

National Credit Union Administration

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(b) *Required expertise and experience.* A federally insured credit union making, purchasing, or holding any commercial loan must internally possess the following experience and competencies:

(1) *Senior executive officers.* A federally insured credit union's senior executive officers overseeing the commercial lending function must understand the federally insured credit union's commercial lending activities. At a minimum, senior executive officers must have a comprehensive understanding of the role of commercial lending in the federally insured credit union's overall business model and establish risk management processes and controls necessary to safely conduct commercial lending.

(2) *Qualified lending personnel.* A federally insured credit union must employ qualified staff with experience in the following areas:

(i) Underwriting and processing for the type(s) of commercial lending in which the federally insured credit union is engaged;

(ii) Overseeing and evaluating the performance of a commercial loan portfolio, including rating and quantifying risk through a credit risk rating system; and

(iii) Conducting collection and loss mitigation activities for the type(s) of commercial lending in which the federally insured credit union is engaged.

(3) *Options to meet the required experience.* A federally insured credit union may meet the experience requirements in paragraphs (b)(1) and (2) of this section by conducting internal training and development, hiring qualified individuals, or using a third-party, such as an independent contractor or a credit union service organization. However, with respect to the qualified lending personnel requirements in paragraph (b)(2) of this section, use of a third-party is permissible only if the following conditions are met:

(i) The third-party has no affiliation or contractual relationship with the borrower or any associated borrowers;

(ii) The actual decision to grant a loan must reside with the federally insured credit union;

(iii) Qualified federally insured credit union staff exercises ongoing oversight over the third party by regularly eval-

uating the quality of any work the third party performs for the federally insured credit union; and

(iv) The third-party arrangement must otherwise comply with § 723.7 of this part.

§ 723.4 Commercial loan policy.

Prior to engaging in commercial lending, a federally insured credit union must adopt and implement a comprehensive written commercial loan policy and establish procedures for commercial lending. The board-approved policy must ensure the federally insured credit union's commercial lending activities are performed in a safe and sound manner by providing for ongoing control, measurement, and management of the federally insured credit union's commercial lending activities. At a minimum, a federally insured credit union's commercial loan policy must address each of the following:

(a) Type(s) of commercial loans permitted.

(b) Trade area.

(c) Maximum amount of assets, in relation to net worth, allowed in secured, unsecured, and unguaranteed commercial loans and in any given category or type of commercial loan and to any one borrower or group of associated borrowers. The policy must specify that the aggregate dollar amount of commercial loans to any one borrower or group of associated borrowers may not exceed the greater of 15 percent of the federally insured credit union's net worth or \$100,000, plus an additional 10 percent of the credit union's net worth if the amount that exceeds the credit union's 15 percent general limit is fully secured at all times with a perfected security interest by readily marketable collateral as defined in § 723.2 of this part. Any insured or guaranteed portion of a commercial loan made through a program in which a federal or state agency (or its political subdivision) insures repayment, guarantees repayment, or provides an advance commitment to purchase the loan in full, is excluded from this limit.

(d) Qualifications and experience requirements for personnel involved in underwriting, processing, approving,

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administering, and collecting commercial loans.

(e) Loan approval processes, including establishing levels of loan approval authority commensurate with the individual's or committee's proficiency in evaluating and understanding commercial loan risk, when considered in terms of the level of risk the borrowing relationship poses to the federally insured credit union.

(f) Underwriting standards commensurate with the size, scope and complexity of the commercial lending activities and borrowing relationships contemplated. The standards must, at a minimum, address the following:

(1) The level and depth of financial analysis necessary to evaluate the financial trends and condition of the borrower and the ability of the borrower to meet debt service requirements;

(2) Thorough due diligence of the principal(s) to determine whether any related interests of the principal(s) might have a negative impact or place an undue burden on the borrower and related interests with regard to meeting the debt obligations with the credit union;

(3) Requirements of a borrower-prepared projection when historic performance does not support projected debt payments. The projection must be supported by reasonable rationale and, at a minimum, must include a projected balance sheet and income and expense statement;

(4) The financial statement quality and the degree of verification sufficient to support an accurate financial analysis and risk assessment;

(5) The methods to be used in collateral evaluation, for all types of collateral authorized, including loan-to-value ratio limits. Such methods must be appropriate for the particular type of collateral. The means to secure various types of collateral, and the measures taken for environmental due diligence must also be appropriate for all authorized collateral; and

(6) Other appropriate risk assessment including analysis of the impact of current market conditions on the borrower and associated borrowers.

(g) Risk management processes commensurate with the size, scope and

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complexity of the federally insured credit union's commercial lending activities and borrowing relationships. These processes must, at a minimum, address the following:

(1) Use of loan covenants, if appropriate, including frequency of borrower and guarantor financial reporting;

(2) Periodic loan review, consistent with loan covenants and sufficient to conduct portfolio risk management. This review must include a periodic re-evaluation of the value and marketability of any collateral;

(3) A credit risk rating system. Credit risk ratings must be assigned to commercial loans at inception and reviewed as frequently as necessary to satisfy the federally insured credit union's risk monitoring and reporting policies, and to ensure adequate reserves as required by generally accepted accounting principles (GAAP); and

(4) A process to identify, report, and monitor loans approved as exceptions to the credit union's loan policy.

§ 723.5 Collateral and security.

(a) A federally insured credit union must require collateral commensurate with the level of risk associated with the size and type of any commercial loan. Collateral must be sufficient to ensure adequate loan balance protection along with appropriate risk sharing with the borrower and principal(s). A federally insured credit union making an unsecured loan must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.

(b) A federally insured credit union that does not require the full and unconditional personal guarantee from the principal(s) of the borrower who has a controlling interest in the borrower must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.

(1) *Transitional provision.* A federally insured credit union that, between May 13, 2016 and January 1, 2017, makes a member business loan and does not require the full and unconditional personal guarantee from the principal(s) of the borrower who has a controlling interest in the borrower is not required to seek a waiver from the requirement