dispose of consumer information. One commenter stated that the proposal balanced the concerns of consumers and the industry by providing reasonable protections from identity theft and the unintended

[1] 12 CFR parts 30, app. B; 208, app. D–2 and 225, app. F; 364, app. B; 570, app. B. *See* 66 FR 8616 Feb. 1, 2001.

disclosure of consumer information while giving FCUs sufficient latitude for the disposal of consumer information. One comment letter, submitted on behalf of seven consumer groups, found the proposed rule weak and inadequate to meet Congress' intended purpose of preventing identity theft and other fraud.

IV. Analysis of Final Rule

Section-by-Section Overview

Section 717.83—Disposal of Consumer Information

As set forth in the proposal, NCUA is establishing a new part 717 to house its fair credit reporting rules and adds a subpart setting forth the duties of users of consumer reports regarding identity theft. To implement section 216, NCUA is adding § 717.83 to require FCUs to develop and maintain, as part of their information security programs, appropriate controls designed to ensure that they properly dispose of consumer information. The final rule retains the statute's rule of construction as proposed stating that this requirement does not impose any requirements to maintain or destroy consumer records beyond those imposed by any other law. The final rule also does not affect any requirement to maintain or destroy consumer records imposed under any other provision of law.

The only revisions to § 717.83 from the proposed rule incorporate examples of appropriate measures to properly dispose of consumer information and clarify ''consumer information'' in its definition and through examples. These additions required a renumbering of the section and are discussed in further detail below.

The final rule also includes a general definitions section, § 717.3, to define the terms ''you'' and ''consumer.'' Although these definitions were not included in the proposed disposal rule, they were published in another FACT Act proposal.[2] The final rule refers to FCUs using the plain language term ''you'' because section 216 requires NCUA to adopt a final disposal rule for FCUs. The final rule also uses the term ''consumer.'' Paragraph (e) of § 717.3 defines the term ''consumer'' to mean an individual, which follows the statutory definition in section 603(c) of the FCRA. 15 U.S.C. 1681a(c). NCUA will add more definitions to § 717.3 as the agency adopts other rules to implement provisions of the FCRA.

Section 748.0—Security Program

The final rule retains § 748.0(c) as proposed. Paragraph (c) cross references the section 216 requirement in § 717.83, for ease of reference when FCUs adopt or modify their information security programs.

Guidelines for Safeguarding Member Information

The final rule amends the Guidelines to specifically address the disposal of consumer information by: (1) Defining ''consumer information'' as defined in § 717.83; (2) adding an objective regarding the proper disposal of member information and consumer information; and (3) providing that an FCU should implement appropriate measures to properly dispose of member information and consumer information. NCUA discusses the final rule's slight variations from the proposal below.

The changes to the Guidelines are intended to provide guidance to FCUs for compliance with § 717.83. As noted above, the requirements of this final rule only apply to FCUs, while federally insured state-chartered credit unions are subject to the jurisdiction of the FTC on this matter. NCUA believes, however, that federally insured state charters may find this guidance helpful in adopting meaningful and effective security programs that deal with the disposal of consumer information.

In accordance with section 216, NCUA has consulted with the Agencies to ensure that, to the extent possible, the final rules issued by the respective agencies to implement section 216 are consistent and comparable.

Proper Disposal of Consumer Information and Member Information

Consumer Information

Proposed § 717.83(c)(1) defined ''consumer information'' to mean ''any record about an individual, whether in paper, electronic, or other form, that is a consumer report or is derived from a consumer report and that is maintained or otherwise possessed by or on behalf of the credit union for a business purpose.'' ''Consumer information'' was also defined to mean ''a compilation of such records.''

Commenters generally supported NCUA's proposed definition of this term, but argued that NCUA should include statements or illustrations to clarify the nature and scope of ''consumer information.'' Several commenters found the proposed phrase ''about an individual'' to be ambiguous and urged NCUA to adopt a definition expressly stating that ''consumer information'' only includes information that identifies a particular individual.

Similarly, some commenters supported NCUA's explanation in the proposal that ''consumer information'' does not include information derived from a consumer report that does not identify any particular consumer, such as the mean credit score derived from a group of consumer reports. These commenters suggested that NCUA include this example or similar examples in the definition.

In § 717.83(d)(1), the final rule defines ''consumer information'' as proposed but modifies the term to expressly exclude from the definition ''any record that does not identify an individual.'' NCUA believes that qualifying the term ''consumer information'' to cover only personally identifiable information appropriately focuses on the information derived from a consumer report that, if improperly disposed, could be used to commit fraud or identity theft against a consumer. NCUA believes that limiting this definition to information that identifies a consumer is consistent with the current law relating to the scope of the term ''consumer report'' under the FCRA and the purposes of section 216 of the FACT Act.

Under the final rule, an FCU must implement measures to properly dispose of consumer information that identifies a consumer, such as the consumer's name and the credit score derived from a consumer report. This requirement, however, does not apply to aggregate information, such as the mean credit score that is derived from a group of consumer reports, or blind data, such as a series of credit scores that do not identify the subjects of consumer reports from which those scores are derived. The final rule includes examples of records that illustrate this aspect, but it does not rigidly define the nature and scope of personally identifiable information. These examples are found in § 717.83(d)(1)(i). NCUA notes that there are a variety of types of information apart from an individual's name, account number, or address that, depending on the circumstances or when used in combination, could identify the individual.

As discussed in the proposal, NCUA notes that the scope of information covered by the terms ''consumer information'' and ''member information'' will sometimes overlap, but will not always coincide. The definition of ''consumer information'' is drawn from the term ''consumer'' in

[2] On April 8, 2004, NCUA issued its first proposal to add a new part 717, implementing section 411 of the FACT Act. *See* 69 FR 23380 (Apr. 28, 2004). This final disposal rule, however, will be the first section to establish the new part 717.

section 603(c) of the FCRA, which defines a ''consumer'' as an individual. 15 U.S.C. 1681a(c). By contrast, ''member information'' under the Guidelines, only covers nonpublic personal information about a ''member,'' as defined in § 716.3(n), namely, an individual who obtains a financial product or service to be used primarily for personal, family, or household purposes and who has a continuing relationship with the FCU.

The relationship between consumer information and member information can be illustrated through the following examples. Payment history information from a consumer report about an individual, who is an FCU's member, will be *both* consumer information because it comes from a consumer report and member information because it is nonpublic personal information about a member. In some circumstances, member information will be broader than consumer information. For instance, information that an FCU maintains about its member's transactions with the FCU would be only member information because it does not come from a consumer report. In other circumstances, consumer information will be broader than member information. Consumer information would include information from a consumer report that an FCU obtains about an individual who guarantees a loan for a business entity or who has applied for employment with the FCU. In these instances, the consumer reports would not be member information because the information would not be about a ''member'' within the meaning of the Guidelines but would be consumer information.

NCUA believes the phrase ''derived from consumer reports'' covers all of the information about a consumer that is taken from a consumer report, including information that results in whole or in part from manipulation of information from a consumer report or information from a consumer report that has been combined with other types of information. Consequently, an FCU that possesses any of this information must properly dispose of it. For example, any record about a consumer derived from a consumer report, such as the consumer's name and credit score, that is shared between an FCU and its credit union service organization (CUSO) affiliate must be disposed of properly by each affiliate that possesses that information. Similarly, a consumer report that is shared among affiliates after the consumer has been given a notice and has elected not to opt out of that sharing, and therefore is no longer a ''consumer report'' under section 603(d)(2)(A)(iii) of the FCRA, would still be consumer information. Accordingly, an affiliate that receives consumer information under these circumstances must properly dispose of the information. NCUA notes that a CUSO affiliate subject to the jurisdiction of the FTC must properly dispose of consumer information in accordance with the FTC's final rule.

The proposed definition of consumer information included the qualification ''for a business purpose,'' as set forth in section 216. NCUA believes that this phrase encompasses any commercial purpose for which an FCU might maintain or possess consumer information. Commenters did not raise concerns about this interpretation.

Proper Disposal

In the proposed rule, NCUA requested comment on the standard for proper disposal. Of the comment letters received by NCUA, five commenters thought that the concept was clear and sufficiently explained the nature and scope of an FCU's responsibilities under the rule, but two of those commenters welcomed additional clarification through guidance or examples. Four commenters believed ''proper disposal'' was not clear in the proposed rule and asked for either a definition or examples in the regulatory text like those used in the FTC's proposed rule. 69 FR 21388 (April 20, 2004). Some of these commenters stated that the rule should adopt a clear standard that requires FCUs to render paper and electronic data unreadable and incapable of being reconstructed. They also asked that the rule provide examples of proper disposal techniques consistent with the FTC's proposed regulatory text.

NCUA believes that there is no need to adopt a definition of the term ''disposal'' because, in the context of the duty imposed under section 216, the ordinary meaning of that term applies. The final rule, however, includes examples of appropriate measures to properly dispose of consumer information as requested by the commenters in renumbered paragraph (b) of § 717.83. NCUA believes these examples will be helpful as illustrative guidance for compliance with the rule.

NCUA notes that any sale, lease, or other transfer of any medium containing consumer information constitutes disposal of the information insofar as the information itself is not the subject of the sale, lease or other transfer between the parties. By contrast, the sale, lease, or other transfer of consumer information from an FCU to another party can be distinguished from the act of throwing out or getting rid of consumer information, and accordingly, does not constitute disposal subject to NCUA's rule.

New Objective for an Information Security Program

NCUA proposed to add a new objective regarding the proper disposal of consumer information in paragraph II.B. of the Guidelines. A few commenters expressed objections to this aspect of the proposal primarily as it relates to service providers.

The final rule slightly revises the proposal to add a new objective in the Guidelines providing that an FCU should design its information security program to ''[e]nsure the proper disposal of member information and consumer information.'' With this revision from the proposal, NCUA omitted the proposed provision stating that an FCU should ensure proper disposal of consumer information ''in a manner consistent with the disposal of member information.'' By making this change and adding the reference to ''member information'' in paragraph II.B., the Guidelines more clearly and fully state an FCU's information security objectives with respect to disposing of information. As noted in the proposal, a credit union should properly dispose of member information as part of designing and maintaining its information security program under the Guidelines. The inclusion of ''member information'' in the objective, therefore, does not establish a new objective in the Guidelines.

NCUA continues to believe that including this additional objective in paragraph II.B. of the Guidelines is important because section 216's disposal requirement applies to an FCU's consumer information maintained or otherwise in the possession of the FCU's service providers. NCUA notes that, under current paragraph III.D.2., an FCU is expected to ''[r]equire its service providers by contract to implement appropriate measures designed to meet the objectives'' of the Guidelines.

By expressly incorporating a provision in paragraph II.B. of the Guidelines, FCUs should contractually require service providers to develop appropriate measures for the proper disposal of consumer information and, where warranted, monitor service providers to confirm that they have satisfied their contractual obligations. As some commenters observed, the particular contractual arrangement that an FCU may negotiate with a service provider may take varied forms or use general terms. As a result, some credit unions already may have existing

contracts that are sufficiently broad to cover the proper disposal of member information and consumer information, and therefore they would not have to be amended. NCUA continues to believe that the parties should have substantial latitude in negotiating the contractual terms appropriate to their arrangement in any manner that satisfies the objectives of the Guidelines. NCUA, therefore, has not prescribed any particular standards that relate to these service provider contracts.

The final rule also amends paragraph III.G.4. of the Guidelines to allow an FCU a reasonable period of time, after the final rule is issued, to amend its contracts with its service providers to incorporate the necessary requirements in connection with the proper disposal of consumer information. After reviewing the varying comments on this provision of the proposal, NCUA has determined that FCUs should modify contracts that will be affected by the final rule's requirements, if necessary, no later than July 1, 2006.

New Provision To Implement Measures to Properly Dispose of Consumer Information

NCUA has amended paragraph III.C. of the Guidelines by adding a new provision stating that an FCU, as part of its information security program, should develop, implement, and maintain, appropriate measures to properly dispose of consumer information and member information. Like the proposal, this new provision also provides that FCUs should implement these measures ''in accordance with the provisions in paragraph III.'' of the Guidelines.

Paragraph III. of the Guidelines presently states that an FCU should undertake measures to design, implement, and maintain its information security program to protect member information and member information systems. Because ''member information systems'' is defined to include any methods used to dispose of member information, an FCU presently must use risk-based measures to protect member information. Building on this provision in the Guidelines, NCUA proposed a provision in paragraph III.C.4. stating that FCUs should develop controls ''in a manner consistent with the disposal of member information.'' Commenters generally supported this provision because FCUs could develop and implement risk-based protections, rather than be subject to a prescriptive standard that required them to adopt particular methods for disposing of consumer information.

In the final rule, NCUA has revised the proposed provision in paragraph III.C.4. by omitting ''in a manner consistent with the disposal of member information.'' In its place, the Guidelines now provide a more direct and general statement that FCUs should develop and maintain risk-based measures to properly dispose of consumer information and member information. Under this final amendment to the Guidelines, an FCU is expected to properly dispose of both classes of information, which is consistent with the Guidelines and the FACT Act.

An FCU should broaden the scope of its risk assessment to include an assessment of the reasonably foreseeable internal and external threats associated with the methods it uses to dispose of consumer information, and adjust its risk assessment in light of the relevant changes relating to such threats. By expressly referencing the disposal requirement in § 748.0(c) and the Guidelines, NCUA expects FCUs to integrate into their information security programs the risk-based measures in paragraph III of the Guidelines for the disposal of consumer information.

After reviewing the comments, NCUA continues to believe that it is not necessary to propose a prescriptive rule describing proper methods of disposal.

Nonetheless, consistent with interagency guidance previously issued through the Federal Financial Institutions Examination Council (FFIEC),[3] NCUA expects FCUs to have appropriate disposal procedures for records maintained in paper-based or electronic form. In addition, as noted above, the final rule includes illustrative examples of appropriate measures to properly dispose of consumer information in § 717.83(b). An FCU's information security program should ensure that paper records containing either member or consumer information should be rendered unreadable as indicated by the FCU's risk assessment, such as by shredding or any other means. FCUs also should recognize that computer-based records present unique disposal problems. Residual data frequently remains on media after erasure. Since that data can be recovered, FCUs should apply additional disposal techniques to sensitive electronic data.[4]

Compliance

The final rule requires FCUs to implement the appropriate measures to properly dispose of consumer information by July 1, 2005. NCUA believes that any changes to an FCU's existing information security program likely will be minimal because many of the measures that an FCU already uses to dispose of member information can be adapted to properly dispose of consumer information. Several commenters agreed with NCUA's assessment and noted that they already have appropriate disposal policies in place. Nevertheless, a comment on behalf of small credit unions and a few comments to the Federal banking agencies noted the proposed period for compliance would be relatively short in light of the work required to amend policies and locate and track consumer information in an institution's existing information system. Accordingly, NCUA has determined that the final rule should afford FCUs a six-month period to adjust their systems and controls.

V. 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 (those under $10 million in assets). The NCUA Board has determined and certifies that the final rule will not have a significant economic impact on a substantial number of small credit unions. Accordingly, a regulatory flexibility analysis is not required.

The rule requires an FCU to implement appropriate controls designed to ensure the proper disposal of consumer information. An FCU must develop and maintain these controls as part of implementing its existing information security program as required by § 748.0.

Any modifications to an FCU's information security program needed to address the proper disposal of consumer information could be incorporated through the process the FCU presently uses to adjust its program under paragraph III.E. of the Guidelines, particularly because of the similarities between the consumer and member information and the measures commonly used to properly dispose of both types of information. To the extent the rule imposes new requirements for certain types of consumer information, developing appropriate measures to properly dispose of that information likely would require only a minor modification of an FCU's existing information security program.

Because some consumer information will be member information and

[3] *See* FFIEC Information Security Booklet, page 63 at: *http://www.ffiec.gov/ffiecinfobase/booklets/information—security/information—security.pdf.*

[4] *See* footnote 3, *supra.*

because segregating particular records for special treatment may entail considerable costs, NCUA believes that many FCUs, including small entities, already are likely to have implemented measures to properly dispose of both member and consumer information. In addition, NCUA and the Federal banking agencies, through the Federal Financial Institutions Examination Council (FFIEC), already have issued guidance regarding their expectations concerning the proper disposal of *all* of an institution's paper and electronic records. *See* FFIEC Information Security Booklet, December 2002, p. 63.[5] Therefore, the rule does not require any significant changes for FCUs that currently have procedures and systems designed to comply with this guidance.

NCUA anticipates that, in light of current practices relating to the disposal of information in accordance with § 748.0, the Guidelines, and the guidance issued by the FFIEC, the final rule would not impose undue costs on FCUs. NCUA believes that the controls that small FCUs would need to develop and implement, if any, to comply with the rule likely pose a minimal economic impact on those entities.

[5] *See* footnote 3, *supra.*

Paperwork Reduction Act

NCUA has determined that the final rule does not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their regulatory actions on State and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. This final rule will not have substantial direct effects on the States, on the relationship between the National Government and the States, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that the final rule does not constitute a policy that has federalism implications for purposes of the executive order.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedures Act. 5 U.S.C. 551. The Office of Management and Budget (OMB) has determined that this rule is not a major rule for the purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

The Treasury and General Government Appropriations Act, 1999—-Assessment of Federal Regulations and Policies on Families

NCUA has determined that this rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

List of Subjects

12 CFR Part 717

Consumer protection, Credit unions, Information, Privacy, Reporting and recordkeeping requirements.

12 CFR Part 748

Credit unions, Crime, Currency, Reporting and recordkeeping requirements, and Security measures.

By the National Credit Union Administration Board on November 18, 2004.

Mary F. Rupp,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Loan Interest Rates

AGENCY: National Credit Union Administration.

ACTION: Final rule.

SUMMARY: The current 18 percent per year federal credit union maximum loan rate is scheduled to revert to 15 percent on March 9, 2005, unless otherwise provided by the NCUA Board (Board). A 15 percent ceiling would restrict certain categories of credit and adversely affect the financial condition of a number of federal credit unions. At the same time, prevailing market rates and economic conditions do not justify a rate higher than the current 18 percent ceiling. Accordingly, the Board hereby continues an 18 percent federal credit union loan rate ceiling for the period March 9, 2005 through September 8, 2006. The Board is prepared to reconsider the 18 percent ceiling at any time should changes in economic conditions warrant.

DATES: Effective February 28, 2005.

FOR FURTHER INFORMATION CONTACT: Daniel Gordon, Senior Investment Officer, Office of Strategic Program Support and Planning, at the National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428, or telephone (703) 518–6620.

SUPPLEMENTARY INFORMATION:

Background

Public Law 96–221, enacted in 1980, raised the loan interest rate ceiling for federal credit unions from one percent per month (12 percent per year) to 15 percent per year. 12 U.S.C. 1757(5)(A)(vi). The law also authorized the Board to set a higher limit, after consulting with Congress, the Department of Treasury and other federal financial agencies, for a period not to exceed 18 months, if the Board determined that: (1) Money market interest rates have risen over the preceding six months; and (2) prevailing interest rate levels threaten the safety and soundness of individual credit unions as evidenced by adverse trends in growth, liquidity, capital, and earnings.

On December 3, 1980, the Board determined that the foregoing conditions had been met. Accordingly, the Board raised the loan ceiling to 21 percent. In the unstable environment of the first half of the 1980s, the Board lowered the loan rate ceiling from 21 percent to 18 percent, effective May 18, 1987. This action was taken in an environment of falling market interest rates from 1980 to early 1987. The ceiling has remained at 18 percent to the present. The Board believes retaining the 18 percent ceiling will permit credit unions to continue to meet their current lending programs and permit the necessary flexibility for credit unions to react to any adverse economic developments.

The Board would prefer not to set loan interest rate ceilings for federal credit unions. Credit unions are cooperatives and establish loan and share rates consistent with the needs of their members and prevailing market interest rates. The Board supports free lending markets and the ability of federal credit union boards of directors to establish loan rates that reflect current market conditions and the interests of their members.

Congress, however, has imposed loan rate ceilings since 1934, and, as stated previously, in 1980, Congress set the ceiling at 15 percent but authorized the Board to set a ceiling in excess of 15 percent, if conditions warrant. The following analysis justifies a ceiling above 15 percent, but at the same time does not support a ceiling above the current 18 percent. The Board is prepared to reconsider this action at any time should changes in economic conditions warrant.

Money Market Interest Rates

As Table 1 below shows, interest rates on United States Treasury securities have increased in maturities of three years and less, in the six month period June 1, 2004 through November 30, 2004.

Table 1.—Change in U.S. Government Yields

[May 30, 2004–November 30, 2004]

Maturity	Rate 5/30/2004 (percent)	Rate 11/30/2004 (percent)	Change (percent)
3-month	1.06	2.22	1.16
6-month	1.38	2.43	1.05
2-year	2.53	3.00	.47
3-year	3.06	3.25	.19
5-year	3.79	3.69	-.10
10-year	4.65	4.35	-.30

In addition, between June 2004 and November 30, 2004, the Board of Governors of the Federal Reserve System raised the federal funds target rate four times, from 1.00 percent to 2.00 percent. In December 2004, the Federal Reserve raised the federal funds target rate another .25 percent. Statements from Federal Reserve officials indicate that further increases in the federal funds target rate are expected. For example, Anthony M. Santomero, President of the Federal Reserve Bank of Philadelphia, said, ''I think it is fair to say a neutral federal funds policy is above our current level.'' Michael H. Moskow, President of the Federal Reserve Bank of Chicago, said, ''There is certainly more ground to cover on interest rates.''

The forward Treasury curve (Table 2) also anticipates higher rates. The expected increases range from 87 basis points in the 1-year maturity to 34 basis points in the 10-year maturity.

Table 2.—Implied 1-Year Forward Rates

[November 30, 2004]

Maturity	Change one-year forward rate (percent)
1-year	.87
2-year	.57
3-year	.52
5-year	.64
10-year	.34

Financial Implications for Credit Unions

For at least 450 federal credit unions, representing 7.79% percent of reporting federal credit unions, the most common rate on unsecured loans was above 15 percent at year-end 2003. While the bulk of credit union lending is below 15 percent, small credit unions and credit unions that have implemented risk-based lending programs require interest rates above 15 percent to maintain liquidity, capital, earnings, and growth. Loans to members who have not yet established credit histories or have weak credit histories have more credit risk. Credit unions must charge rates to cover the potential of higher than usual losses for such loans.

There are undoubtedly more than 450 federal credit unions charging over 15 percent for unsecured loans to such members. Many credit unions have ''credit builder'' or ''credit rebuilder'' loans but report only the most common unsecured loan rates on NCUA Call Reports. Lowering the interest rate ceiling for federal credit unions would discourage these credit unions from making certain loans and many of the affected members would have no alternative but to turn to other lenders who charge higher rates.

Small credit unions would be particularly affected by lower loan rate ceilings since they tend to have higher levels of unsecured loans, typically with lower loan balances. Table 3 shows the number of federal credit unions in each asset group where the most common rate is more than 15 percent for unsecured loans.

Table 3.—Active Federal Credit Unions With Most Common Unsecured Loan Rates Greater Than 15 Percent

[December 2003]

Peer group by asset size	Total all Federal credit unions	Number of Federal credit unions with greater than 15 percent
$0–2 million	1175	92
$2–10 million	1794	164
$10–50 million	1753	123
$50 million+	1051	71
Total	5773	450

Should the interest rate charged on loans be subject to a 15 percent ceiling, a number of federal credit unions, where the majority of members are low-income, will incur significant financial strain. Approximately 12.65 percent of federal credit unions with low-income designation report loan interest rates greater than 15 percent. In contrast, only 7.79 percent of all credit unions report rates above 15 percent. Approximately 14.33 percent of low-income credit unions with assets less than $10 million would be affected.

These credit unions offset the cost of generating low-balance loans by charging increased interest rates. These credit unions generally are not able to provide credit card loans and, instead, grant closed-ended and open-ended loans with the prerequisite underwriting documentation. Further, these smaller credit unions generally maintain a higher expense ratio, since many are involved with high-transaction accounts requiring higher personnel costs and related operational expenses, and lack economies of scale.

Further, among the 450 federal credit unions where the most common rate is more than 15 percent for unsecured loans, 62 credit unions have 20 percent or more of their assets in this category and all but five credit unions have assets of less than $10 million. For these credit unions, lowering the rates would threaten their liquidity, capital, earnings, and growth.

The Board has concluded that conditions exist to retain the federal credit union interest rate ceiling of 18 percent per year for the period March 9, 2005 through September 8, 2006. Finally, the Board is prepared to reconsider the 18 percent ceiling at any time during the extension period should changes in economic conditions warrant.

Regulatory Procedures

Administrative Procedure Act

The Board has determined that notification and public comment on this rule are impractical and not in the public interest. 5 U.S.C. 553(b)(3)(B). Due to the need for a planning period before the March 9, 2005 expiration date of the current rule, and the threat to the safety and soundness of individual credit unions with insufficient flexibility to determine loan rates, final action on the loan rate ceiling is necessary.

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a regulation may have on a substantial number of small credit unions (those under ten million dollars in assets). This final rule provides added flexibility to all federal credit unions regarding the permissible interest rate that may be used in connection with lending. The NCUA Board has determined and certifies that this rule will not have a significant economic impact on a substantial number of small credit unions.

Paperwork Reduction Act

NCUA has determined that this rule does not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their regulatory actions on state and local interest. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. This rule applies only to federal credit unions and, thus, will not have substantial direct effects on the states, on the relationship between the national government and the states, nor materially affect state interests. The NCUA has determined that the rule does not constitute a policy that has any federalism implication for purposes of the executive order.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for

congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this is not a major rule.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

NCUA has determined that this rule will not affect family well-being within the meaning of Section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

List of Subjects in 12 CFR Part 701

Credit, Credit unions, Loan interest rates.

By the National Credit Union Administration Board on January 13, 2005.

Mary F. Rupp,

Secretary to the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 708a

Conversion of Insured Credit Unions to Mutual Savings Banks

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is updating its rule regarding conversion of insured credit unions to mutual savings banks (MSBs). The amendments require a converting credit union to provide its members with additional disclosures about the conversion before conducting a member vote. The amendments also require the vote to be by secret ballot and conducted by an independent entity. Finally, the amendments require a federally-insured State credit union to provide NCUA with conversion related information about the law of the State where the credit union is chartered.

DATES: This final rule is effective January 28, 2005.

FOR FURTHER INFORMATION CONTACT: Frank S. Kressman, Staff Attorney, at (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

The Credit Union Membership Access Act (CUMAA) was enacted into law on August 7, 1998. Public Law 105–21. Section 202 of CUMAA amended the provisions of the Federal Credit Union Act concerning conversion of insured credit unions to MSBs. 12 U.S.C. 1785(b). CUMAA required NCUA to promulgate final rules regarding charter conversions that were: (1) Consistent with CUMAA; (2) consistent with the charter conversion rules promulgated by other financial regulators; and (3) no more or less restrictive than rules applicable to charter conversions of other financial institutions. NCUA issued rules in compliance with this mandate. 63 FR 65532 (November 27, 1998); 64 FR 28733 (May 27, 1999).

Since the enactment of CUMAA, NCUA has become concerned that many credit union members do not appreciate the effect a conversion may have on their ownership interests in the credit union and voting power in the MSB. In February 2004, NCUA amended part 708a to require a converting credit union to disclose additional information to its members to better educate them regarding the conversion. 69 FR 8548 (February 25, 2004). NCUA solicited public comment as part of that rulemaking. Some commenters suggested that, among other things, NCUA should have imposed more disclosures and requirements on converting credit unions. Many offered specific suggestions. NCUA noted at that time that many of those suggestions deserved further consideration but were beyond the scope of that rulemaking and would have to be considered in a future rulemaking. In July 2004, NCUA issued a proposed rule with request for comments to address some of those suggestions and other ongoing concerns NCUA has in connection with protecting members' interests in the conversion process. 69 FR 46111 (August 2, 2004).

B. Discussion

CUMAA provides that an insured credit union may convert to an MSB without the prior approval of NCUA, but it also requires NCUA to administer the member vote on conversion and review the methods and procedures by which the vote is taken. This is reflected in NCUA's conversion rule. The rule requires a converting credit union to provide its members with written notice of its intent to convert. 12 CFR 708a.4. It also specifies that the member notice must adequately describe the purpose and subject matter of the vote on conversion. *Id.* In addition, a converting credit union must notify NCUA of its intent to convert. 12 CFR 708a.5. The credit union must provide NCUA a copy of its member notice, ballot, and all other written materials it has provided or intends to provide to its members in connection with the conversion. *Id.*

A converting credit union has the option of submitting these materials to NCUA before it distributes them to its members. *Id.* This enables the credit union to obtain NCUA's preliminary determination on the methods and procedures of the member vote based on NCUA's review of the written materials. NCUA believes its review of these materials is a practical and unintrusive way of fulfilling, at least part of, its congressionally mandated responsibility to review the methods and procedures of the vote.

If NCUA disapproves of the methods and procedures of the member vote after the vote is conducted, then NCUA is authorized to direct a new vote be taken. 12 CFR 708a.7. NCUA interprets its responsibility to review the methods and procedures of the member vote to include determining that the member notice and other materials sent to the members are accurate and not misleading, all required notices are timely, and the membership vote is conducted in a fair and legal manner.

A charter conversion has consequences that may not surface for a number of years and are often not apparent at the time of conversion to even the most astute members. As a result, members cannot make an informed decision about how the conversion will affect them unless their credit union provides them with this information.

NCUA is aware that credit unions are not providing some important conversion related information effectively to their members. This limits members' ability to make informed decisions about a conversion. NCUA also has become aware that many credit unions may not be equipped to conduct a proper member vote on conversion. Accordingly, NCUA is amending the conversion rule to require a converting credit union to provide additional disclosures to its members. Also, NCUA is providing guidelines to help converting credit unions better understand how they can satisfy the regulatory standard that the member vote be conducted in a fair and legal manner. In addition to the guidelines, NCUA is amending the rule to require the vote be conducted using secret ballots and an independent teller to ensure the integrity of the voting process and the privacy of each member's vote. Finally, NCUA is amending the conversion rule to require a federally-insured State credit union to provide NCUA with information about how the law of the State under which it is chartered relates to NCUA's conversion rule so that NCUA's review of the methods and procedures of the vote includes ensuring compliance with applicable State law.

C. Disclosures

A converting credit union can provide information to its members regarding any aspect of the conversion in any format it wishes, provided all communications are accurate and not misleading. NCUA only requires certain, minimal information be provided in the notice to members. Most converting credit unions choose to provide a great deal more information and, while NCUA recognizes this is a way to educate members, NCUA is concerned that members may be overwhelmed by the great volume of information. NCUA does not, however, wish to dissuade converting credit unions from communicating with their members or limit those communications.

To balance these competing interests, NCUA will continue to allow a converting credit union to communicate with its members as it sees fit, but will require that members receive a short, simple disclosure prepared by NCUA. This disclosure addresses: (1)

Ownership and control of the credit union; (2) operating expenses and their effect on rates and services; (3) the effect of a subsequent conversion to a stock institution; and (4) the costs of conversion. NCUA believes members need to be particularly aware of these topics. NCUA recognizes these topics might be discussed elsewhere in a credit union's communications with its members, but NCUA is concerned that this information may get buried in the great volume of information being provided. Accordingly, a converting credit union must include this disclosure in a prominent place with each written communication it sends to its members regarding the conversion and must take specific steps to ensure that the disclosure is conspicuous to the member. To promote flexibility, a converting credit union may modify the disclosure with the prior consent of the Regional Director and, in the case of a State credit union, the appropriate State supervisory authority (SSA).

Officials of many converting credit unions indicate in their conversion materials that they are unable to raise capital quickly enough to operate their credit unions as they see fit, which often includes a desire to pursue rapid growth. These credit unions encourage their members to support the conversion to an MSB as a way to overcome this capital restraint. They do not, however, inform their members that the conversion process can be expensive and further deplete a credit union's capital. NCUA believes members deserve to know how much of their money will be spent on the conversion effort. Accordingly, NCUA is amending the conversion rule to require converting credit unions to disclose the costs of conversion as part of the above disclosure requirements. An accurate cost estimate must take into account conversion related expenses including printing fees, postage fees, advertising, consulting and professional fees, legal fees, staff time, the cost of holding a special meeting, conducting the vote, and other related expenses.

D. Guidelines for Conducting a Member Vote

A converting credit union must conduct its member vote on conversion in a fair and legal manner. A vote that does not satisfy this standard denies members their democratic right to decide the fate of their credit union and could result in a charter change without the true support of the members. The final rule includes guidelines to avoid these kinds of undesirable results. The guidelines address topics such as: (1) Understanding the relationship between Federal and State law; (2) determining voter eligibility; (3) holding a special meeting.

NCUA does not purport these guidelines are an exhaustive checklist that guarantees a fair and legal vote. Rather, the guidelines are suggestions that provide a framework that, if followed, will help a credit union fulfill its regulatory obligations. A converting credit union should use these guidelines in conjunction with its own independent analysis and planning to tailor the member vote to its particular circumstances.

E. Relationship Between State and Federal Law

Although NCUA's conversion rule applies to all conversions of federally-insured credit unions, federally-insured state credit unions may also be subject to State law on conversions. As stated in previous rulemakings, NCUA's position is that a State legislature or SSA may impose conversion requirements more stringent or restrictive than NCUA's. This position is included in the final rule. In fact, NCUA understands over half the States do not specifically permit conversions of credit unions to MSBs. Reflecting NCUA's support of the dual chartering system, NCUA will defer to a State regulator when appropriate on questions involving interpretation of State law.

When State law applies to a conversion, it can change the procedural and substantive requirements a converting credit union must satisfy. NCUA needs to understand how State law affects those requirements to fulfill its responsibility to review the methods and procedures of the member vote. Accordingly, NCUA requires a federally-insured state credit union to notify NCUA if the State law under which it is chartered permits it to convert to an MSB. The credit union also must inform NCUA if it relies for its authority to convert on a State law parity provision, a provision permitting a state credit union to operate with the same or similar authority as a federal credit union (FCU), and if its State regulatory authority agrees that it may rely on the parity provision for that purpose. Finally, if a federally-insured state credit union relies on a state parity provision for authority to convert, it is required to indicate its State regulatory authority's position as to whether Federal law or State law will control internal governance issues in the conversion such as the requisite membership vote for conversion and the determination of a member's eligibility to vote.

F. Secret Ballots and Third Party Tellers

NCUA understands that members, including those that are employees of the credit union, may be uncomfortable with a voting process that does not protect the privacy of their votes. NCUA is concerned this may lead some members to choose not to vote or to vote in a manner inconsistent with their true wishes. Accordingly, the final rule protects members' privacy by requiring a converting credit union to use a secret ballot and an independent entity to conduct the vote. NCUA requires that a converting credit union use a third party teller to conduct the vote meaning that a third party teller will be responsible for sending ballots, receiving and safe keeping ballots, verifying ballots, and tabulating the vote. Use of a third party teller enhances the integrity of the voting process and provides confidence that members, including employees, will have their votes remain confidential.

G. Written Materials

Since CUMAA, the conversion rule has required a converting credit union to provide NCUA with copies of all written materials it sends or intends to send to its members in connection with the conversion proposal. NCUA is not changing that requirement but is clarifying that it applies to all written materials, including electronic communications posted on Web sites.

H. Summary of Comments

NCUA received 42 comments regarding the proposed rule. Thirty commenters supported the proposal. One so strongly that it stated it was ''criminal'' for credit unions to convert and strip out of the credit union the reserves accumulated over time by many members and put them ''into the pockets of a very few individuals.'' All of the nine commenters who are members of a credit union whose recent conversion campaign failed supported the proposal and many of them indicated that, if the terms of the proposal were in place when their credit union was considering converting, they would have been better informed or the process would have been fairer to members.

Many of the proposal's supporters offered suggestions to improve the rule. For example, ten commenters offered various suggestions to revise the proposed disclosures. Six commenters suggested there should be more required disclosures beyond those proposed.

One of those commenters suggested that paid consultants and service

providers be identified to the members and be required to disclose if they have opened an account at the credit union as a result of their involvement in the conversion. One of the conversion consultants stated that, if the costs of the conversion are to be disclosed, then the credit union should identify the name of the recipients of expenditures. NCUA believes the portion of the proposal that requires a converting credit union to disclose an itemized estimate of the costs of the conversion to its members helps to provide members with necessary information to understand and cast an informed vote on the conversion. NCUA also believes the suggestion that NCUA require a converting credit union to identify by name the recipients of expenditures as part of a detailed itemization of costs is worthy of further consideration. That requirement, however, as well as disclosure of the accountholder status of paid consultants and service providers, are beyond the scope of the proposal and are not adopted in this final rule.

One commenter suggested NCUA provide more voting guidelines than proposed. Another asked NCUA to clarify ''the extent to which the guidelines would be enforced.'' NCUA reiterates the voting guidelines are not regulatory requirements subject to enforcement. Rather, they are suggestions intended to help converting credit unions fulfill their regulatory obligation of conducting its member vote in a fair and legal manner.

Nine commenters stated that the proposed disclosure, which states ''Credit union directors and committee members serve on a volunteer basis,'' is not completely accurate because a number of States allow credit unions to compensate their board members while others are silent on the issue. NCUA is amending the disclosure to reflect these comments.

Seven commenters stated a converting credit union should not be legally required to use Robert's Rules of Order to conduct its special meeting on conversion or suggested there be flexibility to use other parliamentary procedures. One of these commenters also suggested NCUA require a converting credit union to hire an independent parliamentarian to run the meeting. Another commenter did not mention Robert's Rules of Order, but recommended the use of a certified parliamentarian. NCUA discusses the use of Robert's Rules of Order in the voting guidelines section of the proposal. As noted above, the guidelines are not regulatory requirements, and, therefore, a converting credit union is not legally required to follow them including using Robert's Rules of Order in conducting its special meeting relating to the member vote. NCUA recommends, however, that a converting credit union use appropriate parliamentary procedures to conduct its vote, and should enlist the services of an individual knowledgeable and skilled in those procedures. NCUA is revising the voting guidelines to clarify that Robert's Rules of Order are not the only parliamentary procedures a credit union should consider using for its member vote.

Twelve commenters, including the conversion consultants, banking trade organizations, and a bank that was formerly an FCU that had converted to an MSB and subsequently converted to a stock bank, opposed the proposal in general, stating it is inconsistent with CUMAA or obstructs credit unions' right to convert. NCUA fully supports a credit union's right to convert its charter but notes this right belongs to the members of the credit union. Members can only exercise that right in a meaningful way if their credit union provides them with information that is accurate and not misleading. NCUA is aware of the limitations CUMAA places on its authority to approve a conversion but is mindful of its responsibility to oversee the methods and procedures applicable to the member vote on conversion and protect the interests of credit union members.

Some of the commenters who opposed the proposal:

<bullet≤ Believe the disclosure regarding voting rights is inaccurate because an MSB could choose a ''one vote per member'' policy instead of allotting votes based on account balances,

<bullet≤ Highlighted that an MSB to stock conversion requires a number of steps scrutinized by other regulators and stated the disclosure regarding subsequent conversion to a stock institution is misleading and intended to discourage credit union members from voting for the conversion to an MSB,

<bullet≤ Believe NCUA acknowledges the proposal is intended to discourage conversions because NCUA reduced the estimated number of conversions per year in a Paperwork Reduction Act (PRA) filing associated with the proposed rulemaking, and

<bullet≤ Suggested the proposed requirement on state credit unions to provide NCUA with information about State laws affecting the conversion is burdensome or indicated NCUA does not have confidence in SSAs to perform their functions.

The fact that MSBs could choose a ''one vote per member'' policy instead of allotting votes based on account balances is not what MSBs, in fact, usually choose to do. The disclosure regarding voting rights states that, in an MSB, account holders with larger balances ''usually'' have more votes and, thus, greater control. NCUA believes this is an accurate statement. Also, NCUA recognizes that additional steps and member votes are required to approve an MSB to stock institution conversion. This does not lessen NCUA's concern about protecting credit union members' interest in their credit union. Those additional steps and member votes, although possibly scrutinized by other regulators, occur only after the credit union has converted to an MSB and is on its way to converting to the stock form of ownership. Obviously, at that point, the credit union does not exist and the additional requirements can do nothing to enable a credit union member to make an informed decision on the initial conversion from a credit union to an MSB.

The disclosure regarding subsequent conversion to a stock institution is not misleading and not intended to discourage credit union members from voting for the conversion to an MSB. It states that, in a typical conversion to the stock form of ownership, the executives of the institution profit by obtaining stock far in excess of that available to the institution's members. This accurately reflects an executive's ability to obtain stock options, restricted stock or other forms of stock related compensation not available to members not employed by the credit union.

In the normal course of the rulemaking process, NCUA submitted a required PRA filing. In that filing, NCUA reduced the estimated number of conversions per year from a previous submission based on its experience with conversions over the past several years. NCUA would have made the same reduction in the PRA filing based on historical data even if this rule were not being considered.

The requirement on state credit unions to provide NCUA with information about State laws affecting the conversion is not burdensome and does not indicate any lack of confidence in SSAs to perform their functions. NCUA fully acknowledges that a State legislature or SSA may impose conversion requirements more stringent or restrictive than NCUA's. As noted above, when State law applies to a conversion, it can change drastically the procedural and substantive requirements a converting credit union

must satisfy. It is essential for a converting credit union to understand both Federal and State requirements for compliance purposes and for NCUA to do the same to fulfill its responsibility to review the methods and procedures of the member vote as affected by State law. NCUA does not believe it is burdensome for a converting credit union to inform NCUA of State law that the credit union must obtain in any event to assure compliance with all applicable laws. NCUA works closely and cooperatively with SSAs in processing conversions and defers to SSAs in making determinations regarding State law. NCUA believes the subject requirement helps to promote cooperation among the regulators and a more informed converting credit union.

Three commenters disagreed with NCUA's statement that no conversion vote can be fair and legal if some members are improperly excluded. These commenters stated there is no statutory requirement for perfection and that a certain percentage of member exclusions should be tolerated if not the result of wrongful intent on the part of the converting credit union. Since CUMAA, NCUA has disapproved a converting credit union's methods and procedures applicable to the member vote on only one occasion. In that situation, voter disenfranchisement was widespread. NCUA will continue to take a pragmatic approach in reviewing member votes on conversion.

One commenter suggested a converting credit union should be required to prepare a comprehensive three-year business plan for the converted institution similar to the plan required by 12 CFR part 563b for MSBs proposing to convert to stock form. This commenter also stated the plan should be required to be sent to the credit union's members with the notice of intent to convert or the notice should explain how a member can obtain a free copy of the plan. This suggestion is beyond the scope of the proposal, but NCUA will consider it for future inclusion in the conversion rule.

Finally, commenters to previous amendments to the conversion rule have recommended NCUA require converting credit unions to provide members a meaningful way to share their opinions on the conversion and to disclose the views and concerns of the credit union's directors and officers who oppose the conversion. Four commenters to this rulemaking suggested there should be some mechanism in place for members to share their opinions on the conversion with each other and the credit union during the process. NCUA will continue to consider if this is practical and valuable and if it could be accomplished with minimal regulatory burden.

I. Effective Date of Final Rule

Generally, a final rule promulgated by NCUA is effective 30 days following its publication in the **Federal Register**. This final rule, however, is effective immediately upon publication because there is a strong public interest in having this consumer protection rule in place. First, this is necessary to ensure crucial disclosure information is provided to credit union members whose credit union has initiated or is about to initiate the conversion process, so the members may cast an informed and educated vote on the future existence of their credit union and their stake in it. Second, this will provide regulatory certainty to credit unions that are considering converting or beginning the conversion process within the next thirty days and enable them to better understand the regulatory requirements they must follow throughout the entirety of the process.

A converting credit union is required by statute and regulation to provide notice of its intent to convert to its members 90 days, 60 days, and 30 days before the member vote on conversion. 12 U.S.C. 205(b)(2)(C); 12 CFR 708a.4(b). It would be confusing for a converting credit union and its members if this rule became effective during that 90-day period as that would alter the regulatory requirements of the conversion in mid-process. That confusion about which regulatory requirements must be followed at a given point in the conversion process is eliminated for any recently initiated, soon to be initiated, and future conversions by making this rule immediately effective. Accordingly, for good cause, NCUA finds that, pursuant to 5 U.S.C. 553(d)(3), it would be impracticable and contrary to the public interest to delay the effective date of this rule for 30 days following publication. Therefore, this rule is effective immediately upon publication.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a rule may have on a substantial number of small credit unions, defined as those under ten million dollars in assets. This final rule amends the procedures an insured credit union must follow to convert to an MSB. Slightly over twenty credit unions have converted since 1995. NCUA anticipates no more than five credit unions per year will convert in the future and it is unlikely that any will have less than ten million dollars in assets. Accordingly, the amendments would not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

Part 708a contains information collection requirements. As required by the PRA, 44 U.S.C. 3507(d), NCUA previously submitted a copy of this regulation in proposed form as part of an information collection package to the Office of Management and Budget (OMB) for its review and approval of a revision to Collection of Information, Conversion of Insured Credit Unions to Mutual Savings Banks, Control Number 3133–0153.

NCUA estimated the average annual burden per converting credit union to be between 20 and 23 hours and that no more than five credit unions will convert per year. As a result, NCUA estimated the total annual collection burden to be no more than 115 hours. NCUA did not receive any comments addressing the accuracy or methodology for computing the burden. OMB approved the revision.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on State and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the States, on the connection between the National Government and the States, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Public Law 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 708a

Charter conversions, Credit unions.

By the National Credit Union Administration Board on January 13, 2005.

Mary F. Rupp,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 708b

Mergers of Federally-Insured Credit Unions; Voluntary Termination or Conversion of Insured Status

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The National Credit Union Administration (NCUA) is issuing final revisions to its rule on credit union mergers, federal share insurance terminations, and conversions from federal share insurance to nonfederal insurance. The final rule establishes disclosure requirements to ensure that members have the opportunity to be fully and properly informed before they vote on whether to convert from federal insurance to nonfederal insurance. The rule provides protections to members who may lose federal insurance because they have large insured accounts at two federally-insured credit unions that are merging or they have term accounts at a federally-insured credit union that is converting to nonfederal insurance. The rule also requires merging credit unions to analyze the premerger requirements imposed on credit unions by the Hart-Scott-Rodino Act and provides other miscellaneous updates to the existing rule governing credit union mergers, terminations, and conversions of share insurance.

DATES: This rule is effective February 23, 2005.

FOR FURTHER INFORMATION CONTACT: Paul Peterson, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

A. Background

The Federal Credit Union Act (Act) authorizes the NCUA Board to prescribe rules regarding mergers of federally-insured credit unions and changes in insured status and requires written approval of the Board before one or more federally-insured credit unions merge or before a federally-insured credit union terminates federal insurance or converts to nonfederal insurance. 12 U.S.C. 1752(7), 1766(a), 1785(b), 1785(c), and 1789(a). Part 708b of NCUA's rules addresses the merger of federally-insured credit unions and the voluntary termination or conversion of federally-insured status. 12 CFR part 708b.

The Board has a policy of continually reviewing NCUA regulations to ''update, clarify and simplify existing regulations and eliminate redundant and unnecessary provisions.'' NCUA Interpretive Ruling and Policy Statement (IRPS) 87–2, Developing and Reviewing Government Regulations. As a result of the NCUA's 2003 review, the Board determined that part 708b should be updated and modernized. In July 2004, the Board published its proposed amendments for a 60-day public comment. 69 FR 45279 (July 29, 2004).

NCUA received 88 comment letters on the proposed rule. The comments came from a variety of sources, including state supervisory authorities (SSAs), credit unions (federal and state chartered; federally and privately insured), credit union trade organizations, credit union consultants, a law firm, a private share insurer, and members of Congress. Almost all the commenters commented on the share insurance conversion portion of the proposal. A few of the commenters also commented on the merger portion of the proposal.

The majority of the commenters objected to various portions of the proposed share insurance conversion rule. About ninety percent of the credit unions submitting comments objected to various portions of it. Most of the commenting credit union leagues and trade organizations also object to the rule, while two support it. Six members of Congress wrote in general objection to the rule, while two wrote in general support of the rule. Three SSAs wrote in general objection to the rule, while one wrote in support. A private share insurer, American Mutual Share Insurance Corporation (ASI), objects to the rule.

B. General Comments About the Proposed Rulemaking

Several commenters supported the proposed amendments to the share insurance conversion part of the rule, particularly the changes in disclosures and increased NCUA oversight of share insurance communications. These commenters generally thought the proposal would result in credit union members receiving more accurate information when voting on conversions.

Many commenters complained about the proposed rulemaking as it relates to share insurance conversion. Some of the general themes of the commenters who object to the rule are that: NCUA does not have the legal authority to approve or disapprove conversions to private insurance; NCUA is in a conflict of interest situation and is improperly regulating the private share insurer; NCUA is undermining the dual chartering system because it is regulating in an area that is the province of state regulators; NCUA is confusing its role as insurer and regulator and this rulemaking is proof that the functions should be separated; and NCUA has not provided sufficient information about problems with the current conversion process. These commenters believe no rulemaking is necessary.

The NCUA Board disagrees with many of these comments about the proposed share insurance conversion rulemaking. First, the Act charges the NCUA Board with approving or disapproving conversions of federally-insured credit unions to ''noninsured credit unions,'' and the Act defines a noninsured credit union as any credit union that does not have federal insurance, to include uninsured and privately insured credit unions. 12 U.S.C. 1752(7), 1785(b)(1)(D). Second, this proposed regulation does not regulate private insurance or private insurers. The Act charges NCUA with ensuring that the needs of credit union members are met during share insurance conversions and terminations. 12 U.S.C. 1785(c). This rulemaking is about ensuring that members have accurate information. Third, the rule acknowledges the participation of the SSAs in the conversion process. Since federal law assigns an approval function to NCUA, however, the regulation of conversions is not the sole province of state regulators. Accordingly, the proposed rulemaking does not undermine the dual chartering system. Fourth, federal law places both safety and soundness and consumer protection responsibilities on NCUA. The Board believes these responsibilities are not in conflict and this rulemaking does not evidence a need to separate NCUA's ''insurer'' and ''regulator'' functions.

The Board appreciates the requests of some commenters for more information about the need for this rulemaking, particularly the need for increased disclosures and oversight of communications to members during the share insurance conversion process. Additional information on that aspect appears in Section C of the **SUPPLEMENTARY INFORMATION**. Some commenters had concerns with particular provisions in the proposed rule and the final rule contains several changes in response to these comments. Comments on particular provisions and the associated changes are discussed in Sections D and E of the Supplementary Information.

C. The Need for This Rulemaking

Many commenters said they did not understand why NCUA was proposing to change the disclosures to members of

credit unions converting to private insurance and to expand the scope of communications subject to NCUA review. As the Board indicated in the Supplementary Information to the proposed rule:

The Board is concerned about communications that credit unions may make that are intended to influence the member vote. While a credit union seeking to convert or terminate may make its case for conversion or termination to its members, it may not do so by misleading, inaccurate, or deceptive representations. For example, the Board believes that any discussion of NCUA insurance, or any comparison of nonfederal insurance to NCUA insurance, is inaccurate and deceptive if it fails to mention the most important aspect of NCUA insurance: by law, it is backed by the full faith and credit of the United States government. Competitive Equality Banking Act of 1987, Pub. L. No. 100–86, Section 901, 101 Stat. 657 (1987); *Massachusetts Credit Union Share Insurance Corporation* v. *National Credit Union Administration,* 693 F.Supp. 1225, 1230–31 (D.C.D.C. 1988) (''The Court concludes that it was the clear and unambiguous intention of the Congress to guarantee the resources of * * * depository institutions with the full faith and credit of the United States.''). The Board is also concerned about representations that state or imply that it is difficult or impossible to structure accounts at a federally-insured institution to obtain more than $100,000 of share insurance coverage as these representations are also inaccurate and deceptive.

69 FR 45279, 45280–81 (July 29, 2004). The Board's concerns about inaccurate and misleading share insurance communications are not hypothetical but based on actual communications made by credit unions. Some examples follow.

Example 1: Misleading comparison about the relative financial safety of private insurance and NCUSIF insurance.

In comparing the safety of private insurance to the NCUA Share Insurance Fund (NCUSIF), a credit union stated in a 2004 communication to members:

Financial safety of a share insurance program is measured in terms of equity available to pay a claim. ASI's equity is the strongest of all national insurers. For example, the Federal Deposit Insurance Corporation (FDIC) touts having $1.30 for each $1.00 it insures. The National Credit Union Share Insurance Fund has $1.27 as of year end 2001. ASI's stands at $1.33 * * * the highest of all.

This statement inaccurately indicates the equity ratio of the insurance funds is the main determinant of the relative safety and strength of the private and federal funds. While fund equity is important to a private insurer, which may have no real alternative source of funding to pay claims, the comparison to the NCUSIF fails to take into consideration factors such as the relative size of the funds, the relative risk diversification, available lines of credit, and, most importantly, the fact that the NCUSIF is backed by the full faith and credit of the United States government. To avoid misleading credit union members, any comparison of the safety, strength, or relative claims paying ability of the NCUA and a private fund must state that accounts insured by NCUA are guaranteed by the United States government and accounts insured by the private fund are not guaranteed by the federal government or by any state or local government. This fact was not mentioned anywhere in the credit union's communication promoting conversion. NCUA's view is that comment about the relative strength of private insurance funds with the NCUSIF is *per se* misleading if it fails to mention that the NCUSIF is backed by the full faith and credit of the United States Government.

Example 2: Misleading statement that a credit union's assets are safer with private insurance.

A credit union made the following statement to its members in a 2004 newsletter article explaining why its members were better off with private insurance than NCUSIF insurance:

If the worst happened, [name of credit union]'s assets are safer with ASI deposit insurance. In the unlikely event that several credit unions failed at once, [the credit union] could potentially face greater financial risk with federally backed deposit insurance than with ASI private deposit insurance. With federal insurance, all of [the credit union]'s reserves (currently $58 million) could be used to bail out other credit unions. With ASI private deposit insurance, only 3% of [the credit union]'s total assets (currently $19.96 million) could be used.

(Emphasis in original). This statement is inaccurate and misleading for the following reasons.

First, the credit union's statement that ''[w]ith ASI private deposit insurance, only 3% of [name of credit union]'s total assets (currently $19.96 million) could be used'' is wrong. In reality, the credit union's potential liability is unlimited. ASI's Standard Primary Share Insurance Contract (SPSIC) says that ASI requires an insured credit union to make capital contributions sufficient to maintain the normal operating level of its Guarantee Fund. The SPSIC also says that insured credit unions do not have to make contributions or assessments that exceed 3% of their total assets ''unless otherwise ordered by the Superintendent of the Division of Financial Institutions in the Insurer's state of domicile.'' Further, ASI is domiciled in Ohio and Ohio law states that whenever the Ohio SSA or superintendent of insurance considers it necessary for the maintenance of ASI's normal operating level—a minimum of one percent—the superintendent ''shall order'' ASI to levy and collect additions to the capital contributions. Ohio Rev. Code Ann. § § 1761.10(A)(1), § 1761.10(B)(1) (2004). So, contrary to the statement in the credit union's newsletter, if ASI suffered significant financial losses, there is no 3% limit on the credit union's assets subject to additional levies.

The history of depository institutions that lack federal insurance provides another reason why a credit union's assets are not safer with private share insurance. In the event of numerous failures of privately insured credit unions, the depositors at other privately insured institutions, even healthy ones, may lose confidence in their institutions as they hear and read about the failures. This loss of confidence increases the withdrawal rate at all privately-insured institutions, regardless of financial health. The run on these institutions may cause a liquidity crisis and forces them to sell assets. Illiquid assets then must be sold, often at less than fair market value, causing significant losses to these institutions and perhaps even insolvency. By comparison, the threat of heavy withdrawals is not significant for an NCUSIF-insured institution, because the backing of the full faith and credit of the United States maintains the confidence of the depositors in the safety of their funds and limits the potential for disastrous runs.

This potential for a run on privately-insured institutions is not just theoretical. In 1985, and again in 1991, private deposit and share insurers in Ohio, Maryland, and Rhode Island collapsed. One Ohio Congressman said the following about the 1985 collapse:

The experience in Ohio and Maryland demonstrated that once an institution suffers heavy losses a chain reaction can begin in which doubt among consumers about the ability of the [private] insurance fund to cover the losses can quickly erode the public's confidence in the safety of their money at other similarly insured institutions and soon a panic begins * * *. If all the depository institutions in Ohio and Maryland had

been federally insured, the outcome would have been different and consumers would not have gone through the trauma of thinking they were wiped out * * *.

131 Cong. Rec. E3979 (daily ed. Sept. 11, 1985) (Statement of Rep. Oakar). Also, a report on the Rhode Island collapse stated that:

Public confidence is one of the most important assets of a deposit insurer. When the situation at Heritage [a depository institution in financial trouble that was insured by the Rhode Island Share and Deposit Indemnity Corporation (RISDIC), a private share insurer] came to light, the public undoubtedly became more skeptical of RISDIC and its constituent members. Withdrawals from some of the larger institutions further weakened their reserves. Recognizing the potential effects of a RISDIC collapse, state officials encouraged RISDIC institutions to apply for federal insurance in order to protect their depositors.

Vartan Gregorian, *Carved in Sand,* A Report on the Collapse of the Rhode Island Share and Deposit Indemnity Corporation (Brown University, 1991), p. 105.

Example 3: Misleading statement about maximizing federal share insurance coverage.

In comparing the amount of coverage available from NCUA and ASI, a credit union made the following statement in a 2004 communication to its members:

As an ASI-insured member, coverage on your deposit accounts would increase from $100,000 per member, as currently insured by the National Credit Union Share Insurance Fund (NCUSIF), to $250,000 per account under ASI. Instead of members struggling to structure their savings with us to maximize their deposit insurance coverage, as under Federal insurance, members will be able to have multiple deposit relationships with [name of credit union], knowing that each account is separately insured up to $250,000!

Credit union members do not have to struggle to structure their savings to achieve more than $100,000 of share insurance coverage at a federally-insured credit union. Many account forms can be created easily to increase insurance coverage, including payable-on-death accounts, joint accounts, and IRA accounts.

Example 4: Statements Made By the Private Insurer.

Credit unions work closely with ASI, the lone provider of private, primary share insurance in the United States, when converting insurance and ASI mistakenly questions the federal guarantee that backs the NCUSIF. ASI's comment letter to NCUA in this rulemaking states:

ASI objects to the requirement that the Notice state: 'THIS FEDERAL INSURANCE IS BACKED BY THE FULL FAITH AND CREDIT OF THE UNITED STATES GOVERNMENT.' There is no statutory guarantee for the Fund * * *. The only reference to extending the 'full faith and credit' to credit union share insurance is set forth in the 100th Congress' 'findings,' which are not law or in any way binding beyond the 100th Congress.

The Competitive Equality Banking Act of 1987 (CEBA), referred to in ASI's mention of the 100th Congress above, states that it ''is the sense of Congress that it should reaffirm that deposits up to the statutorily prescribed amount in federally insured depository institutions are backed by the full faith and credit of the United States.'' Pub. L. No. 100–86 (1987), § 901. As stated previously, and contrary to ASI's assertion in its comment letter, a federal court found that this statement is binding. *Massachusetts Share Insurance Corporation* v. *National Credit Union Administration,* 693 F.Supp. 1225, 1231 (D.C.D.C. 1988) (''The Court concludes that it was the clear and unambiguous intention of the Congress to guarantee the resources of federal depository institutions with the full faith and credit of the United States.'').

As indicated by Congress' use of the word ''reaffirmation'' in the CEBA, NCUA's insurance program had the backing of the full faith and credit of the United States government even before that 1987 law. The U.S. Department of Justice (DOJ) has stated that ''a guaranty by a Government agency contracted pursuant to a congressional grant of authority for constitutional purposes is an obligation fully binding on the United States despite the absence of statutory language expressly pledging its 'faith' or 'credit' to the redemption of the guaranty and despite the possibility that a future appropriation might be necessary to carry out such redemption.'' *Debt Obligations of the National Credit Union Administration,* 6 Op. Off. Legal Counsel 262, 264 (1982). The chief legal officer of the Legislative Branch has similarly stated that the ''[s]tatutory language expressly pledging the credit of the United States is not required to create obligations of the United States * * *. Rather, when Congress authorizes a federal agency or officer to incur obligations, those obligations are supported by the full faith and credit of the United States, unless the authorizing statute specifically provides otherwise.'' Comptroller General of the United States, B–277814 (October 20, 1997). NCUA is a federal agency; it has a statutory obligation to pay share insurance claims; and, as a matter of law, NCUA's share insurance obligation is backed by the full faith and credit of the United States government.

After reviewing both the communications made by converting credit unions and the views stated by the private insurer about federal insurance, the Board believes it has ample reason to engage in this rulemaking to inform both credit unions and their members.

Sections D and E below discuss the specific amendments proposed by the Board, the comments received on those amendments, and the treatment of those proposed amendments in the final rule.

D. Proposed Amendments—Mergers

1. Amendment Related to the Hart-Scott-Rodino Act

The Hart-Scott-Rodino Act (HSR Act), 15 U.S.C. 18a, requires that parties to certain mergers or acquisitions, including credit unions, notify the Federal Trade Commission (FTC) before consummating the merger or acquisition. Only mergers involving relatively large credit unions require HSR filings because merging entities below a certain asset size are exempt. Generally, credit unions need not file if (1) the merging credit union has less than $50 million in assets or (2) the merging credit union has from $50 million up to $200 million in assets and the continuing credit union is below a certain asset size established by the FTC. The amendment requires a merging credit union that has more than $50 million in assets as reported on its last call report to inform NCUA in its merger proposal if the credit union plans to make an HSR filing and, if not, why not.

One commenter supported the amendment, stating it would provide merging credit unions with an additional safeguard to ensure they comply with HSR. One commenter thought demonstration of HSR compliance was an unnecessary burden. This commenter stated that Congress is considering eliminating this requirement and, if it does, the agency would then have to eliminate the regulation. Another commenter questioned the practical application of the HSR filing requirements to credit union mergers or acquisitions since such mergers lack ''significant anticompetitive effect on the marketplace.''

The final rule retains the requirement that merging credit unions with $50 million or more in assets inform NCUA of whether or not they plan to make an HSR filing. Merging credit unions must comply with the HSR Act, and unless and until the law changes, NCUA wants to make sure credit unions are aware of and comply with their HSR responsibilities.

2. Amendment Requiring Notice to Members of Potential Loss of Insurance in a Merger

The Board proposed an amendment to require notice to members regarding the potential reduction of account insurance coverage resulting from the merger of two federally-insured credit unions. Two credit unions that are proposing to merge may have overlapping fields of membership, and there may be individuals who belong to both credit unions. If these individuals have the same types of accounts at both credit unions in an aggregate amount exceeding $100,000, they run the risk of losing some insurance coverage on their accounts as a result of the merger. To ensure these members are aware of the possible loss of coverage, the amendment requires the continuing credit union either: (1) Notify all members of the continuing credit union of the potential loss of insurance coverage from overlapping fields of membership; (2) notify all individuals who are members of both credit unions of the potential loss of insurance coverage; or (3) determine which members of both credit unions may actually have uninsured funds six months after the merger and notify those members of the potential loss of insurance coverage.

One commenter supported the proposed notification requirements because of the possible loss of share insurance due to merger and the flexibility given to credit unions in the various ways they could carry out the notification. Another commenter opposed the proposed rule, stating that the notice could have the unintended consequence of creating anxiety and uncertainty with regard to the condition of the credit unions involved and the perception that members' deposits are unsafe.

The final rule retains this provision as proposed. The Board believes merging credit unions can craft the notice to the members in a way that mitigates any possible anxiety or uncertainty about the health of the merging credit unions.

3. Amendment Requiring Merging Credit Unions to Analyze Net Worth Before and After Merger

The amendment requires merging credit unions to analyze the net worth of the two credit unions before merger, as calculated under generally accepted accounting principles (GAAP), and compare those figures with the estimated net worth of the continuing credit union after merger. The one commenter who addressed this proposal supports it because the board of directors and management of the two credit unions must consider this information before recommending a merger. The final rule retains this provision as proposed.

E. Proposed Amendments—Credit Union Share Insurance Conversions and Terminations

1. Amendment Requiring Modified and Additional Share Insurance Disclosures

Section 151 of the Federal Deposit Corporation Improvement Act of 1991 (FDICIA) added Section 43 to the Federal Deposit Insurance Act (FDIA). Pub. L. 102–242 (1991), Section 151(a); Pub. L. No. 102–550 (1992), Section 1603(b)(2); and 12 U.S.C. 1831t(b). Section 43 of the FDIA requires, among other things, that depository institutions, including credit unions, that do not have federal account insurance make conspicuous disclosure of that fact and its potential ramifications to their current and potential account holders in various media. For example, nonfederally-insured institutions must make conspicuous disclosures that ''the institution is not federally-insured, and that if the institution fails, the Federal Government does not guarantee that depositors will get back their money.'' 12 U.S.C. 1831t(b)(1).

In a recent report, the U.S. General Accounting Office (GAO) found that ''many privately insured credit unions have not always complied with the disclosure requirements in Section 43 that are designed to notify consumers that the deposits in these institutions are not federally-insured.'' ''Federal Deposit Insurance Act: FTC Best Among Candidates to Enforce Consumer Protection Provisions'', GAO–03–0971, p. 20 (August, 2003). As the title of the report suggests, GAO concluded that FTC is the most appropriate federal agency to enforce the provisions of Section 43 with respect to nonfederally-insured credit unions. NCUA has a responsibility, however, to ensure that members of a federally-insured credit union are fully informed in connection with a vote to terminate federal insurance or convert from federal to nonfederal insurance and believes it is important that management understands its disclosure requirements post-conversion. *See* 12 U.S.C. 1785(c)(5). The proposed amendments provided for revising the requirements in connection with the membership vote of credit unions seeking to terminate or convert from federal insurance, requiring the credit unions to acknowledge Section 43 and certify they will comply with its requirements following termination or conversion.

Federally-insured credit unions intending to terminate federal insurance or convert to nonfederal insurance must first obtain approval from their members, and part 708b currently requires credit unions to use certain language to disclose to members, as part of the notification of member vote, the effects of insurance termination or conversion. The current disclosure language required by part 708b is similar to that required by Section 43 following the loss of federal insurance. The proposal provided for modifying the part 708b disclosures to make them more consistent with the Section 43 disclosures and updating the form notices, ballots, and certifications in subpart C of part 708b.

The current rule does not contain any disclosure requirements for communications other than the disclosures contained in the form notice and ballot. The proposed rule provided for including the following disclosure language in a conspicuous fashion in all share insurance communications: ''IF YOU ARE A MEMBER OF THIS CREDIT UNION, YOUR ACCOUNTS ARE CURRENTLY INSURED BY THE NATIONAL CREDIT UNION ADMINISTRATION, A FEDERAL AGENCY. THIS INSURANCE IS BACKED BY THE FULL FAITH AND CREDIT OF THE UNITED STATES GOVERNMENT. IF THE CREDIT UNION (CONVERTS TO PRIVATE INSURANCE) (TERMINATES ITS FEDERAL INSURANCE), AND THE CREDIT UNION FAILS, THE FEDERAL GOVERNMENT DOES NOT GUARANTEE THAT YOU WILL GET YOUR MONEY BACK.''

This proposed disclosure language tracks the disclosures required of nonfederally-insured credit unions by Section 43(b) of the FDIA after conversion. 12 U.S.C. 1831t(b). The proposal required this language be included in all share insurance communications whether or not the communication requires prior NCUA approval and whether or not the credit union has made a formal decision to seek conversion or termination. The

proposed rule also tracked Section 43(b) by requiring that the disclosure language be conspicuous. To ensure that the disclosure catches the attention of the member, the proposal required the disclosure be on the first page of the communication where conversion is discussed, in capital letters, bolded, offset from the other text by use of a border, and at least one font size larger than any other text (exclusive of headings) used in the communication.

The final rule adopts the amendments as proposed, with some modifications in response to public comments received. A summary of the public comments and the Board's response follows.

Many credit unions submitted a virtually identical comment about the proposed disclosures. These commenters believe that, when Congress enacted FDICIA in 1991, ''it concluded'' that the disclosures only apply to privately insured credit unions. These commenters also contend Congress selected the FTC to regulate and enforce such consumer disclosures, not the NCUA, and believe that the proposed rule is ''contrary to the instructions'' of Congress.

The Board agrees that it is the FTC that has responsibility for enforcement of FDICIA and that FDICIA's provisions only apply to credit unions after they convert to private insurance. As NCUA is charged with the approval of conversions, its focus is on what occurs before the FTC assumes responsibility for enforcement of FDICIA. The NCUA Board believes it makes eminent sense for members to receive the same disclosures about the nature of private insurance before conversion, when considering whether to vote for or against conversion, that they will be entitled to receive afterward. Further, the Board believes credit unions may not be aware of their FDICIA responsibilities if they choose to convert given the fact that, as noted in the previously mentioned GAO report, many privately insured credit unions are not complying with FDICIA. The costs and effects of FDICIA compliance are also factors credit unions should consider in making the conversion decision. Accordingly, the final rule requires a converting credit union to inform NCUA that ''it is aware of the requirements of 12 U.S.C. 1831t(b)'' in lieu of the proposal that would have required the credit union to inform NCUA that ''it will fully comply with the requirements of 12 U.S.C. 1831t(b).''

Several commenters support the proposed amendments to the disclosure provisions. One of these commenters states it will help credit union members make well-informed decisions when voting on insurance conversion and termination issues. This commenter asks that NCUA also consider requiring converting credit unions to notify their members of a vote on share insurance conversion or termination a minimum number of times and that the notice be sent by at least two different means: for example, via a statement stuffer and a direct letter, along with some other general notification efforts, such as a newspaper article or a posting on the credit union's website. According to the commenter, this would help ensure that credit unions make a good faith effort to encourage members to vote on insurance issues and would help avoid the situation in which a handful of members decide for all. Another commenter that supports the proposed disclosures said NCUA should also require disclosure of certain information about the prospective private insurer, such as the shares insured and the amount of resources available to indemnify those shares. This commenter felt this information and an evaluation of the prospective insurer by an independent analyst could be useful for credit union members to make an informed decision.

Additional notification requirements are beyond the scope of the proposed rule, and the Board does not see a need at this time for additional notification requirements. The Act requires that at least 20% of the members vote, which mitigates the possibility that a handful of members will make the decision. While the Board believes a converting credit union should undertake to provide its members as much relevant and accurate information about the private insurer as possible, it believes the amount of information provided is a decision best left to credit union management. The Board is only requiring that the information provided to members beyond the required disclosures not be inaccurate or misleading.

A few commenters believe the capitalization of ''DO NOT approve'' on the proposed member ballot indicates an NCUA bias towards disapproval. This was not the Board's intent and the final rule removes the capitalization.

One commenter believes the proposed rule's requirement that the disclosure, when posted on the web, must be visible without scrolling is impossible to meet, given that a credit union does not have control over a viewer's monitor size or other computer access device, including hand-held devices. The Board appreciates this concern. The language of the final rule has been modified to require converting credit unions to make reasonable efforts to make the disclosure visible without scrolling. If most of the disclosure is visible on a standard-size computer screen without scrolling the Board will consider the placement of the disclosure as reasonable.

A few commenters believe that the current disclosures are already excessive because members are ''bombarded'' with this information before, during, and after conversion. The Board disagrees. The Board believes that, currently, in many conversions the first communications members receive about conversion do not contain the important information in the proposed disclosures, that the members do not focus on the fine print in the notice and ballot when they receive those documents, and that many members are not made aware of this information until after the vote and the conversion are complete.

ASI commented that the FDICIA-like disclosure ''in the context of a conversion vote would give the false impression that privately insured credit unions are more likely to fail than federally-insured credit unions.'' The Board does not agree that the FDICIA-like language gives this impression. Credit unions can fail, regardless of whether they are privately or federally-insured. What the FDICIA language states is that, if a privately insured credit union fails, the federal government does not guarantee that the member will get his or her money back.

One commenter described the proposed disclosures as ''draconian,'' and said that ''[I]f we were to truly disclose, then we would have to add that the reserves of the entire credit union industry would have to be depleted before the Federal Government would step in to make a depositor whole up to the limits of the insurance coverage.'' The Board disagrees. There is nothing in federal law that would require NCUA to deplete the reserves of the entire credit union industry. In the unlikely case of catastrophic losses to the NCUSIF, the Board would go to Congress for it to fulfill its full faith and credit pledge before depleting the reserves of healthy credit unions. This is exactly what the Federal Savings and Loan Insurance Corporation did during the savings and loan crisis.

Many credit unions submitted a virtually identical comment on the proposal to amend the current language in the form notice and ballot to state that ''[t]he basic federal coverage is up to $100,000, but accounts may be structured in different ways, such as joint accounts, payable-on-death accounts, or IRA accounts, to achieve federal coverage of much more than

$100,000.'' These commenters believe the proposed notice and ballot unfairly incorporates language about achieving greater federal insurance coverage but prohibits a credit union from giving its members any positive information about private share insurance or the private share insurer. According to these commenters, this will leave the members grossly uninformed. The Board disagrees with this comment. Nowhere in the proposed rule does it prohibit any communication that is not deceptive or misleading. Subject to this standard, a converting credit union is free to provide its members any information that it wants about the private insurer, the insurance coverage, and the reasons for conversion. There is even a place in the form notice for a credit union to do this.

One commenter was concerned that, while the proposed form notice gives the credit union board an opportunity to provide its reasons for the proposed conversion, there is no place on the ballot to state those reasons. The Board notes that usually the notice accompanies the ballot, so there is no reason to have the reasons for the proposed conversion stated on the ballot. If the converting credit union wishes to amend the ballot, it can seek approval of the regional director to include that language.

One commenter objects to the requirement that the notice list the costs of conducting the vote and associated attorney and consulting fees. This commenter states most of these costs occur before the vote, and cannot be avoided by voting against the conversion. Also, this commenter believes that much of the cost would be associated with complying with NCUA's rules and it would be unfair to associate this cost with private insurance. NCUA believes that members have a right to know about the costs associated with a conversion, whether they are incurred before, during, or after the vote. If the credit union wants to point out in an accurate manner that certain costs were incurred to comply with NCUA's conversion rules, it may do so.

2. Amendment Requiring NCUA To Review and Approve Certain Share Insurance Communications

The currently existing part 708b, that is, as it exists before this final rule takes effect, requires credit unions to use specific language in the notice to members of the pending change in insurance status and associated ballot. 12 CFR part 708b, subpart C. It also requires the approval of the regional director for any modifications to this language and any additional communications concerning insurance coverage included with the notice or ballot. 12 CFR 708b.303. The regional director may not withhold approval unless ''it is determined that the credit union, by inclusion or omission of information, would materially mislead or misinform its membership.'' Id. The proposed rule would have retained the prior approval requirement and the standard of review, but expanded the types of communications subject to prior approval to include all share insurance communications made during the voting period. The purpose of the expanded approval requirement was to ensure that members are accurately informed about the ramifications of the loss of federal insurance coverage and to avoid the types of inaccurate and misleading communications discussed in Section C of this Supplementary Information.

The Board also proposed to amend the current rule to clarify the concept of ''notice.'' Part 708b currently provides that, when the board of directors of a federally-insured credit union adopts a resolution proposing to convert from federal to nonfederal insurance, including an insurance conversion associated with a merger or conversion of charter, it must provide its members with written notice of the proposal to convert insurance and of the date set for the membership vote. To ensure that members are adequately informed about the nature of the insurance conversion, the proposal, like the current rule, prescribed specific forms for this notice. The proposed rule made clear that the first written communication following the resolution to convert, made by or on behalf of the credit union and informing the members that the credit union will seek conversion of insurance, is, in fact, the notice of the proposal to convert and must be in the prescribed form unless the regional director approves a different form.

The Board also proposed to add a cross-reference to § 740.2 of NCUA's advertising regulation, which prohibits the making of false or deceptive representations. 12 CFR 740.2. This cross-reference does not create any new requirement, but, rather, reminds credit unions of an important preexisting obligation.

Several commenters support the proposed prior approval requirements. One of these commenters, an SSA, believes the proposed rule is necessary to ensure that adequate disclosure is provided to members before a conversion vote. This commenter believes it is not clear that members are made fully aware of how such a vote may impact their shares. This SSA believes the proposed rule will provide for more standardization in disclosures and is necessary to ensure that adequate disclosure is provided to members before a conversion vote. Another commenter stated the proposed rule will help prevent deception of members and other evasive or misleading practices.

Many credit unions submitted a virtually identical comment on the preapproval requirements. These commenters complained that NCUA was prohibiting converting credit unions from providing their members with any information regarding share insurance before, during, or after the voting period, unless the communications have been pre-approved by NCUA. These commenters feel members will not fully understand the private share insurance option that they are being asked to vote on.

Several commenters are also concerned about how the preapproval process would work. Some of these commenters state there should be a procedure for resolving disputes between the credit union and NCUA over proposed communications. Some of these commenters also stated there should be parameters as to how long the NCUA may take in the review process. A few commenters thought there should be an appeal process, and one of these commenters stated the state regulators should have a role in the appeal process.

A law firm commenter states that both the current and the proposed share insurance conversion rules requiring prior approval of certain communications and mandating disclosures are violations of the right to free speech under the First Amendment to the U.S. Constitution.

A few commenters state that the proposed definition of a share insurance communication is overbroad. For example, two commenters contend that the prior approval requirement in the proposed rule would apply to internal communications at a credit union. One of these questioned if ''a credit union would violate the rules if it even distributed a private insurer's brochure to two board members for a consideration of placing the topic on the board's agenda.'' Another commenter supported NCUA's formal approval of changes to the notice and ballot, but thought that the proposed requirement to approve other share insurance communications would require NCUA approval of individual letters sent in response to member inquiries if any two or more of the letters had substantially the same information.

One commenter complained that requirement that the notice to members

of the pending conversion and member vote be mailed to the members not less than seven days, nor more than 30 days, before the vote, is too restrictive. This commenter believes the time period should be extended from a minimum of 7 days to a maximum of 120 days to allow sufficient time to obtain the necessary twenty percent quorum.

One commenter believes NCUA should not preapprove communications, but ''if a communication is later deemed incorrect in its facts, then the NCUA can take the appropriate action.''

The Board disagrees that the proposed prior approval requirement is a violation of the First Amendment of the U.S. Constitution. Share insurance communications are commercial speech. While the U.S. Supreme Court has recognized that some commercial speech may be protected under the First Amendment, it generally permits interference with commercial speech when the government's motive is to prevent false or misleading speech. *See Central Hudson Gas & Electric Corp.* v. *Public Service Commission of New York,* 447 U.S. 557, 566 (1980) (''At the outset, we must determine whether the expression is protected by the First Amendment. For commercial speech to come within that provision, it at least must concern lawful activity and not be misleading.''). Here, NCUA is specifically targeting inaccurate and misleading commercial speech.

Nevertheless, after careful consideration of the comments, the Board has decided to modify the preapproval requirement as stated in the proposed rule to a contemporary notice requirement, as suggested by the last commenter above. The final rule, as adopted, allows converting credit unions to make share insurance communications without receiving any prior approval. The converting credit unions need only provide NCUA a copy of the share insurance communication at or before the time it is made. The definition of share insurance communication specifically excludes the forms in subpart C and the final rule retains the requirement in the prior rule and as proposed that any modifications to the forms requires the approval of the regional director.

The Board is making this change for several reasons. First, the Board is sympathetic to the burden a preapproval requirement puts on a converting credit union, particularly those credit unions whose share insurance communications are straightforward. As noted in the comments above, the preapproval requirement injects uncertainty into the sequence and timing of the conversion. Also, if the credit union must make an unanticipated communication on short notice, a preapproval requirement could be particularly burdensome. Second, the Board hopes that the modified and additional disclosures will adequately inform credit union members about important aspects of the conversion and any additional communications about share insurance will not contain misleading information. For example, as one commenter pointed out, a converting credit union may send out short messages that merely exhort their members to vote on the share insurance proposal. The Board also realizes that some communications about why a credit union is converting may be expressions of opinion that do not contain anything false or misleading.

Accordingly, the Board is replacing the preapproval requirement with a simple notice requirement. A converting credit union must provide NCUA a copy of any share insurance communication the credit union will make during the voting period. The regional director must receive the copy at or before the time the credit union makes it available to members. The converting credit union must also inform the regional director when the communication is to be made, to which members it will be directed, and how it will be disseminated.

Although the final rule does not require prior NCUA approval for share insurance communications, the final rule clarifies that, if a converting credit union makes a materially misleading communication to its members, the regional director may take appropriate action, including disapproval of the conversion. Of course, the NCUA is willing to work with any credit union to achieve language that is not misleading. A converting credit union may, at its option, provide an advance copy of any proposed share insurance communication to the regional director for review and comment.

In response to comments about the definition of share insurance communications being overbroad, the Board did not intend for the definition to include internal credit union communications, and the definition of ''share insurance communication'' in the final rule is modified to exclude such communications. Also, if a credit union anticipates it will receive multiple member inquiries with the same or similar question about insurance conversion and anticipates a similar response to all inquiries, it should provide NCUA contemporaneous notice of its response.

In response to the commenter who requests more than thirty days to conduct the vote following the credit union's resolution to convert, the Board notes that this maximum time period is statutory and cannot be changed by regulation. 12 U.S.C. 1786(d)(2). The credit union may, before it resolves to convert, inform its members about the possibility of a resolution to convert and the attendant vote. Any such communication must contain the appropriate disclosures and not otherwise mislead the members.

3. Amendments Relating to the Timing and Sequence of the Conversion Approval Process

Currently, part 708b requires that NCUA must approve a merger before the members vote. By contrast, for insurance conversions, part 708b provides two options as to when a credit union must give notice: ''Notice to the Board may be given when membership approval is solicited, or after membership approval is obtained.'' *Compare 12* CFR 708b.106(a)(1) (mergers) *with* § 708b.203(c) (conversions). These different provisions may create confusion in mergers that also involve insurance conversions. NCUA proposed to eliminate this confusion by changing the notice requirement for insurance conversions to require a converting credit union to notify NCUA and request approval of the conversion before the credit union solicits a member vote.

Many credit unions submitted a virtually identical comment on this proposal. These commenters believe that this change to the proposed regulation would require a converting credit union to gain NCUA's approval twice: once before the member vote, and then again after the member vote. These commenters believe this unfairly takes the decision out of the hands of the members and places it with NCUA.

One commenter supports the proposed rule and believes that, by adjusting the share insurance notification requirement to match the notification requirement in mergers, it will help achieve NCUA's goal of helping to eliminate the confusion present in current part 708b.

The final rule adopts the proposed amendment with one minor change. The Board is adding a sentence at the end of § 708b.203(c) to clarify that, while a credit union must give NCUA notice of its intent before the member vote is solicited, NCUA will only approve or disapprove the proposed conversion once. The Board will generally make its decision after the credit union has certified the member vote to the NCUA as specified in § 708b.203(g).

4. Amendment Allowing Members to Redeem Term Share Accounts Without Penalty

The proposed rule required, as part of the conversion process, that a credit union inform its members in the form notice of member vote that, if the conversion is approved, it will permit members to close share certificate and other term accounts without penalty if done before the effective date of conversion. The proposal was based on the Board's belief that, as a matter of contract law and fundamental fairness, members who entered into term accounts that were federally insured should be given the opportunity to withdraw their funds without penalty if the accounts lose their federal insurance.

A few commenters support the proposed amendment. One of these commenters states that, if a credit union changes its own terms and conditions, members who relied upon the original terms and conditions should be allowed a way out of their contract.

Many credit unions submitted a virtually identical comment in opposition to the proposed amendment. These commenters believe allowing for early withdrawals without penalty is unsafe, unreasonable and unnecessary, and could create a fear in the membership that results in a run on a federally-insured credit union. These commenters also believe this amendment is an effort to sway the vote away from private insurance.

The Board does not believe the amendment will create a run on any institution or is otherwise unsafe and unsound. The Board notes many of the commenters who opposed portions of the proposed rule were credit unions that have already converted to private share insurance. Some of these commenters discussed the effect on their membership of the conversion. All of these commenters claimed that the number of members who complained or left the credit union because of the conversion was insignificant.

Further, the Board does not intend the right of penalty-free early withdrawal to be used to sway members to vote against the conversion. The proposed rule would have required converting credit unions to provide members information about penalty-free withdrawals twice: once in the notice of proposal to convert that precedes the member vote and again, stated conspicuously, in the notice to members that the conversion has been approved. This final rule allows converting credit unions to delete this information from the form notice of proposal to convert (§ § 708b.301(b), 708b.302(b), and 708b.303(b)). If the conversion is approved, however, the credit union must still inform its members in a conspicuous fashion about the right to penalty-free withdrawals as provided in § 708b.204(c)(2). With this change in the final rule—from two required notices of the right to early withdrawal to only one required notice—the Board wants to ensure that members read the important information in the one required notice and have time to act on it. Accordingly, the final rule makes three modifications to the § 708b.204(c)(2) notice: First, to define conspicuous in this context to mean bolded and no smaller than any other font size used elsewhere in the notice; second, to require that the statement appear on the first page of the notice; and, third, to provide that the credit union must deliver the notice at least 30 days before the effective date of the conversion.

One commenter stated the proposed requirement to allow early withdrawals on term accounts without penalty is an unconstitutional interference with contracts in violation of the U.S. Constitution (Art. I, Section 9) and the Constitution of the State of Illinois (Art. I. Section 6). The Board disagrees. There is no legal impediment to the proposed amendment. Federal share insurance is an implied or express condition of any term share account contract opened at a federally-insured credit union. NCUA regulations, for example, require that the official NCUA sign be displayed at any location where the credit union receives shares. The sign clearly indicates to a would-be share purchaser that he or she will be receiving federal insurance on the account.

One commenter who opposed the requirement stated that ''if the member is that concerned about the safety and soundness of his shares, he will most likely be willing to suffer the penalty to retrieve them.'' The Board disagrees. Some members, particularly elderly members, may have their life savings at the credit union and may be the least able to afford the payment of a penalty.

One commenter asked about members who have deposit balances in excess of NCUA share insurance and if the credit union would only have to waive the penalty associated with the federally-insured portion of the funds. The Board agrees that only the federally-insured portion of the accounts should be subject to withdrawal without penalty and has modified the language of the final rule to reflect this.

One commenter stated, ''Giving carte blanche to the members to withdraw the funds from certificates or any term accounts at any time after the conversion in effect makes all the accounts demand accounts for their remaining term. At a minimum this should occur within a preset time period, for instance 90 days after the conversion.'' This commenter misread the proposed rule. The Board has modified the language of the final rule slightly to state more clearly that penalty free withdrawals are only available between the time the conversion is approved and the time that it takes effect. The Board has also added a phrase to clarify that members must request any withdrawals during this time frame.

One SSA suggested that NCUA and the credit union should be able to continue to provide federal insurance for those members concerned about their term accounts. The Board believes there are both legal and policy impediments to a partial insurance arrangement and declines to adopt it.

5. Amendment Requiring Converting Credit Unions To Provide Proof of Eligibility for Nonfederal Insurance

Not all states permit nonfederal primary share insurance. The proposed rule would require, as part of the request for NCUA approval of conversion to nonfederal insurance, that the converting credit union provide proof that the nonfederal insurer is authorized to issue share insurance in the state where the credit union is located and that the insurer will insure the credit union. Several commenters questioned the need for this requirement. The Board believes proof of these facts avoids the possibility of a credit union seeking to convert to private insurance for which it is not eligible. Accordingly, the final rule includes the proposed amendment.

6. Amendment Requiring a Secret Member Vote Conducted by an Independent Entity

To ensure the integrity of the vote, the proposed rule required the vote be conducted by secret ballot and be administered by an independent entity. The proposed rule defined ''independent entity'' as a company with experience in conducting corporate elections.

A few commenters support the use of an ''independent entity'' and a secret ballot for votes on insurance issues to ensure the integrity of the vote. One of these commenters supports the proposal to ensure issues of impropriety are not levied against the credit union's management or its board at a later date with respect to the vote.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

Loans to Members and Lines of Credit to Members

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is amending three subsections of its lending rule and this final rule clarifies: the conditions for applying the rule to loans secured by mobile homes, recreational vehicles, house trailers and boats; that loans secured by manufactured homes may be considered residential real estate loans; and that loans with a partial government guarantee, insurance, or advance commitment to purchase a portion of a loan fall within the rule. The changes incorporate legal interpretations previously issued by its Office of General Counsel (OGC) regarding permissible maturities for certain types of loans and the effect of partial government guarantees. The NCUA Board is making these changes because it believes it is helpful to federal credit unions (FCUs) and others that may consult NCUA regulations to incorporate these interpretations as part of the rule itself rather than having them stated separately in OGC legal opinions.

DATES: *Effective Date:* This rule is effective March 28, 2005.

FOR FURTHER INFORMATION CONTACT: Dianne M. Salva, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION:

Background

The Federal Credit Union Act (the FCU Act) generally limits an FCU's authority on matters of loan maturity, rates of interest, security and prepayment penalties. 12 U.S.C. 1757(5). As permitted under the FCU Act, the NCUA Board (the Board) has promulgated lending regulations allowing loan maturities of 20 years for mobile home loans and up to 40 years, or more with specific Board approval, on residential real estate loans. 12 CFR 701.21(f) and (g). NCUA's lending regulations also address loans secured by a state or federal government insurance or guarantee. 12 CFR 701.21(e). The OGC had recently issued several legal opinions addressing loan guarantees and loan maturities. In the course of the agency's annual review of regulations, the Board determined that the rules on loan guarantees and maturities should be updated to reflect the OGC opinions. Accordingly, on November 18, 2004, the Board issued a proposal to amend the lending regulations to incorporate the recent OGC opinions. 69 FR 68829, Nov. 26, 2004.

Summary of Comments

NCUA received eleven comments: five from state credit union leagues, two from national credit union trade organizations, three from individual credit unions, and one from a banking trade association. The comments were generally positive and supported the proposal to amend the regulation.

All of the comments that specifically addressed the proposed changes to § 701.21(e) of the rule regarding loan guarantees were favorable and supported the change. The final amendment to the rule, which is unchanged from the proposed, clarifies that a partial government guarantee, insurance, or commitment to purchase a loan is sufficient to effect the application of the regulation.

The majority of comments supported the proposed changes to § 701.21(f) and (g) regarding loan maturities for mobile homes, recreational vehicles and boats, and loan maturities for manufactured homes.

The banking trade association opposed the changes regarding loan maturities in whole, describing them as inconsistent with the credit union industry's specified mission of meeting the credit and savings needs of persons of modest means and arguing that they encourage unsafe lending practices. The Board disagrees. Rather, the Board finds that these amendments to the lending rule enhance an FCU's ability to meet the credit needs of its members. This rule allows FCUs to offer credit products that are more affordable to lower income members. Improvements in the quality and standards of construction of manufactured housing, for example, have resulted in increased values that may put the cost of shorter term loans out of the financial reach of individuals of modest means. The Board also disagrees that the longer maturities will encourage unsafe lending practices. To the contrary, as stated in the preamble to the proposed rule, NCUA encourages FCUs to take appropriate steps to ensure their liens are fully protected. Further, these changes to the regulation merely codify what OGC opinions have permitted for several years, and the Board is unaware of any evidence that the longer loan maturities have resulted in unsafe lending practices.

Two commenters raised issues revealing some confusion about the difference between mobile homes, which may have loan maturities up to 20 years, and manufactured homes, which are eligible for longer maturities. One FCU commented about a particular state law and local practices regarding the titling of manufactured housing as real or personal property, ground-leasing, and what constitutes ''permanently affixed,'' which, the commenter contended, could cause confusion and result in risks to FCUs making manufactured housing loans. In part, some confusion may result if the terms manufactured home and mobile home have a different meaning under a state law. In reviewing the FCU's letter, it became apparent that there may be issues under a state law that FCUs will need to address in their lending agreements with borrowers to ensure compliance with NCUA's lending regulation. One trade association suggested clarifying that manufactured housing that is not permanently affixed to the land constitutes a mobile home. The Board notes that, while this will generally be correct because a mobile home does not have to be permanently affixed to land, which is required for a manufactured home loan, a mobile home still must meet certain regulatory criteria to qualify for a maturity of up to 20 years.

The regulation distinguishes between mobile homes and manufactured homes. First, in using the term ''permanently affixed'' to describe manufactured homes as a type of manufactured housing distinguished from mobile homes, the Board intends to limit long-term loans to manufactured homes that are intended to remain in place permanently. In its opinion letter on this topic, the OGC stated:

> Most significantly, we note that a manufactured home, although constructed at a factory and not built on-site, is designed and intended to be permanently affixed to the land. Unlike a mobile home, which is also constructed at a factory, a manufactured home is not intended to be moved once it has reached its ultimate destination.

Legal Opinion OGC 03–0934, dated November 17, 2003. In order for a loan to qualify for the longer maturities of residential mortgage loans under § 701.21(g), a manufactured home must be designed and intended to remain in place permanently.

The same FCU noted above also commented about two issues regarding manufactured home loans discussed in the preamble to the proposed rule. Regarding the statement in the preamble that a manufactured home must qualify as real property and be titled as real

property, the FCU contends the requirement is unnecessary and that state law and local titling practices could cause problems. The Board notes that, for a loan to be eligible for a 30-year or more maturity term, the FCU Act requires that it be a ''residential *real estate* loan.'' 12 U.S.C. 1757(5)(A)(i) (emphasis added). Loans secured by some type of manufactured housing that is titled as personal property are not eligible for 30-year mortgages under the FCU Act but may be able to qualify as 20-year mobile home loans, assuming the criteria of § 701.21(f) are met. To the extent that a particular state law raises questions of how an FCU can ensure its loans comply with NCUA's lending regulation, an FCU may seek interpretive guidance from OGC.

Second, the FCU commented about the Board's suggestion that, for safety and soundness reasons, FCUs engaging in long-term loans for manufactured homes under § 701.21(g) should ensure, if the member is leasing the land where the manufactured home is located, that the term of the lease should be at least as long as the term of the loan. The FCU commented that this requirement is unnecessary and unreasonable, stating that, in practice, most manufactured housing communities permit leases of no longer duration than six months. First, the Board notes its statement in the preamble is not a regulatory requirement but is a statement of guidance. Second, the FCU's reference to a local practice of having short term leases of six months or less is a practice associated with mobile home parks rather than manufactured home locations. A manufactured home, as opposed to a mobile home, is designed and intended to stay in place permanently rather than be moved. The Board's understanding is that, in purchases of manufactured homes, the manufactured home is most often located on land the borrower already owns or is purchasing in conjunction with the purchase of the manufactured home. As noted in the preamble for the proposed rule, as a matter of safety and soundness, an FCU making a manufactured home loan where the land is leased should ensure that the lease is as long as the term of the loan. There may be some rare set of circumstances that would support an FCU making a 30-year loan on a manufactured home located on property that is leased for some lesser period of time. However, where the lease on land is of such a short duration that it places the loan security at a high risk of loss or waste, safety and soundness considerations would weigh against making a 30-year or more loan.

For these reasons, the Board has determined to adopt the proposed rule as a final rule with no changes.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) requires NCUA to prepare an analysis to describe any significant economic impact any regulation may have on a substantial number of small entities. NCUA considers credit unions having less than ten million in assets to be small for purposes of RFA. Interpretive Ruling and Policy Statement (IRPS) 87–2 as amended by IRPS 03–2. The rule clarifies and expands the lending rules to incorporate recent OGC opinions. NCUA has determined and certifies that this rule will not have a significant economic impact on a substantial number of small credit unions. Accordingly, NCUA has determined that a Regulatory Flexibility Analysis is not required.

Paperwork Reduction Act

NCUA has determined that the rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget (OMB). NCUA currently has OMB clearance for § 701.21's collection requirements (OMB No. 3133–0139).

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. This rule applies to only federally chartered credit unions. NCUA has determined that the final rule does not constitute a ''significant regulatory action'' for purposes of the Executive Order.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The rule applies only to federal credit unions. NCUA has determined that the amendments to the rule will not have a substantial direct effect on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the Administrative Procedures Act. 5 U.S.C. 551. NCUA submitted the rule to the Office of Management and Budget, which has determined that it is not major for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 701

Credit unions, loans.

By the National Credit Union Administration Board on February 17, 2005.

Mary Rupp,

Secretary of the Board.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 748

Security Program and Appendix B—Guidance on Response Programs for Unauthorized Access to Member Information and Member Notice

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: NCUA is amending its rule governing security program elements to require federally insured credit unions to include response programs to address instances of unauthorized access to member information. NCUA is also including guidance, in the form of Appendix B, to provide federally insured credit unions with direction on ways to meet the new regulatory requirements.

DATES: This rule is effective on June 1, 2005.

FOR FURTHER INFORMATION CONTACT: Matthew J. Biliouris, Senior Information Systems Officer, Office of Examination & Insurance, Division of Supervision, at telephone (703) 518–6394; or Ross Kendall, Staff Attorney, Office of General Counsel, at telephone (703) 518–6562.

SUPPLEMENTARY INFORMATION: The contents of this preamble are listed in the following outline:

I. Introduction
II. Overview of the Comments Received
III. Overview of the Final Guidance
IV. Section-by-Section Analysis of the Comments Received
A. The ''Background'' Section
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I. Introduction

In 2001, NCUA amended 12 CFR Part 748 to fulfill a requirement in Section 501 of the Gramm-Leach-Bliley Act (Pub. L. 106–102) (GLBA), in which Congress directed both NCUA and the other Federal Financial Institution Examination Council (FFIEC) agencies, including the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision (collectively, the ''Banking Agencies'') to establish standards for financial institutions relating to administrative, technical, and physical safeguards to: (1) Insure the security and confidentiality of customer records and information; (2) protect against any anticipated threats or hazards to the security or integrity of such records; and (3) protect against unauthorized access to or use of such records or information that could result in substantial harm or inconvenience to any customer.

Although NCUA worked with the Banking Agencies to develop the standards described above, the Banking Agencies issued their standards as guidelines under the authority of Section 39 of the Federal Deposit Insurance Act.

Since Section 39 of the Federal Deposit Insurance Act does not apply to NCUA, the NCUA Board determined that it could best meet the congressional directive to prescribe standards through an amendment to its existing regulation governing security programs for federally insured credit unions and by providing guidance to credit unions, substantially identical to the guidelines issued by the Banking Agencies, in an appendix to the regulation. 12 CFR Part 748, Appendix A; 66 FR 8152 (January 30, 2001). The preamble to the final rule discusses the different regulatory framework under which the Banking Agencies issued their guidelines. The final regulation requires each federally insured credit union to establish and maintain a security program implementing the safeguards required by GLBA.

Appendix A, entitled Guidelines for Safeguarding Member Information (Appendix A), is intended to outline industry best practices and assist credit unions to develop meaningful and effective security programs to ensure compliance with the requirements contained in the regulation. Among other things, Appendix A advises credit unions to: (1) Identify reasonably foreseeable internal and external threats that could result in unauthorized disclosure, misuse, alteration, or destruction of member information or member information systems; (2) assess the likelihood and potential damage of these threats, taking into consideration the sensitivity of member information; and (3) assess the sufficiency of policies, procedures, member information systems, and other arrangements in place to control risks.[1]

On October 23, 2003, the NCUA Board approved a proposal to revise 12 CFR Part 748 to include a requirement to respond to incidents of unauthorized access to member information. The Board invited comment on all aspects of the proposed Guidance. The public comment period closed on December 29, 2003.

This final rule further amends Part 748 to require that every federally insured credit union have a security program that contains a provision for responding to incidents of unauthorized access to member information. Appendix B, entitled Guidance on Response Programs for Unauthorized Access to Member Information and Member Notice, is also provided to assist credit unions in developing and maintaining their response programs. Appendix B describes NCUA's expectation that every federally insured credit union develop a response program, including member notification procedures, to address unauthorized access to or use of member information that could result in substantial harm or inconvenience to a member.

NCUA has modified the proposed Guidance to provide credit unions with greater flexibility to design a risk-based response program tailored to the size, complexity and nature of its operations, while continuing to highlight member notice as a key feature of a credit union's response program. In addition, NCUA reorganized the proposed Guidance for greater clarity. A more detailed discussion of the changes follows.

II. Overview of Comments Received

NCUA received 15 comment letters on the proposed Guidance: Six from natural person credit unions, one from a corporate credit union, two from national credit union trade associations, five from state credit union leagues, and one from a service provider. In addition, the Banking Agencies collectively received 65 comment letters. While the NCUA Board carefully considered all comments on its proposed rule, to remain as consistent as practicable with the Banking Agencies, the Board has also made some changes in the final rule as a result of interagency discussions.

As a general matter, commenters agreed that credit unions should have response programs. Indeed, many credit unions and other financial institutions described having such programs in place. Many comments received commended the NCUA and the Banking Agencies for providing guidance on response programs. However, the majority of industry commenters criticized the prescriptive nature of the proposed Guidance. These commenters stated that the rigid approach in the proposed Guidance would stifle innovation and retard the effective evolution of response programs.

[1] 12 CFR Part 748, Appendix A, Paragraph III.B.2.

Industry commenters raised concerns that the specific requirements in the proposed Guidance would not permit a credit union to assess different situations from its own business perspective, specific to its size, operational and system structure, and risk tolerances.

Some industry commenters asserted that there is no need for regulation in this area and recommended that the NCUA and the Banking Agencies withdraw the proposed Guidance. Some of these commenters suggested, instead, that the Agencies re-issue the proposed Guidance as a best practices document. Other industry commenters suggested modifying the proposed Guidance to give credit unions greater discretion to determine how to respond to incidents of unauthorized access to or use of member information.

Two commenters also requested that the Agencies include a transition period allowing adequate time for financial institutions to implement the final Guidance. Some commenters asked for a transition period only for the aspects of the final Guidance that address service provider arrangements.

III. Overview of Final Guidance

The final rule requires that every federally insured credit union must develop and implement a response program designed to address incidents of unauthorized access to member information maintained by the credit union or its service provider. The final Guidance provides each credit union with greater flexibility to design a risk-based response program tailored to the size, complexity and nature of its operations.

The final Guidance, which has been reorganized for greater clarity, continues to highlight member notice as a key feature of a credit union's response program. However, in response to the comments received, the final Guidance modifies the standard describing when notice should be given and provides for a delay at the request of law enforcement. It also modifies which members should be given notice, what a notice should contain, and how it should be delivered.

A more detailed discussion of the final Guidance and the manner in which it incorporates comments NCUA and the Banking Agencies received follows.

IV. Section-by-Section Analysis of the Comments Received

A. The ''Background'' Section

Legal Authority

The legal foundation for the Guidance is set forth in Part 748, which derives from section 501(b) of GLBA and requires that every credit union have a security program. Appendix A to Part 748 describes the elements of a security program and includes measures to protect member information maintained by the credit union or its service providers. The Guidance states that NCUA expects member notification to be a component of such a response program.

One commenter questioned NCUA's and the Banking Agencies' legal authority to issue the Guidance. This commenter asserted that section 501(b) of GLBA only authorizes the Agencies to establish standards requiring financial institutions to safeguard the confidentiality and integrity of customer information and to protect that information from unauthorized access, but does not authorize standards that would require a response to incidents where the security of customer information actually has been breached.

The NCUA Board notes, however, that section 501(b)(3) specifically states that the standards to be established by the Agencies must include various safeguards to protect against not only ''unauthorized access to,'' but also, the ''use of'' customer information that could result in ''substantial harm or inconvenience to any customer.'' The NCUA Board determined that this language provides a legal basis for standards that include response programs to address incidents of unauthorized access to member information. Response programs represent the principal means for a credit union to protect against unauthorized ''use'' of member information that could lead to ''substantial harm or inconvenience'' to the member. For example, member notification is an important tool that enables a member to take steps to prevent identity theft, such as by arranging to have a fraud alert placed in his or her credit file.

Scope of Guidance

The proposed Guidance contained several cross references to definitions used in Appendix A. However, the NCUA Board did not specifically address the scope of the proposed Guidance. A number of commenters had questions and suggestions regarding the scope of the proposed Guidance and the meaning of terms used.

Entities and Information Covered

Some commenters had questions about the entities and information covered by the proposed Guidance. One commenter suggested that NCUA and the Banking Agencies clarify that foreign offices, branches, and affiliates of United States banks are not subject to the final Guidance. Another commenter wanted the NCUA Board to clarify corporate credit unions' responsibilities relating to the Guidance. This commenter wanted to know if corporate credit unions would be expected to follow the same practices of that of a service provider and notify affected natural person credit unions.

Some commenters recommended that the Agencies clarify that the final Guidance only applies to unauthorized access to sensitive information within the control of the financial institution. One commenter thought that the final Guidance should be broad and cover fraud committed against credit union members through the Internet, such as through the misuse of online corporate identities to defraud online banking users through fake web sites (commonly known as ''phishing''). Several commenters requested confirmation in the final Guidance that it applies to consumer accounts and not to business and other commercial accounts.

For greater clarity, NCUA has revised the Background section of the final Guidance to state that the scope and definitions of terms used in the Guidance are identical to those in section 501(b) of the GLBA and Appendix A, which largely cross-reference definitions used in NCUA's Privacy Rule.[2] Therefore, consistent with section 501(b) and Appendix A, this final Guidance applies to the entities enumerated in section 505(a) of the GLBA. This final Guidance does not apply to a credit union's foreign offices, branches, or CUSOs. However, a credit union is responsible for the security of its member information, whether the information is maintained within or outside of the United States, and whether or not it relies on a CUSO to provide certain member services.

As with the guidance contained in Appendix A, natural person credit unions that use corporate credit unions as their ''service providers'' will likely look to the final Guidance in overseeing their service provider arrangements with those corporate credit unions. Accordingly, there is no exemption for corporate credit unions that provide services to natural person credit unions as part of normal processing business.

The final Guidance also applies to ''member information,'' meaning any record containing ''nonpublic personal information'' (as that term is defined in section 716.3(n) of NCUA's Privacy rule) about a credit union's member, whether in paper, electronic, or other form, that

[2] 12 CFR Part 716.

is maintained by or on behalf of the institution.[3] Consequently, the final Guidance applies only to information that is within the control of the credit union and its service providers, and would not apply to information directly disclosed by a member to a third party, for example, through a fraudulent web site.

Moreover, the final Guidance does not apply to information involving business or commercial accounts. Instead, the final Guidance applies to nonpublic personal information about a ''member'' within the meaning of Appendix A, namely, a consumer who obtains a financial product or service from a credit union to be used primarily for personal, family, or household purposes, and who has a continuing relationship with the credit union.[4]

Effect of Other Laws

Several commenters requested NCUA and the Banking Agencies explain how the final Guidance interacts with additional and possibly conflicting state law requirements. Most of these commenters urged that the final Guidance expressly preempt state law. By contrast, one commenter asked the Agencies to clarify that a financial institution must also comply with additional state law requirements. In addition, some commenters asked that the final Guidance provide a safe harbor defense against class action law suits. They suggested that the safe harbor should cover any credit union that takes reasonable steps that regulators require to protect member information, but, nonetheless, experiences an event beyond its control that leads to the disclosure of member information.

These issues do not fall within the scope of this final Guidance. The extent to which section 501(b) of GLBA, Appendix A, and any related NCUA interpretations, such as this final Guidance, preempts state law is governed by Federal law, including the procedures set forth in section 507 of GLBA, 15 U.S.C. 6807.[5] Moreover, there is nothing in Title V of the GLBA that authorizes NCUA to provide credit unions with a safe harbor defense. Therefore, the final Guidance does not address these issues.

Organizational Changes in the ''Background'' Section

For the reasons described earlier, the Background section is adopted essentially as proposed, except that the latter part of the paragraph on ''Service Providers'' and the entire paragraph on ''Response Programs'' are incorporated into the introductory discussion of Section II. The NCUA Board believes that the Background section is now clearer, as it focuses solely on the statutory and regulatory framework upon which the final Guidance is based. Comments and changes with respect to the paragraphs that were relocated are discussed in the next section.

B. The ''Response Program'' Section

There are a number of differences between the discussion of Response Programs in the proposed and final Guidance. The introduction to section II of the proposed Guidance stated that a response program should be a key part of a credit union's information security program required under Part 748. It also described the importance of having a response program and of timely notification of members when warranted. Section II of the proposed Guidance contained four detailed paragraphs describing each of the four components that a response program should contain.

The introductory language in the final Guidance now emphasizes that a credit union's response program should be risk-based and describes the components of a response program in a less prescriptive manner. Section II in the final Guidance specifically states that a credit union should implement security measures, from among the itemized list in Appendix A, designed to prevent unauthorized access to or use of member information, such as by placing access controls on member information systems and conducting background checks[6] for employees who are authorized to access member information. It then states that NCUA expects every credit union to develop and implement a risk-based response program (another security measure enumerated in Appendix A) designed to address incidents of unauthorized access to member information that occur despite measures to prevent security breaches. The final Guidance also states that a response program should be a key part of a credit union's information security program.

This introductory paragraph is intended to make clear that, based upon the prevalence of identity theft in the United States,[7] every credit union should have a response program to be prepared to prevent and address attempts to gain unauthorized access to its member information. The Board's expectation that each credit union will develop a response program is consistent with the provision in Appendix A calling for each credit union to design an information security program to control ''identified risks'' stemming from ''reasonably foreseeable internal and external threats.''[8]

Service Provider Contracts

The Background section of the proposed Guidance elaborated on the specific provisions that a credit union's contracts with its service providers should contain. The proposed Guidance stated that a credit union's contract with its service provider should require the service provider to disclose fully to the credit union information related to any breach in security resulting in an unauthorized intrusion into the credit union's member information systems maintained by the service provider. It stated that this disclosure would permit a credit union to expeditiously implement its response program.

Several commenters on the proposed Guidance agreed that a credit union's contracts with its service providers should require the service provider to disclose fully to the credit union information related to any breach in security resulting in an unauthorized intrusion into the credit union's member information systems maintained by the service provider. However, many commenters suggested modifications to this provision.

The discussion of this aspect of a credit union's contracts with its service providers is in section II of the final Guidance. It has been revised as follows in response to the comments received.

Timing of Service Provider Notification

NCUA and the Banking Agencies received a number of comments regarding the timing of a service

[3] *See* 12 CFR Part 745, Appendix A, Paragraph I.C.2.c.

[4] *See* 12 CFR Part 748, Appendix A, Paragraph I.C.2.b.; 12 CFR Part 716.3(i).

[5] Section 507 provides that state laws that are ''inconsistent'' with the provisions of Title V, Subtitle A of the GLBA are preempted ''only to the extent of the inconsistency.'' State laws are ''not consistent'' if they offer greater protection than Subtitle A, as determined by the Federal Trade Commission, after consultation with the agency or authority with jurisdiction under Section 505(a) of either the person that initiated the complaint or that is the subject of the complaint. *See* 15 U.S.C. 6807.

[6] A footnote has been added to this section to make clear that credit unions should also conduct background checks of employees to ensure that the credit union does not violate 12 U.S.C. 1785(d), which prohibits an institution from hiring an individual convicted of certain criminal offenses or who is subject to a prohibition order under 12 U.S.C. 1786(g).

[7] See, for example, the Federal Trade Commission's Identity Theft Survey Report of September 2003,'' available at *http://www.ftc.gov/os/2003/09synovatereport.pdf* estimating that 10 million Americans were victims of identify theft in 2002.

[8] 12 CFR Part 748, Appendix A, Paragraph III.B. and III.C.

provider's notice to a credit union. One commenter suggested requiring service providers to report incidents of unauthorized access to credit unions within 24 hours after discovery of the incident.

In response to comments on the timing of a service provider's notice to a credit union, the final Guidance states that a credit union's contract with its service provider should require the service provider to take appropriate action to address incidents of unauthorized access to the credit union's member information, including notifying the credit union as soon as possible of any such incident, to enable the credit union to expeditiously implement its response program. The NCUA Board determined that requiring notice within 24 hours of an incident may not be practicable or appropriate in every situation, particularly where, for example, it takes a service provider time to investigate a breach in security. Therefore, the final Guidance does not specify a number of hours or days by which the service provider must give notice to the credit union.

Existing Contracts With Service Providers

Some commenters expressed concerns that they would have to rewrite their contracts with service providers to require the disclosure described in this provision. These commenters asked NCUA to grandfather existing contracts and to apply this provision only prospectively to new contracts. Many commenters also suggested that the final Guidance contain a transition period to permit credit unions to modify their existing contracts.

The NCUA Board has decided not to grandfather existing contracts or to add a transition period to the final Guidance because, as stated in the proposed Guidance, this disclosure provision is consistent with the obligations in Appendix A that relate to service provider arrangements and with existing guidance on this topic previously issued by NCUA.[9] In order to ensure the safeguarding of member information, credit unions that use service providers likely have already arranged to receive notification from the service providers when member information is accessed in an unauthorized manner. In light of the comments received, however, NCUA recognizes that there are credit unions that have not formally included such a disclosure requirement in their contracts. Where this is the case, the credit union should exercise its best efforts to add a disclosure requirement to its contracts and any new contracts should include such a provision.

Thus, the final Guidance adopts the discussion on service provider arrangements largely as proposed. To eliminate any ambiguity regarding the application of this section to foreign-based service providers, however, the final Guidance now makes clear that a covered credit union[10] should be capable of addressing incidents of unauthorized access to member information in member information systems maintained by its domestic and foreign service providers.[11]

Components of a Response Program

As described earlier, commenters criticized the prescriptive nature of proposed Section II that described the four components a response program should contain. The proposed Guidance instructed credit unions to design programs to respond to incidents of unauthorized access to member information by (1) assessing the situation; (2) notifying regulatory and law enforcement agencies; (3) containing and controlling the situation; and (4) taking corrective measures. The proposed Guidance contained detailed information about each of these four components.

The introductory discussion in this section of the final Guidance now makes clear that, as a general matter, a credit union's response program should be risk-based. It applies this principle by modifying the discussion of a number of these components. The NCUA Board determined that the detailed instructions in these components of the proposed Guidance, especially in the ''Corrective Measures'' section, would not always be relevant or appropriate. Therefore, the final Guidance describes, through brief, bulleted points, the elements of a response program, giving credit unions greater discretion to address incidents of unauthorized access to or use of member information that could result in substantial harm or inconvenience to a member.

At a minimum, a credit union's response program should contain procedures for (1) assessing the nature and scope of an incident, and identifying what member information systems and types of member information have been accessed or misused; (2) notifying the appropriate NCUA Regional Director and, in the case of state-chartered credit unions, its applicable state supervisory agency as soon as possible when the credit union becomes aware of an incident involving unauthorized access to or use of sensitive member information, as defined in the final Guidance, (3) immediately notifying law enforcement authorities in situations involving Federal criminal violations requiring immediate attention; (4) taking appropriate steps to contain and control the incident to prevent further unauthorized access to or use of member information, such as by monitoring, freezing, or closing affected accounts, while preserving records and other evidence; and (5) notifying members when warranted.

Assess the Situation

The proposed Guidance stated that a credit union should assess the nature and scope of the incident and identify what member information systems and types of member information have been accessed or misused.

Some commenters stated that NCUA and the Banking Agencies should retain this provision in the final Guidance. One commenter suggested that a credit union should focus its entire response program primarily on addressing unauthorized access to sensitive member information.

The NCUA Board has concluded that a credit union's response program should begin with a risk assessment that allows a credit union to establish the nature of any information improperly accessed. This will allow the credit union to determine whether and how to respond to an incident. Accordingly, the NCUA Board has not changed this provision.

Notify Regulatory and Law Enforcement Agencies

The proposed Guidance provided that a credit union should promptly notify NCUA when it becomes aware of an incident involving unauthorized access to or use of member information that could result in substantial harm or inconvenience to members. To clarify its expectations, the NCUA Board has amended the bullet point addressing notification of the regulator to include notification of the appropriate NCUA Regional Director, as well as any applicable state supervisory agency in the case of state-chartered credit unions.

In addition, the proposed Guidance stated that a credit union should file a Suspicious Activity Report (SAR), if required, in accordance with 12 CFR

[9] *See* FFIEC Information Technology Examination Handbook, Outsourcing Technology Services Booklet, June 2004; NCUA Letter to Credit Unions No. 00–CU–11, December 2000.

[10] *See* footnote 5, *supra*.

[11] *See e.g.*, FFIEC Information Technology Examination Handbook, Outsourcing Technology Services Booklet, June 2004.

Part 748 and various NCUA issuances.[12] The proposed Guidance stated that, consistent with the NCUA's SAR regulation, in situations involving Federal criminal violations requiring immediate attention, the credit union immediately should notify, by telephone, the appropriate law enforcement authorities and its primary regulator, in addition to filing a timely SAR. For the sake of clarity, the final Guidance discusses notice to regulators and notice to law enforcement in two separate, bulleted items.

Standard for Notice to Regulators

The provision regarding notice to regulators in the proposed Guidance prompted numerous comments. Many commenters suggested that NCUA adopt a narrow standard for notifying regulators. These commenters were concerned that notice to regulators, provided under the circumstances described in the proposed Guidance, would be unduly burdensome for credit unions, service providers, and regulators, alike.

Some of these commenters suggested that NCUA adopt the same standard for notifying regulators and members. These commenters recommended that notification occur when a credit union becomes aware of an incident involving unauthorized access to or use of ''sensitive member information,'' a defined term in the proposed Guidance that specified a subset of member information deemed by NCUA as most likely to be misused.

Other commenters recommended that the Agencies narrow this provision so that a credit union will inform a regulator only in connection with an incident that poses a significant risk of substantial harm to a significant number of its members, or only in a situation where substantial harm to members has occurred or is likely to occur, instead of when it could occur.

Other commenters who advocated the adoption of a narrower standard asked NCUA to take the position that filing an SAR constitutes sufficient notice and that notification of other regulatory and law enforcement agencies is at the sole discretion of the credit union. One commenter stated that it is difficult to imagine any scenario that would trigger the response program without requiring a SAR filing. Some commenters asserted that if NCUA believes a lower threshold is advisable for security breaches, it should amend Part 748.

By contrast, some commenters recommended that the standard for notification of regulators remain broad. One commenter advocated that any event that triggers an internal investigation by the credit union should require notice to the appropriate regulator. Another commenter similarly suggested that notification of all security events to federal regulators is critical, not only those involving unauthorized access to or use of member information that could result in substantial harm or inconvenience to its members.

The NCUA Board has concluded that the standard for notification to regulators should provide an early warning to allow NCUA or applicable state supervisory agency to assess the effectiveness of a credit union's response plan, and, where appropriate, to direct that notice be given to members if the credit union has not already done so. Thus, the standard in the final Guidance states that a credit union should notify its primary regulator as soon as possible if the credit union becomes aware of an incident involving unauthorized access to or use of ''sensitive member information.''

''Sensitive member information'' is defined in section III of the final Guidance and means a member's name, address, or telephone number, in conjunction with the member's social security number, driver's license number, account number, credit or debit card number, or a personal identification number or password that would permit access to the member's account. ''Sensitive member information'' also includes any combination of components of member information that would allow someone to log onto or access the member's account, such as user name and password or password and account number.

This standard is narrower than that in the proposed Guidance because a credit union will need to notify NCUA when, and only if, it becomes aware of an incident involving ''sensitive member information.'' Therefore, under the final Guidance, there will be fewer occasions when a credit union should need to notify NCUA. However, under this standard, a credit union will need to notify NCUA at the time that the credit union initiates its investigation to determine the likelihood that the information has been or will be misused, so that NCUA will be able to take appropriate action, if necessary.

Notice to Regulators by Service Providers

Commenters on the proposed Guidance questioned whether a credit union or its service provider should give notice to a regulator when a security incident involves an unauthorized intrusion into the credit union's member information systems maintained by the service provider. One commenter noted that if a security event occurs at a large service provider, regulators could receive thousands of notices from institutions relating to the same event. The commenter suggested that if a service provider is examined by one of the Agencies the most efficient means of providing regulatory notice of such a security event would be to allow the servicer to notify its primary Agency contact. The primary Agency contact then could disseminate the information to the other regulatory agencies as appropriate.

The NCUA Board believes it is the responsibility of the credit union and not the service provider to notify NCUA. Therefore, the final Guidance states that a credit union should notify NCUA as soon as possible when the credit union becomes aware of an incident involving unauthorized access to or use of sensitive member information. Nonetheless, a security incident at a service provider could have an impact on multiple financial institutions that are supervised by different Federal regulators. Therefore, in the interest of efficiency and burden reduction, the last paragraph in section II of the final Guidance makes clear that a credit union may authorize or contract with its service provider to notify the NCUA on the credit union's behalf when a security incident involves an unauthorized intrusion into the credit union's member information systems maintained by the service provider.

Notice to Law Enforcement

Some commenters took issue with the provision in the proposed Guidance regarding notification of law enforcement by telephone. One interagency commenter asked the Banking Agencies to clarify how notification of law enforcement by telephone would work since in many cases it is unclear what telephone number should be used. This commenter maintained that size and sophistication of law enforcement authorities may differ from state to state and this requirement may create confusion and unwarranted action by the law enforcement authority.

The final Guidance adopts this provision as proposed. The NCUA

[12] *See* 12 CFR Part 748.1(c); NCUA Letter to Credit Unions No. 04–CU–03, Suspicious Activity Reports, March 2004; NCUA Regulatory Alert No. 04–RA–01, The Suspicious Activity Report (SAR) Activity Review—Trends, Tips, & Issues, Issue 6, November 2003, February 2004.

Board notes that the provision stating that a credit union should notify law enforcement by telephone in situations involving federal criminal violations requiring immediate attention is consistent with Part 748.

Contain and Control the Situation

The proposed Guidance stated that the credit union should take measures to contain and control a security incident to prevent further unauthorized access to or use of member information while preserving records and other evidence.[13] It also stated that, depending upon the particular facts and circumstances of the incident, measures in connection with computer intrusions could include: (1) Shutting down applications or third party connections; (2) reconfiguring firewalls in cases of unauthorized electronic intrusion; (3) ensuring that all known vulnerabilities in the credit union's computer systems have been addressed; (4) changing computer access codes; (5) modifying physical access controls; and (6) placing additional controls on service provider arrangements.

Few comments were received on this section. One interagency commenter suggested that the Banking Agencies adopt this section unchanged in the final Guidance. Another commenter had questions about the meaning of the phrase ''known vulnerabilities.'' Commenters did, however, note the overlap between proposed section II.C and the corrective measures in proposed section II.D, described as ''flagging accounts'' and ''securing accounts.''

NCUA and the Banking Agencies agree that some sections in the proposed Guidance overlapped. Therefore, the NCUA Board modified this section by incorporating concepts from the proposed Corrective Measures component, and removing the more specific examples in this section, including the terms that confused commenters. This section in the final Guidance gives a credit union greater discretion to determine the measures it will take to contain and control a security incident. It states that credit unions should take appropriate steps to contain and control the incident to prevent further unauthorized access to or use of member information, such as, by monitoring, freezing, or closing affected accounts, while preserving records and other evidence.

Preserving Evidence

One interagency commenter stated that the final Guidance should require financial institutions, as part of the response process, to have an effective computer forensics capability in order to investigate and mitigate computer security incidents as discussed in principle fourteen of the Basel Committee's ''Risk Management for Electronic Banking''[14] and the International Organization for Standardization's ISO 17799.[15]

The NCUA Board notes that the final Guidance addresses not only computer security incidents, but also all other incidents of unauthorized access to member information. Thus, the Board thinks it is not appropriate to include more detail about steps a credit union should take to investigate and mitigate computer security incidents. However, the NCUA Board believes that credit unions should be mindful of industry standards when investigating an incident. Therefore, the final Guidance contains a reference to forensics by generally noting that a credit union should take appropriate steps to contain and control an incident, while preserving records and other evidence.

Corrective Measures

The proposed Guidance stated that once a credit union understands the scope of the incident and has taken steps to contain and control the situation, it should take measures to address and mitigate the harm to individual members. It then described three corrective measures that a credit union should include as a part of its response program in order to effectively address and mitigate harm to individual members: (1) Flagging accounts; (2) securing accounts; and (3) notifying members. The NCUA Board removed the first two corrective measures for the reasons that follow.

Flagging and Securing Accounts

The first corrective measure in the proposed Guidance directed credit unions to ''flag accounts.'' It stated that a credit union should immediately begin identifying and monitoring the accounts of those members whose information may have been accessed or misused. It also stated that a credit union should provide staff with instructions regarding the recording and reporting of any unusual activity, and if indicated given the facts of a particular incident, implement controls to prevent the unauthorized withdrawal or transfer of funds from member accounts.

The second corrective measure directed credit unions to ''secure accounts.'' The proposed Guidance stated that when a share draft, savings, or other member account number, debit or credit card account number, personal identification number (PIN), password, or other unique identifier has been accessed or misused, the credit union should secure the account and all other accounts and services that can be accessed using the same account number or name and password combination. The proposed Guidance stated that accounts should be secured until such time as the credit union and the member agree on a course of action.

Commenters were critical of these proposed measures. Several commenters asserted that the final Guidance should not prescribe responses to security incidents with this level of detail. Other commenters recommended that if NCUA chooses to retain references to ''flagging'' or ''securing'' accounts, it should include the words ''where appropriate'' in order to give credit unions the flexibility to choose the most effective solutions to problems.

Commenters also stated that the decision to flag accounts, the nature of the flag, and the duration of the flag, should be left to an individual credit union's risk-based procedures developed under Appendix A. These commenters asked NCUA to recognize that regular, ongoing fraud prevention and detection methods employed by a credit union may be sufficient.

Commenters representing small credit unions stated that they do not have the technology or other resources to monitor individual accounts. They stated that the financial impact of having to monitor accounts for unusual activity would be enormous, as each credit union would have to purchase expensive technology, hire more personnel, or both. These commenters asked NCUA to provide credit unions with the flexibility to close an account if the credit union detects unusual activity.

With respect to ''securing accounts,'' several commenters stated that if ''secure'' means close or freeze, either is extreme and would have significant adverse consequences for members. Other commenters stated that the requirement that the credit union and the member ''agree on a course of action'' is unrealistic, unworkable and should be eliminated. Some commenters explained that if a member is traveling and the credit union cannot contact the member to obtain the member's consent, freezing or closing a

[13] *See* FFIEC Information Security Booklet, December. 2002, pp. 68–74, avaialble at *http://www.ffiec.gov/ffiecinfobase.html*__pages/it__01.htmlıinfosec.

[14] *http://www.bis.org/publ/bcbs35.htm.*

[15] *http://www.iso.org/iso/en/prods-services/popstds/informationsecurity.html.*

member's account could strand the member with no means of taking care of expenses. They stated that, in the typical case, the credit union would monitor such an account for suspicious transactions.

As described earlier, the NCUA Board is adopting an approach in the final Guidance that is more flexible and risk-based than that in the proposed Guidance. The final Guidance incorporates the general concepts described in the first two corrective measures into the brief bullets describing components of a response program enumerated in section II.C. Therefore, the first and second corrective measures no longer appear in the Guidance.

Member Notice and Assistance

The third corrective measure in the proposed Guidance is titled ''Member Notice and Assistance.'' This proposed measure stated that a credit union should notify and offer assistance to members whose information was the subject of an incident of unauthorized access or use under the circumstances described in section III of the proposed Guidance. The proposed Guidance also described which members should be notified. In addition, this corrective measure contained provisions discussing delivery and contents of the member notice.

The final Guidance now states that a credit union's response program should contain procedures for notifying members when warranted. For clarity's sake, the discussion of which members should be notified, and the delivery and contents of member notice, is now in new section III, titled ''Member Notice.'' Comments and changes with respect to the paragraphs that were relocated are discussed under the section titled ''Member Notice'' that follows.

Responsibility for Notice to Members

Some commenters were confused by the discussion in the proposed Guidance stating that a credit union's contract with its service provider should require the service provider to disclose fully to the credit union information related to any breach in security resulting in an unauthorized intrusion into the credit union's member information systems maintained by the service provider. Commenters stated that this provision appears to create an obligation for both credit unions and their service providers to provide notice of security incidents to the credit union's members. These commenters recommended that the service provider notify its credit union customer so that the credit union can provide appropriate notice to its members. Thus, members would avoid receiving multiple notices relating to a single security incident.

Other commenters asserted that a credit union should not have to notify its members if an incident has occurred because of the negligence of its service provider. These commenters recommended that in this situation, the service provider should be responsible for providing notice to the credit union's members.

As discussed above in connection with notice to regulators, the NCUA Board believes that it is the responsibility of the credit union, and not of the service provider, to notify the credit union's members in connection with an unauthorized intrusion into a credit union's member information systems maintained by the service provider. The responsibility to notify members remains with the credit union whether the incident is inadvertent or due to the service provider's negligence. The NCUA Board notes that the costs of providing notice to the credit union's members as a result of negligence on the part of the service provider may be addressed in the credit union's contract with its service provider.

The last paragraph in section II of the final Guidance, therefore, states that it is the responsibility of the credit union to notify the credit union's members. It also states that the credit union may authorize or contract with its service provider to notify members on the credit union's behalf when a security incident involves an unauthorized intrusion into the credit union's member information systems maintained by the service provider.

C. The ''Member Notice'' Section

Section III of the proposed Guidance described the standard for providing notice to members and defined the term ''sensitive member information'' used in that standard. This section also gave examples of circumstances when a credit union should give notice and when NCUA does not expect a credit union to give notice. It also discussed contents of the notice and proper delivery.

Section III of the final Guidance contains a more comprehensive discussion of member notice. It describes the standard for providing notice to members and defines both the terms ''sensitive member information'' and ''affected members.'' It also discusses the contents of the notice and proper delivery.

Standard for Providing Notice

A key feature of the proposed Guidance was the description of when a credit union should provide member notice. The proposed Guidance stated that a credit union should notify affected members whenever it becomes aware of unauthorized access to ''sensitive member information'' unless the credit union, after an appropriate investigation, reasonably concludes that misuse of the information is unlikely to occur and takes appropriate steps to safeguard the interests of affected members, including by monitoring affected members' accounts for unusual or suspicious activity.

The NCUA Board proposed this standard as a way to strike a balance between notification to members every time the mere possibility of misuse of member information arises from unauthorized access and a situation where the credit union knows with certainty that information is being misused. However, the Board specifically requested comment on whether this is the appropriate standard and invited commenters to offer alternative thresholds for member notification.

Some commenters stated that the proposed standard was reasonable and sufficiently flexible. However, many commenters recommended that the Board provide credit unions with greater discretion to determine when a credit union should notify its members. Some of these commenters asserted that a credit union should not have to give notice unless the credit union believes it ''to be reasonably likely,'' or if circumstances indicated ''a significant risk'' that the information will be misused.

Commenters maintained that because the proposed standard states that a credit union should give notice when fraud or identity theft is merely possible, notification under these circumstances would needlessly alarm members where little likelihood of harm exists. Commenters claimed that, eventually, frequent notices in non-threatening situations will be perceived by members as routine and commonplace, and therefore reduce their effectiveness.

The NCUA Board believes that articulating as part of the Guidance a standard that sets forth when notice to members is warranted is both helpful and appropriate. However, the Board agrees with commenters and is concerned that the proposed threshold inappropriately required credit unions to prove a negative proposition, namely, that misuse of the information accessed

is unlikely to occur. In addition, the Board does not want members of credit unions to receive notices that would not be useful to them. Therefore, the NCUA Board has revised the standard for members notification.

The final Guidance provides that when a credit union becomes aware of an incident of unauthorized access to sensitive member information, the credit union should conduct a reasonable investigation to determine promptly the likelihood that the information has been or will be misused. If the credit union determines that misuse of the information has occurred or is reasonably possible, it should notify affected members as soon as possible.

An investigation is an integral part of the standard in the final Guidance. A credit union should not forego conducting an investigation to avoid reaching a conclusion that member information has been or will be misused and cannot unreasonably limit the scope of the investigation. However, the NCUA Board acknowledges that a full-scale investigation may not be necessary in all cases, such as where the facts readily indicate that information will or will not be misused.

Monitoring for Suspicious Activity

The proposed Guidance stated that a credit union need not notify members if it reasonably concludes that misuse of the information is unlikely to occur and takes appropriate steps to safeguard the interests of affected members, including by monitoring affected members' accounts for unusual or suspicious activity. A number of comments addressed the standard in the proposed Guidance on monitoring affected members' accounts for unusual or suspicious activity.

Some commenters stated that the final Guidance should grant credit unions the discretion to monitor the affected member accounts for a period of time and to the extent warranted by the particular circumstances. Some commenters suggested that monitoring occur during the investigation. One commenter noted that a credit union's investigation may reveal that monitoring is unnecessary. One commenter noted that monitoring the member's accounts at the credit union may not protect the member, because unauthorized access to member information may result in identity theft beyond the accounts held at the specific credit union.

The NCUA Board agrees that under certain circumstances, monitoring may be unnecessary, for example when, on the basis of a reasonable investigation, a credit union determines that information was not misused. The Board also agrees that the monitoring element may not protect the member. Indeed, an identity thief with unauthorized access to certain sensitive member information likely will open accounts at other financial institutions in the member's name.

Accordingly, the Board concludes that monitoring under the circumstances described in the standard for notice would be burdensome for credit unions without a commensurate benefit to members. For these reasons, the Board has removed the reference to monitoring in the final Guidance.

Timing of Notice

The proposed Guidance did not include specific language on the timing of notice to members, and NCUA and the Banking Agencies received many comments on this issue. Some commenters requested clarification of the time frame for member notice. One commenter recommended that NCUA adopt the approach in the proposed Guidance because it does not set forth any circumstances that may delay notification of the affected members. Another commenter maintained that, in light of a member's need to act expeditiously against identity theft, an outside limit of 48 hours after the credit union learns of the breach is a reasonable and timely requirement for notice to members. Many commenters, however, recommended that NCUA make clear that a credit union may take the time it reasonably needs to conduct an investigation to assess the risk resulting from a security incident.

The NCUA Board has responded to these various comments on the timing of notice by providing that a credit union notify an affected member ''as soon as possible'' after concluding that misuse of the member's information has occurred, or is reasonably possible. As the scope and timing of a credit union's investigation is dictated by the facts and circumstances of a particular case, the Board has not designated a specific number of hours or days by which credit unions should provide notice to members. The Board believes that doing so may inhibit a credit union's ability to investigate adequately a particular incident or may result in notice that is not timely.

Delay for Law Enforcement Investigation

The proposed Guidance did not address delay of notice to members while a law enforcement investigation is conducted. Many commenters recommended permitting a credit union to delay notification to members to avoid compromising a law enforcement investigation. These commenters noted that the California Database Protection Act of 2003 (CDPA) requires notification of California residents whose unencrypted personal information was, or is reasonably believed to have been, acquired by an unauthorized person.[16] However, the CDPA permits a delay in notification if a law enforcement agency determines that the notification will impede a criminal investigation.[17] Another commenter suggested that a credit union should not have to obtain a formal determination from a law enforcement agency before it is able to delay notice.

The NCUA Board agrees that it is appropriate to delay member notice if such notice will jeopardize a law enforcement investigation. However, to ensure that such a delay is necessary and justifiable, the final Guidance states that member notice may be delayed if an appropriate law enforcement agency determines that notification will interfere with a criminal investigation and provides the credit union with a written request for the delay.[18]

The NCUA Board is concerned that a delay of notification for a law enforcement investigation could interfere with the ability of members to protect themselves from identity theft and other misuse of their sensitive information. Thus, the final Guidance also provides that a credit union should notify its members as soon as notification will no longer interfere with the investigation and should maintain contact with the law enforcement agency that has requested a delay, in order to learn, in a timely manner, when member notice will no longer interfere with the investigation.

Sensitive Member Information

Scope of Standard

The Banking Agencies received many comments on the limitation of notice in the proposed Guidance to incidents involving unauthorized access to sensitive customer information. The NCUA Board invited comment on whether to modify the proposed standard for notice to apply to other circumstances that compel a credit union to conclude that unauthorized access to information, other than sensitive member information, likely

[16] The CDPA, also known as CA S.B. 1386, amended the Information Practices Act of 1977, California Civil Code, section 1798.82.

[17] *See* California Civil Code, section 1798.29(c).

[18] This includes circumstances when a credit union confirms that an oral request for delay from law enforcement will be followed by a written request.

will result in substantial harm or inconvenience to the affected members.

Most commenters recommended that the standard remain as proposed rather than covering other types of information. One interagency commenter suggested that the Agencies continue to allow a financial institution the discretion to notify affected customers in any other extraordinary circumstances that compel it to conclude that unauthorized access to information other than sensitive customer information likely will result in substantial harm or inconvenience to those affected. However, the commenter did not provide any examples of such extraordinary circumstances.

The NCUA Board continues to believe that the rationale for limiting the standard to sensitive member information expressed in the proposed Guidance is correct. The proposed Guidance explained that, in accordance with Appendix A, a credit union must protect against unauthorized access to or use of member information that could result in substantial harm or inconvenience to a member. Substantial harm or inconvenience is most likely to result from improper access to sensitive member information because this type of information is easily misused, as in the commission of identity theft.

The NCUA Board has not identified any other circumstances that should prompt member notice and continues to believe that it is not likely that a member will suffer substantial harm or inconvenience from unauthorized access to other types of information. Therefore, the standard in the final Guidance continues to be limited to unauthorized access to sensitive member information. Of course, a credit union still may send notices to members in any additional circumstances that it determines are appropriate.

Definition of Sensitive Member Information

NCUA received many comments on the proposed definition of ''sensitive member information'' in the proposed Guidance. The first part of the proposed definition stated that ''sensitive member information'' is a member's social security number, personal identification number (PIN), password or account number, in conjunction with a personal identifier such as the member's name, address, or telephone number. The second part of the proposed definition stated that ''sensitive member information'' includes any combination of components of member information that allow someone to log onto or access another person's account, such as user name and password.

Some commenters agreed with this definition of ''sensitive member information.'' They said that it was sound, workable, and sufficiently detailed. However, many commenters proposed additions, exclusions, or alternative definitions.

Additional Elements

Some commenters suggested that NCUA add various data elements to the definition of sensitive member information, including: A driver's license number or number of other government-issued identification, mother's maiden name, and date of birth. One commenter suggested inclusion of other information that credit unions maintain in their member information systems such as a member's account balance, account activity, purchase history, and investment information. The commenter noted that misuse of this information in combination with a personal identifier can just as easily result in substantial harm or inconvenience to a member.

The NCUA Board has added to the first part of the definition several more specific components, such as driver's license number and debit and credit card numbers, because this information is commonly sought by identity thieves. However, the Board determined that the second part of the definition would cover the remaining suggestions. For example, where date of birth or mother's maiden name are used as passwords, under the final Guidance they will be considered components of member information that allow someone to log onto or access another person's account. Therefore, these specific elements have not been added to the definition.

Exclusions

Commenters also asserted that the proposed definition of sensitive member information is too broad and proposed various exclusions. For example, some commenters asked NCUA to exclude publicly available information, and also suggested that the final Guidance apply only to account numbers for transaction accounts or other accounts from which withdrawals or transfers can be initiated. These commenters explained that access to a mortgage account number (which may also be a public record) does not permit withdrawal of additional funds or otherwise damage the member. Other commenters requested that NCUA exclude encrypted information. Some of these commenters noted that only unencrypted information is covered by the CDPA.[19]

The final Guidance does not adopt any of the proposed exclusions. The NCUA Board believes it would be inappropriate to exclude publicly available information from the definition of sensitive member information, where publicly available information is otherwise covered by the definition of ''member information.''[20] So for instance, while a personal identifier, *i.e.,* name, address, or phone number, may be publicly available, it is sensitive member information when linked with particular nonpublic information such as a credit card account number. However, where the definition of ''member information'' does not cover publicly available information, sensitive member information also would not cover publicly available information. For instance, where an individual's name or address is linked with a mortgage loan account number that is in the public record, and therefore, would not be considered ''member information,''[21] it also would not be considered sensitive member information for purposes of the final Guidance.

In addition, access to a member's personal information and account number, whether or not it is an account from which withdrawals or transfers can be initiated, may permit an identity thief to access other accounts from which withdrawals can be made. Thus, the NCUA Board has determined that the definition of account number should not be limited as suggested by commenters. The Board also believes that a blanket exclusion for all encrypted information is not appropriate, because there are many levels of encryption, some of which do not effectively protect member information.

Alternative Definitions

Most alternative definitions suggested by commenters resembled the definition of ''personal information'' under the CDPA.[22] Under the CDPA, ''personal information'' includes a resident of California's name together with an account number, or credit or debit card

[19] *See* California Civil Code, 1798.29(a).

[20] *See* 12 CFR Part 748, Appendix A, Paragraph I.C.2.c.

[21] *See* 12 CFR § 716.3(p)(3)(i).

[22] Under the California law requiring notice, ''personal information'' means an individual's first name or first initial and last name in combination with any one or more of the following data elements, when either the name or the data elements are not encrypted: (1) Social security number; (2) driver's license number or California Identification Card number; (3) Account number, credit or debit card number, in combination with any required security code access code, or password that would permit access to an individual's financial account.

number only if the information accessed also includes any required security code, access code, or password that would permit access to an individual's financial account. Therefore, some commenters asked that the final Guidance clarify that a name and an account number, together, is not sensitive member information unless these elements are combined with other information that permits access to a member's financial account.

The NCUA Board concluded that it would be helpful if credit unions could more easily compare and contrast the definition of ''personal information'' under the CDPA with the definition of ''sensitive information'' under the final Guidance. Therefore, the elements in the definition of sensitive information in the final Guidance are re-ordered and the Board added the elements discussed earlier.

The final Guidance states that sensitive member information means a member's name, address, or telephone number, in conjunction with the member's social security number, driver's license number, account number, credit or debit card number, or a personal identification number or password that would permit access to the member's account. The final Guidance also states that sensitive member information includes any combination of components of member information that would allow someone to log onto or access the member's account, such as user name and password or a password and account number.

Consistent with the Banking Agencies, the NCUA Board declines to adopt the CDPA standard for several reasons. First, for example, under the CDPA, personal information includes a person's name in combination with other data elements. By contrast, the final Guidance treats address and telephone number in the same manner as a member's name, because reverse directories may permit an address or telephone number to be traced back to an individual member.

In addition, under the CDPA, ''personal information'' includes name together with an account number, or credit or debit card number only if the information accessed also includes any required security code, access code, or password that would permit access to an individual's financial account. The NCUA Board notes that a name and account number, alone, is sufficient to create fraudulent checks, or to direct the unauthorized debit of a member's account even without an access code.[23] Further, a name and credit card number may permit unauthorized access to a member's account. Therefore, the final Guidance continues to define a member's name and account number, or credit or debit card number as sensitive member information.

Affected Customers

The NCUA Board also reviewed many interagency comments on the definition of ''affected members'' in the proposed Guidance. Section II.D.3 of the proposed Guidance provided that if the credit union could determine from its logs or other data precisely which members' information was accessed or misused, it may restrict its notification to those individuals. However, if the credit union cannot identify precisely which members were affected, it should notify each member in any group likely to have been affected, such as each member whose information is stored in the group of files in question.

Commenters were concerned that this provision in the proposed Guidance was overly broad. These commenters stated that providing notice to all members in groups likely to be affected would result in many notices that are not helpful. The commenters suggested that the final Guidance narrow the standard for notifying members to only those members whose information has been or is likely to be misused.

The discussion of ''affected members'' has been relocated and is separately set forth following the definition of ''sensitive member information'' in the final Guidance. The discussion of ''affected members'' in the final Guidance states that if a credit union, based upon its investigation, can determine from its logs or other data precisely which member's information has been improperly accessed,[24] it may notify only those members with respect to whom the credit union determines that misuse of their information has occurred or is reasonably possible. However, the final Guidance further notes that there may be situations where the credit union determines that a group of files has been accessed improperly, but is unable to identify which specific member's information has been accessed. If the circumstances of the unauthorized access lead the credit union to determine that misuse of the information contained in the group of files is reasonably possible, it should notify all members in the group. In this way, the final Guidance reduces the number of notices that should be sent.

Examples

The proposed Guidance described several examples of when a credit union should give notice and when NCUA does not expect a credit union to give notice.

NCUA received a number of comments on the examples. Some commenters thought the examples were helpful and suggested that NCUA add more. Other commenters criticized the examples as too broad. Many commenters suggested numerous ways to modify and clarify the examples.

Since the examples in the proposed Guidance led to interpretive questions, rather than interpretive clarity, the NCUA Board concluded that it is not particularly helpful to offer examples of when notice is and is not expected. In addition, the Board believes that the standard for notice itself has been clarified and examples are no longer necessary. Therefore, there are no examples in the final Guidance.

Content of Member Notice

NCUA received many comments on the discussion of the content of member notice located in section II.D.3.b of the proposed Guidance. The proposed Guidance stated that a notice should describe the incident in general terms and the member's information that was the subject of unauthorized access or use. It stated that the notice should also include a number that members can call for further information and assistance, remind members of the need to remain vigilant over the next 12 to 24 months, and recommend that members promptly report incidents of suspected identity theft. The proposed Guidance described several ''key elements'' that a notice should contain. It also provided a number of ''optional elements'' namely, examples of additional assistance that financial institutions have offered.

Some commenters agreed that the proposed Guidance sufficiently addressed most of the key elements necessary for an effective notice. However, many commenters requested greater discretion to determine the content of the notices that credit unions provide to members. Commenters suggested that NCUA make clear that the various items suggested for inclusion in any member notice are

[23] *See, e.g.,* Griff Witte, *Bogus Charges, Unknowingly Paid: FTC Accuses 2 of Raiding 90,000 Bank Accounts in Card Fraud,* Washington Post, May 29, 2004, at E1 (list of names with associated checking account numbers used by bogus company to debit bank accounts without customer authorization).

[24] NCUA notes that system logs may permit a credit union to determine precisely which members' data has been improperly accessed. *See, e.g.,* FFIEC Information Security Booklet, page 64, available at *http://www.ffiec.gov/ffiecinfobase.html*__pages/it__01.htmlinfosec.

suggestions, and that not every item is mandatory in every notice.

Some commenters took issue with the enumerated items in the proposed Guidance identified as key elements that a notice should contain. For example, many commenters asserted that members should not necessarily be encouraged to place fraud alerts with credit bureaus in every circumstance. Some of these commenters noted that not all situations will warrant having a fraud alert posted to the member's credit file, especially if the credit union took appropriate action to render the information accessed worthless. According to these commenters, the consequences of a fraud alert, such as increased obstacles to obtaining credit, may outweigh any benefit. Some commenters also noted that a proliferation of fraud alerts not related to actual fraud would dilute the effectiveness of the alerts.

Other commenters criticized the optional elements in the proposed Guidance. For instance, some commenters stated that a notice should not inform the member about subscription services that provide notification to the member when there is a request for the member's credit report, or offer to subscribe the member to this service, free of charge, for a period of time. These commenters asserted that member notices should not be converted into a marketing opportunity for subscription services provided by consumer credit bureaus. They stated that offering the service may mislead the member into believing that these expensive services are essential. If the service is offered free of charge, a credit union's choice of service could be interpreted as an endorsement for a specific company and its product.

As a result of the Fair and Accurate Credit Transactions Act of 2003, Public Law 108–159, 117 Stat. 1985–86 (the FACT Act), many of the descriptions of ''key elements'' and ''optional elements'' in the proposed Guidance, and comments on these elements, have been superceded. For example, the frequency and circumstances under which a member may obtain a credit report free-of-charge have changed.

The final Guidance continues to specify that a notice should describe the incident in general terms and the member's information that was the subject of unauthorized access or use. It also continues to state that the notice should include a telephone number that members can call for further information and assistance, remind members of the need to remain vigilant over the next 12 to 24 months, and recommend that members promptly report incidents of suspected identity theft. In addition, the final Guidance also states that the notice should generally describe what the credit union has done to protect the members' information from further unauthorized access.

However, the final Guidance no longer distinguishes between certain other ''key'' items that the notice should contain and those that are ''optional.'' The NCUA Board added greater flexibility to this section to accommodate any new protections afforded to consumers that flow from the FACT Act. Instead of distinguishing between items that the notice should contain and those that are optional, a credit union may now select those items that are appropriate under the circumstances, and that are compatible with the FACT Act. Of course, credit unions may incorporate additional information that is not mentioned in the final Guidance, where appropriate.

Coordination With Credit Reporting Agencies

A trade association representing credit reporting agencies commented that its members are extremely concerned about their ability to comply with all of the duties (triggered under the FACT Act) that result from notices financial institutions send to their customers. This commenter strongly recommended that until a financial institution has contacted each nationwide consumer reporting agency to coordinate the timing, content, and staging of notices as well as the placement of fraud alerts, as necessary, a financial institution should refrain from issuing notices suggesting that customers contact nationwide consumer reporting agencies.

The commenter also stated that a financial institution that includes such suggestions in a notice to its customers should work with the credit reporting agencies to purchase the services the financial institution believes are necessary to protect its customers. The commenter stated that the costs of serving the millions of consumers it projects will receive notices under the proposed Guidance cannot be borne solely by the nationwide consumer reporting agencies.

The commenter also noted that the State of California has provided clear guidance in connection with its law requiring notice and also suggested that coordination with consumer reporting agencies is vital to ensure that a consumer can in fact request a file disclosure in a timely manner. This commenter stated that similar guidance at the federal level is essential.

The NCUA Board believes that the final Guidance addresses this commenter's concerns in several ways. First, for the reasons described earlier, the standard for member notice in the final Guidance likely will result in credit unions sending fewer notices. Second, the final Guidance does not require credit unions to send notices suggesting that consumers contact the nationwide consumer reporting agencies, in every case. Credit unions can use their discretion to determine whether such information should be included in a notice.

It is clear, however, that member notice may prompt more consumer contacts with consumer reporting agencies, as predicted by the commenter. Therefore, the final Guidance encourages a credit union that includes in its notice contact information for nationwide consumer reporting agencies to notify the consumer reporting agencies in advance, prior to sending large numbers of such notices. In this way, the reporting agencies will be on notice that they may have to accommodate additional requests for the placement of fraud alerts, where necessary.

Model Notice

Some commenters stated that if mandatory elements are included in the final Guidance, NCUA should develop a model notice that incorporates all the mandated elements yet allows credit unions to incorporate additional information where appropriate. Given the flexibility that credit unions now have to craft a notice tailored to the circumstances of a particular incident, the NCUA Board believes that any single model notice will be of little use. Therefore, the final Guidance does not contain a model notice.

Other Changes Regarding the Content of a Notice

The general discussion of the content of a notice in the final Guidance states that credit unions should give member notice in a ''clear and conspicuous manner.'' In addition, the final Guidance adopts a commenter's suggestion that credit unions should generally describe what the credit union has done to protect a member's information from further unauthorized access so that a member can make decisions regarding the credit union's member service. This addition allows a member to take measures to protect his or her accounts that are not redundant or in conflict with the credit union's actions.

The final Guidance also states that notice should include a telephone

number that members can call for further information and assistance. The NCUA Board added a new footnote to this text, which explains that the credit union should ensure that it has reasonable policies and procedures in place, including trained personnel, to respond appropriately to member inquiries and requests for assistance.

Delivery of Customer Notice

NCUA received numerous suggestions regarding the delivery of member notice located in section II.D.3.a of the proposed Guidance. The proposed Guidance stated that member notice should be timely, clear, and conspicuous, and delivered in any manner that will ensure that the member is likely to receive it. The proposed Guidance provided several examples of proper delivery and stated that a credit union may choose to contact all members affected by telephone or by mail, or for those members who conduct transactions electronically, using electronic notice.

One interagency commenter representing a large bank trade association agreed that this was a correct standard. However, many other commenters recommended that if it costs an institution more than $250,000 to provide notice to customers, if the affected class of persons to be notified exceeds 500,000, or if an incident warrants large distributions of notices, the final Guidance should permit various forms of mass distribution of information, such as by postings on an Internet web page and in national or regional media outlets. Commenters explained that the CDPA contains such a provision.[25]

One commenter suggested that a credit union should only provide notice in response to inquiries. By contrast, other commenters stated that the final Guidance should make clear that general notice on a web site is inadequate and that credit unions should provide individual notice to members.

The NCUA Board determined that the provision in the proposed Guidance that notice be delivered in a ''timely, clear, and conspicuous'' manner already appears elsewhere in the Guidance and is unnecessary here.

The NCUA Board has decided not to include a provision in the final Guidance that permits notice through a posting on the web or through the media in order to provide notice to a specific number of members or where the cost of notice to individual members would exceed a specific dollar amount. The Board believes that the thresholds suggested by commenters would not be appropriate in every case, especially in connection with incidents involving smaller institutions. Therefore, the final Guidance states that member notice should be delivered in any manner that is designed to ensure that a member can reasonably be expected to receive it. This standard places the responsibility on the credit union to select a method to deliver notice that is designed to ensure that a member is likely to receive notice.

The final Guidance also provides examples of proper delivery, noting that a credit union may choose to contact all members affected by telephone or by mail, or by electronic mail for those members for whom it has a valid e-mail address and who have agreed to receive electronic communications from the credit union. Some commenters questioned the effect of other laws on the proposed Guidance. A few commenters noted that electronic notice should conform to the requirements of the Electronic Signatures in Global and National Commerce Act (E-Sign Act), 15 U.S.C. 7001 *et seq.* The final Guidance does not discuss a credit union's obligations under the E-Sign Act. The NCUA Board notes that the final Guidance specifically contemplates that a credit union may give notice electronically or by telephone. There is no requirement that notice be provided in writing. Therefore, the final Guidance does not trigger any consent requirements under the E-Sign Act.[26]

Still other commenters requested clarification that a telephone call made to a member for purposes of complying with the final Guidance is for ''emergency purposes'' under the Telephone Consumer Protection Act, 47 U.S.C. 227 (TCPA). These commenters noted that this is important because under the TCPA and its implementing regulation,[27] it is unlawful to initiate a telephone call to any residential phone line using an artificial or prerecorded voice to deliver a message, without the prior express consent of the called party, unless such call is for ''emergency purposes.''

The final Guidance does not address the TCPA, because the TCPA is interpreted by the Federal Communications Commission (FCC), and the FCC has not yet taken a position on this issue.[28]

V. Effective date

Many commenters suggested that NCUA include a transition period to allow adequate time for credit unions to implement the final Guidance. In accordance with applicable federal law, the final amendment to Part 748 is effective thirty days after publication in the **Federal Register**.

In addition, given the comments received, the NCUA Board recognizes that not every credit union currently has a response program that is consistent with the final Guidance. The Board expects these credit unions to implement the final Guidance as soon as possible. However, the Board appreciates that some credit unions may need additional time to develop new compliance procedures, modify systems, and train staff in order to implement an adequate response program. The NCUA Board will take into account the good faith efforts made by each credit union to develop a response program that is consistent with the final Guidance, together with all other relevant circumstances, when examining the adequacy of a credit union's information security program.

VII. Impact of Guidance

The NCUA Board invited comment on the potential burden associated with the member notice provisions for credit unions implementing the proposed Guidance. The Board also asked for information about the anticipated burden that may arise from the questions posed by members who receive the notices. In addition, the proposed Guidance asked whether NCUA should consider how the burden

[25] *See* CAL. CIV. CODE § 1798.82(g)(3) (West 2005).

[26] Under the E-Sign Act, if a statute, regulation, or other rule of law *requires* that information be provided or made available to a consumer in writing, certain procedures apply. *See* 15 U.S.C. 7001(c).

[27] 47 CFR 64.1200.

[28] NCUA notes, however, that the TCPA and its implementing regulations generally exempt calls made to any person with whom the caller has an established business relationship at the time the call is made. *See, e.g.,* 47 CFR 64.1200(a)(1)(iv). Thus, the TCPA would not appear to prohibit a credit union's telephone calls to its own members. In addition, the FCC's regulations state that the phrase for ''emergency purposes'' means calls made necessary in any situation affecting the health and safety of consumers. 47 CFR 64.1200(f)(2). *See also* FCC Report and Order adopting rules and regulations implementing the TCPA, October 16, 1992, available at *http://www.fcc.gov/cgb/donotcall/,* paragraph 51 (calls from utilites to notify customers of service outages, and to warn customers of discontinuance of service are included within the exemption for emergencies). Credit unions will give members notice under the final Guidance for a public safety purpose, namely, to permit their members to protect themselves where their sensitive information is likely to be misused, example, to facilitate identity theft. Therefore, the NCUA Board believes that the exemption for emergency purposes likely would include member notice that is provided by telephone using an artificial or prerecorded voice message call.

may vary depending upon the size and complexity of a credit union. The Board also asked for information about the amount of burden, if any, the proposed Guidance would impose on service providers.

Although many commenters representing credit unions stated that they already have a response program in place, they also noted that NCUA had underestimated the burden that would be imposed on credit unions and their members by the proposed Guidance. Some commenters stated that the proposed Guidance would require greater time, expenditure, and documentation for audit and compliance purposes. Other commenters stated that the costs of providing notice and requiring a sufficient number of appropriately trained employees to be available to answer member inquiries and provide assistance could be substantial. Other commenters stated that the Agencies failed to adequately consider the burden to members and customers who begin to receive numerous notices of ''unauthorized access'' to their data. They stated that the stress to members of having to change account numbers, change passwords, and monitor their credit reports would be enormous and could be unnecessary because the standard in the proposed Guidance would require notice when information subject to unauthorized access might be, but would not necessarily be, misused.

Some commenters maintained that the proposed Guidance would be especially burdensome for small credit unions, which one commenter asserted are the lowest risk targets. These commenters stated that the most burdensome elements of the proposed Guidance would be creating a general policy, establishing procedures and training staff. They added that developing and implementing new procedures for determining when, where and how to provide notice and procedures for monitoring accounts would also be burdensome.

Finally, a trade association commenter stated that the notice requirements in the proposed Guidance would impose a large burden on the nationwide consumer reporting agencies, over which they have no control and from which they have no means of recouping costs.

The NCUA Board has addressed the burdens identified by commenters as follows. First, the Board eliminated many of the more prescriptive elements of the response program described in the proposed Guidance. The final Guidance states that a credit union's response program should be risk-based. It lists a number of components that the program should contain.

Second, final Guidance does not detail the steps that a credit union should take to contain and control a security incident to prevent further unauthorized access to or use of member information. It also does not state that a credit union should secure all accounts that can be accessed using the same account number or name and password combination until such time as the credit union and the member can agree on a course of action. Instead, the final Guidance leaves such measures to the discretion of the credit union and gives examples of the steps that a credit union should consider, such as monitoring, freezing, or closing affected accounts. Thus, under the final Guidance a small credit union may choose to close an affected account, rather than monitoring the account, an element of the proposed Guidance that smaller credit unions identified as potentially very costly.

Third, though the final Guidance still states that notification to regulators should be a part of a credit union's response program, it states that notice should only be given when the credit union becomes aware of an incident of unauthorized access to or use of ''sensitive'' member information. This standard should result in fewer instances of notice to the regulators than under the proposed Guidance. The final Guidance also makes clear that when the security incident involves a service provider, the credit union may authorize the service provider to notify the credit union's regulator.

Fourth, the standard of notice to members also has been modified to be less burdensome to credit unions and their members. The NCUA Board believes that under this new standard, members will be less likely to be alarmed needlessly, and credit unions will no longer be asked to prove a negative—namely, that misuse of information is unlikely to occur. In addition, the Board also has provided credit unions with greater discretion to determine what should be contained in a notice to members.

The NCUA Board does not believe that there is a basis for exempting small credit unions from the Guidance. For example, many small credit unions outsource functions to large service providers that have been the target of those seeking to misuse member information. Therefore, the Board believes that all credit unions should prepare member response programs including member notification procedures that can be used in the event the credit union determines that misuse of its information about a member has occurred or is reasonably possible. However, as noted above, the Board recognizes that within the framework of the Guidance, a credit union's program will vary depending on the size and complexity of the credit union and the nature and scope of its activities.

Finally, to address comments relating to the potential burden on the nationwide consumer reporting agencies, as noted previously, the Guidance no longer suggests that member notice always include advice to contact the nationwide consumer reporting agencies. The NCUA Board recognizes that not all security breaches warrant such contacts. For example, the Board recognizes that it may not always be in the best interest of a consumer to have a fraud alert placed in the consumer's file because the fraud alert may have an adverse impact on the consumer's ability to obtain credit.

VIII. Regulatory Procedures

Paperwork Reduction Act

Certain provisions of the final Guidance contain ''collection of information'' requirements as defined in the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*) (PRA). An agency may not conduct or sponsor, and a respondent is not required to respond to, an information collection unless it displays a currently valid Office of Management and Budget (OMB) control number.

The NCUA Board requested comment on a proposed information collection as part of the notice requesting comment on the proposed Guidance. An analysis of the comments related to paperwork burden and commenters' recommendations is provided below. The NCUA submitted its proposed information collection to OMB for review and approval and the collections have been approved.

The NCUA Board has reconsidered the burden estimates published in the Proposed Guidance in light of the comments received asserting that the paperwork burden associated with the information collection were underestimated, and in light of measures taken to reduce burden in this final Guidance. The Board agreed to increase the estimate for the time it will take a credit union to develop notices and determine which members should be notified. However, revisions incorporated into the final Guidance will result in the preparation and issuance of fewer notices than was originally estimated. Therefore, the net change in burden is due to the rounding of numbers. A discussion of the

comments received follows the revised estimates.

New Estimates

Number of Respondents: 9,014.
Estimated Time per Response:

Developing Notices: 24 hours x 9,014 = 216,336 hours.

Notifying Customers: 29 hours x 153 = 4,437 hours.

Total Estimated Annual Burden = 220,773 hours .

Discussion of Comments

The information collection in the proposed Guidance stated that credit unions should: (1) Develop notices to members; and (2) determine which members should receive the notices and send the notices to members. The NCUA Board and the Banking Agencies received various comments regarding the burden estimates, including the estimated time per response and the number of recordkeepers involved.

Some commenters stated that the burden estimates of twenty hours to develop and produce notices and three days to determine which members should receive notice in the proposed Guidance were too low. These commenters stated that the Guidance should include language indicating that a credit union be given as much time as necessary to determine the scope of an incident and examine which members may be affected. One of these commenters stated that ten business days, as recommended by the California Department of Consumer Affairs Office of Privacy Protection, should provide a credit union with a known safe harbor to complete the steps described lest regulated entities be subject to inconsistent notification deadlines from the same incident.

These commenters misunderstood the meaning of PRA burden estimates. PRA burden estimates are judgments by the NCUA regarding the length of time that it would take credit unions to comply with information collection requirements. These estimates do not impose a deadline upon credit unions to complete a requirement within a specific period of time.

The final Guidance states that a credit union should notify members ''as soon as possible'' after an investigation leads it to conclude that misuse of member information has occurred or is reasonably possible. It also states that notification may be delayed at the written request of law enforcement.

The cost of disclosing information is considered part of the burden of an information collection. 5 CFR 1320.3(b)(1)(ix). Many commenters stated that the Agencies had underestimated the cost associated with disclosing security incidents to members pursuant to the proposed Guidance. However, these commenters did not distinguish between the usual and customary costs of doing business and the costs of the disclosures associated with the information collection in the proposed Guidance.

For example, one commenter stated that the Agencies' estimate did not include $0.60 per member for a one-page letter, envelope, and first class postage; the customer service time, handling the enormous number of calls from customers who receive notice; or the costs associated with closing or reopening accounts, printing new checks or embossing new cards. This commenter stated that printing and mailing costs, alone, for one notice to its customer database, at current postal rates, would be at least $500,000.

Some of the costs mentioned in this comment are non-labor costs associated with providing disclosures. Both NCUA and the Banking Agencies assumed that non-labor costs associated with the disclosures would be negligible, because institutions already have in place well-developed systems for providing disclosures to their customers. This comment and any other comments received regarding the Agencies' assumptions about non-labor costs will be taken into account in any future estimate of the burden for this collection.

Other costs mentioned in this comment, such as the cost of customer service time, printing checks, and embossing cards, are costs that the institution would incur regardless of the implementation of the final Guidance. These costs are not associated with an information collection, and, therefore, have not been factored into the NCUA Board's cost estimates.

In addition, the estimates in this comment are based on the assumption that notice should always be provided by mail. However, the final Guidance states that credit unions should deliver member notice in any manner designed to ensure that a member can reasonably be expected to receive it, such as by telephone, mail, or electronically for those members for whom it has a valid e-mail address and who have agreed to receive communications electronically. The NCUA Board assumes that given this flexibility, credit unions may not necessarily choose to mail notices in every case, but may choose less expensive methods of delivery that ensure members will reasonably be expected to receive notice.

Another commenter concerned about the burdens imposed on consumer reporting agencies provided an example of a security breach involving a single company from which identifying information was stolen from about 500,000 military families. Among other things, the company's notice to its customers advised them to contact the nationwide consumer reporting agencies. The commenter stated that the nationwide consumer reporting agencies spent approximately $1.5 million per company, handling approximately 365,000 inquiries from the company's customers.

The final Guidance contains a number of changes that will diminish the costs identified by these commenters. First, the standard for notification in the final Guidance likely will result in fewer notices. In addition, the final Guidance no longer states that all notices should advise members to contact the nationwide consumer reporting agencies. Therefore, the NCUA Board estimates do not factor in the costs to the reporting agencies.

Regulatory Flexibility Act

The Regulatory Flexibility Act (5 U.S.C. 601–612) (RFA) requires an agency to prepare a final regulatory flexibility analysis whenever the agency promulgates a final rule that may have a significant economic impact on a substantial number of small entities. As required by the RFA, the NCUA Board prepared and published an initial regulatory flexibility analysis at the time it issued the proposed rule amending § 748.0 and the proposed guidance in the form of Appendix B. This section contains the Board's final regulatory flexibility analysis.

A. Need for and Objectives of the Rule

As more fully discussed in the preamble to the final rule, section 501 of GLBA requires NCUA to publish standards for federally insured credit unions relating to their security programs to: (1) Insure the security and confidentiality of customer records and information; (2) protect against any anticipated threats or hazards to the security or integrity of such records; and (3) protect against unauthorized access to or use of such records or information that could result in substantial harm or inconvenience to any customer. The final rule establishes that federally insured credit unions must include a response program as an element of their security program, and the final Guidance describes the features that a response program should contain to ensure that breaches of security do not

result in harm or inconvenience to members.

B. Summary of Issues Raised by Public Comment

The NCUA Board received no public comment specifically responding to the initial regulatory flexibility analysis contained in the proposed rule. All federally insured credit unions, regardless of size, are subject to GLBA and the rule. The Board believes the changes in the final Guidance, including the standard for determining when to provide notice to members and the increased emphasis on risk-based factors, make the final Guidance easier for smaller credit unions to use. For example, smaller credit unions that offer a relatively less sophisticated array of products and services present a relatively lower level of risk of security breach affecting member information. For these credit unions, the final Guidance contemplates a relatively less comprehensive response program, commensurate with the relatively lower level of risk. Another example of flexibility benefiting smaller institutions relates to service providers. The final Guidance contemplates that, where a service provider maintains member information, a credit union may delegate authority to that service provider to notify members affected by a security breach on its behalf. The Board believes this flexibility is of particular benefit to smaller credit unions, which typically use service providers and may not have the resources to provide timely and effective notice themselves.

C. Consideration of Alternatives

All federally insured credit unions are already required by GLBA and existing regulation to develop and implement a security program. Development of an effective program involves: Assessing risks to member information; establishing policies, procedures, and training to control risks; testing the program's effectiveness; and managing and monitoring service providers. The NCUA Board believes establishing an information security program is a sound business practice for all credit unions and is already addressed by existing supervisory procedures. The final rule requires that security programs include a provision for appropriate responses to incidents involving a breach of information integrity. Consistent with the position taken by the Banking Agencies, the Board views this as a fundamental element of any information security program. Members of smaller credit unions are entitled to expect their personal financial information will be protected and that their credit union will respond appropriately and effectively to any breach of security. Ultimately, there is no alternative to requiring that all credit unions include an effective response program as an element of their security programs.

Nevertheless, the Board specifically solicited comment in the proposed rule on any significant alternatives, consistent with GLBA, that would minimize the impact on small credit unions. As more fully discussed in the preamble to the final rule and in the preceding section of this analysis, the final Guidance provides substantial flexibility so that any credit union, regardless of size, may adopt an information security program tailored to its individual needs.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The final rule would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Public Law 105–277, 112 Stat. 2681 (1998).

Agency Regulatory Goal

NCUA's goal is to promulgate clear and understandable regulations that impose minimal regulatory burden. We invite your comments on whether the final rule is understandable and minimally intrusive.

List of Subjects in 12 CFR Part 748

Credit unions, Crime, Currency, Reporting and recordkeeping requirements and Security measures.

By the National Credit Union Administration Board on April 14, 2005.

Mary F. Rupp,

Secretary of the Board.

■ For reasons set forth in the preamble, the NCUA Board proposes to amend 12 CFR 748 as follows:

PART 748—SECURITY PROGRAM, REPORT OF CRIME AND CATASTROPHIC ACT AND BANK SECRECY ACT COMPLIANCE

■ 1.The authority citation for part 748 reads as follows:

Authority: 12 U.S.C. 1766(a), 1786(Q); 15 U.S.C. 6801 and 6805(b); 31 U.S.C. 5311 and 5318.

■ 2.In § 748.0 revise paragraph (b) to read as follows:

§ 748.0 Security program.

* * * * * *

(b) The security program will be designed to:

(1) Protect each credit union office from robberies, burglaries, larcenies, and embezzlement;

(2) Ensure the security and confidentiality of member records, protect against the anticipated threats or hazards to the security or integrity of such records, and protect against unauthorized access to or use of such records that could result in substantial harm or serious inconvenience to a member;

(3) Respond to incidents of unauthorized access to or use of member information that could result in substantial harm or serious inconvenience to a member;

(4) Assist in the identification of persons who commit or attempt such actions and crimes, and

(5) Prevent destruction of vital records, as defined in 12 CFR part 749.

■ 3. Add Appendix B to read as follows:

Appendix B to Part 748—Guidance on Response Programs for Unauthorized Access to Member Information and Member Notice

I. Background

This Guidance in the form of Appendix B to NCUA's Security Program, Report of Crime and Catastrophic Act and Bank Secrecy Act Compliance regulation,[29] interprets section 501(b) of the Gramm-Leach-Bliley Act (''GLBA'') and describes response programs, including member notification procedures, that a federally insured credit union should develop and implement to address unauthorized access to or use of member information that could result in substantial harm or inconvenience to a member. The scope of, and definitions of terms used in,

[29] 12 CFR Part 748.

this Guidance are identical to those of Appendix A to Part 748 (Appendix A). For example, the term ''member information'' is the same term used in Appendix A, and means any record containing nonpublic personal information about a member, whether in paper, electronic, or other form, maintained by or on behalf of the credit union.

A. Security Guidelines

Section 501(b) of the GLBA required the NCUA to establish appropriate standards for credit unions subject to its jurisdiction that include administrative, technical, and physical safeguards to protect the security and confidentiality of member information. Accordingly, the NCUA amended Part 748 of its rules to require credit unions to develop appropriate security programs, and issued Appendix A, reflecting its expectation that every federally insured credit union would develop an information security program designed to:

1. Ensure the security and confidentiality of member information;
2. Protect against any anticipated threats or hazards to the security or integrity of such information; and
3. Protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any member.

B. Risk Assessment and Controls

1. Appendix A directs every credit union to assess the following risks, among others, when developing its information security program:

a. Reasonably foreseeable internal and external threats that could result in unauthorized disclosure, misuse, alteration, or destruction of member information or member information systems;

b. The likelihood and potential damage of threats, taking into consideration the sensitivity of member information; and

c. The sufficiency of policies, procedures, member information systems, and other arrangements in place to control risks.[30]

2. Following the assessment of these risks, Appendix A directs a credit union to design a program to address the identified risks. The particular security measures a credit union should adopt will depend upon the risks presented by the complexity and scope of its business. At a minimum, the credit union should consider the specific security measures enumerated in Appendix A,[31] and adopt those that are appropriate for the credit union, including:

a. Access controls on member information systems, including controls to authenticate and permit access only to authorized individuals and controls to prevent employees from providing member information to unauthorized individuals who may seek to obtain this information through fraudulent means;

b. Background checks for employees with responsibilities for access to member information; and

c. Response programs that specify actions to be taken when the credit union suspects or detects that unauthorized individuals have gained access to member information systems, including appropriate reports to regulatory and law enforcement agencies.[32]

C. Service Providers

Appendix A advises every credit union to require its service providers by contract to implement appropriate measures designed to protect against unauthorized access to or use of member information that could result in substantial harm or inconvenience to any member.[33]

II. Response Program

i. Millions of Americans, throughout the country, have been victims of identity theft.[34] Identity thieves misuse personal information they obtain from a number of sources, including credit unions, to perpetrate identity theft. Therefore, credit unions should take preventative measures to safeguard member information against such attempts to gain unauthorized access to the information. For example, credit unions should place access controls on member information systems and conduct background checks for employees who are authorized to access member information.[35] However, every credit union should also develop and implement a risk-based response program to address incidents of unauthorized access to member information in member information systems that occur nonetheless.[36] A response program should be a key part of a credit union's information security program.[37] The program should be appropriate to the size and complexity of the credit union and the nature and scope of its activities.

ii. In addition, each credit union should be able to address incidents of unauthorized access to member information in member information systems maintained by its domestic and foreign service providers. Therefore, consistent with the obligations in this Guidance that relate to these arrangements, and with existing guidance on this topic issued by the NCUA,[38] a credit union's contract with its service provider should require the service provider to take appropriate actions to address incidents of unauthorized access to or use of the credit union's member information, including notification of the credit union as soon as possible of any such incident, to enable the institution to expeditiously implement its response program.

A. Components of a Response Program

1. At a minimum, a credit union's response program should contain procedures for the following:

a. Assessing the nature and scope of an incident, and identifying what member information systems and types of member information have been accessed or misused;

b. Notifying the appropriate NCUA Regional Director, and, in the case of state-chartered credit unions, its applicable state supervisory authority, as soon as possible when the credit union becomes aware of an incident involving unauthorized access to or use of sensitive member information as defined below.

c. Consistent with the NCUA's Suspicious Activity Report (''SAR'') regulations,[39] notifying appropriate law enforcement authorities, in addition to filing a timely SAR in situations involving Federal criminal violations requiring immediate attention, such as when a reportable violation is ongoing;

d. Taking appropriate steps to contain and control the incident to prevent further unauthorized access to or use of member information, for example, by monitoring, freezing, or closing affected accounts, while preserving records and other evidence;[40] and

e. Notifying members when warranted.

2. Where an incident of unauthorized access to member information involves member information systems maintained by a credit union's service providers, it is the responsibility of the credit union to notify the credit union's members and regulator. However, a credit union may authorize or contract with its service provider to notify the credit union's members or regulators on its behalf.

III. Member Notice

i. Credit unions have an affirmative duty to protect their members' information against

[30] *See* 12 CFR Part 748, Appendix A, Paragraph III.B.

[31] *See* Appendix A, paragraph III.C.

[32] *See* Appendix A, Paragraph III.C.

[33] *See* Appendix A, Paragraph III.B. and III.D. Further, the NCUA notes that, in addition to contractual obligations to a credit union, a service provider may be required to implement its own comprehensive information security program in accordance with the Safeguards Rule promulgated by the Federal Trade Commission (ldquo;FTC''), 12 CFR Part 314.

[34] The FTC estimates that nearly 10 million Americans discovered they were victims of some form of identify theft in 2002. *See* The Federal Trade Commission, *Identity Theft Survey Report,* (September 2003), available at *http://www.ftc.gov/os/2003/09synovatereport.pdf.*

[35] Credit unions should also conduct background checks of employees to ensure that the credit union does not violate 12 U.S.C. 1785(d), which prohibits a credit union from hiring an individual convicted of certain criminal offenses or who is subject to a prohibition order under 12 U.S.C. 1786(g).

[36] Under 12 CFR Part 748, Appendix A, a credit union's *member information systems* consists of all of the methods used to access, collect, store, use, transmit, protect, or dispose of member information, including the systems maintained by its service providers. *See* 12 CFR Part 748, Appendix A, Paragraph I.C.2.d.

[37] *See* FFIEC Information Technology Examination Handbook, Information Security Booklet, (December, 2002), available at *http://www.ffiec.gov/ffiecinfobase/html—pages/it—01.htm1●infosec,* for additional guidance on preventing, detecting, and responding to intrusions into financial institution computer systems.

[38] *See* FFIEC Information Technology Examination Handbook, Outsourcing Technology Services Booklet, (June 2004), available at *http://www.ffiec.gov/ffiecinfobase/html—pages/it—01.htm1●outscouring* for additional guidance on managing outsourced relationships.

[39] A credit union's obligation to file a SAR is set out in the NCUA's SAR regulations and guidance. *See* 12 CFR Part 748.1(c); NCUA Letter to Credit Unions No. 04–CU–03, Suspiciouis Activity Reports, March 2004; NCUA Regulatory Alert No. 04–RA–01, The Suspicious Activity Report (SAR) Activity Review—Trends, Tips, & Isues, Issue 6, November 2003, February 2004.

[40] *See* FFIEC Information Technology Examination Handbook, Information Security Booklet, (December 2002), pp. 68–74.

unauthorized access or use. Notifying members of a security incident involving the unauthorized access or use of the member's information in accordance with the standard set forth below is a key part of that duty.

ii. Timely notification of members is important to manage a credit union's reputation risk. Effective notice also may reduce a credit union's legal risk, assist in maintaining good member relations, and enable the credit union's members to take steps to protect themselves against the consequences of identity theft. When member notification is warranted, a credit union may not forgo notifying its customers of an incident because the credit union believes that it may be potentially embarrassed or inconvenienced by doing so.

A. Standard for Providing Notice

When a credit union becomes aware of an incident of unauthorized access to sensitive member information, the credit union should conduct a reasonable investigation to promptly determine the likelihood that the information has been or will be misused. If the credit union determines that misuse of its information about a member has occurred or is reasonably possible, it should notify the affected member as soon as possible. Member notice may be delayed if an appropriate law enforcement agency determines that notification will interfere with a criminal investigation and provides the credit union with a written request for the delay. However, the credit union should notify its members as soon as notification will no longer interfere with the investigation.

1. Sensitive Member Information

Under Part 748.0, a credit union must protect against unauthorized access to or use of member information that could result in substantial harm or inconvenience to any member. Substantial harm or inconvenience is most likely to result from improper access to *sensitive member information* because this type of information is most likely to be misused, as in the commission of identity theft.

For purposes of this Guidance, sensitive member information means a member's name, address, or telephone number, in conjunction with the member's social security number, driver's license number, account number, credit or debit card number, or a personal identification number or password that would permit access to the member's account. *Sensitive member information* also includes any combination of components of member information that would allow someone to log onto or access the member's account, such as user name and password or password and account number.

2. Affected Members

If a credit union, based upon its investigation, can determine from its logs or other data precisely which members' information has been improperly accessed, it may limit notification to those members with regard to whom the credit union determines that misuse of their information has occurred or is reasonably possible. However, there may be situations where the credit union determines that a group of files has been accessed improperly, but is unable to identify which specific member's information has been accessed. If the circumstances of the unauthorized access lead the credit union to determine that misuse of the information is reasonably possible, it should notify all members in the group.

B. Content of Member Notice

1. Member notice should be given in a clear and conspicuous manner. The notice should describe the incident in general terms and the type of member information that was the subject of unauthorized access or use. It also should generally describe what the credit union has done to protect the members' information from further unauthorized access. In addition, it should include a telephone number that members can call for further information and assistance.[41] The notice also should remind members of the need to remain vigilant over the next twelve to twenty-four months, and to promptly report incidents of suspected identity theft to the credit union. The notice should include the following additional items, when appropriate:

a. A recommendation that the member review account statements and immediately report any suspicious activity to the credit union;

b. A description of fraud alerts and an explanation of how the member may place a fraud alert in the member's consumer reports to put the member's creditors on notice that the member may be a victim of fraud;

c. A recommendation that the member periodically obtain credit reports from each nationwide credit reporting agency and have information relating to fraudulent transactions deleted;

d. An explanation of how the member may obtain a credit report free of charge; and

e. Information about the availability of the FTC's online guidance regarding steps a consumer can take to protect against identity theft. The notice should encourage the member to report any incidents of identity theft to the FTC, and should provide the FTC's Web site address and toll-free telephone number that members may use to obtain the identity theft guidance and report suspected incidents of identity theft.[42]

2. NCUA encourages credit unions to notify the nationwide consumer reporting agencies prior to sending notices to a large number of members that include contact information for the reporting agencies.

C. Delivery of Member Notice

Member notice should be delivered in any manner designed to ensure that a member can reasonably be expected to receive it. For example, the credit union may choose to contact all members affected by telephone or by mail, or by electronic mail for those members for whom it has a valid e-mail address and who have agreed to receive communications electronically.

[FR Doc. 05–7836 Filed 4–29–05; 8:45 am]

BILLING CODE 7535–01–P

[41] The credit union should, therefore, ensure that it has reasonable policies and procedures in place, including trained personnel, to respond appropriately to member inquiries and requests for assistance.

[42] Currently, the FTC Web site for the ID Theft brochure and the FTC Hotline phone number are *http://www.ftc.gov/idtheft* and 1–877–IDTHEFT. The credit union may also refer members to any materials developed pursuant to section 15(1)(b) of the FACT Act (educational materials developed by the FTC to teach the public how to prevent identity theft).

DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

12 CFR Part 41

[Docket No. 05–10]

RIN 1557–AC85

FEDERAL RESERVE SYSTEM

12 CFR Parts 222 and 232

[Regulation V and FF; Docket No. R–1188]

FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 334

RIN 3064–AC81

DEPARTMENT OF THE TREASURY

Office of Thrift Supervision

12 CFR Part 571

[No. 2005–16]

RIN 1550–AB88

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 717

Fair Credit Reporting Medical Information Regulations

AGENCIES: Office of the Comptroller of the Currency, Treasury (OCC); Board of Governors of the Federal Reserve System (Board); Federal Deposit Insurance Corporation (FDIC); Office of Thrift Supervision, Treasury (OTS); National Credit Union Administration (NCUA).

ACTION: Interim final rules; request for public comments.

SUMMARY: The OCC, Board, FDIC, OTS, and NCUA (Agencies) are publishing interim final rules to implement section 411 of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act). The interim final rules create exceptions to the statute's general prohibition on creditors obtaining or using medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit for all creditors. The exceptions permit creditors to obtain or use medical information in connection with credit eligibility determinations where necessary and appropriate for legitimate purposes, consistent with the Congressional intent to restrict the use of medical information for inappropriate purposes. The interim final rules also create limited exceptions to permit affiliates to share medical information with each other without becoming consumer reporting agencies.

DATES: This interim final rule is effective March 7, 2006. Comments must be received by July 11, 2005.

ADDRESSES: Comments should be directed to:

OCC: You should include OCC and Docket Number 05–10 in your comment. You may submit comments by any of the following methods:

- *Federal eRulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.
- *OCC Web Site: http://www.occ.treas.gov.* Click on ''Contact the OCC,'' scroll down and click on ''Comments on proposed regulations.''
- *E-mail Address: regs.comments@occ.treas.gov.*
- *Fax:* (202) 874–4448.
- *Mail:* Office of the Comptroller of the Currency, 250 E Street, SW., Mail Stop 1–5, Washington, DC 20219.
- *Hand Delivery/Courier:* 250 E Street, SW., Attn: Public Information Room, Mail Stop 1–5, Washington, DC 20219.

Instructions: All submissions received must include the agency name (OCC) and docket number or Regulatory Information Number (RIN) for this rulemaking. In general, OCC will enter all comments received into the docket without change, including any business or personal information that you provide. You may review comments and other related materials by any of the following methods:

- *Viewing Comments Personally:* You may personally inspect and photocopy comments at the OCC's Public Information Room, 250 E Street, SW., Washington, DC. You can make an appointment to inspect comments by calling (202) 874–5043.
- *Viewing Comments Electronically:* You may request e-mail or CD–ROM copies of comments that the OCC has received by contacting the OCC's Public Information Room at *regs.comments@occ.treas.gov.*
- *Docket:* You may also request available background documents and project summaries using the methods described above.

Board: You may submit comments, identified by Docket No. R–1188, by any of the following methods:

- *Agency Web Site: http://www.federalreserve.gov.* Follow the instructions for submitting comments at *http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm.*
- *Federal eRulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.
- *E-mail: regs.comments@federalreserve.gov.* Include docket number in the subject line of the message.
- *Fax:* 202/452–3819 or 202/452–3102.
- *Mail:* Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments are available from the Board's Web site at *http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm* as submitted, except as necessary for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper in Room MP–500 of the Board's Martin Building (20th and C Streets, NW.) between 9 a.m. and 5 p.m. on weekdays.

FDIC: You may submit comments, identified by RIN number by any of the following methods:

- *Agency Web Site: http://www.fdic.gov/regulations/laws/federal/propose.html.* Follow instructions for submitting comments on the Agency Web Site.
- *E-Mail: Comments@FDIC.gov.* Include the RIN number in the subject line of the message.
- *Mail:* Robert E. Feldman, Executive Secretary, Attention: Comments, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.
- *Hand Delivery/Courier:* Guard station at the rear of the 550 17th Street Building (located on F Street) on business days between 7 a.m. and 5 p.m.
- *Instructions:* All submissions received must include the agency name and RIN for this rulemaking. All comments received will be posted without change to *http://www.fdic.gov/regulations/laws/federal/propose.html* including any personal information provided.

OTS: You may submit comments, identified by number 2005–16, by any of the following methods:

- *Federal eRulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.
- *E-mail Address: regs.comments@ots.treas.gov.* Please include number 2005–16 in the subject line of the message and include your name and telephone number in the message.
- *Fax:* (202) 906–6518.
- *Mail:* Regulation Comments, Chief Counsel's Office, Office of Thrift

Supervision, 1700 G Street, NW., Washington, DC 20552, Attention: No. 2005–16.

• *Hand Delivery/Courier:* Guard's Desk, East Lobby Entrance, 1700 G Street, NW., from 9 a.m. to 4 p.m. on business days, Attention: Regulation Comments, Chief Counsel's Office, Attention: No. 2005–16.

Instructions: All submissions received must include the agency name and docket number or Regulatory Information Number (RIN) for this rulemaking. All comments received will be posted without change to the OTS Internet Site at *http://www.ots.treas.gov/pagehtml.cfm?catNumber=67&an=1,* including any personal information provided.

Docket: For access to the docket to read background documents or comments received, go to *http://www.ots.treas.gov/pagehtml.cfm?catNumber=67&an=1.* In addition, you may inspect comments at the Public Reading Room, 1700 G Street, NW., by appointment. To make an appointment for access, call (202) 906–5922, send an e-mail to *public.info@ots.treas.gov,* or send a facsimile transmission to (202) 906–7755. (Prior notice identifying the materials you will be requesting will assist us in serving you.) We schedule appointments on business days between 10 a.m. and 4 p.m. In most cases, appointments will be available the next business day following the date we receive a request.

NCUA: You may submit comments by any of the following methods (Please send comments by one method only):

• *Federal eRulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.

• *NCUA Web Site: http://www.ncua.gov/RegulationsOpinionsLaws/proposed*__regs/proposed__regs.html. Follow the instructions for submitting comments.

• *E-mail:* Address to *regcomments@ncua.gov.* Include ''[Your name] Comments on Interim Final Rule Part 717, Fair Credit Reporting—Medical Information'' in the e-mail subject line.

• *Fax:* (703) 518–6319. Use the subject line described above for e-mail.

• *Mail:* Address to Mary Rupp, Secretary of the Board, National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428.

• *Hand Delivery/Courier:* Address to Mary Rupp, Secretary of the Board, National Credit Union Administration. Deliver to guard station in the lobby of 1775 Duke Street, Alexandria, Virginia 22314–3428, on business days between 8 a.m. and 5 p.m.

All public comments are available on the agency's Web site at *http://www.ncua.gov/RegulationsOpinionsLaws/comments* as submitted, except as may not be possible for technical reasons. Public comments will not be edited to remove any identifying or contact information. Paper copies of comments may be inspected in NCUA's law library, at 1775 Duke Street, Alexandria, Virginia 22314, by appointment weekdays between 9 a.m. and 3 p.m. To make an appointment, call (703) 518–6546 or send an e-mail to *OGCMail@ncua.gov.*

FOR FURTHER INFORMATION CONTACT:

OCC: Amy Friend, Assistant Chief Counsel, (202) 874–5200; Michael Bylsma, Director, or Stephen Van Meter, Assistant Director, Community and Consumer Law, (202) 874–5750; Patrick T. Tierney, Senior Attorney, Legislative and Regulatory Activities Division, (202) 874–5090; or Carol Turner, Compliance Specialist, Compliance Department, (202) 874–4858, Office of the Comptroller of the Currency, 250 E Street, SW., Washington, DC 20219.

Board: David A. Stein, Counsel; Minh-Duc T. Le, Ky Tran-Trong, or Krista P. DeLargy, Senior Attorneys, Division of Consumer and Community Affairs, (202) 452–3667 or (202) 452–2412; or Andrew Miller, Counsel, Legal Division, (202) 452–3428, Board of Governors of the Federal Reserve System, 20th and C Streets, NW., Washington, DC 20551.

FDIC: Richard M. Schwartz, Counsel, Legal Division, (202) 898–7424; David Lafleur, Policy Analyst, (202) 898–6569, or Patricia Cashman, Senior Policy Analyst, Division of Supervision and Consumer Protection, (202) 898–6534, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.

OTS: Elizabeth Baltierra, Program Analyst (Compliance), Compliance Policy, (202) 906–6540; Richard Bennett, Counsel, (202) 906–7409; Judith A. McCormick, Director, Consumer Protection and Specialty Programs, (202) 906–5636, Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552.

NCUA: Regina M. Metz, Staff Attorney, Office of General Counsel, (703) 518–6540, National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314–3428.

SUPPLEMENTARY INFORMATION:

I. Background

The FACT Act became law on December 4, 2003. Pub. L. 108–159, 117 Stat. 1952. In general, the FACT Act amends the Fair Credit Reporting Act (FCRA or Act) to enhance the ability of consumers to combat identity theft, increase the accuracy of consumer reports, and allow consumers to exercise greater control regarding the type and amount of marketing solicitations they receive. Section 411 of the FACT Act generally limits the ability of creditors to obtain or use medical information in connection with credit eligibility determinations, consumer reporting agencies to disclose medical information, and all persons to share medical information and other medical-related information with affiliates.

Section 411(a) of the FACT Act adds a new section 604(g)(1) to the FCRA to restrict the circumstances under which consumer reporting agencies may furnish consumer reports that contain medical information about consumers. Under section 604(g)(1), a consumer reporting agency may not furnish a consumer report that contains medical information about a consumer unless:

(1) The report is furnished in connection with an insurance transaction, and the consumer affirmatively consents to the furnishing of the report;

(2) The report is furnished for employment purposes or in connection with a credit transaction, the information to be furnished is relevant to process or effect the employment or credit transaction, and the consumer provides specific written consent for the furnishing of the report that describes in clear and conspicuous language the use for which the information will be furnished; or

(3) The information to be furnished pertains solely to transactions, accounts, or balances relating to debts arising from the receipt of medical services, products, or devices, where such information, other than account status or amounts, is restricted or reported using codes that do not identify, or do not provide information sufficient to infer, the specific provider or the nature of such services, products, or devices.

Section 411(c) of the FACT Act revises the definition of ''medical information'' in section 603(i) to mean information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to the past, present, or future physical, mental, or behavioral health or condition of an individual, the provision of health care to an individual, or the payment for the provision of health care to an individual. The term ''medical

information'' does not include the age or gender of a consumer, demographic information about the consumer, including a consumer's residence address or e-mail address, or any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy.

Section 411(a) also amends the FCRA by adding new section 604(g)(2) to prohibit creditors from obtaining or using medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit. Section 604(g)(2) contains two independent prohibitions—a prohibition on obtaining medical information and a prohibition on using medical information. The statute contains no prohibition, however, on creditors obtaining or using medical information other than in connection with a determination of the consumer's eligibility, or continued eligibility, for credit. For example, section 604(g)(2) does not prohibit a creditor from obtaining medical information in connection with employment purposes. Nevertheless, a creditor that obtains medical information in connection with employment purposes may not subsequently use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit. Section 604(g)(5)(A) requires the Agencies to prescribe regulations that permit transactions that are determined to be necessary and appropriate to protect legitimate operational, transactional, risk, consumer, and other needs (including administrative verification purposes), consistent with Congressional intent to restrict the use of medical information for inappropriate purposes.

Section 411(b) of the FACT Act adds a new section 603(d)(3) to the FCRA to restrict the sharing of medically related information with affiliates if that information meets the definition of ''consumer report'' in section 603(d)(1) of the FCRA. Specifically, section 603(d)(3) provides that the standard exclusions from the definition of ''consumer report'' contained in section 603(d)(2)—such as sharing transaction or experience information among affiliates or sharing other information among affiliates after notice and an opportunity to opt-out—do not apply if medically related information is disclosed to an affiliate. Medically related information includes medical information, as described above, as well as an individualized list or description based on payment transactions for medical products or services, and an aggregate list of identified consumers based on payment transactions for medical products or services.

Section 604(g)(3), however, provides several exceptions that allow institutions to share medically related information with affiliates in accordance with the standard exclusions that apply to the sharing of non-medically related information. These exceptions provide that an institution may share medically related information with an affiliate without having the communication categorically treated as a consumer report if the information is disclosed to an affiliate:

(1) In connection with the business of insurance or annuities (including the activities described in section 18B of the model Privacy of Consumer Financial and Health Information Regulation issued by the National Association of Insurance Commissioners, as in effect on January 1, 2003);

(2) For any purpose permitted without authorization under the Standards for Individually Identifiable Health Information promulgated by the Department of Health and Human Services (HHS) pursuant to the Health Insurance Portability and Accountability Act of 1996 (HIPAA);

(3) For any purpose referred to under section 1179 of HIPAA;

(4) For any purpose described in section 502(e) of the Gramm-Leach-Bliley Act; or

(5) As otherwise determined to be necessary and appropriate, by regulation or order, by the Federal Trade Commission (FTC), the Agencies, or an applicable State insurance authority.

Section 604(g)(4), as added by section 411(a)(4) of the FACT Act, also provides that any person that receives medical information from an affiliate pursuant to an exception in section 604(g)(3) or from a consumer reporting agency under section 604(g)(1) must not disclose such information to any other person, except as necessary to carry out the purpose for which the information was initially disclosed, or as otherwise permitted by statute, regulation, or order.

II. Overview of Comments Received

On April 28, 2004, the Agencies published a notice of proposed rulemaking in the **Federal Register** (69 FR 23380) to implement the provisions of section 411 of the FACT Act. The Agencies proposed to create exceptions to the general prohibition against creditors obtaining or using medical information in connection with credit eligibility determinations, as required by section 604(g)(5)(A), to permit transactions necessary and appropriate to protect legitimate operational, transactional, risk, consumer, and other needs (including administrative verification purposes), consistent with the intent of Congress to restrict the use of medical information for inappropriate purposes. In addition, the Agencies proposed to create additional exceptions to the special restrictions in section 603(d)(3) on sharing medically related information with affiliates, as permitted by section 604(g)(3)(C).

Each of the Agencies received up to 40 comment letters in response to the proposal, although many commenters sent copies of the same letter to more than one Agency. Comments were received from a variety of industry commenters, including banks, thrifts, credit unions, credit card companies, mortgage lenders and other non-bank creditors, and industry trade associations. Comments were also received from insurance companies and insurance industry trade associations. Other comments were received from consumer and community groups, privacy advocates, and health care associations. A comment letter was received from two Members of Congress, and another comment letter was received from the Federal Trade Commission.

Most commenters supported the proposed rule. Commenters offered a number of suggested changes, with the most common suggestions including: broadening the scope of coverage to apply to all creditors; broadening the scope of coverage to apply to an individual's credit eligibility made in connection with business credit; clarifying the definition of ''medical information'; implementing the statute by relying primarily on interpretations of the statute rather than exceptions; addressing debt cancellation contracts, debt suspension agreements, and credit insurance products through an exception; and revising the language and scope of various exceptions to the general prohibition on obtaining and using medical information.

The Agencies have modified the proposed rule in light of the comments received. These comments, and the Agencies' responses to the comments, are discussed in the following section-by-section analysis. As discussed below, the Agencies are adopting these rules as interim final rules so that interested parties may comment on the expanded scope of the exceptions for obtaining and using medical information in connection with credit eligibility determinations.

III. Section-by-Section Analysis

Section __.2 Examples

Section __.2 of the proposal discussed the scope and effect of the examples included in the proposed rule. Commenters supported the provision regarding the scope and effect of examples. Section __.2 is therefore adopted as proposed.

Section __.3 Definitions

Section __.3 of the proposal contained definitions for the terms ''affiliate'' (as well as the related terms ''company'' and ''control''), ''consumer,'' ''medical information,'' and ''you.'' The proposed definition of ''you'' has not been included in the interim final rule as unnecessary.[1]

Affiliate

Several FCRA provisions apply to information sharing with persons ''related by common ownership or affiliated by corporate control,'' ''related by common ownership or affiliated by common corporate control,'' or ''affiliated by common ownership or common corporate control.'' *E.g.*, FCRA, sections 603(d)(2), 615(b)(2), and 624(b)(2). Each of these provisions was enacted as part of the 1996 amendments to the FCRA. Similarly, section 2 of the FACT Act defines the term ''affiliate'' to mean persons that are related by common ownership or affiliated by corporate control.

Under the proposal, the Agencies proposed to define ''affiliate'' to mean any company that controls, is controlled by, or is under common control with another company, which is identical to the definition of ''affiliate'' in section 509 of the GLB Act and the GLB Act privacy regulations. The Agencies received very few comments on the definition of ''affiliate'' and none that suggested changes to the definition.

In the interim final rules, the Agencies have revised the definition of ''affiliate'' to track more closely the definition contained in section 2 of the FACT Act. Section __.3(b) of the interim final rules defines ''affiliate'' to mean any company that is related by common ownership or common corporate control with another company.[2]

The Agencies believe there is no substantive difference between the FACT Act definition of ''affiliate'' and the definition of ''affiliate'' in section 509 of the GLB Act. The Agencies are not aware of any circumstances in which two entities would be affiliates for purposes of the FCRA but not for purposes of the GLB Act privacy rules, or vice versa. Furthermore, even though affiliated entities have had to comply with different formulations of the ''affiliate'' definition under the FCRA and the GLB Act since 1999, the Agencies are not aware of any compliance difficulties or disputes resulting from the two statutes using somewhat different wording to describe what constitutes an affiliate.

Under the GLB Act privacy rules, the definition of ''control'' determines whether two or more entities meet the definition of ''affiliate.'' [3] The Agencies included the same definition of ''control'' in the proposal. The Agencies received no comments on the proposed definition of ''control.'' Accordingly, the Agencies interpret the phrase ''related by common ownership or common corporate control'' as used in the FACT Act to have the same meaning as ''control'' in the GLB Act privacy rules. For example, if an individual owns 25 percent of two companies, the companies would be affiliates under both the GLB Act and FCRA definitions. However, the individual would not be considered an affiliate of the companies because the definition of ''affiliate'' is limited to companies.

For purposes of clarity, the Agencies are revising the defined term from ''control'' (as in the proposal) to ''common ownership or common corporate control'' in order to track more closely the terminology used in the FACT Act.[4] In addition, the Agencies believe that certain types of persons, for example, governments or governmental agencies or individuals are not subject to control, as that term is defined in the interim final rules, for purposes of defining an affiliate.

The proposal also included a definition of ''company,'' which was defined to include any corporation, limited liability company, business trust, general or limited partnership, association, or similar organization. Omitted from the definition of ''company'' are some entities that are ''persons'' under the FCRA, including estates, cooperatives, and governments or governmental subdivisions or agencies, as well as individuals. The Agencies received no comments on the proposed definition of ''company,'' which is adopted as proposed.

The interim final rule includes a definition of ''person'' to reflect that the definition of ''affiliate'' now refers to a ''person'' rather than to a ''company.'' The definition of ''person'' tracks the statutory definition and means any individual, partnership, corporation, trust, estate, cooperative, association, government or governmental subdivision or agency, or other entity.

Medical Information

Under the proposed rule, paragraph (k) defined the term ''medical information'' to mean information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to (1) the past, present, or future physical, mental, or behavioral health or condition of an individual; (2) the provision of health care to an individual; or (3) the payment for the provision of health care to an individual. Proposed paragraph (k) also made clear that the term ''medical information'' did not include the age or gender of a consumer, demographic information about the consumer, including a consumer's residence address or e-mail address, or any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy. The definition in the proposal tracked the statutory definition of ''medical information.''

The Agencies requested comment on whether coded information furnished by a consumer reporting agency in accordance with section 604(g)(1)(C) of the FCRA should be deemed to fall outside the definition of ''medical information.'' Industry commenters generally believed that coded information should be excluded from the definition of ''medical information'' because Congress, by requiring coding by consumer reporting agencies, determined the appropriate protection for this information. Privacy advocates, consumer and community groups, and health care associations urged the Agencies not to exclude coded information from the definition of ''medical information'' because they believed it would be an inappropriate narrowing of the statutory definition and would effectively remove such information from the anti-discrimination protections of proposed § __.30(c) by allowing creditors to treat medical debts, if coded, differently than non-medical debts. Based on the

[1] The OTS previously added a definition of ''you'' to § 571.3(o) in connection with its disposal rule. *See* 69 FR 77610, 77621 (Dec. 28, 2004). That definition remains in the OTS's rule.

[2] For purposes of the regulation, an ''affiliate'' includes an operating subsidiary of a bank or savings association, and a credit union service organization that is controlled by a Federal credit union.

[3] *See* 12 CFR 40.3(g), 216.3(g), 332.3(g), 573.3(g), and 716.3(g).

[4] For purposes of the regulation, NCUA presumes that a Federal credit union has a controlling influence over the management or policies of a credit union service organization if it is 67 percent owned by credit unions.

comments received and an analysis of the terms and structure of the FACT Act, the Agencies have determined to treat coded information as ''medical information'' for purposes of the Agencies'' rules. The statutory definition of ''medical information'' is quite broad. In addition, the wording of section 604(g)(1) indicates that ''medical information about a consumer'' includes both coded and uncoded information from a consumer report. How creditors may obtain and use this information is discussed below.

A number of commenters asked the Agencies to clarify that ''medical information'' must relate or pertain to a specific consumer. Commenters requested this clarification to ensure that creditors can continue to use databases containing aggregate, non-personally identifiable information about consumers to analyze consumer behavior patterns without violating the restrictions on obtaining or using medical information. The FTC recommended that the Agencies clarify that information about collateral is not ''medical information'' because information about collateral does not pertain to an individual.

The Agencies believe that the statutory definition of ''medical information'' applies only to information that is associated with a specific consumer because such information must relate to the condition ''of an individual'' or the provision of health care or payment for the provision of health care ''to an individual.'' In the interim final rule, the Agencies have clarified that the term ''medical information'' does not include information that does not identify a specific consumer. Section __.3(k)(2)(iv) contains this clarification. The interim final rule does not categorically exclude information about collateral from the definition of medical information because the relationship between information about collateral and medical information about an individual may depend upon the facts and circumstances.

One commenter asked the Agencies to clarify that information about the death of an individual is not medical information. The Agencies believe that the fact that a consumer is deceased generally is not ''medical information.'' However, certain information associated with the death of a consumer, such as information about the medical condition that resulted in the consumer's death, may be medical information.

Creditors are reminded that other laws, such as the Americans with Disabilities Act, the Fair Housing Act (FHA), the GLB Act, the Health Insurance Portability and Accountability Act (HIPAA), and other parts of the FCRA, may limit or regulate the use, collection, and sharing of consumer information, including medical information. These and other laws, such as the Equal Credit Opportunity Act (ECOA), also may prohibit creditors from using certain information that is excluded from the restrictions on obtaining or using medical information, such as age or gender information, in determining eligibility for credit or for other purposes. The exceptions created by this rule do not override or modify, or in any way limit the responsibility of creditors to comply with all applicable Federal and state fair lending laws. The OTS reminds creditors subject to its rules that they must comply with the requirements of the OTS's anti-discrimination rules when seeking to obtain and use medical information in reliance on the exceptions in this rule.[5]

Section __.30 Obtaining or Using Medical Information in Connection With a Determination of Eligibility for Credit

Section 411(a) of the FACT Act adds a new section 604(g)(2) to the FCRA, which contains a broad new limitation on the ability of creditors to either obtain or use medical information in connection with credit eligibility determinations.

A. Scope of Rules on Obtaining or Using Medical Information

Section 604(g)(2) (as added by section 411 of the FACT Act) prohibits any ''creditor'' from obtaining or using ''medical information'' in connection with any determination of the consumer's eligibility, or continued eligibility, for credit.[6] The definition of ''medical information'' adopted in the FACT Act broadly includes information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or a consumer that relates to the past, present, or future physical, mental, or behavioral health or condition of an individual, the provision of health care to an individual, or the payment for the provision of health care to an individual.[7] The definition encompasses important financial information about consumers that is typically used in the credit underwriting process, such as information about the payment history and status of medical debts and the amount of a consumer's disability income.

Section 111 of the FACT Act added a definition of ''creditor'' to the FCRA that is also very broad and includes any person who regularly extends, renews, or continues credit, any person who regularly arranges for the extension, renewal, or continuation of credit, or any assignee of an original creditor who participates in the decision to extend, renew, or continue credit.[8] A ''creditor'' includes depository institutions as well as entities that are neither depository institutions nor affiliates of depository institutions, such as independent finance companies, loan brokers, health care providers, and automobile dealers. Accordingly, section 604(g)(2) prohibits all creditors from obtaining or using key financial information that is also medical information in the credit underwriting process.

Section 604(g) does not contain any specific statutory exception to this broad prohibition. Instead, section 604(g)(5) directs the Agencies to prescribe regulations to permit ''transactions'' in which creditors obtain or use medical information that are ''necessary and appropriate to protect legitimate operational, transactional, risk, consumer, and other needs consistent with the intent of paragraph (2) to restrict the use of medical information for inappropriate purposes.'' [9] Section 604(g)(5) does not by its terms limit the scope of the creditors that may rely on exceptions granted by the Agencies.

Proposed § __.1(b)(2) identified the persons to which the rules relating to obtaining and using medical information in proposed §§ __.30(a)–(d) applied. As proposed, each Agency's rule and the exceptions created by those rules applied to creditors subject to the regulatory jurisdiction of the respective Agency. The most significant issue raised by commenters in connection with the proposal related to the classes of creditors to which the exceptions to the statutory prohibition in section 604(g)(2) would apply. Many commenters strongly urged the Agencies to make clear that the regulatory exceptions apply to *all* creditors that are subject to the statutory prohibition on

[5] The OTS's anti-discrimination regulations are found at 12 CFR part 528.

[6] 15 U.S.C. 1681b(g)(2).

[7] *Id.* at § 1681a(i). ''Medical information'' does not include the age or gender of a consumer, demographic information about the consumer, including a consumer's residence address or e-mail address, or any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy. *Id.*

[8] The meaning of ''creditor'' in the FCRA has the same meaning as in the Equal Credit Opportunity Act (''ECOA''). *Id.* at §§ 1681a(r)(5) and 1691a(e).

[9] *Id.* at § 1681b(g)(5)(A).

obtaining or using medical information, not just bank and thrift creditors and their affiliates and Federal credit unions. Many financial institution creditors indicated that, if the exceptions failed to apply to all creditors, the lending activities of financial institutions would be adversely affected because financial institutions often originate loans through, or purchase loans from, persons that are creditors for purposes of the FCRA but are not financial institutions. In particular, commenters noted that arrangers of credit (which are creditors for purposes of the FCRA) may include doctors and other health care providers that inform consumers of medical financing options and act as a liaison between the consumer and the creditor.

Finally, commenters argued that, without clarification that the classes of creditors that could rely on the Agencies' regulatory exceptions were the same as the classes of creditors subject to the statutory prohibition, a significant number of creditors unaffiliated with banks, thrifts, or Federal credit unions would be in doubt about their ability to obtain and use excepted medical information in the same way and to the same extent as the Agencies' rules allow creditors that are banks, thrifts, Federal credit unions, or affiliates of those institutions to obtain and use the identical information. This result could reduce the availability of credit generally because of the breadth of the statute's definition of medical information. Two Members of Congress who sponsored section 411 of the FACT Act, submitted a comment letter supporting this view and indicating that it was their intention that the exceptions would apply to non-bank finance companies, state-chartered credit unions, and doctors, medical suppliers, and other medical professionals.

The prohibition on creditors obtaining or using medical information in connection with credit eligibility determinations in section 604(g)(2) applies to all creditors. As noted above, section 605(g)(5) does not, by its terms, limit the creditors that may rely on the exceptions granted by the Agencies. Moreover, that section, by its terms, applies to ''transactions'' for which the Agencies determine exceptions are necessary, not to ''creditors'' that the Agencies determine must be protected by the exceptions. Accordingly, the combined scope of the exceptions adopted pursuant to section 604(g)(5) in the interim final rules is as broad as the prohibition to which it applies, and is available to all creditors.

The final action is comprised of six rules. The applicability of the section of each Agency's rule addressing the prohibition on and exceptions for creditors obtaining or using medical information in connection with credit eligibility determinations is set forth in § __.30(a) and covers transactions in which certain enumerated entities participate as creditors. Under § __.30(a)(2), other entities that participate as creditors in transactions in which an enumerated entity also participates as a creditor are also subject to that Agency's rule.

In addition, a separate rule, codified in part 232 of the Board's chapter of the *Code of Federal Regulations* (hereafter ''separate rule''), affords the exceptions to the prohibition against obtaining and using medical information for credit eligibility determinations generally to all creditors, except for creditors that are subject to one of the other Agencies' rules. This combination of rules establishes uniform coverage and exceptions for transactions involving any creditor that is subject to the prohibition on obtaining or using medical information in section 411. The separate rule has been located in the Board's chapter of the Code of Federal Regulations as a matter of convenience because many creditors are accustomed to looking to the Board's regulations implementing other statutes, such as the Truth-in-Lending Act and the Equal Credit Opportunity Act.

The Agencies believe it is important that rules prescribing exceptions to the prohibitions from obtaining or using medical information in connection with credit eligibility determinations be consistent. Thus, in developing the proposed and interim final rules, the Agencies have consulted and coordinated with each other to establish identical rules. The Agencies will consult and coordinate with each other regarding any amendments to the rules for the purpose of assuring, to the extent possible, that the regulations prescribed by each Agency remain consistent and comparable with the regulations prescribed by the other Agencies.

These rules are being adopted on an interim final basis with a delayed effective date. While a number of commenters urged clarification of the scope of the availability of the exceptions, the Agencies are concerned that uncertainty about this matter may have led creditors that believed they could not avail themselves of the exceptions not to comment on the appropriateness and details of the exceptions.

B. General Prohibition on Obtaining or Using Medical Information

Proposed paragraph (a)(1) incorporated the statute's general rule prohibiting creditors from obtaining or using medical information pertaining to a consumer in connection with any determination of a consumer's eligibility, or continued eligibility, for credit, except as provided in the regulations under subpart D. The supplementary information to the proposal noted the consumer's eligibility for credit typically would be determined when an initial decision is made on whether to grant or deny credit to the consumer, but could also include decisions whether to terminate an account or adjust a credit limit following an account review. The Agencies received no comments on this restatement of the statutory prohibition in the proposal. Renumbered paragraph (b)(1) in each Agency's rule and § __.1(b) of the separate rule contain this provision, which is adopted as proposed.

Proposed paragraph (a)(2) clarified the meaning of certain terms used in the statutory prohibition and the proposed rule, including ''eligibility, or continued eligibility, for credit,'' ''credit,'' and ''creditor.'' Commenters had no comments on the definitions of ''credit'' and ''creditor,'' which tracked the FACT Act's definition of those terms. In the interim final rule, renumbered paragraphs (b)(2)(i) and (ii) of each Agency's rule and § __.1(c)(2) and (3) of the separate rule contain the definitions of ''credit'' and ''creditor,'' which are adopted as proposed.

The proposed rule interpreted the phrase ''eligibility, or continued eligibility, for credit'' to mean the consumer's qualification or fitness to receive, or continue to receive, credit, including the terms on which credit is offered, primarily for personal, family, or household purposes. The proposal further clarified that the phrase ''eligibility, or continued eligibility, for credit'' did not include the following: (1) The consumer's qualification or fitness to be offered employment, insurance products, or other non-credit products or services; (2) a determination of whether the provisions of a debt cancellation contract, debt suspension agreement, credit insurance product, or similar forbearance practice or program are triggered; (3) authorizing, processing, or documenting a payment or transaction on behalf of a consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit; or (4) maintaining or servicing a

consumer's account in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit.

Commenters offered a substantial number of suggestions regarding the meaning of ''eligibility, or continued eligibility, for credit.'' Industry commenters supported limiting the term to credit primarily for personal, family, or household purposes consistent with the traditional scope of the FCRA. Privacy advocates, consumer and community groups, and health care associations, on the other hand, objected to the exclusion of business credit from the general prohibition on obtaining or using medical information. These commenters argued that the proposed limitation to consumer credit conflicted with the FCRA definitions of ''credit'' and ''creditor,'' which incorporate the ECOA definitions of those terms. Moreover, these commenters noted that Congress initially used the Truth in Lending Act (TILA) definitions of ''credit'' and ''creditor'' in the draft FACT Act legislation, but subsequently adopted the ECOA definitions of those terms. ECOA applies to business purpose credit, whereas TILA does not.

The Federal banking agencies (OCC, Board, FDIC, and OTS) have previously taken the position that a creditor has a permissible purpose to obtain a consumer report on a consumer in connection with a business credit transaction under section 604(a)(3)(A) of the FCRA if the consumer is or will be personally liable on the loan, such as in the case of a guarantor, co-signer, or, in most instances, an individual proprietor. An informal FTC staff opinion letter concurred with the banking agencies' position. *See* Letter from Joel Winston to Julie L. Williams, J. Virgil Mattingly, William F. Kroener, III, and Carolyn Buck, June 22, 2001. A copy of this letter is available from the FTC's Internet Web site at *http://www.ftc.gov/os/statutes/fcra/tatelbaum2.htm.* To ensure consistency with the prior interpretation, the Agencies are deleting the phrase ''primarily for personal, family, or household purposes'' from the definition of ''eligibility, or continued eligibility, for credit.'' In order for the prohibition in section 604(g)(3) to apply, a creditor must obtain or use medical information about a consumer in connection with a determination of a consumer's eligibility, or continued eligibility, for credit. Accordingly, the general prohibition would apply to business credit if a consumer would be personally liable for repayment of a business loan.

Commenters also pointed to an ambiguity in the proposal: proposed paragraph (a)(2)(i)(A) referred to insurance products while proposed paragraph (a)(2)(i)(B) referred to credit insurance products. To eliminate this ambiguity, the interim final rule has been revised so that renumbered paragraph (b)(2)(iii)(A) of each Agency's rule and section __.1(c)(4)(i) of the separate rule applies to insurance products other than credit insurance products. Additional, non-substantive changes have been made to these paragraphs for clarity.

Commenters made a number of suggestions regarding debt cancellation contracts, debt suspension agreements, and credit insurance products, which were addressed in proposed paragraph (a)(2)(i)(B). Most commenters believed that these contracts, agreements, and products should be addressed through an exception, rather than through an interpretation. In the interim final rule, debt cancellation contracts, debt suspension agreements, and credit insurance products are addressed in two new exceptions, which are discussed below.

Forbearance practices or programs were also addressed in proposed paragraph (a)(2)(i)(B). Most commenters believed that forbearance practices and programs should be addressed through an exception, rather than through an interpretation. In the interim final rule, forbearance practices or programs are addressed in a new exception, which is discussed below.

Under the proposal, the term ''eligibility, or continued eligibility, for credit'' did not include authorizing, processing, or documenting a payment or transaction on behalf of a consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit. The interim final rule retains this interpretation in paragraph (b)(2)(iii)(B). *See also* section __.1(c)(4)(ii) of the separate rule. A few commenters asked the Agencies to clarify that over limit transactions or fees and the use of transaction codes fall within this interpretation. Typically, the routine processing of over limit transactions or the imposition of over limit fees would not involve a determination of the consumer's eligibility, or continued eligibility, for credit. If, however, a creditor has medical information about the consumer and uses that information to determine whether or not to raise the consumer's credit limit, such use must fall within an exception in §§ __.30(d) or (e) of each Agency's rule or §§ __.3 or __.4 of the separate rule to be permissible. Similarly, the use of transaction codes that identify payments to merchants of medical products or services typically would not involve a determination of the consumer's eligibility, or continued eligibility, for credit, unless the creditor uses the medically related codes to make a judgment about whether, and on what terms, to extend credit to the consumer.

Under the proposal, the term ''eligibility, or continued eligibility, for credit'' did not include maintaining or servicing a consumer's account in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit. The interim final rule retains this interpretation in paragraph (b)(2)(iii)(C) of each Agency's rule. *See also* section __.1(c)(4)(iii) of the separate rule.

The FTC recommended adding a number of additional interpretations and deleting or revising references suggesting that the proposed interpretations and rule of construction were not statutory interpretations. In the interim final rule, the Agencies have deleted references that may have suggested that the interpretations are not interpretations of the statute. Most of the additional interpretations recommended by the FTC are addressed elsewhere in this preamble.

One FTC suggestion not addressed elsewhere is the recommendation to interpret the statute to permit doctors and other providers of medical goods and services to extend credit to consumers where the credit is incidental to the provision of medical goods or services. The Agencies agree that providers of medical goods and services ordinarily would obtain medical information pertaining to a consumer in connection with rendering medical care, and not in connection with credit eligibility decisions. Moreover, if a provider did not use that medical information in connection with determining the consumer's eligibility to receive credit, then the provider clearly would not violate the prohibition. For example, a doctor who treats a patient before billing the patient for her services, without considering the patient's payment history or other medical information relating to the patient, would not have obtained and used medical information in connection with an eligibility determination for credit.

As discussed above, the definition of medical information is very broad and includes not only the health or condition of an individual, but information relating to the payment for the provision of health care. *See* section 603(i) of the FCRA (15 U.S.C. 1681a(i)). If a provider uses medical information,

such as a consumer's history of not paying medical bills promptly, in determining whether and on what terms to extend credit to the consumer, then the provider, as a creditor, has used medical information in connection with a credit eligibility determination in contravention of the general prohibition. Thus, the Agencies conclude that an interpretation that excludes incidental credit from the statutory prohibition is not supported by the statute because medical service providers that extend incidental credit may, in some instances, use medical information to determine the consumer's eligibility for such credit.

C. Receiving Unsolicited Medical Information and Coded and Uncoded Information from a Consumer Reporting Agency

Section __.30(b) of the proposal contained a rule of construction regarding the receipt of unsolicited medical information in recognition of the fact that creditors may receive medical information without specifically asking for it. A creditor may receive unsolicited medical information, for example, when a consumer informs the loan officer that she needs a loan to pay for treatment for a particular medical condition, or when a consumer, in response to a general request on a credit application for information about outstanding debts, lists debts owed to hospitals and doctors for medical services. The Agencies proposed a rule of construction to make clear that a creditor would not violate the prohibition on obtaining medical information if the creditor received medical information without specifically asking for or requesting such information and did not use it.

Commenters generally supported the rule of construction for unsolicited medical information. Industry commenters generally favored a rule of construction over an exception.

In addition, the Agencies solicited comment on how to treat information in consumer reports containing information described in section 604(g)(1) of the FCRA. The Agencies solicited comment on three options for allowing creditors to obtain and use coded information contained in a consumer report pursuant to section 604(g)(1)(C). One approach was to interpret ''medical information'' to exclude coded information that may be furnished under section 604(g)(1)(C) of the Act. Another approach was to interpret the prohibition on obtaining or using medical information in section 604(g)(2) as qualified by the provisions in section 604(g)(1) that authorize consumer reporting agencies to furnish consumer reports containing medical information under certain circumstances. A final approach was to require creditors that intend to obtain and use coded medical information in connection with credit eligibility determinations to do so in accordance with the financial information exception in proposed § __.30(c).

Industry commenters generally believed that coded information should be excluded from the definition of ''medical information.'' Privacy advocates, consumer and community groups, and health care associations, on the other hand, maintained that coded information fell within the definition of ''medical information'' and opposed the creation of a separate consumer report exception as in proposed paragraph (d)(1)(iii). These commenters believed that the other proposed exceptions were sufficient to protect legitimate uses of both coded and uncoded medical information obtained from a consumer report. The FTC urged the Agencies to interpret the general prohibition on creditors obtaining and using medical information in section 604(g)(2) as qualified by the provisions in section 604(g)(1) applicable to consumer reporting agencies that furnish consumer reports containing medical information.

As noted above, the Agencies interpret coded information provided pursuant to section 604(g)(1)(C) as meeting the broad statutory definition of ''medical information.'' Under the interim final rules, a creditor that receives medical information from a consumer reporting agency, whether coded or uncoded, without specifically requesting that information does not obtain medical information in violation of the prohibition. Such information, however, may be used only in accordance with the exceptions contained in renumbered paragraphs 30(d) or (e) of each Agency's rule or §§ __.3 or __.4 of the separate rule.

The proposal also included a separate exception for uncoded medical information furnished by a consumer reporting agency in a consumer report pursuant to section 604(g)(1)(B) in proposed paragraph (d)(1)(iii). The proposed exception has been omitted from the interim final rule as unnecessary. Commenters generally did not support this exception. A number of these commenters believed that the other exceptions were sufficient and that no separate exception should be created for consumer reports. The FTC urged the Agencies to treat coded and uncoded medical information furnished by consumer reporting agencies the same by interpreting the general statutory prohibition as inapplicable to such information.

The Agencies believe that the exceptions in renumbered paragraphs (d) and (e) of each Agency's rule and in §§ __.3 and __.4 of the separate rule provide creditors sufficient flexibility with respect to the use of medical information contained in consumer reports. The rule of construction for unsolicited medical information adequately protects creditors that receive coded or uncoded medical information in consumer reports furnished by consumer reporting agencies without specifically requesting medical information. If, however, a creditor specifically requests medical information from a consumer reporting agency in connection with a credit eligibility determination, the creditor must meet one of the exceptions in renumbered paragraphs (d) and (e) of each Agency's rule or §§ __.3 and __.4 of the separate rule in order to obtain and use that information.

Renumbered paragraph (c) of the interim final rule adopts the rule of construction for unsolicited medical information with certain revisions. Section __.2 of the separate rule contains the identical provision. The interim final rule provides that a creditor does not *obtain* medical information in violation of the prohibition if it receives such information from a consumer, a consumer reporting agency, or any other person in connection with any determination of the consumer's eligibility, or continued eligibility, for credit without specifically requesting medical information. The rule of construction is retained as an interpretation, rather than as an exception because it interprets the statutory language regarding when a creditor ''obtains'' medical information in violation of the prohibition.

The introductory language to the rule of construction has been revised for clarity to provide that a creditor does not obtain medical information ''in violation of the prohibition'' if it meets the specified criteria. In addition, the cross-reference to the general prohibition has been deleted because the rule of construction is an interpretation of the statute.

Proposed paragraph (b)(1)(ii), which prohibited the use of unsolicited medical information, has been deleted because the rule of construction focuses on when a creditor does not obtain medical information in violation of the statute. The Agencies believe that incorporating a use limitation in the rule of construction would be

inconsistent with the exceptions in renumbered paragraphs (d) and (e). Instead, the Agencies have added a new paragraph (c)(2) to clarify that a creditor that receives unsolicited medical information may use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit only to the extent the creditor can rely on one of the exceptions in renumbered paragraphs (d) or (e).

The examples of the rule of construction have been moved to renumbered paragraph (c)(3) in the interim final rules and all references to restrictions on the use of unsolicited medical information have been deleted from the examples consistent with the changes discussed above. In addition, paragraph (c)(3)(iii) adds a new example to illustrate how the rule of construction applies to medical information furnished by a consumer reporting agency.

Commenters had several other comments concerning the rule of construction. Privacy advocates, consumer and community groups, and health care associations suggested that the Agencies clarify that the phrase ''without specifically requesting medical information'' means information obtained voluntarily without any pressure, prompting, or direct or indirect solicitation by the creditor. These commenters also sought an additional requirement that creditors destroy unsolicited medical information as soon as reasonably practicable and suggested making the rule of construction an exception. Some industry commenters suggested that consumers should have the burden of proving that unsolicited medical information was used in a credit eligibility determination because it may be difficult for creditors to prove that unsolicited medical information was not used. Some industry commenters suggested permitting a creditor to use unsolicited medical information in a manner no less favorably than it would use comparable medical information.

The statute does not specifically address the burden of proof to be applied when disputes arise regarding the use of medical information. The Agencies find it unnecessary to address this issue because the interim final rule allows unsolicited medical information to be used as permitted by the exceptions in renumbered paragraphs (d) and (e). The Agencies thus decline to impose on consumers the burden of proving that unsolicited medical information was used in a credit eligibility determination. Furthermore, even if the consumer requests that a creditor use unsolicited medical information in connection with a credit eligibility determination, the creditor is not required to do so. The phrase ''without specifically requesting medical information'' along with the examples makes clear that the rule of construction does not apply to medical information obtained through a specific request or solicitation for such information. No further clarification is necessary. The destruction of unsolicited medical information would not be appropriate in many circumstances, thus the Agencies decline to adopt such a rule.

D. Financial Information Exception for Obtaining and Using Medical Information

As noted above, section 604(g)(5)(A) of the Act gives the Agencies the authority to prescribe regulations, after notice and opportunity for comment, to permit transactions in which creditors may obtain and use medical information in connection with determinations of credit eligibility that the Agencies determine to be necessary and appropriate to protect legitimate operational, transactional, risk, consumer, and other needs (including actions necessary for administrative verification purposes), consistent with the intent of the statute to restrict the use of medical information for inappropriate purposes. Applying this standard, the Agencies proposed a number of exceptions to the general prohibition on creditors obtaining or using medical information in connection with credit eligibility determinations. The exceptions were contained in proposed paragraphs (c)–(d). In the interim final rule, these exceptions are contained in renumbered paragraphs (d) and (e) of each Agency's rule and in §§ __.3 and __.4 of the separate rule.

Section __.30(c) of the proposal contained the proposed financial information exception. Proposed paragraph (c)(1) provided that a creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit so long as the following three elements were met. First, the information must relate to debts, expenses, income, benefits, collateral, or the purpose of the loan, including the use of proceeds. Second, the creditor must use the information in a manner and to an extent no less favorable than it would use comparable information that is not medical information in a credit transaction. Third, the creditor must not take the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis into account as part of any such determination of credit eligibility.

Commenters generally supported the proposed three-part test for the financial information exception. Privacy advocates, consumer and community groups, and health care associations suggested limiting the exception to circumstances where the creditor has not specifically requested medical information on its application for credit, but rather has made a generic request for financial information. These commenters also suggested including the phrase ''financial information'' in the text of the rule. Industry commenters suggested revising the first prong to apply to a non-exclusive list of information routinely used in the underwriting process. These commenters noted that the Agencies may have unintentionally omitted certain items, such as assets, that should be included in the list. Commenters generally supported the second prong of the test. One commenter suggested that the third prong of the test was inconsistent with and undermined the ''no less favorable'' principle set forth in the second prong and could prove detrimental to consumers. Another commenter found the three-part test complicated and difficult to implement.

The interim final rule retains the three-part test for the financial information exception, with certain modifications. The Agencies agree with those commenters that believe the better approach is to have a non-exclusive list of types of information that are routinely used in making credit eligibility determinations. The first prong of the test, therefore, has been revised to include all information of the type routinely used in making credit eligibility determinations and provides a non-exclusive list of such types of information (*i.e.*, information relating to debts, expenses, income, benefits, assets, collateral, or the purpose of the loan, including the use of proceeds). The Agencies do not believe it would be helpful to include the words ''financial information'' in the text of the exception because there is no bright line between financial information and medical information.

The second prong of the test is adopted as proposed. Commenters appeared comfortable with requiring a creditor to use medical information in a manner and to an extent no less favorable than it would use comparable non-medical information in a credit transaction. As noted in the proposal, a creditor may deny credit to the

consumer because the consumer owes a debt to a hospital if the creditor would have denied credit to the consumer if the consumer had owed the same amount of debt with the same payment history to a retailer. Nothing in the rule prevents the creditor from treating information about medical debts (or expenses or income) more favorably than non-medical debts.

The third prong of the test is also adopted as proposed. Other, more narrowly focused exceptions, such as the medical accommodation exception, permit a creditor to take the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis into account in limited circumstances as part of a consumer's credit eligibility determination. For this type of core medical information, the Agencies believe it is appropriate to more strictly limit the circumstances in which creditors may obtain or use this information.

Since creditors generally are prohibited from obtaining medical information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit, a creditor ordinarily would not specifically request medical information on an application, but would obtain such information in response to a generic question on an application about debts, income, and other information routinely used in credit eligibility determinations. Thus, except where a creditor has a specific application for the financing of medical procedures, a creditor generally would be prohibited from specifically asking for medical information on a credit application.

Proposed paragraph (c)(2) provided several non-exclusive examples to illustrate when creditors may obtain and use medical information under the financial information exception. Commenters generally supported the proposed examples. One commenter requested a clarification of the example in proposed paragraph (c)(2)(iii)(B). In that example, a consumer meets with a loan officer of a creditor to apply for a mortgage loan. While filling out the loan application, the consumer informs the loan officer orally that she has a potentially terminal disease. The consumer meets the creditor's established requirements for the requested mortgage loan. The loan officer recommends to the credit committee that the consumer be denied credit because the consumer has that disease. The commenter recommended adding a statement that the bank acted on the loan officer's recommendation and denied the application because the consumer had a potentially terminal disease to clarify that the creditor, in fact, used medical information in a manner inconsistent with the exception. The Agencies believe this clarification is helpful and, in the interim final rule, have revised the example in renumbered paragraph (d)(2)(iii)(B) of each Agency's rule accordingly. *See also* section __.3(b)(3)(ii) of the separate rule.

In addition, a new example has been added in paragraph (d)(2)(iii)(C) of each Agency's rule and § __.3(b)(3)(iii) of the separate rule to illustrate that a creditor cannot use a consumer's apparent medical condition as the basis for requiring the consumer to obtain debt cancellation, debt suspension, or credit insurance coverage as a condition for the extension of credit. Even though the use of medical information to determine the consumer's eligibility for a debt cancellation contract, debt suspension agreement, or credit insurance product generally is subject to an exception to the general prohibition pursuant to paragraphs (e)(1)(viii) or (e)(1)(ix), a creditor may not condition an extension of credit to the consumer on the consumer obtaining debt cancellation, debt suspension, or credit insurance coverage based on the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis.

In addition, the heading of renumbered paragraph (d)(2)(i) has been revised in the interim final rule to reflect changes made to the first prong of the test to encompass the type of information routinely used in making credit eligibility determinations. Non-substantive revisions have also been made to the examples in renumbered paragraphs (d)(2)(ii)(A) and (C) for clarity. Aside from these changes, the examples are adopted as proposed.

E. Specific Exceptions for Obtaining and Using Medical Information

Section __.30(d) of the proposal contained a number of specific exceptions to the general prohibition. These exceptions would allow creditors to obtain and use medical information for a limited number of particular purposes in connection with a determination of the consumer's eligibility, or continued eligibility, for credit. A creditor that obtains medical information pursuant to one of these specific exceptions may not subsequently use the information in connection with determining the consumer's eligibility, or continued eligibility, for credit unless an exception applies. In the interim final rule, the specific exceptions are contained in renumbered paragraph (e) of each Agency's rule. Section __.4 of the separate rule contains the identical exceptions in paragraphs (a)(1)–(9).

Determination of power of attorney, legal representative and legal capacity. Proposed paragraph (d)(1)(i) provided that a creditor may obtain and use medical information to determine whether the use of a power of attorney or legal representative is necessary and appropriate. This exception was designed to permit a creditor to verify, in connection with a credit eligibility determination, that the exercise of a power of attorney or legal representative is necessary and appropriate. Some industry commenters suggested that the exception clarify that creditors may obtain and use medical information to determine the consumer's competency or legal capacity to contract. Privacy advocates, consumer and community groups, and health care associations suggested limiting the power of attorney exception to circumstances where a power of attorney is triggered by a medical condition or where there is a legitimate question about the consumer's legal capacity to contract when a person asserts the exercise of a power or attorney or claims to act as a legal representative on behalf of a consumer. The FTC commented that the limited circumstances where medical information may be obtained and used to determine whether a power of attorney is necessary and appropriate would not be in connection with a credit eligibility determination, and therefore should be addressed through an interpretation of the statute, rather than through an exception.

The interim final rule revises the exception for the use of a power of attorney or legal representative. Renumbered paragraph (e)(1)(i) of the interim final rule permits a creditor to obtain and use medical information in connection with determining the consumer's credit eligibility to determine whether the use of a power of attorney or legal representative that is triggered by a medical event or condition is necessary and appropriate or whether the consumer has the legal capacity to contract when a person seeks to exercise a power of attorney or act as legal representative for a consumer based on an asserted medical event or condition. The interim final rule makes two substantive changes in response to the comments received. First, the exception has been narrowed to permit a creditor to obtain and use medical information only when the power of attorney or legal representative is triggered by a medical event or condition. Second, the exception has been revised to permit a creditor to

determine whether the consumer has the legal capacity to contract where a person seeks to exercise a power of attorney or act as a legal representative based on an asserted medical event or condition. This revision is designed to clarify that creditors may obtain and use medical information to verify that the asserted medical event or condition triggering the power of attorney or legal representative has, in fact, occurred and renders the consumer legally incapable of contracting. Where use of a power of attorney or legal representative is triggered by non-medical events or conditions, creditors should not need to obtain or use medical information.

In response to the FTC's comments, the Agencies recognize that a power of attorney or legal representative may be used in a variety of circumstances, many of which have no connection with a determination of a consumer's eligibility, or continued eligibility, for credit. For example, a power of attorney or legal representative may be used in connection with establishing a deposit or other asset account. In those circumstances, the general prohibition on obtaining or using medical information would not apply because the information would not be obtained or used in connection with any determination of the consumer's eligibility, or continued eligibility, for credit. The introductory language to renumbered paragraph (e) of the interim final rules makes clear that the specific exceptions apply to a creditor that ''may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit.'' A creditor that obtains and uses medical information in circumstances not connected with a credit eligibility determination is not subject to the general statutory prohibition and does not have to rely upon the power of attorney or any other exception.

Compliance with applicable law. Proposed paragraph (d)(1)(ii) provided an exception to permit a creditor to obtain and use medical information to comply with applicable requirements of local, state, or Federal laws. The Agencies received only a few comments on this proposed exception. One commenter asked the Agencies to clarify that this exception covered laws that prohibit unfair and deceptive acts or practices. The FTC suggested that the financial abuse statutes referenced in the preamble as an example do not involve credit eligibility determinations, and therefore a statutory interpretation was more appropriate than an exception.

In the interim final rule, renumbered paragraph (e)(1)(ii) is adopted as proposed. Although many legal requirements do not have any connection with credit eligibility, other laws may have such a connection. As noted above, a creditor that obtains and uses medical information to comply with applicable laws in circumstances that are not connected with a credit eligibility determination is not subject to the general statutory prohibition and does not have to rely upon the exception. However, the exception is retained to cover those circumstances where it may be needed to protect creditors from inconsistent legal obligations.

Special credit program or credit-related assistance program. One commenter suggested that the proposed compliance with applicable laws exception would not be sufficient to permit creditors to obtain and use medical information in connection with special credit or credit-related programs, such as programs established by government-sponsored enterprises. Such programs may require creditors as part of the program requirements to obtain and use medical information in ways not covered by the other exceptions. Consistent with the policy goals established by Congress, the prohibition on creditors obtaining or using medical information should not interfere with the ability of creditors to assist consumers to qualify for beneficial special programs established by government-sponsored enterprises, not-for-profit organizations, or others.

To address this concern, the interim final rule contains a new exception in renumbered paragraph (e)(1)(iii) that permits creditors to obtain and use medical information in connection with a determination of the consumer's eligibility, or continued eligibility, for credit, to determine, at the consumer's request, whether the consumer qualifies for a legally permissible special credit program or credit-related assistance program that is: (a) Designed to meet the special needs of consumers with medical conditions and (b) established and administered pursuant to a written plan of the plan sponsor that identifies the class of persons that the program is designed to benefit and sets forth the procedures and standards for extending credit or providing other credit-related assistance under the program. Because not all potentially eligible consumers may seek to qualify for a special credit or credit assistance program, this exception applies only when the consumer requests to be considered for the program. A creditor, however, may provide consumers with information about such programs to educate consumers about their options. In addition, any special credit or credit assistance program must meet the requirements of all applicable fair lending laws. The plan sponsor may include a government agency, charitable organization, the creditor, or any other person. This exception is modeled after the provisions relating to special purpose credit programs in the ECOA and the Board's Regulation B, 12 CFR part 202. What programs are permissible and what inquiries to determine medical eligibility are permissible, however, are governed by other laws, including applicable fair lending laws, and are beyond the scope of this rule.

Renumbered paragraph (e)(2) of the interim final rule provides an example to illustrate this exception. In the example, a not-for-profit organization establishes a credit assistance program pursuant to a written plan that is designed to assist disabled veterans purchase homes by subsidizing the down payment for the home purchase mortgage loans of qualifying veterans. The organization works through mortgage lenders and requires mortgage lenders to obtain medical information about the disability of any consumer that seeks to qualify for the program, use that information to verify the consumer's eligibility for the program, and forward that information to the organization. A consumer who is a veteran applies to a creditor for a home purchase mortgage loan. The creditor informs the consumer about the credit assistance program for disabled veterans and the consumer seeks to qualify for the program. The example states that, assuming that the program complies with all applicable law, including applicable fair lending laws, the creditor may obtain and use medical information about the medical condition and disability, if any, of the consumer to determine whether the consumer qualifies for the credit assistance program.

Fraud prevention or detection. Proposed paragraph (d)(1)(iv) provided that a creditor may obtain and use medical information for purposes of fraud prevention and detection. Industry commenters supported the proposed exception. Privacy advocates, consumer and community groups, and health care associations believed the proposed exception was overbroad and unnecessary in light of the other exceptions.

The interim final rule retains the fraud prevention or detection exception in renumbered paragraph (e)(1)(iv), although the language has been revised to make clear that the exception is

available only to the extent necessary to prevent or detect fraud. The Agencies anticipate that creditors would find it necessary to obtain and use medical information for purposes of fraud prevention and detection in limited circumstances. Creditors relying on this exception should have the systems in place to demonstrate the necessity for obtaining and using medical information to prevent or detect fraud. Creditors that actually use medical information in legitimate fraud prevention or detection programs should be able to make this demonstration. Blanket assertions of a fraud prevention or detection purpose alone, however, are not sufficient to justify the collection of medical information about consumers under the anti-fraud exception.

Financing medical products or services. Proposed paragraph (d)(1)(v) provided that a creditor may obtain and use medical information in connection with credit eligibility determinations in the case of credit for the purpose of financing medical products or services to determine and verify the medical purpose of a loan and the use of proceeds. As noted in the proposal, certain creditors have established specialized loan programs that finance specific medical procedures, such as vision correction surgery, but not others. In such cases, the creditor may need to obtain and use medical information in connection with determining whether the purpose of the loan is within the scope of the creditor's established loan program. The proposal also provided examples of this exception.

Commenters generally supported the medical financing exception. Several commenters suggested revising the example in proposed paragraph (d)(2)(i) to permit the creditor to verify that the procedure to be financed will be performed, in conformance with the language of the exception, rather than permitting a creditor to confirm the consumer's medical eligibility.

Renumbered paragraph (e)(1)(v) of the interim final rule retains the medical financing exception as proposed. The examples of the medical financing exception have been moved to paragraph (e)(3) in the interim final rule. The example in paragraph (e)(3)(i) of the interim final rule has been revised from the proposal in accordance with the commenters' suggestions.

Medical accommodation. Section __.30(d)(1)(vi) of the proposal provided that a creditor may obtain and use medical information if the consumer or the consumer's legal representative requested in writing, on a separate document signed by the consumer or the consumer's legal representative, that the creditor use specific medical information for a specific purpose in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular circumstances. Under the proposal, the signed, written request had to describe the specific medical information that the consumer requested the creditor to use and the specific purpose for which the information would be used. The proposal contemplated an individualized process in which the consumer would inform the creditor about the specific medical information that the consumer would like the creditor to use and for what purpose. As noted in the preamble to the proposal, this exception was not intended to allow creditors to obtain consent on a routine basis or as a part of loan applications or documentation. The proposal provided examples of the medical accommodation exception.

Commenters had a number of recommendations regarding the medical accommodation exception. Privacy advocates, consumer and community groups, and health care associations suggested that the regulation should explicitly state that creditors may not request medical information or consent to obtain medical information on a routine basis or as part of a loan application. Several commenters also suggested clarifying that the request must be voluntary and initiated by the consumer. In addition, commenters suggested including language in the regulation to clarify that the exception is not met by a form that contains a pre-printed description of various types of medical information and the uses to which it might be put. Some commenters urged the Agencies to add a disposal requirement on creditors that obtain information that is not needed. Consumer and community groups also suggested eliminating the forbearance interpretation, folding that interpretation into the medical accommodation exception, and adding anti-discrimination protections to the provision, similar to the ''no less favorable'' standard used in renumbered paragraph (d).

Industry commenters generally believed that the medical accommodation was too restrictive. Some industry commenters suggested that the use of pre-printed consent forms or other routine form of consent should be sufficient to trigger the exception. Other commenters suggested that the consumer should be able to request the use of medical information through oral and electronic means, not simply through a signed writing. One commenter noted that many creditors include a section on their credit applications where the consumer may describe special circumstances or other information that the consumer would like the creditor to consider. This commenter recommended relaxing the requirements of the medical accommodation exception to enable the exception to apply in this circumstance. Another commenter noted that the medical accommodation exception was drafted so narrowly that it may prohibit a creditor from obtaining or using additional medical information to verify or corroborate the facts necessary to support a consumer's medical accommodation request.

In the interim final rule, the medical accommodation exception in renumbered paragraph (e)(1)(vi) has been revised to address commenters' concerns. Paragraph (e)(1)(vi) provides an exception for circumstances where the consumer or the consumer's legal representative specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular circumstances, and such request is documented by the creditor. Any such accommodation must be consistent with safe and sound practices. The requirement for a separate signed writing by the consumer that describes the specific medical information and the specific purpose for which it is to be used has been deleted in the interim final rule. Instead, the interim final rule focuses on the specific request of the consumer and the creditor's documentation of that request. As revised, the interim final rule permits the medical accommodation exception to be triggered by the consumer's oral, electronic, or written request. A consumer may make a specific request by responding to a generic inquiry on a credit application that invites the consumer to describe any special circumstances or other information (not limited to medical information) that the consumer would like the creditor to consider in evaluating the consumer's application. The disposal of records connected with a specific request for a medical accommodation is beyond the scope of this rule and may not be appropriate in certain circumstances.

The proposal contained examples to illustrate the medical accommodation exception. In the interim final rule, the examples have been moved to paragraph (e)(4) and revised and expanded to address commenters' concerns.

By its terms, the medical accommodation exception incorporates a non-discrimination provision, because

a creditor may only use medical information to ''accommodate'' or favor the consumer's particular circumstances. Using medical information to discriminate against or disadvantage the consumer would not meet the requirements of the exception. Nothing in this rule, however, requires a creditor to consider medical information at the consumer's request or to provide an accommodation to the consumer. Under this rule, a creditor may disregard medical information obtained in connection with a consumer's specific request for an accommodation and evaluate the consumer in accordance with the creditor's otherwise applicable underwriting criteria. Other applicable laws, including applicable fair lending laws, may require creditors to consider such requests in certain circumstances. Consideration of circumstances governed by other applicable laws is beyond the scope of this rule. The example in renumbered paragraph (e)(4)(i) has been revised to clarify the creditor's options when presented with a specific request from a consumer for a medical accommodation.

The example in renumbered paragraph (e)(4)(ii) has been revised to apply to a specific request made by telephone and documented by the creditor. The example in paragraph (e)(4)(iii) is new and illustrates how a specific request may be made by the consumer on a credit application.

A consumer who specifically requests a medical accommodation may not provide sufficient information to enable a creditor to determine whether such an accommodation is warranted. In that case, a creditor may request additional information as necessary to verify or corroborate the information provided or to enable the creditor to determine whether to make a medical accommodation for the consumer's particular circumstances. The consumer at any time may decline to provide further medical information, withdraw the request for an accommodation, and choose to be evaluated according to the creditor's otherwise applicable underwriting criteria. The example in paragraph (e)(4)(iv) is new and illustrates how creditor requests for additional information may be handled.

As noted in the proposal, creditors may not rely on the medical accommodation exception to routinely obtain and use medical information about consumers in connection with credit eligibility determinations. This exception is triggered when the consumer specifically requests an accommodation. The requirement for a specific request from the consumer is not satisfied by a creditor routinely including boilerplate language in a credit application which indicates that by applying for credit the consumer authorizes or consents to the creditor obtaining and using medical information in connection with credit eligibility determinations. The example in paragraph (e)(4)(v) is new and illustrates that routine requests by creditors do not fall within the exception.

Forbearance. In the proposal, forbearance practices and programs were addressed as an interpretation, rather than as an exception. Industry commenters believed that the proposed interpretation was too narrow because it only covered the triggering of forbearance practices and programs. These commenters believed that medical information should be available for use in determining whether to offer forbearance practices or programs to the consumer. Several industry commenters also requested clarification that informal forbearance practices would be covered by this interpretation. Privacy advocates, consumer and community groups, and health care associations suggested limiting the proposed interpretation to forbearance practices and programs triggered by a medically related event.

In the interim final rule, forbearance practices and programs are addressed in a new exception in paragraph (e)(1)(vii). Forbearance practices and programs may be established to address both medical and non-medical events. The exception, however, applies only to forbearance practices and programs that are triggered by medical events or conditions. Accordingly, paragraph (e)(1)(vii) of the interim final rule creates an exception to permit creditors to obtain and use medical information ''consistent with safe and sound practices, to determine whether the provisions of a forbearance practice or program that is triggered by a medical event or condition apply to a consumer.'' This exception is flexible enough to cover both formal and informal forbearance practices and programs. Application of a forbearance practice or program may or may not be based on the request of the consumer. Paragraph (e)(5) provides an example of a forbearance practice or program.

Debt cancellation contracts, debt suspension agreements, or credit insurance products. As noted above, the proposal addressed debt cancellation contracts, debt suspension agreements, and credit insurance products through an interpretation. Most commenters believed that it was more appropriate to address these contracts, agreements, and products through an exception. The FTC, however, recommended that the Agencies continue to address debt cancellation contracts, debt suspension agreements, and credit insurance products through an interpretation. The Agencies believe that the better approach is to create exceptions and, thus, have created two new exceptions in paragraphs (e)(1)(viii) (covering debt cancellation contracts and debt suspension agreements) and (e)(1)(ix) (covering credit insurance products) for the reasons discussed below.

Industry commenters believed that the proposed interpretation was too narrow because it only covered the triggering of debt cancellation contracts, debt suspension agreements, and credit insurance products. These commenters believed that medical information should be available for use in determining the consumer's eligibility for, the triggering of, or the reactivation of those contracts, agreements, or products. Privacy advocates, consumer and community groups, and health care associations believed that the proposed interpretation was too broad because debt cancellation contracts and debt suspension agreements are often triggered by events such as loss of employment or divorce that have no connection with medical information. Privacy advocates, consumer and community groups, and health care associations urged the Agencies to delete credit insurance from the proposed provision, maintaining that creditors typically do not offer credit insurance directly. Industry commenters had various suggestions regarding credit insurance, including creating a separate exception for credit insurance, referencing credit insurance in the preceding paragraph (a)(2)(i)(A) (now paragraph (b)(2)(iii)(A)), or broadening the proposed interpretation to cover eligibility and reactivation determinations.

In the interim final rule, debt cancellation contracts and debt suspension agreements are addressed in one exception (paragraph (e)(1)(viii)) and credit insurance products are addressed in a separate exception (paragraph (e)(1)(ix)) in recognition of the distinct character of those products. *See also* sections __.4(a)(8) and (9) of the separate rule.

Under this rule, a creditor may not use medical information about a consumer to determine whether the consumer will be required to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product. For example, a consumer who is in a wheelchair cannot be required to obtain credit insurance

because of the consumer's disability. An example in paragraph (d)(2)(iii)(C) of each Agency's rule and in § __.3(b)(3)(iii) of the separate rule illustrates this limitation. Also, a creditor would not violate this particular rule if it requires all consumers who seek a particular type of credit, such as credit to finance the purchase of a home with a small down payment, to obtain credit insurance or a similar product.

The rule makes clear that creditors may use medical information to underwrite credit insurance, or to underwrite related credit products, such as debt cancellation contracts and debt suspension agreements, if a medical condition or event is a triggering event for the provision of benefits. However, denial of these products cannot be used as a subterfuge to consider medical information in making a determination about eligibility or continued eligibility for the underlying loan.

In addition, other laws and regulations, including applicable anti-tying rules and fair lending laws, may prohibit or otherwise restrict a creditor from requiring a consumer to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product in connection with an extension of credit.[10] A discussion of the circumstances prohibited by other laws and regulations is beyond the scope of this rule.

Finally, creditors are reminded that when a creditor offers a consumer a debt cancellation contract, debt suspension agreement, or credit insurance product that is related to a credit product that the consumer obtains or seeks to obtain from the creditor, it may not be clear to the consumer why the creditor is seeking to obtain medical information. As discussed below, creditors generally would be prohibited from specifically asking for medical information on a credit application, except where a creditor has a specific application for the financing of medical procedures. Whether medical information is collected on the credit application or through other means, creditors should make it clear to consumers that the purpose for obtaining medical information relates to debt cancellation contracts, debt suspension agreements, or credit insurance products, rather than to the credit itself. Moreover, where obtaining those products is voluntary, the consumer should be told that it is not necessary to provide medical information and that the failure to answer medically related questions will have no impact on the credit decision.

Deleted exceptions and additional exceptions requested by commenters. Proposed paragraph (d)(1)(iii) provided that a creditor may obtain and use uncoded medical information included in a consumer report furnished by a consumer reporting agency in accordance with section 604(g)(1)(B) of the FCRA, if such information is used for the purpose for which the consumer provided specific written consent. As discussed above, this proposed exception has been eliminated.

Proposed paragraph (d)(1)(vii) provided that a creditor may obtain and use medical information as otherwise permitted by order of the appropriate agency. Privacy advocates, consumer and community groups, and health care associations objected to this provision. The Agencies believe this paragraph is unnecessary and have omitted it from the interim final rule because the Agencies are adopting identical exceptions and, as noted above, intend to make any amendments to the rules in consultation and coordination with each other.

Commenters also requested the creation of a number of additional exceptions for flexible spending programs tied to credit cards, for products tied to a consumer's life expectancy, and to facilitate resolution of direct disputes with consumers. The Agencies believe that additional exceptions are not needed and that commenters' concerns are adequately addressed by the interpretation of ''eligibility, or continued eligibility, for credit'' and the existing exceptions.

Section __.31 Limits on Redisclosure of Information

Proposed section __.30(e) incorporated the statutory provision regarding the limits on redisclosure of medical information. In the proposal, this paragraph provided that a person that receives medical information about a consumer from a consumer reporting agency or an affiliate is prohibited from disclosing that information to any other person, except as necessary to carry out the purposes for which the information was initially disclosed, or as otherwise permitted by statute, regulation, or order.

Some commenters requested clarification of the phrase ''as otherwise permitted by statute, regulation, or order'' that is used in the statute and proposed regulation. Other commenters requested clarification that a redisclosure may be made for any purpose described in section 502(e) of the GLB Act. The Agencies believe that the redisclosure language, which was taken directly from the statute, is clear and that no further clarification is necessary.

In the interim final rules, the Agencies are adopting this provision in a new section __.31 in each Agency's rule pursuant to their joint rulemaking authority under section 621(e) of the FCRA. The separate rule does not contain a similar provision on redisclosure limits.

Section __.32 Sharing Medical Information With Affiliates

Section __.31 of the proposal addressed the sharing of medically related information with affiliates. In the interim final rule, these provisions are contained in section __.32.

Proposed paragraph (a) provided that the standard exclusions from the definition of ''consumer report'' contained in section 603(d)(2) of the Act—including the exclusions for sharing transaction or experience information among affiliates or sharing other eligibility information among affiliates after notice and an opportunity to opt-out—do not apply if medical information, an individualized list or description based on payment transactions for medical products or services, or an aggregate list or description based on payment transactions for medical products or services is disclosed to an affiliate.

Proposed paragraph (b) provided that the special restrictions on sharing medically related information with affiliates did not apply, and the standard exclusions from the definition of consumer report remained in effect, if the information was disclosed to an affiliate in certain circumstances. The proposal incorporated each of the exceptions enumerated in section 604(g)(3)(A) and (B) of the Act.

The first statutory exception is when medically related information is shared with an affiliate in connection with the business of insurance or annuities (including the activities described in section 18B of the model Privacy of Consumer Financial and Health Information Regulation issued by the National Association of Insurance Commissioners (NAIC), as in effect on January 1, 2003). Some commenters questioned the adequacy of the comment period based on the fact that the NAIC model privacy regulation is

[10] For example, banks are prohibited from conditioning an extension of credit on the consumer obtaining some additional credit, property or service from the bank or its affiliate other than a loan, discount, deposit or trust service, *see* Bank Holding Company Amendments of 1970 § 106(b) (12 U.S.C. 1972); *see also* 12 CFR 37.3(a) (providing that a national bank may not extend credit nor alter the terms or conditions of an extension of credit conditioned upon the customer entering into a debt cancellation contract or debt suspension agreement with the bank).

not readily available to the public, but must be purchased from NAIC. The reference to the NAIC model privacy regulation is a statutory reference that the Agencies have incorporated into the regulation. Interested parties may purchase a copy of the NAIC model Privacy of Consumer Financial and Health Information Regulation at *http://www.naic.org.*

The second statutory exception is when medically related information is shared with an affiliate for any purpose permitted without authorization under the Standards for Individually Identifiable Health Information promulgated by the Department of Health and Human Services (HHS) pursuant to the Health Insurance Portability and Accountability Act of 1996 (HIPAA). One commenter asked the Agencies to broaden this exception by deleting the phrase ''for any purpose permitted without authorization'' and replacing it with a reference to any sharing ''as permitted under'' the HIPAA regulations issued by HHS. The Agencies find no basis for altering the specific exceptions adopted by Congress. Furthermore, the Agencies note that the special affiliate sharing restrictions do not apply unless the communication of medically related information would otherwise meet the definition of a ''consumer report.''

The third statutory exception is when medically related information is shared with an affiliate for any purpose referred to under section 1179 of HIPAA. Section 1179 of HIPAA provides that to the extent that an entity is engaged in activities of a financial institution or is engaged in authorizing, processing, clearing, settling, billing, transferring, reconciling or collecting payments for a financial institution, the HIPAA standards and requirements do not apply to the entity with respect to such activities. Section 1179 also provides as an example of a use or disclosure of information not covered by that statute, the use or disclosure of information for authorizing, processing, clearing, settling, billing, transferring, reconciling, or collection, a payment for, or related to, health care premiums or health care. Some commenters requested that the Agencies contact the Department of Health and Human Services (HHS) to clarify an issue regarding the scope of section 1179. Any consultation with HHS regarding section 1179 of HIPAA would be independent of this rulemaking.

The fourth statutory exception is when medically related information is shared with an affiliate for any purpose described in section 502(e) of the GLB Act. As previously noted in the proposal, some of the purposes described in section 502(e) of the GLB Act may be germane to the sharing of information among affiliates—for example, sharing with the consent of the consumer, for fraud prevention purposes, or as necessary to effect, administer, or enforce a transaction requested or authorized by the consumer—while other purposes described in section 502(e) are not—for example, sharing information with law enforcement or regulatory authorities.

The fifth exception is not set forth in the statute and provides that the special restrictions on sharing medically related information with affiliates do not apply, and the standard exclusions from the definition of consumer report remain in effect, if the information is disclosed to an affiliate in connection with a determination of the consumer's eligibility, or continued eligibility, for credit consistent with § __.30 of this subpart. Industry commenters supported this exception. Privacy advocates, consumer and community groups, and health care associations requested the deletion of this exception or, as an alternative, that this exception not apply to uncoded medical information obtained from a consumer reporting agency with the consumer's specific written consent or to information obtained pursuant to the medical accommodation exception. This exception is adopted as proposed in paragraph (b)(5).

The Agencies continue to believe that it is necessary and appropriate to allow a person to share medically related information with an affiliate in connection with a determination of the consumer's eligibility, or continued eligibility, for credit consistent with the provisions of § __.30. In response to commenters' concerns, the Agencies note that the interim final rule permits uncoded medical information from a consumer reporting agency to be used only as permitted by the exceptions in § __.30(d) and (e). Moreover, the medical accommodation exception restricts creditors from routinely obtaining and using medical information because the exception is triggered by a consumer's specific request. Thus, the Agencies believe that the provisions of § __.30(d) and (e) are sufficient to prevent the inappropriate sharing of medical information with and the inappropriate use of medical information by affiliates.

Finally, the sixth exception provides that the special restrictions on sharing medically related information with affiliates would not apply if otherwise permitted by order of the appropriate agency. This exception incorporates the authority delegated to the Agencies by the Congress to create exceptions through orders. Privacy advocates, consumer and community groups, and health care associations acknowledged the authority of the Agencies to expand the affiliate-sharing exceptions by order. This exception is adopted as proposed in paragraph (b)(6).

As noted in the proposal, the prohibitions on obtaining or using medical information in § __.30 operate independently from the exceptions that permit the sharing of that information among affiliates in accordance with the provisions of section 603(d)(2) of the Act. For example, if a mortgage lender has obtained and used medical information in accordance with one of the exceptions in § __.30(c) or (d), the mortgage lender may share that information with its credit card affiliate without becoming a consumer reporting agency if one of the exceptions in § __.32(b) applies. However, the credit card affiliate may not obtain or use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit, except to the extent permitted by § __.30.

Effective Date and Solicitation of Comments

The statute provides that the final rules shall take effect on the later of 90 days after the rules are issued in final form, or the date specified in the regulations. Commenters believed that the effective date of the final rules should be no sooner than 90 days after the rules are issued in final form, although many commenters requested a longer period before the final rules take effect. Commenters generally believed that the effective date should be synchronized with the statutory prohibition, so that creditors would not be subject to the prohibition on obtaining or using medical information before the effective date of the regulatory exceptions. The interim final rules shall take effect on March 7, 2006, which is 270 days after the date of publication in the **Federal Register**. Comments on the interim final rule must be received by July 11, 2005.

V. Regulatory Analysis

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506, *et seq.*) and its implementing regulations at 5 CFR part 1320, including Appendix A.1, the Agencies have reviewed the interim final rules and determined that they contain no collections of information. The Board

made this determination under authority delegated by the Office of Management and Budget.

Regulatory Flexibility Analysis

OCC: The OCC received no comment on its Initial Regulatory Flexibility Analysis published in connection with the April 28, 2004, NPRM. Upon further review, the OCC certifies that this interim final rule will not have a significant economic impact on a substantial number of small entities.

Under section 605(b) of the Regulatory Flexibility Act (RFA), 5 U.S.C. 605(b), the regulatory flexibility analysis otherwise required under section 604 of the RFA is not required if an agency certifies, along with a statement providing the factual basis for such certification, that the rule will not have a significant economic impact on a substantial number of small entities. The OCC has reviewed the impact of this interim final rule on small entities and certifies that it will not have a significant economic impact on a substantial number of small entities.

The Small Business Administration (SBA) has defined ''small entities'' for banking purposes as a bank or savings institution with assets of $150 million or less. *See* 13 CFR 121.201. The interim final rule implements section 411 of the FACT Act and imposes only minimal economic impact on national banks. The interim final rule creates exceptions to the FACT Act's prohibition against national banks obtaining and using a consumer's medical information in connection with credit determinations. Additionally, the interim final rule implements the FACT Act's restrictions on the sharing of medical information among affiliates and includes exceptions to permit the sharing of medical information in certain circumstances. The interim final rule applies to national banks, Federal branches and agencies, their respective subsidiaries, and persons that participate in a credit transaction involving a national bank, Federal Branch or agency, or their respective subsidiaries (''entities'') that obtain or use medical information in connection with credit determinations, regardless of their size. However, it is likely that small entities, because of the nature and size of their operations, will encounter fewer instances where they might obtain or use medical information. Therefore, the interim final rule is not expected to result in a significant economic impact for small national entities.

Board: The Board has prepared a final regulatory flexibility analysis as required by the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*).

1. *Statement of the need for and objectives of the interim final rule.* The FACT Act amends the FCRA and was enacted, in part, for the purpose of protecting consumers' medical information. Section 411 of the FACT Act contains a general prohibition on creditors obtaining or using medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit. Section 411 authorizes the Board, together with the other Agencies, to create exceptions to allow creditors to obtain or use medical information for eligibility purposes where necessary and appropriate to protect legitimate operational, transactional risk, consumer, and other needs, consistent with the Congressional intent to restrict the use of medical information for inappropriate purposes.

Section 411 also limits the ability of an institution to share medical information with its affiliates without becoming a consumer reporting agency, subject to certain exceptions, and restricts the redisclosure of medical information. The statute authorizes the Board to issue regulations to create additional exceptions that are determined to be necessary and appropriate to permit the sharing of medical information among affiliates. The Board is adopting the interim final rule to create exceptions that permit creditors to obtain and use medical information in credit eligibility determinations, restate the limits on redisclosure, and restate and add to the exceptions that allow sharing among affiliates. The **SUPPLEMENTARY INFORMATION** above contains information on the objectives of the interim final rule.

2. *Summary of issues raised by comments in response to the initial regulatory flexibility analysis.* In accordance with section 3(a) of the Regulatory Flexibility Act, the Board conducted an initial regulatory flexibility analysis in connection with the proposed rule. The Board did not receive any comments on its initial regulatory flexibility analysis.

3. *Description of small entities affected by the proposal.* Each section of the interim final rule applies to different types of small entities and specifies the types of small entities subject to that section. The interim final rule would apply, in whole or in part, to banks that are members of the Federal Reserve System (other than national banks) and their subsidiaries, branches and Agencies of foreign banks (other than Federal branches, Federal Agencies, and insured State branches of foreign banks) and their subsidiaries, commercial lending companies owned or controlled by foreign banks, organizations operating under section 25 or 25A of the Federal Reserve Act (12 U.S.C. 601 *et seq.*, and 611 *et seq.*), bank holding companies and affiliates of such holding companies (other than depository institutions and consumer reporting agencies), and creditors that participate in a transaction with one of the above-mentioned entities. A separate rule would apply to creditors not otherwise subject to one of the Agency rules. The Board's interim final rule will apply to the following institutions (numbers approximate): State member banks (932), bank holding companies (5,152), holding company non-bank subsidiaries (2,131), U.S. branches and agencies of foreign banks (289), and Edge and agreement corporations (75), for a subtotal of approximately 8,579 institutions. The Board estimates that over 5,000 of these institutions could be considered small institutions with assets less than $150 million. The Board is unable to estimate the number of creditors that may participate in transactions with such institutions or the number of other creditors that may be covered by the separate rule.

All small entities that are creditors will be affected by the provision of the interim final rule that addresses the prohibition on, and exceptions to, creditors obtaining or using medical information in connection with credit eligibility determinations. All small creditors will have to comply with the exceptions if they obtain or use medical information about consumers in connection with any credit eligibility determination.

4. *Recordkeeping, reporting, and compliance requirements.* The interim final rule requires certain documentation to qualify for some of the specific exceptions, as discussed in the **SUPPLEMENTARY INFORMATION** above. The interim final rule contains no reporting or disclosure requirements.

5. *Steps taken to minimize the economic impact on small entities.* The Board solicited comment on how to minimize the economic impact on small entities. The Board did not receive any comments on this issue. By adopting consistent rules and exceptions, the Board and the other Agencies have attempted to minimize the economic impact on small entities.

FDIC: The Agencies received no comments on their initial regulatory flexibility analyses. Upon further analysis, the FDIC certifies that this rule creating exceptions to the FACT Act's general prohibition on creditors obtaining or using medical information

pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit will not have a significant economic impact on small entities. This interim final rule, as authorized by section 411 of the FACT Act, creates exceptions to allow creditors to obtain or use medical information for eligibility purposes where necessary and appropriate to protect legitimate operational, transactional risk, consumer, and other needs, consistent with the Congressional intent to restrict the use of medical information for inappropriate purposes. The rule also excludes, in certain situations, medical information shared by a covered entity with an affiliate from the definition of a consumer report in section 603(d) of the FCRA, and addresses the reuse and redisclosure of medical information.

OTS: In accordance with section 603(a) of the Regulatory Flexibility Act (RFA) (5 U.S.C. 603(a)), OTS conducted an initial regulatory flexibility analysis in connection with the April 28, 2004 proposed rule. OTS did not receive any comments on its initial regulatory flexibility analysis.

Upon further analysis, OTS certifies in accordance with section 605(b) of the RFA (5 U.S.C. 605(b)) that this interim final rule will not have a significant economic impact on a substantial number of small entities. The Small Business Administration (SBA) has generally defined small savings institutions for RFA purposes as those with assets of $150 million or less. 13 CFR 121.201.

This interim final rule implements section 411 of the FACT Act and imposes only minimal economic impact. Section 571.30 creates exceptions to allow creditors to obtain or use medical information for credit eligibility purposes where necessary and appropriate to protect legitimate operational, transactional risk, consumer, and other needs, consistent with the congressional intent to restrict the use of medical information for inappropriate purposes. It applies to all any of the following, regardless of size, that participates as a creditor in a transaction: (1) A savings association; (2) a subsidiary owned in whole or in part by a savings association; (3) a savings and loan holding company; (4) a subsidiary of a savings and loan holding company other than a bank or subsidiary of a bank; (5) a service corporation owned in whole or in part by a savings association; or (6) any other person that participates as a creditor in a transaction involving a person described (1)–(5).

Section 571.31 implements the FACT Act's restrictions on the redisclosure of information. Section 571.32 implements the FACT Act's restrictions on the sharing of medical information among affiliates and includes exceptions to permit the sharing of medical information in certain circumstances. These sections apply to savings associations and Federal savings association operating subsidiaries, regardless of size.

As referenced elsewhere in this **SUPPLEMENTARY INFORMATION,** other laws and regulations, such as the Fair Housing Act, the Americans with Disabilities Act, and OTS's anti-discrimination rules in 12 CFR part 528, also limit or regulate obtaining and using medical information for credit eligibility determinations in a manner that discriminates against persons whose medical condition constitutes a ''disability'' or ''handicap'' under those authorities. Other laws, such as the GLB Act, HIPAA, and other parts of the FCRA, also limit or regulate the use, collection, and sharing of consumer information, including medical information. The industry's preexisting familiarity and compliance with the requirements of these other authorities to the extent applicable is one factor that OTS expects will minimize the economic impact of today's interim final rule.

NCUA: The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact any regulation may have on a substantial number of small entities. NCUA considers credit unions having less than ten million dollars in assets to be small for purposes of the Regulatory Flexibility Act. NCUA Interpretive Ruling and Policy Statement (IRPS) 87–2, as amended by IRPS 03–2. NCUA conducted an initial regulatory flexibility analysis in connection with the proposed rule and did not receive any comments on it.

Upon further review, NCUA certifies that this interim final rule will not have a significant economic impact on a substantial number of small entities. The interim final rule applies to all Federal credit unions that obtain or use a consumer's medical information in connection with credit determinations, regardless of credit union size. The interim final rule creates exceptions to the FACT Act's prohibition against Federal credit unions obtaining and using such information in connection with credit determinations. Additionally, the interim final rule implements the FACT Act's restrictions on the sharing of medical information among Federal credit union affiliates, credit union service organizations (CUSOs), and includes exceptions to permit the sharing of medical information in certain circumstances.

FDIC—Small Business Regulatory Enforcement Act

The Small Business Regulatory Enforcement Act of 1996 (SBREFA) (Pub. L. 104–121, 110 Stat. 857) provides generally for agencies to report rules to Congress and for Congress to review these rules. The reporting requirement is triggered in instances where the FDIC issues a final rule as defined by the Administrative Procedure Act (APA) (5 U.S.C. 55, *et seq.*). Because the FDIC is issuing a final rule as defined by the APA, the FDIC will file the reports required by SBREFA.

OCC and OTS Executive Order 12866 Determination

The OCC and OTS each has determined that its portion of the rule is not a significant regulatory action under Executive Order 12866.

OCC Executive Order 13132 Determination

The OCC has determined that this rule does not have any Federalism implications, as required by Executive Order 13132.

NCUA Executive Order 13132 Determination

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, the NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The rule applies only to federally chartered credit unions and would not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. The NCUA has determined that this rule does not constitute a policy that has federalism implications for purposes of the executive order.

OCC and OTS Unfunded Mandates Reform Act of 1995 Determination

Section 202 of the Unfunded Mandates Reform Act of 1995, Public Law 104–4 (Unfunded Mandates Act) requires that an agency prepare a budgetary impact statement before promulgating a rule that includes a Federal mandate that may result in expenditure by State, local, and tribal

governments, in the aggregate, or by the private sector, of $100 million or more in any one year. If a budgetary impact statement is required, section 205 of the Unfunded Mandates Act also requires an agency to identify and consider a reasonable number of regulatory alternatives before promulgating a rule. The OCC and OTS each has determined that this rule will not result in expenditures by State, local, and tribal governments, or by the private sector, of $100 million or more. Accordingly, neither the OCC nor the OTS has prepared a budgetary impact statement or specifically addressed the regulatory alternatives considered.

NCUA: The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Plain Language Requirement

Section 722 of the Gramm-Leach-Bliley Act (GLBA) (12 U.S.C. 4809), requires the Federal banking agencies to use plain language in all proposed and final rules published after January 1, 2000. The proposed rule requested comments on how the rule might be changed to reflect the requirements of GLBA. No GLBA comments were received.

List of Subjects

12 CFR Part 41

Banks, banking, Consumer protection, National banks, Reporting and recordkeeping requirements.

12 CFR Part 222

Banks, banking, Consumer protection, Credit, Fair Credit Reporting Act, Holding companies, Privacy, Reporting and recordkeeping requirements, State member banks.

12 CFR Part 232

Consumer protection, Credit, Fair Credit Reporting Act, Privacy, Reporting and recordkeeping requirements.

12 CFR Part 334

Administrative practice and procedure, Bank deposit insurance, Banks, banking, Reporting and recordkeeping requirements, Safety and soundness.

12 CFR Part 571

Consumer protection, Credit, Fair Credit Reporting Act, Privacy, Reporting and recordkeeping requirements, Savings associations.

12 CFR Part 717

Consumer protection, Credit unions, Fair credit reporting, Medical information, Privacy, Reporting and recordkeeping requirements.

Office of the Comptroller of the Currency

12 CFR Chapter I.

Authority and Issuance

■ For the reasons set forth in the preamble, the OCC amends Chapter I of Title 12 of the Code of Federal Regulations as follows:

PART 41—FAIR CREDIT

■ 1. Revise the authority citation for part 41 to read as follows:

Authority: 12 U.S.C. 1 *et seq.*, 24(Seventh), 93a, 481, 484, and 1818; 15 U.S.C. 1681a, 1681b, 1681s, 1681w, 6801, and 6805.

■ 2. Revise subpart A to read as follows:

Subpart A—General Provisions

§ 41.2 Examples.

The examples in this part are not exclusive. Compliance with an example, to the extent applicable, constitutes compliance with this part. Examples in a paragraph illustrate only the issue described in the paragraph and do not illustrate any other issue that may arise in this part.

§ 41.3 Definitions.

As used in this part, unless the context requires otherwise:

(a) *Act* means the Fair Credit Reporting Act (15 U.S.C. 1681 *et seq.*).

(b) *Affiliate* means any company that is related by common ownership or common corporate control with another company.

(c) [Reserved]

(d) *Company* means any corporation, limited liability company, business trust, general or limited partnership, association, or similar organization.

(e) *Consumer* means an individual.

(f) [Reserved]

(g) [Reserved]

(h) [Reserved]

(i) *Common ownership or common corporate control* means a relationship between two companies under which:

(1) One company has, with respect to the other company:

(i) Ownership, control, or power to vote 25 percent or more of the outstanding shares of any class of voting security of a company, directly or indirectly, or acting through one or more other persons;

(ii) Control in any manner over the election of a majority of the directors, trustees, or general partners (or individuals exercising similar functions) of a company; or

(iii) The power to exercise, directly or indirectly, a controlling influence over the management or policies of a company, as the OCC determines; or

(2) Any other person has, with respect to both companies, a relationship described in paragraphs (i)(1)(i)-(i)(1)(iii) of this section.

(j) [Reserved]

(k) *Medical information* means:

(1) Information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to—

(i) The past, present, or future physical, mental, or behavioral health or condition of an individual;

(ii) The provision of health care to an individual; or

(iii) The payment for the provision of health care to an individual.

(2) The term does not include:

(i) The age or gender of a consumer;

(ii) Demographic information about the consumer, including a consumer's residence address or e-mail address;

(iii) Any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy; or

(iv) Information that does not identify a specific consumer.

(l) *Person* means any individual, partnership, corporation, trust, estate cooperative, association, government or governmental subdivision or agency, or other entity.

■ 3. Add subpart D to read as follows:

Subpart D—Medical Information

§ 41.30 Obtaining or using medical information in connection with a determination of eligibility for credit.

(a) *Scope.* This section applies to:

(1) Any person that participates as a creditor in a transaction and that is a national bank, a Federal branch or agency of a foreign bank, and their respective subsidiaries; or

(2) Any other person that participates as a creditor in a transaction involving a person described in paragraph (a)(1) of this section.

(b) *General prohibition on obtaining or using medical information.* (1) *In general.* A creditor may not obtain or use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for

credit, except as provided in this section.

(2) *Definitions.* (i) *Credit* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(ii) *Creditor* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(iii) *Eligibility, or continued eligibility, for credit* means the consumer's qualification or fitness to receive, or continue to receive, credit, including the terms on which credit is offered. The term does not include:

(A) Any determination of the consumer's qualification or fitness for employment, insurance (other than a credit insurance product), or other non-credit products or services;

(B) Authorizing, processing, or documenting a payment or transaction on behalf of the consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit; or

(C) Maintaining or servicing the consumer's account in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit.

(c) *Rule of construction for obtaining and using unsolicited medical information.* (1) *In general.* A creditor does not obtain medical information in violation of the prohibition if it receives medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit without specifically requesting medical information.

(2) *Use of unsolicited medical information.* A creditor that receives unsolicited medical information in the manner described in paragraph (c)(1) of this section may use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit to the extent the creditor can rely on at least one of the exceptions in § 41.30(d) or (e).

(3) *Examples.* A creditor does not obtain medical information in violation of the prohibition if, for example:

(i) In response to a general question regarding a consumer's debts or expenses, the creditor receives information that the consumer owes a debt to a hospital.

(ii) In a conversation with the creditor's loan officer, the consumer informs the creditor that the consumer has a particular medical condition.

(iii) In connection with a consumer's application for an extension of credit, the creditor requests a consumer report from a consumer reporting agency and receives medical information in the consumer report furnished by the agency even though the creditor did not specifically request medical information from the consumer reporting agency.

(d) *Financial information exception for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit so long as:

(i) The information is the type of information routinely used in making credit eligibility determinations, such as information relating to debts, expenses, income, benefits, assets, collateral, or the purpose of the loan, including the use of proceeds;

(ii) The creditor uses the medical information in a manner and to an extent that is no less favorable than it would use comparable information that is not medical information in a credit transaction; and

(iii) The creditor does not take the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis into account as part of any such determination.

(2) *Examples.* (i) *Examples of the types of information routinely used in making credit eligibility determinations.* Paragraph (d)(1)(i) of this section permits a creditor, for example, to obtain and use information about:

(A) The dollar amount, repayment terms, repayment history, and similar information regarding medical debts to calculate, measure, or verify the repayment ability of the consumer, the use of proceeds, or the terms for granting credit;

(B) The value, condition, and lien status of a medical device that may serve as collateral to secure a loan;

(C) The dollar amount and continued eligibility for disability income or benefits related to health or a medical condition that is relied on as a source of repayment; or

(D) The identity of creditors to whom outstanding medical debts are owed in connection with an application for credit, including but not limited to, a transaction involving the consolidation of medical debts.

(ii) *Examples of uses of medical information consistent with the exception.* (A) A consumer includes on an application for credit information about two $20,000 debts. One debt is to a hospital; the other debt is to a retailer. The creditor contacts the hospital and the retailer to verify the amount and payment status of the debts. The creditor learns that both debts are more than 90 days past due. Any two debts of this size that are more than 90 days past due would disqualify the consumer under the creditor's established underwriting criteria. The creditor denies the application on the basis that the consumer has a poor repayment history on outstanding debts. The creditor has used medical information in a manner and to an extent no less favorable than it would use comparable non-medical information.

(B) A consumer indicates on an application for a $200,000 mortgage loan that she receives $15,000 in long-term disability income each year from her former employer and has no other income. Annual income of $15,000, regardless of source, would not be sufficient to support the requested amount of credit. The creditor denies the application on the basis that the projected debt-to-income ratio of the consumer does not meet the creditor's underwriting criteria. The creditor has used medical information in a manner and to an extent that is no less favorable than it would use comparable non-medical information.

(C) A consumer includes on an application for a $10,000 home equity loan that he has a $50,000 debt to a medical facility that specializes in treating a potentially terminal disease. The creditor contacts the medical facility to verify the debt and obtain the repayment history and current status of the loan. The creditor learns that the debt is current. The applicant meets the income and other requirements of the creditor's underwriting guidelines. The creditor grants the application. The creditor has used medical information in accordance with the exception.

(iii) *Examples of uses of medical information inconsistent with the exception.* (A) A consumer applies for $25,000 of credit and includes on the application information about a $50,000 debt to a hospital. The creditor contacts the hospital to verify the amount and payment status of the debt, and learns that the debt is current and that the consumer has no delinquencies in her repayment history. If the existing debt were instead owed to a retail department store, the creditor would approve the application and extend credit based on the amount and repayment history of the outstanding debt. The creditor, however, denies the application because the consumer is indebted to a hospital. The creditor has used medical information, here the identity of the medical creditor, in a manner and to an extent that is less favorable than it would use comparable non-medical information.

(B) A consumer meets with a loan officer of a creditor to apply for a

mortgage loan. While filling out the loan application, the consumer informs the loan officer orally that she has a potentially terminal disease. The consumer meets the creditor's established requirements for the requested mortgage loan. The loan officer recommends to the credit committee that the consumer be denied credit because the consumer has that disease. The credit committee follows the loan officer's recommendation and denies the application because the consumer has a potentially terminal disease. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis as part of a determination of eligibility or continued eligibility for credit.

(C) A consumer who has an apparent medical condition, such as a consumer who uses a wheelchair or an oxygen tank, meets with a loan officer to apply for a home equity loan. The consumer meets the creditor's established requirements for the requested home equity loan and the creditor typically does not require consumers to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product in connection with such loans. However, based on the consumer's apparent medical condition, the loan officer recommends to the credit committee that credit be extended to the consumer only if the consumer obtains a debt cancellation contract, debt suspension agreement, or credit insurance product. The credit committee agrees with the loan officer's recommendation. The loan officer informs the consumer that the consumer must obtain a debt cancellation contract, debt suspension agreement, or credit insurance product to qualify for the loan. The consumer obtains one of these products from a third party and the creditor approves the loan. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis in setting conditions on the consumer's eligibility for credit.

(e) *Specific exceptions for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit—

(i) To determine whether the use of a power of attorney or legal representative that is triggered by a medical event or condition is necessary and appropriate or whether the consumer has the legal capacity to contract when a person seeks to exercise a power of attorney or act as legal representative for a consumer based on an asserted medical event or condition;

(ii) To comply with applicable requirements of local, State, or Federal laws;

(iii) To determine, at the consumer's request, whether the consumer qualifies for a legally permissible special credit program or credit-related assistance program that is—

(A) Designed to meet the special needs of consumers with medical conditions; and

(B) Established and administered pursuant to a written plan that—

(*1*) Identifies the class of persons that the program is designed to benefit; and

(*2*) Sets forth the procedures and standards for extending credit or providing other credit-related assistance under the program.

(iv) To the extent necessary for purposes of fraud prevention or detection;

(v) In the case of credit for the purpose of financing medical products or services, to determine and verify the medical purpose of a loan and the use of proceeds;

(vi) Consistent with safe and sound practices, if the consumer or the consumer's legal representative specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular circumstances, and such request is documented by the creditor;

(vii) Consistent with safe and sound practices, to determine whether the provisions of a forbearance practice or program that is triggered by a medical event or condition apply to a consumer;

(viii) To determine the consumer's eligibility for, the triggering of, or the reactivation of a debt cancellation contract or debt suspension agreement if a medical condition or event is a triggering event for the provision of benefits under the contract or agreement; or

(ix) To determine the consumer's eligibility for, the triggering of, or the reactivation of a credit insurance product if a medical condition or event is a triggering event for the provision of benefits under the product.

(2) *Example of determining eligibility for a special credit program or credit assistance program.* A not-for-profit organization establishes a credit assistance program pursuant to a written plan that is designed to assist disabled veterans in purchasing homes by subsidizing the down payment for the home purchase mortgage loans of qualifying veterans. The organization works through mortgage lenders and requires mortgage lenders to obtain medical information about the disability of any consumer that seeks to qualify for the program, use that information to verify the consumer's eligibility for the program, and forward that information to the organization. A consumer who is a veteran applies to a creditor for a home purchase mortgage loan. The creditor informs the consumer about the credit assistance program for disabled veterans and the consumer seeks to qualify for the program. Assuming that the program complies with all applicable law, including applicable fair lending laws, the creditor may obtain and use medical information about the medical condition and disability, if any, of the consumer to determine whether the consumer qualifies for the credit assistance program.

(3) *Examples of verifying the medical purpose of the loan or the use of proceeds.* (i) If a consumer applies for $10,000 of credit for the purpose of financing vision correction surgery, the creditor may verify with the surgeon that the procedure will be performed. If the surgeon reports that surgery will not be performed on the consumer, the creditor may use that medical information to deny the consumer's application for credit, because the loan would not be used for the stated purpose.

(ii) If a consumer applies for $10,000 of credit for the purpose of financing cosmetic surgery, the creditor may confirm the cost of the procedure with the surgeon. If the surgeon reports that the cost of the procedure is $5,000, the creditor may use that medical information to offer the consumer only $5,000 of credit.

(iii) A creditor has an established medical loan program for financing particular elective surgical procedures. The creditor receives a loan application from a consumer requesting $10,000 of credit under the established loan program for an elective surgical procedure. The consumer indicates on the application that the purpose of the loan is to finance an elective surgical procedure not eligible for funding under the guidelines of the established loan program. The creditor may deny the consumer's application because the purpose of the loan is not for a particular procedure funded by the established loan program.

(4) *Examples of obtaining and using medical information at the request of*

the consumer. (i) If a consumer applies for a loan and specifically requests that the creditor consider the consumer's medical disability at the relevant time as an explanation for adverse payment history information in his credit report, the creditor may consider such medical information in evaluating the consumer's willingness and ability to repay the requested loan to accommodate the consumer's particular circumstances, consistent with safe and sound practices. The creditor may also decline to consider such medical information to accommodate the consumer, but may evaluate the consumer's application in accordance with its otherwise applicable underwriting criteria. The creditor may not deny the consumer's application or otherwise treat the consumer less favorably because the consumer specifically requested a medical accommodation, if the creditor would have extended the credit or treated the consumer more favorably under the creditor's otherwise applicable underwriting criteria.

(ii) If a consumer applies for a loan by telephone and explains that his income has been and will continue to be interrupted on account of a medical condition and that he expects to repay the loan by liquidating assets, the creditor may, but is not required to, evaluate the application using the sale of assets as the primary source of repayment, consistent with safe and sound practices, provided that the creditor documents the consumer's request by recording the oral conversation or making a notation of the request in the consumer's file.

(iii) If a consumer applies for a loan and the application form provides a space where the consumer may provide any other information or special circumstances, whether medical or non-medical, that the consumer would like the creditor to consider in evaluating the consumer's application, the creditor may use medical information provided by the consumer in that space on that application to accommodate the consumer's application for credit, consistent with safe and sound practices, or may disregard that information.

(iv) If a consumer specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit and provides the creditor with medical information for that purpose, and the creditor determines that it needs additional information regarding the consumer's circumstances, the creditor may request, obtain, and use additional medical information about the consumer as necessary to verify the information provided by the consumer or to determine whether to make an accommodation for the consumer. The consumer may decline to provide additional information, withdraw the request for an accommodation, and have the application considered under the creditor's otherwise applicable underwriting criteria.

(v) If a consumer completes and signs a credit application that is not for medical purpose credit and the application contains boilerplate language that routinely requests medical information from the consumer or that indicates that by applying for credit the consumer authorizes or consents to the creditor obtaining and using medical information in connection with a determination of the consumer's eligibility, or continued eligibility, for credit, the consumer has not specifically requested that the creditor obtain and use medical information to accommodate the consumer's particular circumstances.

(5) *Example of a forbearance practice or program.* After an appropriate safety and soundness review, a creditor institutes a program that allows consumers who are or will be hospitalized to defer payments as needed for up to three months, without penalty, if the credit account has been open for more than one year and has not previously been in default, and the consumer provides confirming documentation at an appropriate time. A consumer is hospitalized and does not pay her bill for a particular month. This consumer has had a credit account with the creditor for more than one year and has not previously been in default. The creditor attempts to contact the consumer and speaks with the consumer's adult child, who is not the consumer's legal representative. The adult child informs the creditor that the consumer is hospitalized and is unable to pay the bill at that time. The creditor defers payments for up to three months, without penalty, for the hospitalized consumer and sends the consumer a letter confirming this practice and the date on which the next payment will be due.

§ 41.31 Limits on redisclosure of information.

(a) *Scope.* This section applies to national banks, Federal branches and agencies of foreign banks, and their respective operating subsidiaries.

(b) *Limits on redisclosure.* If a person described in paragraph (a) of this section receives medical information about a consumer from a consumer reporting agency or its affiliate, the person must not disclose that information to any other person, except as necessary to carry out the purpose for which the information was initially disclosed, or as otherwise permitted by statute, regulation, or order.

§ 41.32 Sharing medical information with affiliates.

(a) *Scope.* This section applies to national banks, Federal branches and agencies of foreign banks, and their respective operating subsidiaries.

(b) *In general.* The exclusions from the term ''consumer report'' in section 603(d)(2) of the Act that allow the sharing of information with affiliates do not apply if a person described in paragraph (a) of this section communicates to an affiliate—

(1) Medical information;

(2) An individualized list or description based on the payment transactions of the consumer for medical products or services; or

(3) An aggregate list of identified consumers based on payment transactions for medical products or services.

(c) *Exceptions.* A person described in paragraph (a) may rely on the exclusions from the term ''consumer report'' in section 603(d)(2) of the Act to communicate the information in paragraph (b) to an affiliate—

(1) In connection with the business of insurance or annuities (including the activities described in section 18B of the model Privacy of Consumer Financial and Health Information Regulation issued by the National Association of Insurance Commissioners, as in effect on January 1, 2003);

(2) For any purpose permitted without authorization under the regulations promulgated by the Department of Health and Human Services pursuant to the Health Insurance Portability and Accountability Act of 1996 (HIPAA);

(3) For any purpose referred to in section 1179 of HIPAA;

(4) For any purpose described in section 502(e) of the Gramm-Leach-Bliley Act;

(5) In connection with a determination of the consumer's eligibility, or continued eligibility, for credit consistent with § 41.30; or

(6) As otherwise permitted by order of the OCC.

Board of Governors of the Federal Reserve System

12 CFR Chapter II.

Authority and Issuance

■ For the reasons set forth in the joint preamble, title 12, chapter II, of the

Code
of Federal Regulations is amended as follows:

PART 222—FAIR CREDIT REPORTING (REGULATION V)

■ 1. The authority citation for part 222 is revised to read as follows:

Authority: 15 U.S.C. 1681b and 1681s; Secs. 3, 214, and 217, Pub. L. 108–159, 117 Stat. 1952.

Subpart A—General Provisions

■ 2. Amend subpart A to part 222 by adding §§ 222.2 and 222.3 to read as follows:

§ 222.2 Examples.

The examples in this part are not exclusive. Compliance with an example, to the extent applicable, constitutes compliance with this part. Examples in a paragraph illustrate only the issue described in the paragraph and do not illustrate any other issue that may arise in this part.

§ 222.3 Definitions.

As used in this part, unless the context requires otherwise:

(a) *Act* means the Fair Credit Reporting Act (15 U.S.C. 1681 *et seq.*).

(b) *Affiliate* means any company that is related by common ownership or common corporate control with another company.

(c) [Reserved]

(d) *Company* means any corporation, limited liability company, business trust, general or limited partnership, association, or similar organization.

(e) *Consumer* means an individual.

(f) [Reserved]

(g) [Reserved]

(h) [Reserved]

(i) *Common ownership or common corporate control* means a relationship between two companies under which:

(1) One company has, with respect to the other company:

(i) Ownership, control, or power to vote 25 percent or more of the outstanding shares of any class of voting security of a company, directly or indirectly, or acting through one or more other persons;

(ii) Control in any manner over the election of a majority of the directors, trustees, or general partners (or individuals exercising similar functions) of a company; or

(iii) The power to exercise, directly or indirectly, a controlling influence over the management or policies of a company, as the Board determines; or

(2) Any other person has, with respect to both companies, a relationship described in paragraphs (i)(1)(i)–(i)(1)(iii) of this section.

(j) [Reserved]

(k) *Medical information* means:

(1) Information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to—

(i) The past, present, or future physical, mental, or behavioral health or condition of an individual;

(ii) The provision of health care to an individual; or

(iii) The payment for the provision of health care to an individual.

(2) The term does not include:

(i) The age or gender of a consumer;

(ii) Demographic information about the consumer, including a consumer's residence address or e-mail address;

(iii) Any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy; or

(iv) Information that does not identify a specific consumer.

(l) *Person* means any individual, partnership, corporation, trust, estate cooperative, association, government or governmental subdivision or agency, or other entity.

■ 3. Subpart D is added to part 222 to read as follows:

Subpart D—Medical Information

Sec.
222.30 Obtaining or using medical information in connection with a determination of eligibility for credit.
222.31 Limits on redisclosure of information.
222.32 Sharing medical information with affiliates.

Subpart D—Medical Information

§ 222.30 Obtaining or using medical information in connection with a determination of eligibility for credit.

(a) *Scope.* This section applies to

(1) Any of the following that participates as a creditor in a transaction—

(i) A bank that is a member of the Federal Reserve System (other than national banks) and its subsidiaries;

(ii) A branch or Agency of a foreign bank (other than Federal branches, Federal Agencies, and insured State branches of foreign banks) and its subsidiaries;

(iii) A commercial lending company owned or controlled by foreign banks;

(iv) An organization operating under section 25 or 25A of the Federal Reserve Act (12 U.S.C. 601 *et seq.*, and 611 *et seq.*);

(v) A bank holding company and an affiliate of such holding company (other than depository institutions and consumer reporting agencies); or

(2) Any other person that participates as a creditor in a transaction involving a person described in paragraph (a)(1) of this section.

(b) *General prohibition on obtaining or using medical information.* (1) *In general.* A creditor may not obtain or use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit, except as provided in this section.

(2) *Definitions.* (i) *Credit* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(ii) *Creditor* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(iii) *Eligibility, or continued eligibility, for credit* means the consumer's qualification or fitness to receive, or continue to receive, credit, including the terms on which credit is offered. The term does not include:

(A) Any determination of the consumer's qualification or fitness for employment, insurance (other than a credit insurance product), or other non-credit products or services;

(B) Authorizing, processing, or documenting a payment or transaction on behalf of the consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit; or

(C) Maintaining or servicing the consumer's account in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit.

(c) *Rule of construction for obtaining and using unsolicited medical information.* (1) *In general.* A creditor does not obtain medical information in violation of the prohibition if it receives medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit without specifically requesting medical information.

(2) *Use of unsolicited medical information.* A creditor that receives unsolicited medical information in the manner described in paragraph (c)(1) of this section may use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit to the extent the creditor can rely on at least one of the exceptions in § 222.30(d) or (e).

(3) *Examples.* A creditor does not obtain medical information in violation of the prohibition if, for example:

(i) In response to a general question regarding a consumer's debts or expenses, the creditor receives information that the consumer owes a debt to a hospital.

(ii) In a conversation with the creditor's loan officer, the consumer informs the creditor that the consumer has a particular medical condition.

(iii) In connection with a consumer's application for an extension of credit, the creditor requests a consumer report from a consumer reporting agency and receives medical information in the consumer report furnished by the agency even though the creditor did not specifically request medical information from the consumer reporting agency.

(d) *Financial information exception for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit so long as:

(i) The information is the type of information routinely used in making credit eligibility determinations, such as information relating to debts, expenses, income, benefits, assets, collateral, or the purpose of the loan, including the use of proceeds;

(ii) The creditor uses the medical information in a manner and to an extent that is no less favorable than it would use comparable information that is not medical information in a credit transaction; and

(iii) The creditor does not take the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis into account as part of any such determination.

(2) *Examples.* (i) *Examples of the types of information routinely used in making credit eligibility determinations.* Paragraph (d)(1)(i) of this section permits a creditor, for example, to obtain and use information about:

(A) The dollar amount, repayment terms, repayment history, and similar information regarding medical debts to calculate, measure, or verify the repayment ability of the consumer, the use of proceeds, or the terms for granting credit;

(B) The value, condition, and lien status of a medical device that may serve as collateral to secure a loan;

(C) The dollar amount and continued eligibility for disability income or benefits related to health or a medical condition that is relied on as a source of repayment; or

(D) The identity of creditors to whom outstanding medical debts are owed in connection with an application for credit, including but not limited to, a transaction involving the consolidation of medical debts.

(ii) *Examples of uses of medical information consistent with the exception.* (A) A consumer includes on an application for credit information about two $20,000 debts. One debt is to a hospital; the other debt is to a retailer. The creditor contacts the hospital and the retailer to verify the amount and payment status of the debts. The creditor learns that both debts are more than 90 days past due. Any two debts of this size that are more than 90 days past due would disqualify the consumer under the creditor's established underwriting criteria. The creditor denies the application on the basis that the consumer has a poor repayment history on outstanding debts. The creditor has used medical information in a manner and to an extent no less favorable than it would use comparable non-medical information.

(B) A consumer indicates on an application for a $200,000 mortgage loan that she receives $15,000 in long-term disability income each year from her former employer and has no other income. Annual income of $15,000, regardless of source, would not be sufficient to support the requested amount of credit. The creditor denies the application on the basis that the projected debt-to-income ratio of the consumer does not meet the creditor's underwriting criteria. The creditor has used medical information in a manner and to an extent that is no less favorable than it would use comparable non-medical information.

(C) A consumer includes on an application for a $10,000 home equity loan that he has a $50,000 debt to a medical facility that specializes in treating a potentially terminal disease. The creditor contacts the medical facility to verify the debt and obtain the repayment history and current status of the loan. The creditor learns that the debt is current. The applicant meets the income and other requirements of the creditor's underwriting guidelines. The creditor grants the application. The creditor has used medical information in accordance with the exception.

(iii) *Examples of uses of medical information inconsistent with the exception.* (A) A consumer applies for $25,000 of credit and includes on the application information about a $50,000 debt to a hospital. The creditor contacts the hospital to verify the amount and payment status of the debt, and learns that the debt is current and that the consumer has no delinquencies in her repayment history. If the existing debt were instead owed to a retail department store, the creditor would approve the application and extend credit based on the amount and repayment history of the outstanding debt. The creditor, however, denies the application because the consumer is indebted to a hospital. The creditor has used medical information, here the identity of the medical creditor, in a manner and to an extent that is less favorable than it would use comparable non-medical information.

(B) A consumer meets with a loan officer of a creditor to apply for a mortgage loan. While filling out the loan application, the consumer informs the loan officer orally that she has a potentially terminal disease. The consumer meets the creditor's established requirements for the requested mortgage loan. The loan officer recommends to the credit committee that the consumer be denied credit because the consumer has that disease. The credit committee follows the loan officer's recommendation and denies the application because the consumer has a potentially terminal disease. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis as part of a determination of eligibility or continued eligibility for credit.

(C) A consumer who has an apparent medical condition, such as a consumer who uses a wheelchair or an oxygen tank, meets with a loan officer to apply for a home equity loan. The consumer meets the creditor's established requirements for the requested home equity loan and the creditor typically does not require consumers to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product in connection with such loans. However, based on the consumer's apparent medical condition, the loan officer recommends to the credit committee that credit be extended to the consumer only if the consumer obtains a debt cancellation contract, debt suspension agreement, or credit insurance product. The credit committee agrees with the loan officer's recommendation. The loan officer informs the consumer that the consumer must obtain a debt cancellation contract, debt suspension agreement, or credit insurance product to qualify for the loan. The consumer obtains one of these products from a third party and the creditor approves the loan. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's

physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis in setting conditions on the consumer's eligibility for credit.

(e) *Specific exceptions for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit—

(i) To determine whether the use of a power of attorney or legal representative that is triggered by a medical event or condition is necessary and appropriate or whether the consumer has the legal capacity to contract when a person seeks to exercise a power of attorney or act as legal representative for a consumer based on an asserted medical event or condition;

(ii) To comply with applicable requirements of local, State, or Federal laws;

(iii) To determine, at the consumer's request, whether the consumer qualifies for a legally permissible special credit program or credit-related assistance program that is—

(A) Designed to meet the special needs of consumers with medical conditions; and

(B) Established and administered pursuant to a written plan that—

(*1*) Identifies the class of persons that the program is designed to benefit; and

(*2*) Sets forth the procedures and standards for extending credit or providing other credit-related assistance under the program.

(iv) To the extent necessary for purposes of fraud prevention or detection;

(v) In the case of credit for the purpose of financing medical products or services, to determine and verify the medical purpose of a loan and the use of proceeds;

(vi) Consistent with safe and sound practices, if the consumer or the consumer's legal representative specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular circumstances, and such request is documented by the creditor;

(vii) Consistent with safe and sound practices, to determine whether the provisions of a forbearance practice or program that is triggered by a medical event or condition apply to a consumer;

(viii) To determine the consumer's eligibility for, the triggering of, or the reactivation of a debt cancellation contract or debt suspension agreement if a medical condition or event is a triggering event for the provision of benefits under the contract or agreement; or

(ix) To determine the consumer's eligibility for, the triggering of, or the reactivation of a credit insurance product if a medical condition or event is a triggering event for the provision of benefits under the product.

(2) *Example of determining eligibility for a special credit program or credit assistance program.* A not-for-profit organization establishes a credit assistance program pursuant to a written plan that is designed to assist disabled veterans in purchasing homes by subsidizing the down payment for the home purchase mortgage loans of qualifying veterans. The organization works through mortgage lenders and requires mortgage lenders to obtain medical information about the disability of any consumer that seeks to qualify for the program, use that information to verify the consumer's eligibility for the program, and forward that information to the organization. A consumer who is a veteran applies to a creditor for a home purchase mortgage loan. The creditor informs the consumer about the credit assistance program for disabled veterans and the consumer seeks to qualify for the program. Assuming that the program complies with all applicable law, including applicable fair lending laws, the creditor may obtain and use medical information about the medical condition and disability, if any, of the consumer to determine whether the consumer qualifies for the credit assistance program.

(3) *Examples of verifying the medical purpose of the loan or the use of proceeds.* (i) If a consumer applies for $10,000 of credit for the purpose of financing vision correction surgery, the creditor may verify with the surgeon that the procedure will be performed. If the surgeon reports that surgery will not be performed on the consumer, the creditor may use that medical information to deny the consumer's application for credit, because the loan would not be used for the stated purpose.

(ii) If a consumer applies for $10,000 of credit for the purpose of financing cosmetic surgery, the creditor may confirm the cost of the procedure with the surgeon. If the surgeon reports that the cost of the procedure is $5,000, the creditor may use that medical information to offer the consumer only $5,000 of credit.

(iii) A creditor has an established medical loan program for financing particular elective surgical procedures. The creditor receives a loan application from a consumer requesting $10,000 of credit under the established loan program for an elective surgical procedure. The consumer indicates on the application that the purpose of the loan is to finance an elective surgical procedure not eligible for funding under the guidelines of the established loan program. The creditor may deny the consumer's application because the purpose of the loan is not for a particular procedure funded by the established loan program.

(4) *Examples of obtaining and using medical information at the request of the consumer.* (i) If a consumer applies for a loan and specifically requests that the creditor consider the consumer's medical disability at the relevant time as an explanation for adverse payment history information in his credit report, the creditor may consider such medical information in evaluating the consumer's willingness and ability to repay the requested loan to accommodate the consumer's particular circumstances, consistent with safe and sound practices. The creditor may also decline to consider such medical information to accommodate the consumer, but may evaluate the consumer's application in accordance with its otherwise applicable underwriting criteria. The creditor may not deny the consumer's application or otherwise treat the consumer less favorably because the consumer specifically requested a medical accommodation, if the creditor would have extended the credit or treated the consumer more favorably under the creditor's otherwise applicable underwriting criteria.

(ii) If a consumer applies for a loan by telephone and explains that his income has been and will continue to be interrupted on account of a medical condition and that he expects to repay the loan by liquidating assets, the creditor may, but is not required to, evaluate the application using the sale of assets as the primary source of repayment, consistent with safe and sound practices, provided that the creditor documents the consumer's request by recording the oral conversation or making a notation of the request in the consumer's file.

(iii) If a consumer applies for a loan and the application form provides a space where the consumer may provide any other information or special circumstances, whether medical or non-medical, that the consumer would like the creditor to consider in evaluating the consumer's application, the creditor may use medical information provided by the consumer in that space on that application to accommodate the consumer's application for credit,

consistent with safe and sound practices, or may disregard that information.

(iv) If a consumer specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit and provides the creditor with medical information for that purpose, and the creditor determines that it needs additional information regarding the consumer's circumstances, the creditor may request, obtain, and use additional medical information about the consumer as necessary to verify the information provided by the consumer or to determine whether to make an accommodation for the consumer. The consumer may decline to provide additional information, withdraw the request for an accommodation, and have the application considered under the creditor's otherwise applicable underwriting criteria.

(v) If a consumer completes and signs a credit application that is not for medical purpose credit and the application contains boilerplate language that routinely requests medical information from the consumer or that indicates that by applying for credit the consumer authorizes or consents to the creditor obtaining and using medical information in connection with a determination of the consumer's eligibility, or continued eligibility, for credit, the consumer has not specifically requested that the creditor obtain and use medical information to accommodate the consumer's particular circumstances.

(5) *Example of a forbearance practice or program.* After an appropriate safety and soundness review, a creditor institutes a program that allows consumers who are or will be hospitalized to defer payments as needed for up to three months, without penalty, if the credit account has been open for more than one year and has not previously been in default, and the consumer provides confirming documentation at an appropriate time. A consumer is hospitalized and does not pay her bill for a particular month. This consumer has had a credit account with the creditor for more than one year and has not previously been in default. The creditor attempts to contact the consumer and speaks with the consumer's adult child, who is not the consumer's legal representative. The adult child informs the creditor that the consumer is hospitalized and is unable to pay the bill at that time. The creditor defers payments for up to three months, without penalty, for the hospitalized consumer and sends the consumer a letter confirming this practice and the date on which the next payment will be due.

§ 222.31 Limits on redisclosure of information.

(a) *Scope.* This section applies to banks that are members of the Federal Reserve System (other than national banks) and their respective operating subsidiaries, branches and agencies of foreign banks (other than Federal branches, Federal Agencies, and insured State branches of foreign banks), commercial lending companies owned or controlled by foreign banks, organizations operating under section 25 or 25A of the Federal Reserve Act (12 U.S.C. 601 *et seq.*, and 611 *et seq.*), and bank holding companies and affiliates of such holding companies (other than depository institutions and consumer reporting agencies).

(b) *Limits on redisclosure.* If a person described in paragraph (a) of this section receives medical information about a consumer from a consumer reporting agency or its affiliate, the person must not disclose that information to any other person, except as necessary to carry out the purpose for which the information was initially disclosed, or as otherwise permitted by statute, regulation, or order.

§ 222.32 Sharing medical information with affiliates.

(a) *Scope.* This section applies to banks that are members of the Federal Reserve System (other than national banks) and their respective operating subsidiaries, branches and agencies of foreign banks (other than Federal branches, Federal Agencies, and insured State branches of foreign banks), commercial lending companies owned or controlled by foreign banks, organizations operating under section 25 or 25A of the Federal Reserve Act (12 U.S.C. 601 *et seq.*, and 611 *et seq.*).

(b) *In general.* The exclusions from the term ''consumer report'' in section 603(d)(2) of the Act that allow the sharing of information with affiliates do not apply to a person described in paragraph (a) of this section if that person communicates to an affiliate—

(1) Medical information;

(2) An individualized list or description based on the payment transactions of the consumer for medical products or services; or

(3) An aggregate list of identified consumers based on payment transactions for medical products or services.

(c) Exceptions. A person described in paragraph (a) of this section may rely on the exclusions from the term ''consumer report'' in section 603(d)(2) of the Act to communicate the information in paragraph (b) of this section to an affiliate—

(1) In connection with the business of insurance or annuities (including the activities described in section 18B of the model Privacy of Consumer Financial and Health Information Regulation issued by the National Association of Insurance Commissioners, as in effect on January 1, 2003);

(2) For any purpose permitted without authorization under the regulations promulgated by the Department of Health and Human Services pursuant to the Health Insurance Portability and Accountability Act of 1996 (HIPAA);

(3) For any purpose referred to in section 1179 of HIPAA;

(4) For any purpose described in section 502(e) of the Gramm-Leach-Bliley Act;

(5) In connection with a determination of the consumer's eligibility, or continued eligibility, for credit consistent with § 222.30 of this part; or

(6) As otherwise permitted by order of the Board.

■ 4. A new part 232 is added to read as follows:

PART 232—OBTAINING AND USING MEDICAL INFORMATION IN CONNECTION WITH CREDIT (REGULATION FF)

Sec.

232.1 Scope, general prohibition and definitions.
232.2 Rule of construction for obtaining and using unsolicited medical information.
232.3 Financial information exception for obtaining and using medical information.
232.4 Specific exceptions for obtaining and using medical information.

Authority: 15 U.S.C. 1681b.

§ 232.1 Scope, general prohibition and definitions.

(a) *Scope.* This part applies to creditors, as defined in paragraph (c)(3) of this section, except for creditors that are subject to §§ 41.30, 222.30, 334.30, 571.30, or 717.30.

(b) *In general.* A creditor may not obtain or use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit, except as provided in this section.

(c) *Definitions.* (1) *Consumer* means an individual.

(2) *Credit* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(3) *Creditor* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(4) *Eligibility, or continued eligibility, for credit* means the consumer's qualification or fitness to receive, or continue to receive, credit, including the terms on which credit is offered. The term does not include:

(i) Any determination of the consumer's qualification or fitness for employment, insurance (other than a credit insurance product), or other non-credit products or services;

(ii) Authorizing, processing, or documenting a payment or transaction on behalf of the consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit; or

(iii) Maintaining or servicing the consumer's account in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit.

(5) *Medical information* means:

(i) Information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to—

(A) The past, present, or future physical, mental, or behavioral health or condition of an individual;

(B) The provision of health care to an individual; or

(C) The payment for the provision of health care to an individual.

(ii) The term does not include:

(A) The age or gender of a consumer;

(B) Demographic information about the consumer, including a consumer's residence address or e-mail address;

(C) Any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy; or

(D) Information that does not identify a specific consumer.

(6) *Person* means any individual, partnership, corporation, trust, estate cooperative, association, government or governmental subdivision or agency, or other entity.

§ 232.2 Rule of construction for obtaining and using unsolicited medical information.

(a) *In general.* A creditor does not obtain medical information in violation of the prohibition if it receives medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit without specifically requesting medical information.

(b) *Use of unsolicited medical information.* A creditor that receives unsolicited medical information in the manner described in paragraph (a) of this section may use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit to the extent the creditor can rely on at least one of the exceptions in § 232.3 or § 232.4.

(c) *Examples.* A creditor does not obtain medical information in violation of the prohibition if, for example:

(1) In response to a general question regarding a consumer's debts or expenses, the creditor receives information that the consumer owes a debt to a hospital.

(2) In a conversation with the creditor's loan officer, the consumer informs the creditor that the consumer has a particular medical condition.

(3) In connection with a consumer's application for an extension of credit, the creditor requests a consumer report from a consumer reporting agency and receives medical information in the consumer report furnished by the agency even though the creditor did not specifically request medical information from the consumer reporting agency.

§ 232.3 Financial information exception for obtaining and using medical information.

(a) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit so long as:

(1) The information is the type of information routinely used in making credit eligibility determinations, such as information relating to debts, expenses, income, benefits, assets, collateral, or the purpose of the loan, including the use of proceeds;

(2) The creditor uses the medical information in a manner and to an extent that is no less favorable than it would use comparable information that is not medical information in a credit transaction; and

(3) The creditor does not take the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis into account as part of any such determination.

(b) *Examples.* (1) *Examples of the types of information routinely used in making credit eligibility determinations.* Paragraph (a)(1) of this section permits a creditor, for example, to obtain and use information about:

(i) The dollar amount, repayment terms, repayment history, and similar information regarding medical debts to calculate, measure, or verify the repayment ability of the consumer, the use of proceeds, or the terms for granting credit;

(ii) The value, condition, and lien status of a medical device that may serve as collateral to secure a loan;

(iii) The dollar amount and continued eligibility for disability income or benefits related to health or a medical condition that is relied on as a source of repayment; or

(iv) The identity of creditors to whom outstanding medical debts are owed in connection with an application for credit, including but not limited to, a transaction involving the consolidation of medical debts.

(2) *Examples of uses of medical information consistent with the exception.* (i) A consumer includes on an application for credit information about two $20,000 debts. One debt is to a hospital; the other debt is to a retailer. The creditor contacts the hospital and the retailer to verify the amount and payment status of the debts. The creditor learns that both debts are more than 90 days past due. Any two debts of this size that are more than 90 days past due would disqualify the consumer under the creditor's established underwriting criteria. The creditor denies the application on the basis that the consumer has a poor repayment history on outstanding debts. The creditor has used medical information in a manner and to an extent no less favorable than it would use comparable non-medical information.

(ii) A consumer indicates on an application for a $200,000 mortgage loan that she receives $15,000 in long-term disability income each year from her former employer and has no other income. Annual income of $15,000, regardless of source, would not be sufficient to support the requested amount of credit. The creditor denies the application on the basis that the projected debt-to-income ratio of the consumer does not meet the creditor's underwriting criteria. The creditor has used medical information in a manner and to an extent that is no less favorable than it would use comparable non-medical information.

(iii) A consumer includes on an application for a $10,000 home equity loan that he has a $50,000 debt to a medical facility that specializes in treating a potentially terminal disease. The creditor contacts the medical facility to verify the debt and obtain the repayment history and current status of the loan. The creditor learns that the debt is current. The applicant meets the income and other requirements of the creditor's underwriting guidelines. The creditor grants the application. The

creditor has used medical information in accordance with the exception.

(3) *Examples of uses of medical information inconsistent with the exception.* (i) A consumer applies for $25,000 of credit and includes on the application information about a $50,000 debt to a hospital. The creditor contacts the hospital to verify the amount and payment status of the debt, and learns that the debt is current and that the consumer has no delinquencies in her repayment history. If the existing debt were instead owed to a retail department store, the creditor would approve the application and extend credit based on the amount and repayment history of the outstanding debt. The creditor, however, denies the application because the consumer is indebted to a hospital. The creditor has used medical information, here the identity of the medical creditor, in a manner and to an extent that is less favorable than it would use comparable non-medical information.

(ii) A consumer meets with a loan officer of a creditor to apply for a mortgage loan. While filling out the loan application, the consumer informs the loan officer orally that she has a potentially terminal disease. The consumer meets the creditor's established requirements for the requested mortgage loan. The loan officer recommends to the credit committee that the consumer be denied credit because the consumer has that disease. The credit committee follows the loan officer's recommendation and denies the application because the consumer has a potentially terminal disease. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis as part of a determination of eligibility or continued eligibility for credit.

(iii) A consumer who has an apparent medical condition, such as a consumer who uses a wheelchair or an oxygen tank, meets with a loan officer to apply for a home equity loan. The consumer meets the creditor's established requirements for the requested home equity loan and the creditor typically does not require consumers to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product in connection with such loans. However, based on the consumer's apparent medical condition, the loan officer recommends to the credit committee that credit be extended to the consumer only if the consumer obtains a debt cancellation contract, debt suspension agreement, or credit insurance product. The credit committee agrees with the loan officer's recommendation. The loan officer informs the consumer that the consumer must obtain a debt cancellation contract, debt suspension agreement, or credit insurance product to qualify for the loan. The consumer obtains one of these products from a third party and the creditor approves the loan. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis in setting conditions on the consumer's eligibility for credit.

§ 232.4 Specific exceptions for obtaining and using medical information.

(a) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit—

(1) To determine whether the use of a power of attorney or legal representative that is triggered by a medical event or condition is necessary and appropriate or whether the consumer has the legal capacity to contract when a person seeks to exercise a power of attorney or act as legal representative for a consumer based on an asserted medical event or condition;

(2) To comply with applicable requirements of local, State, or Federal laws;

(3) To determine, at the consumer's request, whether the consumer qualifies for a legally permissible special credit program or credit-related assistance program that is—

(i) Designed to meet the special needs of consumers with medical conditions; and

(ii) Established and administered pursuant to a written plan that—

(A) Identifies the class of persons that the program is designed to benefit; and

(B) Sets forth the procedures and standards for extending credit or providing other credit-related assistance under the program.

(4) To the extent necessary for purposes of fraud prevention or detection;

(5) In the case of credit for the purpose of financing medical products or services, to determine and verify the medical purpose of a loan and the use of proceeds;

(6) Consistent with safe and sound practices, if the consumer or the consumer's legal representative specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular circumstances, and such request is documented by the creditor;

(7) Consistent with safe and sound practices, to determine whether the provisions of a forbearance practice or program that is triggered by a medical event or condition apply to a consumer;

(8) To determine the consumer's eligibility for, the triggering of, or the reactivation of a debt cancellation contract or debt suspension agreement if a medical condition or event is a triggering event for the provision of benefits under the contract or agreement; or

(9) To determine the consumer's eligibility for, the triggering of, or the reactivation of a credit insurance product if a medical condition or event is a triggering event for the provision of benefits under the product.

(b) *Example of determining eligibility for a special credit program or credit assistance program.* A not-for-profit organization establishes a credit assistance program pursuant to a written plan that is designed to assist disabled veterans in purchasing homes by subsidizing the down payment for the home purchase mortgage loans of qualifying veterans. The organization works through mortgage lenders and requires mortgage lenders to obtain medical information about the disability of any consumer that seeks to qualify for the program, use that information to verify the consumer's eligibility for the program, and forward that information to the organization. A consumer who is a veteran applies to a creditor for a home purchase mortgage loan. The creditor informs the consumer about the credit assistance program for disabled veterans and the consumer seeks to qualify for the program. Assuming that the program complies with all applicable law, including applicable fair lending laws, the creditor may obtain and use medical information about the medical condition and disability, if any, of the consumer to determine whether the consumer qualifies for the credit assistance program.

(c) *Examples of verifying the medical purpose of the loan or the use of proceeds.* (1) If a consumer applies for $10,000 of credit for the purpose of financing vision correction surgery, the creditor may verify with the surgeon that the procedure will be performed. If the surgeon reports that surgery will not be performed on the consumer, the creditor may use that medical information to deny the consumer's application for credit, because the loan

would not be used for the stated purpose.

(2) If a consumer applies for $10,000 of credit for the purpose of financing cosmetic surgery, the creditor may confirm the cost of the procedure with the surgeon. If the surgeon reports that the cost of the procedure is $5,000, the creditor may use that medical information to offer the consumer only $5,000 of credit.

(3) A creditor has an established medical loan program for financing particular elective surgical procedures. The creditor receives a loan application from a consumer requesting $10,000 of credit under the established loan program for an elective surgical procedure. The consumer indicates on the application that the purpose of the loan is to finance an elective surgical procedure not eligible for funding under the guidelines of the established loan program. The creditor may deny the consumer's application because the purpose of the loan is not for a particular procedure funded by the established loan program.

(d) *Examples of obtaining and using medical information at the request of the consumer.* (1) If a consumer applies for a loan and specifically requests that the creditor consider the consumer's medical disability at the relevant time as an explanation for adverse payment history information in his credit report, the creditor may consider such medical information in evaluating the consumer's willingness and ability to repay the requested loan to accommodate the consumer's particular circumstances, consistent with safe and sound practices. The creditor may also decline to consider such medical information to accommodate the consumer, but may evaluate the consumer's application in accordance with its otherwise applicable underwriting criteria. The creditor may not deny the consumer's application or otherwise treat the consumer less favorably because the consumer specifically requested a medical accommodation, if the creditor would have extended the credit or treated the consumer more favorably under the creditor's otherwise applicable underwriting criteria.

(2) If a consumer applies for a loan by telephone and explains that his income has been and will continue to be interrupted on account of a medical condition and that he expects to repay the loan liquidating assets, the creditor may, but is not required to, evaluate the application using the sale of assets as the primary source of repayment, consistent with safe and sound practices, provided that the creditor documents the consumer's request by recording the oral conversation or making a notation of the request in the consumer's file.

(3) If a consumer applies for a loan and the application form provides a space where the consumer may provide any other information or special circumstances, whether medical or non-medical, that the consumer would like the creditor to consider in evaluating the consumer's application, the creditor may use medical information provided by the consumer in that space on that application to accommodate the consumer's application for credit, consistent with safe and sound practices, or may disregard that information.

(4) If a consumer specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit and provides the creditor with medical information for that purpose, and the creditor determines that it needs additional information regarding the consumer's circumstances, the creditor may request, obtain, and use additional medical information about the consumer as necessary to verify the information provided by the consumer or to determine whether to make an accommodation for the consumer. The consumer may decline to provide additional information, withdraw the request for an accommodation, and have the application considered under the creditor's otherwise applicable underwriting criteria.

(5) If a consumer completes and signs a credit application that is not for medical purpose credit and the application contains boilerplate language that routinely requests medical information from the consumer or that indicates that by applying for credit the consumer authorizes or consents to the creditor obtaining and using medical information in connection with a determination of the consumer's eligibility, or continued eligibility, for credit, the consumer has not specifically requested that the creditor obtain and use medical information to accommodate the consumer's particular circumstances.

(e) *Example of a forbearance practice or program.* After an appropriate safety and soundness review, a creditor institutes a program that allows consumers who are or will be hospitalized to defer payments as needed for up to three months, without penalty, if the credit account has been open for more than one year and has not previously been in default, and the consumer provides confirming documentation at an appropriate time. A consumer is hospitalized and does not pay her bill for a particular month. This consumer has had a credit account with the creditor for more than one year and has not previously been in default. The creditor attempts to contact the consumer and speaks with the consumer's adult child, who is not the consumer's legal representative. The adult child informs the creditor that the consumer is hospitalized and is unable to pay the bill at that time. The creditor defers payments for up to three months, without penalty, for the hospitalized consumer and sends the consumer a letter confirming this practice and the date on which the next payment will be due.

Federal Deposit Insurance Corporation

12 CFR Chapter III.

Authority and Issuance

■ For the reasons set forth in the joint preamble, the Federal Deposit Insurance Corporation amends part 334 of chapter III of title 12 of the Code of Federal Regulations as follows:

PART 334—FAIR CREDIT REPORTING

■ 1. The authority citation for part 334 is revised to read as follows:

Authority: 12 U.S.C. 1819 (Tenth) and 1818; 15 U.S.C. 1681b and 1681s.

■ 2. Subpart A is added to part 334 to read as follows:

Subpart A—General Provisions

Sec.
334.1 [Reserved]
334.2 Examples.
334.3 Definitions.

Subpart A—General Provisions

§ 334.1 [Reserved]

§ 334.2 Examples.

The examples in this part are not exclusive. Compliance with an example, to the extent applicable, constitutes compliance with this part. Examples in a paragraph illustrate only the issue described in the paragraph and do not illustrate any other issue that may arise in this part.

§ 334.3 Definitions.

As used in this part, unless the context requires otherwise:

(a) *Act* means the Fair Credit Reporting Act (15 U.S.C. 1681 *et seq.*).

(b) *Affiliate* means any company that is related by common ownership or common corporate control with another company.

(c) [Reserved]

(d) *Company* means any corporation, limited liability company, business

trust, general or limited partnership, association, or similar organization.

(e) *Consumer* means an individual.

(f) [Reserved]

(g) [Reserved]

(h) [Reserved]

(i) *Common ownership or common corporate control* means a relationship between two companies under which:

(1) One company has, with respect to the other company:

(i) Ownership, control, or power to vote 25 percent or more of the outstanding shares of any class of voting security of a company, directly or indirectly, or acting through one or more other persons;

(ii) Control in any manner over the election of a majority of the directors, trustees, or general partners (or individuals exercising similar functions) of a company; or

(iii) The power to exercise, directly or indirectly, a controlling influence over the management or policies of a company, as the FDIC determines; or

(2) Any other person has, with respect to both companies, a relationship described in paragraphs (i)(1)(i)–(i)(1)(iii) of this section.

(j) [Reserved]

(k) *Medical information* means:

(1) Information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to—

(i) The past, present, or future physical, mental, or behavioral health or condition of an individual;

(ii) The provision of health care to an individual; or

(iii) The payment for the provision of health care to an individual.

(2) The term does not include:

(i) The age or gender of a consumer;

(ii) Demographic information about the consumer, including a consumer's residence address or e-mail address;

(iii) Any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy; or

(iv) Information that does not identify a specific consumer.

(l) *Person* means any individual, partnership, corporation, trust, estate cooperative, association, government or governmental subdivision or agency, or other entity.

■ 3. Subpart D is added to part 334 to read as follows:

Subpart D—Medical Information

§ 334.30 Obtaining or using medical information in connection with a determination of eligibility for credit.

(a) *Scope.* This section applies to:

(1) Any of the following that participates as a creditor in a transaction—

(i) A State bank insured by the FDIC (other than members of the Federal Reserve System);

(ii) An insured State branch of a foreign bank; or

(2) Any other person that participates as a creditor in a transaction involving a person described in paragraph (a)(1) of this section.

(b) *General prohibition on obtaining or using medical information.* (1) *In general.* A creditor may not obtain or use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit, except as provided in this section.

(2) *Definitions.* (i) *Credit* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(ii) *Creditor* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(iii) *Eligibility, or continued eligibility, for credit* means the consumer's qualification or fitness to receive, or continue to receive, credit, including the terms on which credit is offered. The term does not include:

(A) Any determination of the consumer's qualification or fitness for employment, insurance (other than a credit insurance product), or other non-credit products or services;

(B) Authorizing, processing, or documenting a payment or transaction on behalf of the consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit; or

(C) Maintaining or servicing the consumer's account in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit.

(c) *Rule of construction for obtaining and using unsolicited medical information.* (1) *In general.* A creditor does not obtain medical information in violation of the prohibition if it receives medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit without specifically requesting medical information.

(2) *Use of unsolicited medical information.* A creditor that receives unsolicited medical information in the manner described in paragraph (c)(1) of this section may use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit to the extent the creditor can rely on at least one of the exceptions in § 334.30(d) or (e).

(3) *Examples.* A creditor does not obtain medical information in violation of the prohibition if, for example:

(i) In response to a general question regarding a consumer's debts or expenses, the creditor receives information that the consumer owes a debt to a hospital.

(ii) In a conversation with the creditor's loan officer, the consumer informs the creditor that the consumer has a particular medical condition.

(iii) In connection with a consumer's application for an extension of credit, the creditor requests a consumer report from a consumer reporting agency and receives medical information in the consumer report furnished by the agency even though the creditor did not specifically request medical information from the consumer reporting agency.

(d) *Financial information exception for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit so long as:

(i) The information is the type of information routinely used in making credit eligibility determinations, such as information relating to debts, expenses, income, benefits, assets, collateral, or the purpose of the loan, including the use of proceeds;

(ii) The creditor uses the medical information in a manner and to an extent that is no less favorable than it would use comparable information that is not medical information in a credit transaction; and

(iii) The creditor does not take the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis into account as part of any such determination.

(2) *Examples.* (i) *Examples of the types of information routinely used in making credit eligibility determinations.* Paragraph (d)(1)(i) of this section permits a creditor, for example, to obtain and use information about:

(A) The dollar amount, repayment terms, repayment history, and similar information regarding medical debts to calculate, measure, or verify the repayment ability of the consumer, the use of proceeds, or the terms for granting credit;

(B) The value, condition, and lien status of a medical device that may serve as collateral to secure a loan;

(C) The dollar amount and continued eligibility for disability income or benefits related to health or a medical condition that is relied on as a source of repayment; or

(D) The identity of creditors to whom outstanding medical debts are owed in connection with an application for credit, including but not limited to, a transaction involving the consolidation of medical debts.

(ii) *Examples of uses of medical information consistent with the exception.* (A) A consumer includes on an application for credit information about two $20,000 debts. One debt is to a hospital; the other debt is to a retailer. The creditor contacts the hospital and the retailer to verify the amount and payment status of the debts. The creditor learns that both debts are more than 90 days past due. Any two debts of this size that are more than 90 days past due would disqualify the consumer under the creditor's established underwriting criteria. The creditor denies the application on the basis that the consumer has a poor repayment history on outstanding debts. The creditor has used medical information in a manner and to an extent no less favorable than it would use comparable non-medical information.

(B) A consumer indicates on an application for a $200,000 mortgage loan that she receives $15,000 in long-term disability income each year from her former employer and has no other income. Annual income of $15,000, regardless of source, would not be sufficient to support the requested amount of credit. The creditor denies the application on the basis that the projected debt-to-income ratio of the consumer does not meet the creditor's underwriting criteria. The creditor has used medical information in a manner and to an extent that is no less favorable than it would use comparable non-medical information.

(C) A consumer includes on an application for a $10,000 home equity loan that he has a $50,000 debt to a medical facility that specializes in treating a potentially terminal disease. The creditor contacts the medical facility to verify the debt and obtain the repayment history and current status of the loan. The creditor learns that the debt is current. The applicant meets the income and other requirements of the creditor's underwriting guidelines. The creditor grants the application. The creditor has used medical information in accordance with the exception.

(iii) *Examples of uses of medical information inconsistent with the exception.* (A) A consumer applies for $25,000 of credit and includes on the application information about a $50,000 debt to a hospital. The creditor contacts the hospital to verify the amount and payment status of the debt, and learns that the debt is current and that the consumer has no delinquencies in her repayment history. If the existing debt were instead owed to a retail department store, the creditor would approve the application and extend credit based on the amount and repayment history of the outstanding debt. The creditor, however, denies the application because the consumer is indebted to a hospital. The creditor has used medical information, here the identity of the medical creditor, in a manner and to an extent that is less favorable than it would use comparable non-medical information.

(B) A consumer meets with a loan officer of a creditor to apply for a mortgage loan. While filling out the loan application, the consumer informs the loan officer orally that she has a potentially terminal disease. The consumer meets the creditor's established requirements for the requested mortgage loan. The loan officer recommends to the credit committee that the consumer be denied credit because the consumer has that disease. The credit committee follows the loan officer's recommendation and denies the application because the consumer has a potentially terminal disease. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis as part of a determination of eligibility or continued eligibility for credit.

(C) A consumer who has an apparent medical condition, such as a consumer who uses a wheelchair or an oxygen tank, meets with a loan officer to apply for a home equity loan. The consumer meets the creditor's established requirements for the requested home equity loan and the creditor typically does not require consumers to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product in connection with such loans. However, based on the consumer's apparent medical condition, the loan officer recommends to the credit committee that credit be extended to the consumer only if the consumer obtains a debt cancellation contract, debt suspension agreement, or credit insurance product. The credit committee agrees with the loan officer's recommendation. The loan officer informs the consumer that the consumer must obtain a debt cancellation contract, debt suspension agreement, or credit insurance product to qualify for the loan. The consumer obtains one of these products from a third party and the creditor approves the loan. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis in setting conditions on the consumer's eligibility for credit.

(e) *Specific exceptions for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit—

(i) To determine whether the use of a power of attorney or legal representative that is triggered by a medical event or condition is necessary and appropriate or whether the consumer has the legal capacity to contract when a person seeks to exercise a power of attorney or act as legal representative for a consumer based on an asserted medical event or condition;

(ii) To comply with applicable requirements of local, State, or Federal laws;

(iii) To determine, at the consumer's request, whether the consumer qualifies for a legally permissible special credit program or credit-related assistance program that is—

(A) Designed to meet the special needs of consumers with medical conditions; and

(B) Established and administered pursuant to a written plan that—

(*1*) Identifies the class of persons that the program is designed to benefit; and

(*2*) Sets forth the procedures and standards for extending credit or providing other credit-related assistance under the program.

(iv) To the extent necessary for purposes of fraud prevention or detection;

(v) In the case of credit for the purpose of financing medical products or services, to determine and verify the medical purpose of a loan and the use of proceeds;

(vi) Consistent with safe and sound practices, if the consumer or the consumer's legal representative specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular

circumstances, and such request is documented by the creditor;

(vii) Consistent with safe and sound practices, to determine whether the provisions of a forbearance practice or program that is triggered by a medical event or condition apply to a consumer;

(viii) To determine the consumer's eligibility for, the triggering of, or the reactivation of a debt cancellation contract or debt suspension agreement if a medical condition or event is a triggering event for the provision of benefits under the contract or agreement; or

(ix) To determine the consumer's eligibility for, the triggering of, or the reactivation of a credit insurance product if a medical condition or event is a triggering event for the provision of benefits under the product.

(2) *Example of determining eligibility for a special credit program or credit assistance program.* A not-for-profit organization establishes a credit assistance program pursuant to a written plan that is designed to assist disabled veterans in purchasing homes by subsidizing the down payment for the home purchase mortgage loans of qualifying veterans. The organization works through mortgage lenders and requires mortgage lenders to obtain medical information about the disability of any consumer that seeks to qualify for the program, use that information to verify the consumer's eligibility for the program, and forward that information to the organization. A consumer who is a veteran applies to a creditor for a home purchase mortgage loan. The creditor informs the consumer about the credit assistance program for disabled veterans and the consumer seeks to qualify for the program. Assuming that the program complies with all applicable law, including applicable fair lending laws, the creditor may obtain and use medical information about the medical condition and disability, if any, of the consumer to determine whether the consumer qualifies for the credit assistance program.

(3) *Examples of verifying the medical purpose of the loan or the use of proceeds.* (i) If a consumer applies for $10,000 of credit for the purpose of financing vision correction surgery, the creditor may verify with the surgeon that the procedure will be performed. If the surgeon reports that surgery will not be performed on the consumer, the creditor may use that medical information to deny the consumer's application for credit, because the loan would not be used for the stated purpose.

(ii) If a consumer applies for $10,000 of credit for the purpose of financing cosmetic surgery, the creditor may confirm the cost of the procedure with the surgeon. If the surgeon reports that the cost of the procedure is $5,000, the creditor may use that medical information to offer the consumer only $5,000 of credit.

(iii) A creditor has an established medical loan program for financing particular elective surgical procedures. The creditor receives a loan application from a consumer requesting $10,000 of credit under the established loan program for an elective surgical procedure. The consumer indicates on the application that the purpose of the loan is to finance an elective surgical procedure not eligible for funding under the guidelines of the established loan program. The creditor may deny the consumer's application because the purpose of the loan is not for a particular procedure funded by the established loan program.

(4) *Examples of obtaining and using medical information at the request of the consumer.* (i) If a consumer applies for a loan and specifically requests that the creditor consider the consumer's medical disability at the relevant time as an explanation for adverse payment history information in his credit report, the creditor may consider such medical information in evaluating the consumer's willingness and ability to repay the requested loan to accommodate the consumer's particular circumstances, consistent with safe and sound practices. The creditor may also decline to consider such medical information to accommodate the consumer, but may evaluate the consumer's application in accordance with its otherwise applicable underwriting criteria. The creditor may not deny the consumer's application or otherwise treat the consumer less favorably because the consumer specifically requested a medical accommodation, if the creditor would have extended the credit or treated the consumer more favorably under the creditor's otherwise applicable underwriting criteria.

(ii) If a consumer applies for a loan by telephone and explains that his income has been and will continue to be interrupted on account of a medical condition and that he expects to repay the loan by liquidating assets, the creditor may, but is not required to, evaluate the application using the sale of assets as the primary source of repayment, consistent with safe and sound practices, provided that the creditor documents the consumer's request by recording the oral conversation or making a notation of the request in the consumer's file.

(iii) If a consumer applies for a loan and the application form provides a space where the consumer may provide any other information or special circumstances, whether medical or non-medical, that the consumer would like the creditor to consider in evaluating the consumer's application, the creditor may use medical information provided by the consumer in that space on that application to accommodate the consumer's application for credit, consistent with safe and sound practices, or may disregard that information.

(iv) If a consumer specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit and provides the creditor with medical information for that purpose, and the creditor determines that it needs additional information regarding the consumer's circumstances, the creditor may request, obtain, and use additional medical information about the consumer as necessary to verify the information provided by the consumer or to determine whether to make an accommodation for the consumer. The consumer may decline to provide additional information, withdraw the request for an accommodation, and have the application considered under the creditor's otherwise applicable underwriting criteria.

(v) If a consumer completes and signs a credit application that is not for medical purpose credit and the application contains boilerplate language that routinely requests medical information from the consumer or that indicates that by applying for credit the consumer authorizes or consents to the creditor obtaining and using medical information in connection with a determination of the consumer's eligibility, or continued eligibility, for credit, the consumer has not specifically requested that the creditor obtain and use medical information to accommodate the consumer's particular circumstances.

(5) *Example of a forbearance practice or program.* After an appropriate safety and soundness review, a creditor institutes a program that allows consumers who are or will be hospitalized to defer payments as needed for up to three months, without penalty, if the credit account has been open for more than one year and has not previously been in default, and the consumer provides confirming documentation at an appropriate time. A consumer is hospitalized and does not pay her bill for a particular month. This consumer has had a credit account

with the creditor for more than one year and has not previously been in default. The creditor attempts to contact the consumer and speaks with the consumer's adult child, who is not the consumer's legal representative. The adult child informs the creditor that the consumer is hospitalized and is unable to pay the bill at that time. The creditor defers payments for up to three months, without penalty, for the hospitalized consumer and sends the consumer a letter confirming this practice and the date on which the next payment will be due.

§ 334.31 Limits on redisclosure of information.

(a) *Scope.* This section applies to State banks insured by the FDIC (other than members of the Federal Reserve System) and insured State branches of foreign banks.

(b) *Limits on redisclosure.* If a person described in paragraph (a) of this section receives medical information about a consumer from a consumer reporting agency or its affiliate, the person must not disclose that information to any other person, except as necessary to carry out the purpose for which the information was initially disclosed, or as otherwise permitted by statute, regulation, or order.

§ 334.32 Sharing medical information with affiliates.

(a) *Scope.* This section applies to State banks insured by the FDIC (other than members of the Federal Reserve System) and insured State branches of foreign banks.

(b) *In general.* The exclusions from the term ''consumer report'' in section 603(d)(2) of the Act that allow the sharing of information with affiliates do not apply if a person described in paragraph (a) of this section communicates to an affiliate—

(1) Medical information;

(2) An individualized list or description based on the payment transactions of the consumer for medical products or services; or

(3) An aggregate list of identified consumers based on payment transactions for medical products or services.

(c) *Exceptions.* A person described in paragraph (a) of this section may rely on the exclusions from the term ''consumer report'' in section 603(d)(2) of the Act to communicate the information in paragraph (b) of this section to an affiliate—

(1) In connection with the business of insurance or annuities (including the activities described in section 18B of the model Privacy of Consumer Financial and Health Information Regulation issued by the National Association of Insurance Commissioners, as in effect on January 1, 2003);

(2) For any purpose permitted without authorization under the regulations promulgated by the Department of Health and Human Services pursuant to the Health Insurance Portability and Accountability Act of 1996 (HIPAA);

(3) For any purpose referred to in section 1179 of HIPAA;

(4) For any purpose described in section 502(e) of the Gramm-Leach-Bliley Act;

(5) In connection with a determination of the consumer's eligibility, or continued eligibility, for credit consistent with § 334.30; or

(6) As otherwise permitted by order of the FDIC.

Office of Thrift Supervision

12 CFR Chapter V.

Authority and Issuance

■ For the reasons set forth in the joint preamble, the Office of Thrift Supervision amends chapter V of title 12 of the Code of Federal Regulations as follows:

PART 571—FAIR CREDIT REPORTING

■ 1. The authority citation for part 571 is revised to read as follows:

Authority: 12 U.S.C. 1462a, 1463, 1464, 1467a, 1828, 1831p–1, and 1881–1884; 15 U.S.C. 1681b, 1681s, and 1681w; 15 U.S.C. 6801 and 6805(b)(1).

Subpart A—General Provisions

■ 2. Revise § 571.1(b)(2) to read as follows:

§ 571.1 Purpose and Scope.

* * * * *

(b) * * *

(2) *Scope in general.* Except as otherwise provided in this part, this part applies to savings associations whose deposits are insured by the Federal Deposit Insurance Corporation (and Federal savings association operating subsidiaries in accordance with § 559.3(h)(1) of this chapter).

■ 3. Add § 571.2 to read as follows:

§ 571.2 Examples.

The examples in this part are not exclusive. Compliance with an example, to the extent applicable, constitutes compliance with this part. Examples in a paragraph illustrate only the issue described in the paragraph and do not illustrate any other issue that may arise in this part.

■ 4. Amend § 571.3 by revising the introductory text and paragraphs (a) through (n) to read as follows:

§ 571.3 Definitions.

As used in this part, unless the context requires otherwise:

(a) *Act* means the Fair Credit Reporting Act (15 U.S.C. 1681 *et seq.*).

(b) *Affiliate* means any company that is related by common ownership or common corporate control with another company.

(c) [Reserved]

(d) *Company* means any corporation, limited liability company, business trust, general or limited partnership, association, or similar organization.

(e) *Consumer* means an individual.

(f)–(h) [Reserved]

(i) *Common ownership or common corporate control* means a relationship between two companies under which:

(1) One company has, with respect to the other company:

(i) Ownership, control, or power to vote 25 percent or more of the outstanding shares of any class of voting security of a company, directly or indirectly, or acting through one or more other persons;

(ii) Control in any manner over the election of a majority of the directors, trustees, or general partners (or individuals exercising similar functions) of a company; or

(iii) The power to exercise, directly or indirectly, a controlling influence over the management or policies of a company, as the OTS determines; or

(2) Any other person has, with respect to both companies, a relationship described in paragraphs (i)(1)(i)–(i)(1)(iii) of this section.

(j) [Reserved]

(k) *Medical information* means:

(1) Information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to—

(i) The past, present, or future physical, mental, or behavioral health or condition of an individual;

(ii) The provision of health care to an individual; or

(iii) The payment for the provision of health care to an individual.

(2) The term does not include:

(i) The age or gender of a consumer;

(ii) Demographic information about the consumer, including a consumer's residence address or e-mail address;

(iii) Any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy; or

(iv) Information that does not identify a specific consumer.

(l) *Person* means any individual, partnership, corporation, trust, estate

cooperative, association, government or governmental subdivision or agency, or other entity.

(m)–(n) [Reserved]

* * * * *

■ 5. Add subpart D to part 571 to read as follows:

Subpart D—Medical Information

§ 571.30 Obtaining or using medical information in connection with a determination of eligibility for credit.

(a) *Scope.* This section applies to:

(1) Any of the following that participates as a creditor in a transaction—

(i) A savings association;

(ii) A subsidiary owned in whole or in part by a savings association;

(iii) A savings and loan holding company;

(iv) A subsidiary of a savings and loan holding company other than a bank or subsidiary of a bank; or

(v) A service corporation owned in whole or in part by a savings association; or

(2) Any other person that participates as a creditor in a transaction involving a person described in paragraph (a)(1) of this section.

(b) *General prohibition on obtaining or using medical information.* (1) *In general.* A creditor may not obtain or use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit, except as provided in this section.

(2) *Definitions.* (i) *Credit* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(ii) *Creditor* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(iii) *Eligibility, or continued eligibility, for credit* means the consumer's qualification or fitness to receive, or continue to receive, credit, including the terms on which credit is offered. The term does not include:

(A) Any determination of the consumer's qualification or fitness for employment, insurance (other than a credit insurance product), or other non-credit products or services;

(B) Authorizing, processing, or documenting a payment or transaction on behalf of the consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit; or

(C) Maintaining or servicing the consumer's account in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit.

(c) *Rule of construction for obtaining and using unsolicited medical information.* (1) *In general.* A creditor does not obtain medical information in violation of the prohibition if it receives medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit without specifically requesting medical information.

(2) *Use of unsolicited medical information.* A creditor that receives unsolicited medical information in the manner described in paragraph (c)(1) of this section may use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit to the extent the creditor can rely on at least one of the exceptions in § 571.30(d) or (e).

(3) *Examples.* A creditor does not obtain medical information in violation of the prohibition if, for example:

(i) In response to a general question regarding a consumer's debts or expenses, the creditor receives information that the consumer owes a debt to a hospital;

(ii) In a conversation with the creditor's loan officer, the consumer informs the creditor that the consumer has a particular medical condition; or

(iii) In connection with a consumer's application for an extension of credit, the creditor requests a consumer report from a consumer reporting agency and receives medical information in the consumer report furnished by the agency even though the creditor did not specifically request medical information from the consumer reporting agency.

(d) *Financial information exception for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit so long as:

(i) The information is the type of information routinely used in making credit eligibility determinations, such as information relating to debts, expenses, income, benefits, assets, collateral, or the purpose of the loan, including the use of proceeds;

(ii) The creditor uses the medical information in a manner and to an extent that is no less favorable than it would use comparable information that is not medical information in a credit transaction; and

(iii) The creditor does not take the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis into account as part of any such determination.

(2) *Examples.* (i) *Examples of the types of information routinely used in making credit eligibility determinations.* Paragraph (d)(1)(i) of this section permits a creditor, for example, to obtain and use information about:

(A) The dollar amount, repayment terms, repayment history, and similar information regarding medical debts to calculate, measure, or verify the repayment ability of the consumer, the use of proceeds, or the terms for granting credit;

(B) The value, condition, and lien status of a medical device that may serve as collateral to secure a loan;

(C) The dollar amount and continued eligibility for disability income or benefits related to health or a medical condition that is relied on as a source of repayment; or

(D) The identity of creditors to whom outstanding medical debts are owed in connection with an application for credit, including but not limited to, a transaction involving the consolidation of medical debts.

(ii) *Examples of uses of medical information consistent with the exception.* (A) A consumer includes on an application for credit information about two $20,000 debts. One debt is to a hospital; the other debt is to a retailer. The creditor contacts the hospital and the retailer to verify the amount and payment status of the debts. The creditor learns that both debts are more than 90 days past due. Any two debts of this size that are more than 90 days past due would disqualify the consumer under the creditor's established underwriting criteria. The creditor denies the application on the basis that the consumer has a poor repayment history on outstanding debts. The creditor has used medical information in a manner and to an extent no less favorable than it would use comparable non-medical information.

(B) A consumer indicates on an application for a $200,000 mortgage loan that she receives $15,000 in long-term disability income each year from her former employer and has no other income. Annual income of $15,000, regardless of source, would not be sufficient to support the requested amount of credit. The creditor denies the application on the basis that the projected debt-to-income ratio of the consumer does not meet the creditor's underwriting criteria. The creditor has used medical information in a manner and to an extent that is no less favorable than it would use comparable non-medical information.

(C) A consumer includes on an application for a $10,000 home equity loan that he has a $50,000 debt to a

medical facility that specializes in treating a potentially terminal disease. The creditor contacts the medical facility to verify the debt and obtain the repayment history and current status of the loan. The creditor learns that the debt is current. The applicant meets the income and other requirements of the creditor's underwriting guidelines. The creditor grants the application. The creditor has used medical information in accordance with the exception.

(iii) *Examples of uses of medical information inconsistent with the exception.* (A) A consumer applies for $25,000 of credit and includes on the application information about a $50,000 debt to a hospital. The creditor contacts the hospital to verify the amount and payment status of the debt, and learns that the debt is current and that the consumer has no delinquencies in her repayment history. If the existing debt were instead owed to a retail department store, the creditor would approve the application and extend credit based on the amount and repayment history of the outstanding debt. The creditor, however, denies the application because the consumer is indebted to a hospital. The creditor has used medical information, here the identity of the medical creditor, in a manner and to an extent that is less favorable than it would use comparable non-medical information.

(B) A consumer meets with a loan officer of a creditor to apply for a mortgage loan. While filling out the loan application, the consumer informs the loan officer orally that she has a potentially terminal disease. The consumer meets the creditor's established requirements for the requested mortgage loan. The loan officer recommends to the credit committee that the consumer be denied credit because the consumer has that disease. The credit committee follows the loan officer's recommendation and denies the application because the consumer has a potentially terminal disease. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis as part of a determination of eligibility or continued eligibility for credit.

(C) A consumer who has an apparent medical condition, such as a consumer who uses a wheelchair or an oxygen tank, meets with a loan officer to apply for a home equity loan. The consumer meets the creditor's established requirements for the requested home equity loan and the creditor typically does not require consumers to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product in connection with such loans. However, based on the consumer's apparent medical condition, the loan officer recommends to the credit committee that credit be extended to the consumer only if the consumer obtains a debt cancellation contract, debt suspension agreement, or credit insurance product. The credit committee agrees with the loan officer's recommendation. The loan officer informs the consumer that the consumer must obtain a debt cancellation contract, debt suspension agreement, or credit insurance product to qualify for the loan. The consumer obtains one of these products from a third party and the creditor approves the loan. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis in setting conditions on the consumer's eligibility for credit.

(e) *Specific exceptions for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit—

(i) To determine whether the use of a power of attorney or legal representative that is triggered by a medical event or condition is necessary and appropriate or whether the consumer has the legal capacity to contract when a person seeks to exercise a power of attorney or act as legal representative for a consumer based on an asserted medical event or condition;

(ii) To comply with applicable requirements of local, State, or Federal laws;

(iii) To determine, at the consumer's request, whether the consumer qualifies for a legally permissible special credit program or credit-related assistance program that is—

(A) Designed to meet the special needs of consumers with medical conditions; and

(B) Established and administered pursuant to a written plan that—

(*1*) Identifies the class of persons that the program is designed to benefit; and

(*2*) Sets forth the procedures and standards for extending credit or providing other credit-related assistance under the program.

(iv) To the extent necessary for purposes of fraud prevention or detection;

(v) In the case of credit for the purpose of financing medical products or services, to determine and verify the medical purpose of a loan and the use of proceeds;

(vi) Consistent with safe and sound practices, if the consumer or the consumer's legal representative specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular circumstances, and such request is documented by the creditor;

(vii) Consistent with safe and sound practices, to determine whether the provisions of a forbearance practice or program that is triggered by a medical event or condition apply to a consumer;

(viii) To determine the consumer's eligibility for, the triggering of, or the reactivation of a debt cancellation contract or debt suspension agreement if a medical condition or event is a triggering event for the provision of benefits under the contract or agreement; or

(ix) To determine the consumer's eligibility for, the triggering of, or the reactivation of a credit insurance product if a medical condition or event is a triggering event for the provision of benefits under the product.

(2) *Example of determining eligibility for a special credit program or credit assistance program.* A not-for-profit organization establishes a credit assistance program pursuant to a written plan that is designed to assist disabled veterans in purchasing homes by subsidizing the down payment for the home purchase mortgage loans of qualifying veterans. The organization works through mortgage lenders and requires mortgage lenders to obtain medical information about the disability of any consumer that seeks to qualify for the program, use that information to verify the consumer's eligibility for the program, and forward that information to the organization. A consumer who is a veteran applies to a creditor for a home purchase mortgage loan. The creditor informs the consumer about the credit assistance program for disabled veterans and the consumer seeks to qualify for the program. Assuming that the program complies with all applicable law, including applicable fair lending laws, the creditor may obtain and use medical information about the medical condition and disability, if any, of the consumer to determine whether the consumer qualifies for the credit assistance program.

(3) *Examples of verifying the medical purpose of the loan or the use of proceeds.* (i) If a consumer applies for

$10,000 of credit for the purpose of financing vision correction surgery, the creditor may verify with the surgeon that the procedure will be performed. If the surgeon reports that surgery will not be performed on the consumer, the creditor may use that medical information to deny the consumer's application for credit, because the loan would not be used for the stated purpose.

(ii) If a consumer applies for $10,000 of credit for the purpose of financing cosmetic surgery, the creditor may confirm the cost of the procedure with the surgeon. If the surgeon reports that the cost of the procedure is $5,000, the creditor may use that medical information to offer the consumer only $5,000 of credit.

(iii) A creditor has an established medical loan program for financing particular elective surgical procedures. The creditor receives a loan application from a consumer requesting $10,000 of credit under the established loan program for an elective surgical procedure. The consumer indicates on the application that the purpose of the loan is to finance an elective surgical procedure not eligible for funding under the guidelines of the established loan program. The creditor may deny the consumer's application because the purpose of the loan is not for a particular procedure funded by the established loan program.

(4) *Examples of obtaining and using medical information at the request of the consumer.* (i) If a consumer applies for a loan and specifically requests that the creditor consider the consumer's medical disability at the relevant time as an explanation for adverse payment history information in his credit report, the creditor may consider such medical information in evaluating the consumer's willingness and ability to repay the requested loan to accommodate the consumer's particular circumstances, consistent with safe and sound practices. The creditor may also decline to consider such medical information to accommodate the consumer, but may evaluate the consumer's application in accordance with its otherwise applicable underwriting criteria. The creditor may not deny the consumer's application or otherwise treat the consumer less favorably because the consumer specifically requested a medical accommodation, if the creditor would have extended the credit or treated the consumer more favorably under the creditor's otherwise applicable underwriting criteria.

(ii) If a consumer applies for a loan by telephone and explains that his income has been and will continue to be interrupted on account of a medical condition and that he expects to repay the loan by liquidating assets, the creditor may, but is not required to, evaluate the application using the sale of assets as the primary source of repayment, consistent with safe and sound practices, provided that the creditor documents the consumer's request by recording the oral conversation or making a notation of the request in the consumer's file.

(iii) If a consumer applies for a loan and the application form provides a space where the consumer may provide any other information or special circumstances, whether medical or non-medical, that the consumer would like the creditor to consider in evaluating the consumer's application, the creditor may use medical information provided by the consumer in that space on that application to accommodate the consumer's application for credit, consistent with safe and sound practices, or may disregard that information.

(iv) If a consumer specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit and provides the creditor with medical information for that purpose, and the creditor determines that it needs additional information regarding the consumer's circumstances, the creditor may request, obtain, and use additional medical information about the consumer as necessary to verify the information provided by the consumer or to determine whether to make an accommodation for the consumer. The consumer may decline to provide additional information, withdraw the request for an accommodation, and have the application considered under the creditor's otherwise applicable underwriting criteria.

(v) If a consumer completes and signs a credit application that is not for medical purpose credit and the application contains boilerplate language that routinely requests medical information from the consumer or that indicates that by applying for credit the consumer authorizes or consents to the creditor obtaining and using medical information in connection with a determination of the consumer's eligibility, or continued eligibility, for credit, the consumer has not specifically requested that the creditor obtain and use medical information to accommodate the consumer's particular circumstances.

(5) *Example of a forbearance practice or program.* After an appropriate safety and soundness review, a creditor institutes a program that allows consumers who are or will be hospitalized to defer payments as needed for up to three months, without penalty, if the credit account has been open for more than one year and has not previously been in default, and the consumer provides confirming documentation at an appropriate time. A consumer is hospitalized and does not pay her bill for a particular month. This consumer has had a credit account with the creditor for more than one year and has not previously been in default. The creditor attempts to contact the consumer and speaks with the consumer's spouse, who is not the consumer's legal representative. The spouse informs the creditor that the consumer is hospitalized and is unable to pay the bill at that time. The creditor defers payments for up to three months, without penalty, for the hospitalized consumer and sends the consumer a letter confirming this practice and the date on which the next payment will be due.

§ 571.31 Limits on redisclosure of information.

(a) *Scope.* This section applies to savings associations and federal savings association operating subsidiaries.

(b) *Limits on redisclosure.* If a person described in paragraph (a) of this section receives medical information about a consumer from a consumer reporting agency or its affiliate, the person must not disclose that information to any other person, except as necessary to carry out the purpose for which the information was initially disclosed, or as otherwise permitted by statute, regulation, or order.

§ 571.32 Sharing medical information with affiliates.

(a) *Scope.* This section applies to savings associations and Federal savings association operating subsidiaries.

(b) *In general.* The exclusions from the term ''consumer report'' in section 603(d)(2) of the Act that allow the sharing of information with affiliates do not apply if a person described in paragraph (a) of this section communicates to an affiliate—

(1) Medical information;

(2) An individualized list or description based on the payment transactions of the consumer for medical products or services; or

(3) An aggregate list of identified consumers based on payment transactions for medical products or services.

(c) *Exceptions.* A person described in paragraph (a) of this section may rely on

the exclusions from the term ''consumer report'' in section 603(d)(2) of the Act to communicate the information in paragraph (b) of this section to an affiliate—

(1) In connection with the business of insurance or annuities (including the activities described in section 18B of the model Privacy of Consumer Financial and Health Information Regulation issued by the National Association of Insurance Commissioners, as in effect on January 1, 2003);

(2) For any purpose permitted without authorization under the regulations promulgated by the Department of Health and Human Services pursuant to the Health Insurance Portability and Accountability Act of 1996 (HIPAA);

(3) For any purpose referred to in section 1179 of HIPAA;

(4) For any purpose described in section 502(e) of the Gramm-Leach-Bliley Act;

(5) In connection with a determination of the consumer's eligibility, or continued eligibility, for credit consistent with § 571.30; or

(6) As otherwise permitted by order of the OTS.

National Credit Union Administration

■ For the reasons set out in the preamble, 12 CFR chapter VII is amended as follows:

PART 717—FAIR CREDIT REPORTING

■ 1. Revise the authority citation for part 717 to read as follows:

Authority: 15 U.S.C. 1681a, 1681b, 1681s, 1681w, 6801 and 6805.

■ 2. Amend part 717 by revising subpart A to read as follows:

Subpart A—General Provisions

Sec.
717.1 Purpose.
717.2 Examples.
717.3 Definitions.

Subpart A—General Provisions

§ 717.1 Purpose.

(a) *Purpose.* The purpose of this part is to establish standards for Federal credit unions regarding consumer report information. In addition, the purpose of this part is to specify the extent to which Federal credit unions may obtain, use or share certain information. This part also contains a number of measures Federal credit unions must take to combat consumer fraud and related crimes, including identity theft.

(b) [Reserved]

§ 717.2 Examples.

The examples in this part are not exclusive. Compliance with an example, to the extent applicable, constitutes compliance with this part. Examples in a paragraph illustrate only the issue described in the paragraph and do not illustrate any other issue that may arise in this part.

§ 717.3 Definitions.

As used in this part, unless the context requires otherwise:

(a) *Act* means the Fair Credit Reporting Act (15 U.S.C. 1681 *et seq.*).

(b) *Affiliate* means any company that is related by common ownership or common corporate control with another company. For example, an affiliate of a Federal credit union is a credit union service corporation (CUSO), as provided in 12 CFR part 712, that is controlled by the Federal credit union.

(c) [Reserved]

(d) *Company* means any corporation, limited liability company, business trust, general or limited partnership, association, or similar organization.

(e) *Consumer* means an individual.

(f) [Reserved]

(g) [Reserved]

(h) [Reserved]

(i) *Common ownership or common corporate control* means a relationship between two companies under which:

(1) One company has, with respect to the other company:

(i) Ownership, control, or power to vote 25 percent or more of the outstanding shares of any class of voting security of a company, directly or indirectly, or acting through one or more other persons;

(ii) Control in any manner over the election of a majority of the directors, trustees, or general partners (or individuals exercising similar functions) of a company; or

(iii) The power to exercise, directly or indirectly, a controlling influence over the management or policies of a company, as the NCUA determines; or

(iv) Example. NCUA will presume a credit union has a controlling influence over the management or policies of a CUSO, if the CUSO is 67% owned by credit unions.

(2) Any other person has, with respect to both companies, a relationship described in paragraphs (i)(1)(i)–(i)(1)(iii) of this section.

(j) [Reserved]

(k) *Medical information* means:

(l) Information or data, whether oral or recorded, in any form or medium, created by or derived from a health care provider or the consumer, that relates to—

(i) The past, present, or future physical, mental, or behavioral health or condition of an individual;

(ii) The provision of health care to an individual; or

(iii) The payment for the provision of health care to an individual.

(2) The term does not include:

(i) The age or gender of a consumer;

(ii) Demographic information about the consumer, including a consumer's residence address or e-mail address;

(iii) Any other information about a consumer that does not relate to the physical, mental, or behavioral health or condition of a consumer, including the existence or value of any insurance policy; or

(iv) Information that does not identify a specific consumer.

(l) *Person* means any individual, partnership, corporation, trust, estate cooperative, association, government or governmental subdivision or agency, or other entity.

■ 3. Subpart D is added to part 717 to read as follows:

Subpart D—Medical Information

§ 717.30 Obtaining or using medical information in connection with a determination of eligibility for credit.

(a) *Scope.* This section applies to:

(1) A Federal credit union that participates as a creditor in a transaction; or

(2) Any other person that participates as a creditor in a transaction involving a person described in paragraph (1).

(b) *General prohibition on obtaining or using medical information.* (1) *In general.* A creditor may not obtain or use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit, except as provided in this section.

(2) *Definitions.* (i) *Credit* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(ii) *Creditor* has the same meaning as in section 702 of the Equal Credit Opportunity Act, 15 U.S.C. 1691a.

(iii) *Eligibility, or continued eligibility, for credit* means the consumer's qualification or fitness to receive, or continue to receive, credit, including the terms on which credit is offered. The term does not include:

(A) Any determination of the consumer's qualification or fitness for employment, insurance (other than a credit insurance product), or other non-credit products or services;

(B) Authorizing, processing, or documenting a payment or transaction on behalf of the consumer in a manner that does not involve a determination of the consumer's eligibility, or continued eligibility, for credit; or

(C) Maintaining or servicing the consumer's account in a manner that

does not involve a determination of the consumer's eligibility, or continued eligibility, for credit.

(c) *Rule of construction for obtaining and using unsolicited medical information.* (1) *In general.* A creditor does not obtain medical information in violation of the prohibition if it receives medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit without specifically requesting medical information.

(2) *Use of unsolicited medical information.* A creditor that receives unsolicited medical information in the manner described in paragraph (1) may use that information in connection with any determination of the consumer's eligibility, or continued eligibility, for credit to the extent the creditor can rely on at least one of the exceptions in § 717.30(d) or (e).

(3) *Examples.* A creditor does not obtain medical information in violation of the prohibition if, for example:

(i) In response to a general question regarding a consumer's debts or expenses, the creditor receives information that the consumer owes a debt to a hospital.

(ii) In a conversation with the creditor's loan officer, the consumer informs the creditor that the consumer has a particular medical condition.

(iii) In connection with a consumer's application for an extension of credit, the creditor requests a consumer report from a consumer reporting agency and receives medical information in the consumer report furnished by the agency even though the creditor did not specifically request medical information from the consumer reporting agency.

(d) *Financial information exception for obtaining and using medical information.*

(1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit so long as:

(i) The information is the type of information routinely used in making credit eligibility determinations, such as information relating to debts, expenses, income, benefits, assets, collateral, or the purpose of the loan, including the use of proceeds;

(ii) The creditor uses the medical information in a manner and to an extent that is no less favorable than it would use comparable information that is not medical information in a credit transaction; and

(iii) The creditor does not take the consumer's physical, mental, or behavioral health, condition or history, type of treatment, or prognosis into account as part of any such determination.

(2) *Examples.* (i) *Examples of the types of information routinely used in making credit eligibility determinations.* Paragraph (d)(1)(i) of this section permits a creditor, for example, to obtain and use information about:

(A) The dollar amount, repayment terms, repayment history, and similar information regarding medical debts to calculate, measure, or verify the repayment ability of the consumer, the use of proceeds, or the terms for granting credit;

(B) The value, condition, and lien status of a medical device that may serve as collateral to secure a loan;

(C) The dollar amount and continued eligibility for disability income or benefits related to health or a medical condition that is relied on as a source of repayment; or

(D) The identity of creditors to whom outstanding medical debts are owed in connection with an application for credit, including but not limited to, a transaction involving the consolidation of medical debts.

(ii) *Examples of uses of medical information consistent with the exception.* (A) A consumer includes on an application for credit information about two $20,000 debts. One debt is to a hospital; the other debt is to a retailer. The creditor contacts the hospital and the retailer to verify the amount and payment status of the debts. The creditor learns that both debts are more than 90 days past due. Any two debts of this size that are more than 90 days past due would disqualify the consumer under the creditor's established underwriting criteria. The creditor denies the application on the basis that the consumer has a poor repayment history on outstanding debts. The creditor has used medical information in a manner and to an extent no less favorable than it would use comparable non-medical information.

(B) A consumer indicates on an application for a $200,000 mortgage loan that she receives $15,000 in long-term disability income each year from her former employer and has no other income. Annual income of $15,000, regardless of source, would not be sufficient to support the requested amount of credit. The creditor denies the application on the basis that the projected debt-to-income ratio of the consumer does not meet the creditor's underwriting criteria. The creditor has used medical information in a manner and to an extent that is no less favorable than it would use comparable non-medical information.

(C) A consumer includes on an application for a $10,000 home equity loan that he has a $50,000 debt to a medical facility that specializes in treating a potentially terminal disease. The creditor contacts the medical facility to verify the debt and obtain the repayment history and current status of the loan. The creditor learns that the debt is current. The applicant meets the income and other requirements of the creditor's underwriting guidelines. The creditor grants the application. The creditor has used medical information in accordance with the exception.

(iii) *Examples of uses of medical information inconsistent with the exception.* (A) A consumer applies for $25,000 of credit and includes on the application information about a $50,000 debt to a hospital. The creditor contacts the hospital to verify the amount and payment status of the debt, and learns that the debt is current and that the consumer has no delinquencies in her repayment history. If the existing debt were instead owed to a retail department store, the creditor would approve the application and extend credit based on the amount and repayment history of the outstanding debt. The creditor, however, denies the application because the consumer is indebted to a hospital. The creditor has used medical information, here the identity of the medical creditor, in a manner and to an extent that is less favorable than it would use comparable non-medical information.

(B) A consumer meets with a loan officer of a creditor to apply for a mortgage loan. While filling out the loan application, the consumer informs the loan officer orally that she has a potentially terminal disease. The consumer meets the creditor's established requirements for the requested mortgage loan. The loan officer recommends to the credit committee that the consumer be denied credit because the consumer has that disease. The credit committee follows the loan officer's recommendation and denies the application because the consumer has a potentially terminal disease. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis as part of a determination of eligibility or continued eligibility for credit.

(C) A consumer who has an apparent medical condition, such as a consumer who uses a wheelchair or an oxygen

tank, meets with a loan officer to apply for a home equity loan. The consumer meets the creditor's established requirements for the requested home equity loan and the creditor typically does not require consumers to obtain a debt cancellation contract, debt suspension agreement, or credit insurance product in connection with such loans. However, based on the consumer's apparent medical condition, the loan officer recommends to the credit committee that credit be extended to the consumer only if the consumer obtains a debt cancellation contract, debt suspension agreement, or credit insurance product. The credit committee agrees with the loan officer's recommendation. The loan officer informs the consumer that the consumer must obtain a debt cancellation contract, debt suspension agreement, or credit insurance product to qualify for the loan. The consumer obtains one of these products from a third party and the creditor approves the loan. The creditor has used medical information in a manner inconsistent with the exception by taking into account the consumer's physical, mental, or behavioral health, condition, or history, type of treatment, or prognosis in setting conditions on the consumer's eligibility for credit.

(e) *Specific exceptions for obtaining and using medical information.* (1) *In general.* A creditor may obtain and use medical information pertaining to a consumer in connection with any determination of the consumer's eligibility, or continued eligibility, for credit—

(i) To determine whether the use of a power of attorney or legal representative that is triggered by a medical event or condition is necessary and appropriate or whether the consumer has the legal capacity to contract when a person seeks to exercise a power of attorney or act as legal representative for a consumer based on an asserted medical event or condition;

(ii) To comply with applicable requirements of local, State, or Federal laws;

(iii) To determine, at the consumer's request, whether the consumer qualifies for a legally permissible special credit program or credit-related assistance program that is—

(A) Designed to meet the special needs of consumers with medical conditions; and

(B) Established and administered pursuant to a written plan that—

(*1*) Identifies the class of persons that the program is designed to benefit; and

(*2*) Sets forth the procedures and standards for extending credit or providing other credit-related assistance under the program.

(iv) To the extent necessary for purposes of fraud prevention or detection;

(v) In the case of credit for the purpose of financing medical products or services, to determine and verify the medical purpose of a loan and the use of proceeds;

(vi) Consistent with safe and sound practices, if the consumer or the consumer's legal representative specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit, to accommodate the consumer's particular circumstances, and such request is documented by the creditor;

(vii) Consistent with safe and sound practices, to determine whether the provisions of a forbearance practice or program that is triggered by a medical event or condition apply to a consumer;

(viii) To determine the consumer's eligibility for, the triggering of, or the reactivation of a debt cancellation contract or debt suspension agreement if a medical condition or event is a triggering event for the provision of benefits under the contract or agreement; or

(ix) To determine the consumer's eligibility for, the triggering of, or the reactivation of a credit insurance product if a medical condition or event is a triggering event for the provision of benefits under the product.

(2) *Example of determining eligibility for a special credit program or credit assistance program.* A not-for-profit organization establishes a credit assistance program pursuant to a written plan that is designed to assist disabled veterans in purchasing homes by subsidizing the down payment for the home purchase mortgage loans of qualifying veterans. The organization works through mortgage lenders and requires mortgage lenders to obtain medical information about the disability of any consumer that seeks to qualify for the program, use that information to verify the consumer's eligibility for the program, and forward that information to the organization. A consumer who is a veteran applies to a creditor for a home purchase mortgage loan. The creditor informs the consumer about the credit assistance program for disabled veterans and the consumer seeks to qualify for the program. Assuming that the program complies with all applicable law, including applicable fair lending laws, the creditor may obtain and use medical information about the medical condition and disability, if any, of the consumer to determine whether the consumer qualifies for the credit assistance program.

(3) *Examples of verifying the medical purpose of the loan or the use of proceeds.* (i) If a consumer applies for $10,000 of credit for the purpose of financing vision correction surgery, the creditor may verify with the surgeon that the procedure will be performed. If the surgeon reports that surgery will not be performed on the consumer, the creditor may use that medical information to deny the consumer's application for credit, because the loan would not be used for the stated purpose.

(ii) If a consumer applies for $10,000 of credit for the purpose of financing cosmetic surgery, the creditor may confirm the cost of the procedure with the surgeon. If the surgeon reports that the cost of the procedure is $5,000, the creditor may use that medical information to offer the consumer only $5,000 of credit.

(iii) A creditor has an established medical loan program for financing particular elective surgical procedures. The creditor receives a loan application from a consumer requesting $10,000 of credit under the established loan program for an elective surgical procedure. The consumer indicates on the application that the purpose of the loan is to finance an elective surgical procedure not eligible for funding under the guidelines of the established loan program. The creditor may deny the consumer's application because the purpose of the loan is not for a particular procedure funded by the established loan program.

(4) *Examples of obtaining and using medical information at the request of the consumer.* (i) If a consumer applies for a loan and specifically requests that the creditor consider the consumer's medical disability at the relevant time as an explanation for adverse payment history information in his credit report, the creditor may consider such medical information in evaluating the consumer's willingness and ability to repay the requested loan to accommodate the consumer's particular circumstances, consistent with safe and sound practices. The creditor may also decline to consider such medical information to accommodate the consumer, but may evaluate the consumer's application in accordance with its otherwise applicable underwriting criteria. The creditor may not deny the consumer's application or otherwise treat the consumer less favorably because the consumer specifically requested a medical accommodation, if the creditor would have extended the credit or treated the

consumer more favorably under the creditor's otherwise applicable underwriting criteria.

(ii) If a consumer applies for a loan by telephone and explains that his income has been and will continue to be interrupted on account of a medical condition and that he expects to repay the loan by liquidating assets, the creditor may, but is not required to, evaluate the application using the sale of assets as the primary source of repayment, consistent with safe and sound practices, provided that the creditor documents the consumer's request by recording the oral conversation or making a notation of the request in the consumer's file.

(iii) If a consumer applies for a loan and the application form provides a space where the consumer may provide any other information or special circumstances, whether medical or non-medical, that the consumer would like the creditor to consider in evaluating the consumer's application, the creditor may use medical information provided by the consumer in that space on that application to accommodate the consumer's application for credit, consistent with safe and sound practices, or may disregard that information.

(iv) If a consumer specifically requests that the creditor use medical information in determining the consumer's eligibility, or continued eligibility, for credit and provides the creditor with medical information for that purpose, and the creditor determines that it needs additional information regarding the consumer's circumstances, the creditor may request, obtain, and use additional medical information about the consumer as necessary to verify the information provided by the consumer or to determine whether to make an accommodation for the consumer. The consumer may decline to provide additional information, withdraw the request for an accommodation, and have the application considered under the creditor's otherwise applicable underwriting criteria.

(v) If a consumer completes and signs a credit application that is not for medical purpose credit and the application contains boilerplate language that routinely requests medical information from the consumer or that indicates that by applying for credit the consumer authorizes or consents to the creditor obtaining and using medical information in connection with a determination of the consumer's eligibility, or continued eligibility, for credit, the consumer has not specifically requested that the creditor obtain and use medical information to accommodate the consumer's particular circumstances.

(5) *Example of a forbearance practice or program.* After an appropriate safety and soundness review, a creditor institutes a program that allows consumers who are or will be hospitalized to defer payments as needed for up to three months, without penalty, if the credit account has been open for more than one year and has not previously been in default, and the consumer provides confirming documentation at an appropriate time. A consumer is hospitalized and does not pay her bill for a particular month. This consumer has had a credit account with the creditor for more than one year and has not previously been in default. The creditor attempts to contact the consumer and speaks with the consumer's adult child, who is not the consumer's legal representative. The adult child informs the creditor that the consumer is hospitalized and is unable to pay the bill at that time. The creditor defers payments for up to three months, without penalty, for the hospitalized consumer and sends the consumer a letter confirming this practice and the date on which the next payment will be due.

§ 717.31 Limits on redisclosure of information.

(a) *Scope.* This section applies to Federal credit unions.

(b) *Limits on redisclosure.* If a Federal credit union receives medical information about a consumer from a consumer reporting agency or its affiliate, the person must not disclose that information to any other person, except as necessary to carry out the purpose for which the information was initially disclosed, or as otherwise permitted by statute, regulation, or order.

§ 717.32 Sharing medical information with affiliates.

(a) *Scope.* This section applies to Federal credit unions.

(b) *In general.* The exclusions from the term ''consumer report'' in section 603(d)(2) of the Act that allow the sharing of information with affiliates do not apply if a Federal credit union communicates to an affiliate—

(1) Medical information;

(2) An individualized list or description based on the payment transactions of the consumer for medical products or services; or

(3) An aggregate list of identified consumers based on payment transactions for medical products or services.

(c) *Exceptions.* A Federal credit union may rely on the exclusions from the term ''consumer report'' in section 603(d)(2) of the Act to communicate the information in paragraph (b) to an affiliate—

(1) In connection with the business of insurance or annuities (including the activities described in section 18B of the model Privacy of Consumer Financial and Health Information Regulation issued by the National Association of Insurance Commissioners, as in effect on January 1, 2003);

(2) For any purpose permitted without authorization under the regulations promulgated by the Department of Health and Human Services pursuant to the Health Insurance Portability and Accountability Act of 1996 (HIPAA);

(3) For any purpose referred to in section 1179 of HIPAA;

(4) For any purpose described in section 502(e) of the Gramm-Leach-Bliley Act;

(5) In connection with a determination of the consumer's eligibility, or continued eligibility, for credit consistent with § 717.30; or

(6) As otherwise permitted by order of the NCUA.

By order of the Board of Governors of the Federal Reserve System, June 2, 2005.

Jennifer J. Johnson,

Secretary of the Board.

Dated: May 25, 2005.

Julie L. Williams,

Acting Comptroller of the Currency.

Dated at Washington, DC, this 16th day of May, 2005.

By order of the Board of Directors.

Federal Deposit Insurance Corporation.

Robert E. Feldman,

Executive Secretary.

Dated: May 19, 2005.

By the Office of Thrift Supervision.

Richard M. Riccobono,

Acting Director.

By the National Credit Union Administration Board on June 1, 2005.

Mary F. Rupp,

Secretary of the Board.

[FR Doc. 05–11356 Filed 6–9–05; 8:45 am]

BILLING CODE 4810–33–P, 6210–01–P, 6714–10–P, 6720–01–P, 7535–01–P

Many credit unions submitted a virtually identical comment in opposition to the proposed amendment. These commenters believe there is no reason to conduct conversion votes any differently from credit union election votes where the credit union's supervisory committee or independent certified public accountant assumes the responsibility for the accuracy and reporting of the vote. These commenters state the new requirement will increase the cost of the conversion vote and implies mistrust of a board of directors to conduct an accurate and honest vote. These commenters note that NCUA seldom audits conversion votes and has never challenged a conversion vote.

Several commenters also stated the requirement is onerous, particularly for small credit unions. One commenter wrote that it is highly unlikely that the independent entity conducting the vote will attest to the accuracy of the credit union's count of the total number of members.

The final rule retains the secret ballot and independent teller requirements. These requirements will help ensure the integrity and accuracy of the conversion vote. The Board does not believe these requirements are onerous and notes that the private insurer assists converting credit unions, including small credit unions, during the conversion process. Also, if the credit union is maintaining up-to-date records of its membership, the Board believes both the credit union and the independent entity should be able to certify the number of members at the credit union. If there is some question about the exact number, but the range of possible error is not material to the outcome of the vote, the credit union and independent entity may footnote the certification and attach a detailed explanation.

One commenter stated that the 20% quorum requirement is overly burdensome, and another commenter incorrectly stated that the requirement was NCUA-imposed. The Act, not NCUA, imposes the 20% quorum requirement. 12 U.S.C. 1786(d)(2). One commenter complained that the requirement that the notice to members of the pending conversion and member vote be mailed to the members not less than seven days, nor more than 30 days, before the vote, was too restrictive. This requirement is also imposed by the Act. *Id.*

7. Miscellaneous Amendments

The proposed rule would also have clarified that the terms ''insurance'' and ''insured'' as used in part 708b refer to primary share or deposit insurance, not to excess insurance. The proposed rule would also have made other minor changes to modernize the language of the rule. There were no comments received specifically on these amendments, and the final rule adopts them as proposed.

F. Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to describe any significant economic impact a proposed rule may have on a substantial number of small credit unions (those under ten million dollars in assets). Each year, there are about 300 mergers that involve federally-insured credit unions, and about 250 of these mergers involve small credit unions. In almost all cases, however, the small credit union merges into a much larger continuing credit union. The larger credit union is available to assist the small credit union with each step in the merger process, keeping the economic impact on the small credit union to a minimum. In addition, there are only one or two small credit unions a year on average that undertake an insurance conversion, and the private insurer assists these converting credit unions with the conversion process. Accordingly, the Board certifies that this final rule will not have a significant economic impact on a substantial number of small credit unions, and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

Section 708b contains information collection requirements. As required by the Paperwork Reduction Act of 1995, 44 U.S.C. 3507(d), NCUA submitted a copy of this proposed rule as part of an information collection package to the Office of Management and Budget (OMB) for its review and approval for revision of Collection of Information, Mergers of Federally Insured Credit Unions, Control Number 3133–0024. OMB approved the Collection of Information on October 7, 2004.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. One commenter stated that the proposed requirement for state chartered credit unions to obtain the prior approval of the state supervisory authority (SSA) of share insurance communications, in tandem with NCUA, would impose a tremendous burden on the SSA with implications under Executive Order 13132. As the final rule eliminates any requirement for NCUA prior approval, it also eliminates any requirement for the prior approval of SSAs. Accordingly, the final rule will not have substantial direct effects on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget has determined that this rule is not a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects in 12 CFR Part 708b

Credit Unions, Mergers of Credit Unions, Reporting and Recordkeeping Requirements.

By the National Credit Union Administration Board on January 13, 2005.

Mary Rupp,

Secretary of the Board.