

GC/SAA/MFR:bhs
SSIC 6100
97-1015a

TO:

FROM: Sheila A. Albin, Associate General Counsel

SUBJ: Nonstandard Bylaw Amendment -
Your Memorandum dated October 3, 1997.

DATE: December 9, 1997

You have asked for our comments on a request from [] Federal Credit Union (the FCU) for a nonstandard bylaw amendment to Article XII, Section 1 of the Federal Credit Union Standard Bylaw Amendments. Loans to nonnatural persons are, by definition, business loans. NCUA's bylaw, standard bylaw amendment, and nonstandard bylaw amendments dealing with loans to nonnatural persons have tracked our business loan regulation. As explained below, the requested amendment is legally permissible with an additional restriction.

Article XII, Section 1 of the Federal Credit Union Bylaws only permits loans to nonnatural persons if they are secured by shares in the credit union. This bylaw provision parallels the exception in the business loan regulation for "[a] loan that is fully secured by shares in the credit union or deposits in other financial institutions." 12 C.F.R. §701.21(h)(1)(i)(B).

The standard bylaw amendment provides an alternative to the requirement that a loan to a nonnatural person be shared-secured. The standard bylaw amendment imposes the requirement of the personal liability of natural person members. This parallels a provision in the business loan regulation. The standard bylaw amendment permits loans to nonnatural persons, in addition to the case when the loan is share-secured, if the loan is:

- co-signed by the principals; or
- in the case of an association, a majority of the members co-sign.

This alternative bylaw parallels the provision in the business loan regulation that a business loan must generally be personally guaranteed by natural person members. 12 C.F.R. §701.21(h)(2)(ii)(B). The exception to this requirement in the business loan regulation is for a "not-for-profit organization as defined by the Internal Revenue Service Code (26 U.S.C. 501)." *Id.* We have allowed nonstandard bylaw amendments that parallel this provision of the business regulation.

The FCU is seeking a nonstandard amendment which would allow it to make loans to its sponsor, [], without the requirement of being share secured or being personally guaranteed by individual members. While [] receives special tax treatment under §833 of the Internal Revenue Code, 26 U.S.C. §833, it is not classified as a not-for-profit organization under §501(c)(3). Therefore, it does not fall within the exception in §701.21(h)(2)(ii)(B). Thus, if the loan would otherwise fall within the business lending regulation, personal guarantees would be required.

You indicate that the loan to [] would be under \$50,000. The member business loan rule does not apply to loans under \$50,000, if the total loans to the borrower are under \$50,000. 12 C.F.R. §701.21(h)(1)(i)(C). If the member business loan rule does not apply, we are not aware of any other statutory or regulatory requirements that the loan be share secured or personally guaranteed.

We conclude that the bylaw amendment is legally permissible if the loan is not a business loan. To ensure that it is not a business loan, the following language should be added to the proposed amendment after "Internal Revenue Code:" and the total loans to the organization are less than \$50,000.