CREDIT UNION COMMISSION

Rules Committee Meeting

Credit Union Department Building
914 East Anderson Lane
Austin, Texas

Thursday, July 12, 2018
1:00 p.m.

AGENDA

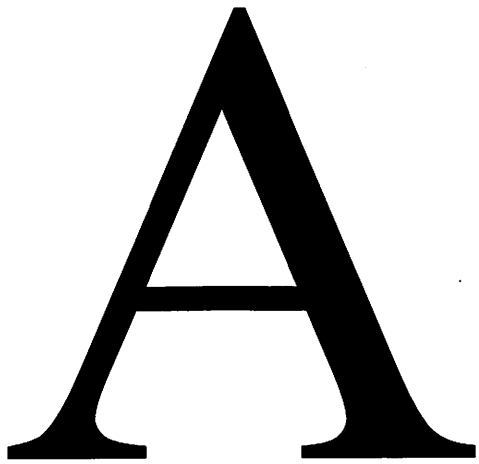
The Committee may discuss and take action regarding any item on this agenda

Adjournment

Note: This is a meeting of the Rules Committee of the Credit Union Commission. Because a quorum of the Credit Union Commission may attend this meeting of the Rules Committee, it is being posted, simultaneously, as a meeting of the entire Commission.

Meeting Recess: In the event the Commission does not finish deliberation of an item on the first day for which it was posted, the Commission might recess the meeting until the following day at the time and place announced at the time of recess.

Meeting Accessibility: Under the Americans with Disabilities Act, the Credit Union Commission will accommodate special needs. Those requesting auxiliary aids or services should notify Michelle Archie, Texas Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752--(512) 837-9236, as far in advance of the meeting as possible.



CALL TO ORDER

CREDIT UNION COMMISSION

RULES COMMITTEE

Committee Members

- ***Kay Stewart, Chair***
- ***Yusuf Farran, Vice Chair***
- ***Steven "Steve" Gilman***
- ***Rick Ybarra***
- ***Allyson "Missy" Morrow, Ex-Officio***

Legal Counsel

- ***Melissa Juarez***

Staff

- ***Harold E. Feeney***
- ***Isabel Velasquez***

FUTURE COMMITTEE MEETING DATES

The committee meets on an "as needed" or "subject to the call of the chair" schedule. If a meeting is necessary, it would normally be held the day before a regularly scheduled commission meeting.

B

RULES COMMITTEE MEETING MINUTES

A draft copy of the minutes of the Committee's meeting held on November 2, 2017, is located under ***TAB B***.

RECOMMENDED ACTION: The Department requests that the Committee approve the minutes as presented.

RECOMMENDED MOTION: I move that the minutes of the Committee's November 2, 2017, meeting be approved as presented.

TEXAS CREDIT UNION COMMISSION
RULES COMMITTEE MEETING MINUTES
Credit Union Department Building
914 East Anderson Lane
Austin, Texas
November 2, 2017

A. CALL TO ORDER – Chairwoman Kay Stewart called the meeting to order at 2:01 p.m. in the conference room of the Credit Union Department Building, Austin, Texas pursuant to Chapter 551 of the Government Code, and declared that a quorum was present. Other members present included Yusuf Farran, Steven "Steve" Gilman, and Commission Chair Allyson "Missy" Morrow, ex-officio member. Commission Members Sherri Merket and James L. Minge were in attendance, however, they did not participate in the discussion or vote on any items during this meeting. Assistant Attorney General Melissa Juarez was present and served as legal counsel. Representing the Department staff were Harold E. Feeney, Commissioner; and Isabel Velasquez, Executive Assistant. Chairwoman Stewart appointed Isabel Velasquez as recording secretary. The Chair inquired and the Commissioner confirmed that the notice of the meeting was properly posted **(October 23, 2017, TRD#2017012031).**

- **INVITATION FOR PUBLIC INPUT FOR FUTURE CONSIDERATION**–Chairwoman Stewart invited public input on matters regarding rulemaking for future consideration by the committee. There was none.

B. RECEIVE MINUTES OF PREVIOUS MEETING (July 7, 2016)

Mr. Farran moved to approve the minutes of July 7, 2016 as presented. Mr. Gilman seconded the motion, and the motion was unanimously adopted.

C. NEW BUSINESS

(a) Recommendation that the Credit Union Commission Adopt Amendments to 7 TAC Section 91.101 Concerning Definition and Interpretations. Commissioner Feeney explained that the amendments will add one new definition, modify four definitions and remove two definitions. He noted that no comments were received during the comment period

Mr. Gilman moved to recommend that the Commission adopt the proposed amendments to **7 TAC Section 91.101** as previously published in the *Texas Register*. Mr. Farran seconded the motion and the motion was unanimously adopted.

(b) Recommendation that the Credit Union Commission Adopt Amendments to 7 TAC Section 91.115 Concerning User Safety at Unmanned Teller Machines. Commissioner Feeney indicated that the amendments will, among other things, reduce regulatory burden by authorizing delivery of the notice of safety precautions by electronic means in certain circumstances. He noted that no comments were received during the comment period.

Mr. Gilman moved to recommend that the Commission adopt the proposed amendments to **7 TAC Section 91.115** as previously published in the *Texas Register*. Mr. Farran seconded the motion and the motion was unanimously adopted.

(c) Recommendation that the Credit Union Commission Adopt Amendments to 7 TAC Section 91.121 Concerning the Form of Consumer Complaint Notice. Commissioner Feeney indicated that the amendments will alter the content of the required notice to include the department's facsimile number and an email address as well as provide clarification and better readability. He noted that no comments were received during the comment period.

(d) Recommendation that the Credit Union Commission Adopt Amendments to 7 TAC Section 91.205 Concerning the Name of a Credit Union. Commissioner Feeney indicated that the amendments will make it clear that credit unions are solely responsible for any unauthorized use or infringement on a business trade name. He noted that no comments were received during the comment period.

(e) Recommendation that the Credit Union Commission Adopt Amendments to 7 TAC Section 91.209 Concerning the Submission of Call Reports and Other Information Requests. Commissioner Feeney indicated that the amendments will eliminate the specific due date for submission of call reports to avoid any conflict or confusion should the National Credit Union Administration (NCUA) establish a different date for submitting its Form 5300. He noted that no comments were received during the comment period.

Mr. Gilman moved to recommend that the Commission adopt the proposed amendments to **7 TAC Sections 91.121, 91.205, and 91.209** as previously published in the *Texas Register*. Mr. Farran seconded the motion and the motion was unanimously adopted.

(f) Recommendation that the Credit Union Commission Adopt Amendments to 7 TAC Section 91.1003 Concerning Mergers/Consolidations. Commissioner Feeney indicated that the amendments will require credit unions to include in any merger plan a description of financial arrangements providing a substantial increase in compensation or benefits, of any sort, to a board member or senior management employee in connection with the merger/consolidation. The amendments will also define the term "substantial to be an amount that exceeds $1,000 in total. He noted that one comment was received during the comment period.

After consideration of the comment received, Mr. Gilman moved to recommend that the Commission adopt the proposed amendments to **7 TAC Section 91.1003** as previously published in the *Texas Register*. Mr. Farran seconded the motion and the motion was unanimously adopted.

Committee Member Rick Ybarra joined the meeting at 2:15 p.m.

(g) Recommendation that the Credit Union Commission Withdraw the Previously Published Version of the Rule and Approval for Publication and Comment the Revised New 7 TAC Section 91.1010 Concerning Voluntary Liquidations. Commissioner Feeney indicated that no comments were received on the original published proposal, however, staff believes that a revised proposal would improve readability, provide better clarity on voting requirements, and prevent any director or senior management employee from receiving any economic benefit in connection with the voluntary liquidation. In general, he noted that the proposal will provide guidance to credit unions when they are considering a voluntary liquidation of the institution. The guidelines should enable the board of directors or liquidating agent to conduct the liquidation of the credit union in a more orderly and expeditious manner and to arrange distribution of the assets to the members without undue delay.

After a brief discussion, Mr. Gilman moved to recommend that the Commission withdraw the previously published version of new 7 TAC Section 91.1010 and approve for publication and comment the modified version of proposed new **7 TAC Section 91.1010** concerning voluntary liquidations. Mr. Farran seconded the motion and the motion was unanimously adopted.

(h) Recommendation that the Credit Union Commission Readopt the Rules in 7 TAC, Part 6, Chapter 91, Subchapters D (Powers of Credit Unions),

M (Electronic Operations), and N (Emergency or Permanent Closing of Office or Operation). Commissioner Feeney briefly explained that in accordance with the Commission's Rule Review Plan, staff has reviewed all of the rules in the noted subchapters and believes certain revisions would be appropriate. He noted that the amendments would be presented separately for proposal. Mr. Feeney noted that staff believes that the reasons for adopting the rules in these subchapters continue to exist and, subject to the proposed amendments, the rules should be readopted.

Mr. Gilman moved to recommend that the Commission find that the reasons for adopting the rules in **7 TAC Chapter 91, Subchapters D, M, and N** continue to exist and that the Commission, subject to the concurrently proposed amendments, readopt the rules in these subchapters. Mr. Farran seconded the motion and the motion was unanimously adopted.

(i) Recommendation that the Credit Union Commission Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.4001 Concerning Authority to Conduct Electronic Operations. Commissioner Feeney indicated that as a result of the review of Chapter 91, Subchapter M, staff is proposing amendments that would impose a new requirement, on credit unions using electronic means or facilities, to develop and reasonably test an incident response plan to minimize the impact of a data breach or other incident on members.

Melodie Durst, Executive Director, Credit Union Coalition of Texas. Mrs. Durst indicated that the Coalition would suggest that the term "electronic" be inserted in the proposed new language in subparagraph (c)(3) between the terms "Other" and "Incident" to provide better clarity, and to delete the words "on members" from the proposed rule.

After a brief discussion, Mr. Gilman moved to recommend that the Commission approve for publication and comment the proposed changes to **7 TAC Section 91.4001**, as amended by the Committee. Mr. Farran seconded the motion and the motion was unanimously adopted.

(j) Recommendation that the Credit Union Commission Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.4002 Concerning Transactional Web Site Notice Requirements and Security. Commissioner Feeney indicated that as a result of the review of Chapter 91, Subchapter M, staff is proposing amendments that would require a credit union to review the adequacy of its web site's security measures annually instead of once every two years.

Mr. Gilman moved to recommend that the Commission approve for publication and comment the proposed amendments to **7 TAC Section 91.4002** concerning transactional web site notice requirements and security. Mr. Ybarra seconded the motion and the motion was unanimously adopted.

(k) Recommendation that the Credit Union Commission Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.5001 Concerning Emergency Closing. Commissioner Feeney indicated that as a result of the review of Chapter 91, Subchapter N, staff is proposing amendments that would encourage a credit union to post notice of an emergency closing of an office or operation on its website and any social media pages.

Mr. Gilman moved to recommend that the Commission approve for publication and comment the proposed amendments to **7 TAC Section 91.5001** concerning emergency closing. Mr. Farran seconded the motion and the motion was unanimously adopted.

(l) Recommendation that the Credit Union Commission Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.5005 Concerning Permanent Closing of an Office. Commissioner Feeney indicated that as a result of the review of Chapter 91, Subchapter N, staff is proposing amendments that would require a credit union to post notice of a permanent closing of an office on its website and any social media pages at least 30 days prior to the proposed closing.

After a brief discussion, Mr. Gilman moved to recommend that the Commission approve for publication and comment the proposed amendments to **7 TAC Section 91.5005** concerning permanent closing of an office. Mr. Farran seconded the motion and the motion was unanimously adopted.

(m) Recommendation that the Credit Union Commission Approve for Publication and Comment the Proposed Amendments, a New Section, and a Repeal in 7 TAC, Part 8, Chapter 153 Concerning Home Equity Lending. Commissioner Feeney indicated that main purpose of the proposal is to implement SJR 60, passed by the Texas Legislature in 2017. SJR 60 amends Section 50 of the Texas Constitution and applies to home equity loans entered on or after January 1, 2018. He further noted that SJR 60 is Proposition 2 on the November 7th ballot.

After a brief discussion, Mr. Gilman moved to recommend that the Commission conditionally approve for publication and comment the proposed amendments, a new section, and a repeal in **7 TAC, Part 8, Chapter 153** concerning home equity lending, subject to a favorable vote on Proposition 2 in the November 7, 2017 Constitutional Amendment Election. Mr. Ybarra seconded the motion and the motion was unanimously adopted.

(n) Discussion and Consideration on Potential Rules to Implement HB 471 (Proposition 7 on the November 7 Ballot). Commissioner Feeney indicated that HB 471 is the enabling legislation for HJR 37 (Proposition 7 on the November 7 Ballot) He noted that if Proposition 7 is passed by the voters, HB 471 would authorize the Legislature to permit credit unions and other financial institutions to hold savings promotion raffles. Mr. Feeney explained that HB 471 also requires the Credit Union Commission and the Finance Commission of Texas to adopt rules to enforce the provisions of the bill. He further indicated that staff currently believes credit unions could conduct savings promotion raffles without any additional rules but staff was soliciting thoughts from interested parties on the need to promulgate rules.

There was a brief discussion, however, no suggestions were presented and the Committee took no action on the item.

(o) Discussion of and Vote to Establish Date for Next Committee Meeting. Chairwoman Stewart noted that the next meeting is tentatively scheduled for March 8, 2018.

ADJOURNMENT -- There being no other items to come before the Committee, and without objection, the meeting was adjourned at 2:45 p.m.

Kay Stewart Chairwoman	Isabel Velasquez Recording Secretary

Distribution:

Legislative Reference Library

C

PROCEDURES FOR ADOPTING A PROPOSED RULE

1. A proposed rule is prepared by Credit Union Department staff and presented to legal counsel (Attorney General) for review.

2. The proposed rule is presented to the commission for consideration.

3. The commission reviews, amends, adopts, refers back to staff, or tables the proposed rule.

4. The proposed rule is adjusted by staff (if required), furnished to legal counsel, and transmitted to the ***Texas Register*** for publication as a "proposed" rule.

5. A 30-day comment period follows initial publication which also is made in the Department's monthly newsletter or by a special mailing to credit unions.

6. The commission may reconsider the rule anytime after the 30-day comment period. Any comments received are considered and the rule is available for adoption as "final" if no substantive changes are made. Any substantive change will result in the rule reverting to step four.

7. The rule is adopted as "final" and transmitted to the ***Texas Register*** for publication as a final rule. The rule becomes effective 20 days following filing for publication.

8. The rule is published or announced through the Department's newsletter.

EMERGENCY RULES

Rules, which are approved by the commission for emergency adoption, are transmitted to the ***Texas Register*** for filing. These rules become effective immediately upon filing unless another effective date is specified. They can be effective only for 120 days with a renewal provision for an additional 60 days -- a maximum of 180 days. "Day one" is the day of filing or the date specified as the effective date. While these emergency rules are in effect, regular rules should be initiated using the normal procedure described above. The Department rarely adopts emergency rules.

PROCEDURES FOR REQUIRED RULE REVIEW

Section 2001.39, Government Code, requires that a state agency review and consider for re-adoption each rule not later than the fourth anniversary of the date on which the rule took effect and every four years after that date. To comply with this requirement, the Commission follows the procedure below:

1. Every four years, the Commission adopts and publishes a Rule Review Plan, which establishes a date for the required review of each existing rule.
2. At least sixty days prior to a particular rule's scheduled review date, the Department publishes notice in the Newsletter reminding interested persons of the review and encouraging comments on the rules up for review.
3. Staff reviews each rule to determine whether it is obsolete, whether the rule reflects current legal and policy considerations, and whether the rule's structure as well as the specific language used is both clear and understandable.
4. If in reviewing existing rules, staff believes certain amendments may be appropriate, proposed amendments are prepared by staff and presented to the Rules Committee for review.
5. At a public meeting, the Rules Committee accepts public testimony on each rule subject to review and considers staff recommended changes. The Committee reviews each rule and then amends the staff proposal and refers it to the Commission, refers the proposal back to staff, or refers the proposal, as recommended by staff, to the Commission.
6. The Committee's recommendation is presented to the Commission for consideration.
7. The Commission reviews, amends, approves the proposal for publications, refers it back to the Committee, or tables the proposed amendment.
8. If the Commission approves the proposal for publication, it is transmitted to the ***Texas Register*** for publication as a "proposed" rule amendment.
9. A 30-day comment period follows initial publication which also is announced in the Department's monthly newsletter.
10. The commission may reconsider the rule anytime after the 30-day comment period. Any comments received are considered and the rule is available for adoption as "final" if no substantive changes are made. Any substantive change will result in re-publication of the proposal.

11. The rule as amended is adopted and transmitted to the ***Texas Register*** for publication as a final rule. The rule becomes effective 20 days following filing for publication.
12. The amended rule is announced through the Department's newsletter and copies are made available to credit unions.

ADMINISTRATIVE PROCEEDINGS

C. (a) Discussion, Consideration and Possible Vote to Recommend that the Credit Union Commission Take Action to Adopt Amendments, a New Section and three Repeals in 7 TAC, Part 6, Chapter 93 Concerning Administrative Proceedings.

BACKGROUND: At its March meeting, the Commission approved for publication and comment in the *Texas Register* the proposed amendments, a New Section and three Repeals to Chapter 93. No comments were received in regards to the proposed amendments.

In general, the purpose of the proposed amendments relate to four areas: (1) consistency with the Administrative Procedure Act Texas Government Code, Chapter 2001 (APA), (2) consistency with the State Office of Administrative Hearings (SOAH) procedural rules, (3) better readability and clarification, and (4) technical corrections.

RECOMMENDED ACTION: The Department requests that the Committee recommend to the Commission approve and adopt the proposed amendments.

RECOMMENDED MOTION: I move that the Committee recommend that the Commission take action to adopt the proposed amendments, a New Section and three Repeals to Chapter 93 as previously published in the *Texas Register*.

TITLE 7. BANKING AND SECURITIES
Part 6. Credit Union Department
Chapter 93. Administrative Proceedings

The Credit Union Commission (the Commission) adopt amendments to 7 TAC, Chapter 93, Sections 93.101, 93.201, 93.204, 93.205, 93.208, 93.209, 93.210, 93.211, 93.212, 93.301, 93.303, 93.401, 93.501, 93.604, and 93.605; adopts new 7 TAC Section 93.201; and adopts the repeal of existing 7 TAC Sections 93.201, 93.206, and 93.601, concerning administrative proceedings. The adopted changes affect rules contained in Subchapter A, concerning Common Terms; Subchapter B, concerning General Rules; Subchapter C, concerning Appeals of Preliminary Determinations on Applications; Subchapter D, concerning Appeals of Cease and Desist Orders and Orders of Removal; Subchapter E, concerning Appeals of Orders of Conservation; and Subchapter F, concerning Appeals of Commissioner's Final Determination to the Commission.

The Commission adopts the amendments to Sections 93.101, 93.201, 93.204, 93.205, 93.208, 93.209, 93.210, 93.211, 93.212, 93.301, 93.303, 93.401, 93.501, 93.604, and 93.605; adopts new 7 TAC Section 93.201; and adopts the repeal of existing 7 TAC Sections 93.201, 93.206, and, 93.601 without changes to the proposed text as published in the March 23, 2018 issue of the *Texas Register* (43 TexReg 1779).

In general, the purpose of the adoption is to implement changes resulting from the Commission's review of Chapter 93, under Texas Government Code, Section 2001.039, which the Commission completed in March 2018.

The Commission received no written comments on the proposed rules.

The adoption generally relates to four areas: (1) consistency with the Administrative Procedure Act (Texas Government Code, Chapter 2001), (2) consistency with the State Office of Administrative Hearings (SOAH) procedural rules, (3) better readability and clarification, and (4) technical corrections.

Regarding Subchapter A, concerning common terms, many of the adopted amendments update the defined terms and conform the rule to current practices. Specifically, in Section 93.101 definitions for "APA", "Applicant", "Person", "Respondent", and "Sanction" are adopted for use throughout the chapter. The Scope is expanded to more accurately reflect current practice and the Severability provision was changed to specify that the rules of construction that apply to interpretations of Texas statutes and codes and the definitions in the APA govern interpretations of Chapter 93.

Regarding Subchapter B, concerning general rules, many of the adopted amendments are to rename the heading of the subchapter, clarify, better organize, improve readability, and make technical changes. Several amendments better align the rules with the APA and SOAH procedural rules.

Existing Section 93.201 is adopted for repeal because it is deemed unnecessary given SOAH procedural rules. A new Section 93.201, entitled, Appeals to the Commission, Appointment of SOAH, is adopted to reflect when the Commission is required to take action on an appeal and to officially designate SOAH as the Department's finder of fact in a contested case. However, the Department specifically retains its right to determine sanction and make final decisions on any contested case. The new rule also delineates when SOAH acquires jurisdiction over a contested case and provides clarification that SOAH procedural rules control while SOAH has jurisdiction, addresses conflicts in laws, and describes other sections of the chapter.

The adopted amendments in Section 93.204 remove all language related to contested case hearings, including the section title, which will be addressed in adopted new Section 93.201. The amendments also provide that any stipulation or agreed settlement must be written and signed by the parties, dictated into the record during the course of a hearing, or incorporated in an order bearing written consent to be enforceable.

The adopted amendments in Section 93.205 remove the detailed prescription of the information that must be included in a notice of hearing and replaces it with a general statement that any action subject to this chapter is initiated by the service of such notice as is required by applicable law and SOAH procedural rules. The adopted amendments also prescribe that a respondent or applicant must enter an appearance with SOAH within 10 days of the notice of hearing being served. In addition, the adopted amendments prescribe that Default Proceedings are governed by SOAH procedural rules.

Existing Section 93.206 is adopted for repeal as it will be unnecessary given SOAH's procedural rules and the adopted amendments to Section 93.205 previously discussed.

In Section 93.208 the adopted amendments will clarify that the delegation of authority is only intended to apply to ministerial duties. Delegation of discretionary authority is not allowed unless it is expressly authorized or necessarily implied by statute.

In Section 93.209 the adopted amendments will clarify that if the compliance date for a subpoena is less than ten days after service, the compliance date must be specifically detailed in the subpoena.

The adopted amendments in Section 93.210 will clarify that parties have discovery rights as delineated in the Administrative Procedure Act.

In Section 93.211 the adopted amendments make clear that the costs of a transcript of an administrative proceeding requested by a party are paid by that party. The amendments also improve the readability of the provisions dealing with payment of costs to transmit a copy of the record to a reviewing court in the event of an appeal of a final decision or order. In addition, language that conflicted with the Administrative Procedure Act relating to the ALJ transmitting a certified copy of the record was removed.

The adopted amendments in Section 93.212 make technical changes and provide a specific reference to the Administrative Procedure Act relating to the standards that must be followed in changing a recommendation of the ALJ in lieu of delineating the standards specifically in the rule.

Regarding Subchapter C, concerning appeals of preliminary determinations on applications, the adopted amendments are to clarify and improve readability.

The adopted amendments in Section 93.301 generally provide clarification and improve the readability of the rule concerning finality of decision, request for SOAH hearing, and waiver of appeal.

In Section 93.303 the adopted amendments to subsection (a) improve the readability of the rule concerning hearings on applications.

Regarding Subchapter D, concerning appeals of cease and desist orders and orders of removal, the adopted amendment to Section 93.401, subsection (a) is to clarify that an order becomes final and "non-appealable" when the applicable statutory time for filing an appeal expires and a timely appeal has not been filed.

Regarding Subchapter E, concerning appeals of orders of conservation, the adopted amendments delete duplicative text and improve readability. In Section 93.501 the adopted amendment to subsection (a) clarifies that unless a timely appeal is filed, the commissioner's order of conservation becomes final and non-appealable upon the expiration of the appeal deadline. The adopted amendments to 93.501, subsection (b) clarify the procedure for filing an appeal, and those to subsection (e) clarify the timeframes within which to file exceptions to the PFD. The adopted changes also improve the readability of the provision related to the timeframes for filing exceptions to PFDs.

Regarding Subchapter F, concerning Appeals of Commissioner's Final Determination to the Commission, the heading of the subchapter is renamed Review and Decision by the Commission; the remaining adopted amendments clarify, make technical changes, and improve consistency with the APA.

The adopted repeal of 93.601, includes moving the language contained in the repealed rule to more appropriate locations in the Chapter in sections 93.201 and 93.602.

In Section 93.604 the adopted amendments delete subsection (b) in its entirety, as it is unnecessary, and subsections are appropriately renumbered. The procedures and deadlines in the APA govern motions for rehearing.

The adopted amendments to Section 93.605 subsection (b) clarify that a person must exhaust all administrative remedies before seeking judicial review of a final decision or order. The amendments also delete the language related to the evidence rule the Courts would employ in reviewing a final decision or order.

The amendments, new section, and the three repeals are adopted under the authority granted by the Texas Legislature to the Commission pursuant to Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Title 2 Chapter 15 and Title 3, Subchapter D of the Texas Finance Code.

The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Chapter 15 and Chapters 121 – 149.

The agency certifies that legal counsel has reviewed the adoption and found it to be a valid exercise of the agency's legal authority.

§93.101. Scope; Definitions; Severability.

(a) This chapter provides for an efficient and uniform system of practice and procedure before the Department. This chapter governs the institution, conduct, and determination of adjudicative proceedings, required or permitted by law, whether instituted by the Department or by filing of an application, notice, or any other pleading. This chapter does not enlarge, diminish, modify, or otherwise alter the jurisdiction, powers, or authority of the Department, or the substantive rights or any person or agency. All contested case hearings will be conducted by the State Office of Administrative Hearings and will be governed by Title 1, Chapter 155 of the Texas Administrative Code and this chapter.

(b) The following words and terms, when used in this chapter, shall have the following meanings, unless the context clearly indicates otherwise.

(1) ADR -- alternative dispute resolution.

(2) ALJ -- administrative law judge employed by the State Office of Administrative Hearings.

(3) APA -- The Administrative Procedure Act (Texas Government Code, Chapter 2001).

(4) Applicant -- Any person seeking a certificate, charter, or approval of an application from the Department.

(5) Contested case or proceeding -- a proceeding in which the legal rights, duties, or privileges of a party are to be determined by the commissioner or the Commission after an opportunity for adjudicative hearing. A contested case at the Department commences upon the filing of a proper and timely request for hearing.

(6) Party -- A person admitted to participate in a contested case.

(7) Person -- Any individual, credit union, or other legal entity, including a state agency or government subdivision.

(8) PFD -- a proposal for decision issued by an ALJ.

(9) Respondent -- A credit union or other person against whom a sanction is directed by the Department.

(10) Sanction -- Any administrative penalty, disciplinary action, or enforcement action imposed by the Department.

(11) SOAH -- the State Office of Administrative Hearings.

(12) TAC -- Texas Administrative Code.

(c) The same rules of construction that apply to interpretations of Texas statutes and codes, the definitions in the APA Section 2001.003, and the definitions in subsection (b) of this section govern the interpretation of this chapter. If any section of this chapter is found to conflict with an applicable and controlling provision of other state or federal law, the section involved shall be void to the extent of the conflict without affecting the validity of any other provision of this chapter.

§93.201. Appeals to the Commission, Appointment of SOAH.

(a) The Department appoints SOAH to be its finder of fact in contested cases. The Department does not delegate to the ALJ and retains for itself the right to determine the sanctions and make the final decision in any contested case.

(b) Contested cases shall be conducted in accordance with the APA and SOAH's procedural rules (1 TAC Chapter 155) and shall be heard by an ALJ assigned by SOAH. When the Department submits a request to docket a case, SOAH acquires jurisdiction over a contested case

and retains jurisdiction until SOAH issues a proposal for decision (PFD) or final amendments or corrections, if any, to the PFD, or upon SOAH's remand of the case to the Department. In case of conflict with the Commission's rules, SOAH's rules control while SOAH has jurisdiction.

§93.204. Informal Disposition.

At any time during the proceedings, [the commissioner may make an] informal disposition may be made of any contested case by stipulation of the parties, agreed settlement, consent order, or default. No stipulation or agreed settlement between the parties shall be enforced unless it shall have been reduced to writing and signed by parties and made part of the record, or unless it shall have been dictated into the record by them during the course of a hearing or incorporated in an order bearing their written consent.

§93.205. Notice of Hearing.

(a) An action subject to this chapter is initiated by the service of such notices as are required to be served under the substantive law governing the particular proceeding. Unless other law authorizing a different notice period is applicable to the particular proceeding, all hearings in contested cases must be preceded by at least 10 day notice, as required by the APA §2001.051. Credit unions shall keep the Department informed as to their correct current mailing address and may be served with initial process by regular, certified, or registered mail to the address furnished the agency.
(b) If a credit union does not file a written answer or other written responsive pleading to the notice required by subsection (a) of this section on or before the 10th day after the date on which the credit union was served with the notice, or if the credit union fails to attend the hearing, the Commissioner may dispose of the case without hearing and grant the relief set forth in the notice.
(c) The Respondent or Applicant shall enter an appearance, with a copy to the Department, within 10 days of the date on which the notice of hearing was served on the person. For purposes of this section, entering an appearance means the filing of a written answer or other responsive pleading with SOAH.
(d) SOAH rules relating to Default Proceedings (1 TAC §155.501) and Dismissal Proceedings (1 TAC §155.501) apply when a Respondent or Applicant fails to appear on the day and time set for the contested case hearing. In that case, the Department may move either for dismissal of the case from SOAH's docket or for the issuance of a default PFD by the ALJ or remand to the Department for entry of default by the Commission or the Commissioner, as appropriate. If the ALJ issues an order dismissing the case from SOAH docket or issues a default PFD, or a remand for entry of default by the Commission, the factual allegations against the Respondent at SOAH are admitted and the Commissioner or the Commission, as appropriate, shall enter a default order against the Respondent. Any claims raised or applications for approval submitted by an Applicant will be deemed denied.

§93.208. Delegation of Authority.

Unless otherwise provided by law, the commission or the commissioner may delegate to a representative any ministerial duly imposed on the commission or the commissioner, respectively.

The provisions of any rule referring to the commission or the commissioner shall be construed to also apply to the duly authorized representative of the commission or the commissioner.

§93.209. Subpoenas.

(a) Any party desiring the issuance of a subpoena to compel the appearance of a witness or the production of documents at any hearing shall file a written request with the commissioner setting forth the name and address of the witness, time and place of appearance, and any documents or tangible things sought to be produced. Each request shall contain a statement of the reasons why the subpoena should be issued.

(b) Upon a finding that a party has shown good cause for the issuance of the subpoena, the commissioner shall issue the subpoena as prescribed by Government Code §2001.089. The party requesting the subpoena shall be responsible for the payment of any fees or expenses as set out in Government Code §2001.103.

(c) Within ten days after service of the subpoena or, if the compliance date is less than ten days after service, before the compliance date stated in the subpoena, the person to whom the subpoena is directed shall serve upon the commissioner, the ALJ, and the attorney or party designated in the subpoena, any written objection to the subpoena, appearance or to the inspection or copying of any or all of the designated material. The party serving the subpoena shall have five days to file a written response to the objection. No oral argument shall be heard on the objection unless the commissioner or ALJ directs.

§93.210. Discovery; Protective Orders; Motions To Compel.

Except as modified by SOAH, parties have the discovery rights set out in the Administrative Procedure Act. If a party or witness is asked to produce information that is exempt or privileged under the Texas Rules of Civil Procedure or the Texas Rules of Civil Evidence, the party, in addition to filing a written objection under §93.209(c) of this title (relating to Subpoenas), may make a motion with the ALJ for a protective order. The objecting party must request an *in camera* inspection as set out in 1 TAC §155.251(c)(7). The ALJ shall rule on all objections and motions under this section.

§93.211. Administrative Record.

(a) The cost of a transcript of an administrative proceeding requested by a party is paid by the party requesting the transcript. If the ALJ *sua sponte* orders that an administrative hearing be recorded by a court reporter, the cost of a transcript of the administrative proceeding is split equally between the parties.

(b) In the event a final decision or final order is appealed to district court and the Department is required to transmit to the reviewing court a copy of the administrative record of the administrative proceeding, or any part thereof, the appealing party shall pay all of the costs of the preparation of any original or certified copy of the administrative record of the administrative proceeding, including the preparation of any transcript of the hearing that is required to be sent to the reviewing court. If more than one party appeals the decision, the cost of the preparation of the administrative record shall be divided equally among the appealing parties or as agreed by the parties.

§93.212. Proposal for Decision.

(a) Following a contested case hearing, the ALJ shall review the evidence and testimony and prepare a PFD which shall include findings of fact and conclusions of law, and, if appropriate, may include recommendations for an appropriate decision or sanction.
(b) The ALJ shall serve copies of the PFD on all parties of record within 30 days after conclusion of the hearing. The parties may submit exceptions to the PFD and replies to the exceptions. Exceptions, replies to exceptions, and related briefs must be submitted to the ALJ and to the commission through the department and, unless otherwise indicated, must be filed within deadlines established by the ALJ. The ALJ may amend the PFD in response to the exceptions, replies, or briefs submitted. If the ALJ makes substantive revisions, the ALJ shall circulate the amended PFD to the parties for additional exceptions and briefs before submitting the PFD to the Department.
(c) The ALJ shall submit the PFD together with all materials listed in the APA §2001.060, to the Department. No additional briefs may be submitted after the case is under submission to the commission for decision unless requested by the commission. The APA §2001.058 provides the standards the commission must follow if its decision differs from the PFD.
(d) The commission shall make a decision regarding the PFD within 30 days of the date of receipt of the PFD.

§93.301. Finality of Decision; Request for SOAH Hearing; Waiver of Appeal.

(a) The commissioner shall issue a preliminary decision on all applications. Unless a party files a timely written appeal to the commission, the preliminary decision of the commissioner will become final and non-appealable when the time for appeal set out in Finance Code §122.007 or §122.011 expires. If a party submits a written waiver of its right to appeal, the preliminary commissioner's decision becomes final and non-appealable on receipt of the waiver. If a party files a timely appeal, the commissioner's preliminary decision is automatically withdrawn and the Department will refer the matter to SOAH. The commissioner may, at the commissioner's sole discretion, refer any matter to SOAH for hearing prior to and in lieu of entering a preliminary decision.
(b) Notwithstanding subsection (a) of this section, if an application is approved without modification, and no protest or comment was received during the notice period, the commissioner may determine that the preliminary decision of approval should become final immediately.

§93.303. Hearings on Applications.

(a) If ADR is not used or if it fails to resolve the controversy, an applicant or other person aggrieved by the commissioner's preliminary determination may appeal to the commission. In such a case, the commissioner shall refer the matter to SOAH and will furnish to the ALJ all statutes, rules and policies upon which the preliminary decision, if any, was based.
In preparing a PFD, the ALJ shall consider this information along with the testimony and documentary evidence presented at the hearing.
(b) Burden of Proof for Unprotested Applications. The applicant must prove each of the statutory and regulatory requirements for approval by a preponderance of the evidence.
(c) Burden of Proof for Protested Applications. The applicant must prove each of the statutory and regulatory requirements for approval by a preponderance of the evidence. In cases in which field of membership is at issue, the protestant must establish by a preponderance of the evidence that

overlapping fields of membership will unreasonably harm the protestant. For the purposes of this section, to constitute "unreasonable harm" an overlap must threaten the protestant's welfare and stability or its financial viability to such an extent that it would adversely impact its safety and soundness as a credit union.

§93.401. Appeals Of Cease And Desist Orders And Orders Of Removal.

(a) Unless the board of directors or person affected by the order files a timely written appeal, the commissioner's cease and desist order or order of removal becomes final and non-appealable when the applicable statutory time for appeal expires.
(b) If a timely request for appeal is filed, the commissioner shall forward the matter to SOAH to set a hearing.
(c) The hearing on a cease and desist order or order of removal is closed to the public. The orders, correspondence, and records relating thereto, are confidential and cannot be revealed to the public. Parties with access to confidential information during the contested case must sign a confidentiality agreement as provided in §91.8000(f) of this title (relating to Discovery of Confidential Information).
(d) At the hearing, the commissioner must establish a prima facie case that the statutory or regulatory violations or the unsafe or unsound practices justify the cease and desist order or order of removal.

§93.501. Appeals of Orders of Conservation.

(a) Unless the credit union's former board of directors files a timely written appeal, the commissioner's order of conservation becomes final and non-appealable when the statutory time for appeal expires.
(b) If a timely request for hearing is filed with the appeal, the commissioner shall forward the matter to SOAH to set a hearing.
(c) The credit union's former board of directors has the burden to prove by a preponderance of the evidence that the board should regain control of the credit union.
(d) The SOAH hearing on an order of conservation is closed to the public. All orders and correspondence relating thereto are confidential and may not be revealed to the public. Parties with access to confidential information during the contested case must sign a confidentiality agreement as provided in §91.8000(f) of this title (relating to Discovery of Confidential Information).
(e) Parties must file exceptions, if any, to the PFD within five days after the date of service of the PFD. Replies to exceptions shall be filed within three days of the date of service of the exceptions.
(f) The Commission shall meet to consider the PFD no later than 45 days after the Department receives the PFD from SOAH.

§93.604. Motion for Rehearing.

The procedures and deadlines of APA govern the filing of a motion for rehearing with the Commission.

§93.605. Final Decisions and Appeals.

(a) The Commission's decision is final and non-appealable:

(1) if a motion for rehearing is not filed on time, upon the expiration of the period for filing a motion for rehearing; or

(2) if a motion for rehearing is filed on time, on the date the order overruling the motion for rehearing is rendered; or the motion is overruled by operation of law.

(b) A party to a contested case who has exhausted all administrative remedies and who is aggrieved by a final decision of the Commission in a contested case may seek judicial review of the decision.

MANDATORY RULE REVIEW

C. (b) Discussion, Consideration, and Possible Vote to Recommend that the Credit Union Commission Take Action on the Completed Rule Review of 7 TAC, Part 6, Chapter 91, Subchapters G Concerning Lending Powers.

BACKGROUND: Section 2001.039, Government Code, requires that a state agency review and consider for readoption each rule not later than the fourth anniversary of the date on which the rule took effect and every four years after that date. As provided in the noted section, the reviews must include, at a minimum, an assessment by the agency as to whether the reason for adopting the rule continues to exist. At its July 2016 meeting, the Commission approved a plan which establishes a date for the required review for each of the affected rules. In accordance with that plan, staff has reviewed 7 TAC, Part 6, Chapter 91, Subchapter G (Lending Powers) and believes certain revisions are appropriate and necessary. Amendments to the noted chapter are being separately presented for proposal.

Notice of the review and a request for comments on the rules in this chapter was published in the April 20, 2018 issue of the *Texas Register*. No comments were received regarding the review. The Department believes that the reasons for adopting the noted rules continue to exist.

RECOMMENDED ACTION: The Department requests that the Committee recommend to the Commission approve and adopt the rule review as the reasons for these rules continue to exist.

RECOMMENDED MOTION: I move that the Committee recommend that the Commission find that the reasons for adopting 7 TAC Chapter 91, Subchapter G (Lending Powers) continue to exist and that Commission readopt the rules in this chapter.

TITLE 7. BANKING AND SECURITIES
Part 6. Credit Union Department
Chapter 91, Subchapter G, Lending Powers

The Credit Union Commission (the Commission) has completed its review of Chapter 91, Subchapter G (Lending Powers), consisting of Sections 91.701, and 91.703—91.720. The Commission proposes to readopt these rules.

The rules were reviewed as a result of the Department's general four-year rule review under Texas Government Code Section 2001.039.

Notice of the review of 7 TAC, Part 6, Chapter 91, Subchapter G was published in the *Texas Register* as required on April 29, 2018, 43 TexReg 2455. The Department received no comments on the notice of intention to review.

As a result of the internal review by the Department, the Commission has determined that the reasons for initially adopting the rules continue to exist, and that most of them should be readopted, but that certain revisions are appropriate and necessary. The Commission is concurrently proposing amendments to Chapter 91, Subchapter G, as published elsewhere in this issue of the *Texas Register*. Subject to the concurrently proposed amendments to Chapter 91, Subchapter G, the Commission finds that the reasons for initially adopting these rules continue to exist, and readopts Chapter 91, Subchapter G in accordance with the requirements of Texas Government Code, Section 2001.039. This concludes the review of 7 TAC, Part 6, Chapter 91, Subchapter G.

The Department hereby certifies that the rules have been reviewed by legal counsel and found to be with the agency's legal authority to readopt.

Subchapter G. Lending Powers

§91.701. Lending Powers.

(a) Authorization. A credit union may originate, invest in, sell, purchase, service, or participate in loans or otherwise extend credit in accordance with the Act, these Rules, and other applicable law.

(b) Written Policies. Before engaging in any lending activity, each credit union shall establish written lending policies that set prudent credit underwriting and documentation standards for each specific type of lending activity. The lending policies shall contain a general outline of the manner in which loans are made, serviced, and collected. In addition the policies must:

(1) Be consistent with safe and sound credit union practices;

(2) Be appropriate to the size and financial condition of the credit union and the nature and scope of its operations;

(3) Be compatible with the size and expertise of the credit union's lending staff;

(4) Be compliant with all related laws and regulations;

(5) Be reviewed and approved by the credit union's board of directors at inception and annually, thereafter;

(6) Address loan portfolio diversification standards to avoid undue concentrations of risk;

(7) Address loan documentation and underwriting standards that are clear and measurable;

(8) Address loan administration procedures for monitoring the loss exposure from the loan portfolio;

(9) Address loan pricing guidelines to ensure that the rate of return is consistent with the risk from the lending activity; and

(10) State the lending authority delegated to any individuals or committees by the board of directors.

(c) Loan Documentation. The lending policies shall include loan documentation practices that:

(1) Enable the credit union to make an informed lending decision and to assess risk, as necessary, on an ongoing basis;

(2) Identify the purpose of a loan and the source of repayment, and assess the ability of the borrower to repay the indebtedness in a timely manner; and

(3) Ensure that any claim against a member is legally enforceable.

(d) Credit Underwriting. A credit union shall establish and maintain prudent credit underwriting practices that:

(1) Are commensurate with the types of loans the credit union will make and consider the terms and conditions under which they will be made;

(2) Consider the nature of the markets in which loans will be made;

(3) Provide for consideration of the member's overall financial condition and resources, the financial responsibility of any guarantor, the nature and value of any underlying collateral, and the member's character and willingness to repay as agreed;

(4) Take adequate account of concentration of credit risk; and

(5) Are appropriate to the size of the credit union and the nature and scope of its activities.

(e) Loan Maturity Limit. Except when a higher maturity date is provided for elsewhere in this chapter, the maturity of any loan or extension of credit to a member may not exceed 15 years.

Minimum payments, on a line of credit balance must be sufficient to amortize the outstanding balance over a reasonable period of time and not cause negative amortization.

(f) Liquidity. In addition to establishing controls for credit risks, credit unions shall establish procedures and guidelines to monitor and limit the total volume of loans outstanding, to ensure adequate liquidity. In setting such guidelines, the credit union shall consider various factors such as credit demand, the volatility of shares and deposits, and availability of alternative funding sources.

(g) Waivers. The commissioner in the exercise of discretion may grant a waiver in writing of any lending requirement described in this chapter. A decision to deny a waiver, however, is not subject to appeal. A waiver request must contain the following:

(1) The requirement to be waived, the higher limit or the ratio sought;

(2) An explanation of the need for the waiver or to raise the limit or ratio; and

(3) Documentation supporting the credit union's ability to manage the additional risk from this activity.

§91.703. Interest Rates.

(a) Loans made by each credit union shall bear interest at a rate or rates as may be determined by the credit union's board of directors. A board may delegate all or part of its power to determine the interest rates on any lending transactions. The board may also authorize a refund of interest on loans under the conditions it may prescribe.

(b) A loan may provide for variable interest rates, so long as the factor or index governing the extent of the variation is not under the control of the credit union and can be readily ascertained from sources available to the public or any other index approved in writing by the commissioner which is not available to the public.

§91.704. Real Estate Lending.

(a) Definitions. For the purposes of this section, the following words and terms shall have the following meanings, unless the context clearly indicates otherwise.

(1) First lien means any mortgage that takes priority over any other lien or encumbrance on the same property and that must be satisfied before other liens or encumbrances may share in proceeds from the property's sale.

(2) Home loan means a loan that is:

(A) made to one or more individuals for personal, family, or household purposes; and

(B) secured in whole or part by:

(i) a manufactured home, as defined by Finance Code <*>347.002, used or to be used as the borrower's principal residence; or

(ii) real property improved by a dwelling designed for occupancy by four or fewer families and used or to be used as the borrower's principal residence.

(3) Improved residential real estate means residential real estate containing offsite improvements, such as access to streets, curbs, and utility connections, sufficient to make the property ready for residential construction, and real estate in the process of being improved by a building.

(4) Other acceptable collateral means any collateral in which the credit union has a perfected security interest, that has a quantifiable value, and is accepted by the credit union in accordance with safe and sound lending practices.

(5) Owner-occupied means that the owner of the underlying real property occupies a dwelling unit of the real property as a principal residence.

(6) Readily marketable collateral means insured deposits, financial instruments, and bullion in which the credit union has a perfected interest. Financial instruments and bullion must be saleable under ordinary circumstances with reasonable promptness at a fair market value determined by quotations based on actual transactions, on an auction or similarly available daily bid and ask price market.

(b) Written Policies. Before engaging in any real estate lending, a credit union shall adopt and maintain written policies that are appropriate for the size of the credit union and the nature and scope of its operation. When formulating the real estate lending policy, the credit union should consider both internal and external factors, such as its size and condition, expertise of its lending staff, avoidance of undue concentrations of risk, compliance with all real estate laws and rules, and general market conditions. Each policy must be consistent with safe and sound lending practices and establish appropriate limits and standards for extensions of credit that are secured by liens on or interests in real estate, or that are made for the purpose of financing permanent improvements to real estate. The policies shall, in addition to the general requirements of §91.701(b) of this title (relating to Lending Powers), address the following, as applicable:

(1) Title insurance;

(2) Escrow administration;

(3) Loan payoffs;

(4) Collection and foreclosure; and

(5) Servicing and participation agreements.

(c) Loan to Value Limitations.

(1) The board of directors shall establish its own internal loan-to-value limits for real estate loans based on type of loan. These internal limits, however, shall not exceed the following regulatory limits:

(A) Unimproved land held for investment/speculation--Loan to value limit 60%

(B) Construction and Development: commercial, multifamily, and other nonresidential--Loan to value limit 75%

(C) Interim Construction: owner-occupied residential real estate--Loan to value limit 90%

(D) Owner occupied residential real estate (other than home equity)--Loan to value limit 95%

(E) Other residential real estate such as a second or vacation home--Loan to value limit 90%

(F) Home equity--Loan to value limit 80%

(G) All Other--Loan to value limit 80%

(2) The regulatory loan-to-value limits should be applied to the underlying property that collateralizes the loan. In determining the loan to-value ratio, a credit union shall include the aggregate amount of all sums borrowed, including the 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.

(d) Maximum Maturities. Notwithstanding the general 15-year maturity limit on lending transactions to members, credit unions engaged in real estate lending are expected to have loan policies that establish prudent standards for loan structure including tenor and amortization that are within the risk parameters approved by the board of directors and consistent with the following regulatory limits:

(1) Improved residential real estate loans (principal residence, first lien)--40 years

(2) Improved residential real estate loans (secondary residence, first lien)--30 years

(3) Improved residential real estate loans (investment property, first lien)--20 years
(4) Interim construction loans--18 months
(5) Manufactured home (first lien)--20 years
(6) Home equity loans--20 years (second lien)--30 years (first lien)
(7) Home improvement loans--20 years
(8) A loan secured 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 or any agency of the Federal Government, may be made for the maturity specified in the law, regulations or program under which the insurance, guarantee or commitment is provided

(e) Mortgage Fraud Notice. A credit union must provide to each applicant for a home loan a written notice at closing. The notice must be provided on a separate document, be in at least 14-point type, and have the following or substantially similar language: "Warning: Intentionally or knowingly making a materially false or misleading written statement to obtain property or credit, including a mortgage loan, is a violation of §32.32, Texas Penal Code, and, depending on the amount of the loan or value of the property, is punishable by imprisonment for a term of 2 years to 99 years and a fine not to exceed $10,000. "I/we, the undersigned home loan applicant(s), represent that I/we have received, read, and understand this notice of penalties for making a materially false or misleading written statement to obtain a home loan."I/we represent that all statements and representations contained in my/our written home loan application, including statements or representations regarding my/our identity, employment, annual income, and intent to occupy the residential real property secured by the home loan, are true and correct as of the date of loan closing." On receipt of the notice, the applicant shall verify the information and execute the notice. A credit union must keep the signed notice on file with the records required under §91.701 of this title.

(f) Excluded Transactions. It is recognized that there are a number of lending situations in which other factors significantly outweigh the need to apply the regulatory loan-to-value limits. As a result, an exception to the loan-to-value limits is permissible for the following loan categories:

(1) Loans that are covered through appropriate credit enhancements in the form of readily marketable collateral or other acceptable collateral.

(2) Loans guaranteed or insured by the U.S. government or its agencies, provided that the amount of the guaranty or insurance is at least equal to the portion of the loan that exceeds the regulatory loan-to-value limit.

(3) Loans guaranteed, insured, or otherwise backed by the full faith and credit of the state, a municipality, a county government, or an agency thereof, provided that the amount of the guaranty, insurance, or assurance is at least equal to the portion of the loan that exceeds the regulatory loan-to-value limit.

(4) Loans that are to be sold promptly after origination, without recourse, to a financially responsible third party.

(5) Loans that are renewed, refinanced, or restructured without the advancement of new funds or an increase in the line of credit (except for reasonable closing costs) where consistent with safe and sound credit union practices and part of a clearly defined and well-documented program to achieve orderly liquidation of the debt, reduce risk of loss, or maximize recovery on the loan.

(6) Loans that facilitate the sale of real estate acquired by the credit union in the ordinary course of collecting a debt previously contracted in good faith.

(g) Loans to 100% of Value. A credit union may make a loan in an amount up to 100% of the value of real property security if that part of the loan that exceeds the regulatory loan-to-value limit is guaranteed or insured by a private corporation, organization, or other entity. The board of directors must ensure that the credit union exercises appropriate due diligence to ensure that any

contained in Part 722 of the National Credit Union Administration Rules and Regulations.

(b) Loans Over $250,000. For real estate loans in which the amount of the loan or extension of credit exceeds $250,000, the credit union shall obtain a professional appraisal report by a state certified or licensed appraiser. The appraisal report shall be in writing and conform to generally accepted appraisal standards as evidenced by the Uniform Standards of Professional Appraisal Practice promulgated by the Appraisal Standards Board of the Appraisal Foundation, in Washington, D.C.

(c) Loans $250,000 or Less. For a real estate loans with an amount of the loan or extension of credit of $250,000 or less, the services of a state certified or licensed appraiser is not necessary; however, the credit union must obtain an appropriate evaluation of real property collateral that is supported by a written estimate of market value either performed by a qualified individual who

(3) Independent Review. Periodic independent reviews should be conducted by a person who is both qualified to conduct such a review and independent of the function being reviewed. The review should provide an objective assessment of the overall commercial loan portfolio quality and verify the accuracy of ratings and the operational effectiveness of the credit union's risk management processes. A credit union is not required to hire an outside third party to conduct this independent review, if it can be done in-house by a competent person that is considered unconnected to the function being reviewed.

(e) Collateral and Security for Commercial Loans.

(1) Collateral. A commercial loan must be secured by collateral commensurate with the level of risk associated with the size and type of the commercial loan. The collateral must be sufficient to ensure the credit union is protected by a prudent loan-to-value ratio for collateral along with appropriate risk sharing with the borrower and principal(s). A credit union making an unsecured commercial loan must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk of making an unsecured loan.

(2) Personal Guarantees. A credit union that does not require the full and unconditional personal guarantee from all principals of the borrower who have a controlling interest, as defined by subsection (a)(3) of this section, in the borrower must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.

(f) Construction and Development Loans.

(1) Terms. In this subsection:

(A) "construction or development loan" means any financing arrangement to enable the borrower to acquire property or rights to property, including land or structures, with the intent to construct or renovate an income producing property, such as residential housing for rental or sale, or a commercial building, that may be used for commercial, agricultural, industrial, or other similar purposes. It also means a financing arrangement for the construction, major expansion or renovation of the property types referenced in this subsection. The collateral valuation for securing a construction or development loan depends on the satisfactory completion of the proposed construction or renovation where the loan proceeds are disbursed in increments as the work is completed. A loan to finance maintenance, repairs, or other improvements to an existing income-producing property that does not change the property's use or does not materially impact the property is not a construction or development loan.

(B) "cost to complete" means the sum of all qualifying costs necessary to complete a construction project and documented in an approved construction budget. Qualifying costs generally include on- or off-site improvements; building construction; other reasonable and customary costs paid to construct or improve a project, including a general contractor's fees; other expenses normally included in a construction contract such as bonding and contractor insurance; the value of the land, determined as the sum of the cost of any improvements to the land and the lesser of appraised market value or purchase price; interest as provided by this subparagraph; project costs as provided by this subparagraph; a contingency account to fund unanticipated overruns; and other development costs such as fees and related pre-development expenses. Interest expense is a qualifying cost only to the extent it is included in the construction budget and is calculated based on the projected changes in the loan balance up to the expected "as-complete" date for owner-occupied non-income-producing commercial real property or the "as stabilized" date for income-producing real estate. Project costs for related parties, such as developer fees, leasing expenses, brokerage commissions and management fees, are included in qualifying costs only if reasonable in comparison to the cost of similar services from a third party. Qualifying costs exclude interest or preferred returns payable to equity partners or subordinated debt holders, the developer's general corporate overhead, and selling costs to be funded out of sales proceeds such as brokerage commissions and other closing costs.

(C) "prospective market value" means the market value opinion determined by an independent appraiser in compliance with the relevant standards set forth in the Uniform Standards of Professional Appraisal Practice. Prospective value opinions are intended to reflect the current expectations and perceptions of market participants, based on available data. Two (2) prospective value opinions may be required to reflect the time frame during which development, construction, or occupancy occur. The prospective market value "as-completed" reflects the real property's market value as of the time that development is to be completed. The prospective market value "as-stabilized" reflects the real property's market value as of the time the real property is projected to achieve stabilized occupancy. For an income producing property, stabilized occupancy is the occupancy level that a property is expected to achieve after the real property is exposed to the market for lease over a reasonable period of time and at comparable terms and conditions to other similar real properties.

(2) Policies. A credit union that elects to make a construction or development loan must ensure that its commercial loan policies under subsection (c) of this section meets the following conditions:

(A) qualified personnel representing the interest of the credit union must conduct a review and approval of any line item construction budget prior to closing the loan;

(B) a requisition and loan disbursement process approved by the credit union is established;

(C) release or disbursement of loan funds occurs only after on-site inspections which are documented in a written report by qualified personnel who represents the interest of the credit union and certifies that the work requisitioned for payment has been satisfactorily completed, and the remaining funds available to be disbursed from the construction and development loan is sufficient to complete the project; and

(D) each loan disbursement is subject to confirmation that no intervening liens have been filed.

(3) Establishing Collateral Values. The current collateral value must be established by prudent and accepted commercial loan practices and comply with all regulatory requirements. The collateral value depends on the satisfactory completion of the proposed construction or renovation where the loan proceeds are disbursed in increments as the work is completed and is the lesser of the project's cost to complete or its prospective market value.

(4) Controls and Processes for Loan Advances. A credit union that elects to make a construction and development loan must have effective commercial loan control procedures in place to ensure sound loan advances and that liens are paid and released in a timely manner. Effective controls should include segregation of duties, delegation of duties to appropriate qualified personnel, and dual approval of loan disbursements.

(g) Commercial Loan Prohibitions.

(1) Ineligible borrowers. A credit union may not grant a commercial loan to the following:

(A) any senior management employee directly or indirectly involved in the credit union's commercial loan underwriting, servicing, and collection process, and any of their immediate family members;

(B) any person meeting the requirements of subsection (i) of this section concerning aggregations and attribution for commercial loans, with respect to persons identified in subparagraph (A) of this paragraph; or

(C) any director, unless the credit union's board of directors approves granting the loan and the borrowing director was recused from the board's decision making process.

(2) Equity Agreements and Joint Ventures. A credit union may not grant a commercial loan if any additional income received by the credit union or its senior management employees is tied to the profit or sale of any business or commercial endeavor that benefits from the proceeds

of the loan.

(3) Fees. No director, committee member, volunteer official, or senior management employee of a credit union, or immediate family member of such director, committee member, volunteer official, or senior management employee, may receive, directly or indirectly, any commission, fee, or other compensation in connection with any commercial loan made by the credit union. Employees, other than senior management, may be partially compensated on a commission or performance based incentive, provided the compensation is governed by a written policy and internal controls established by the board of directors. The board must review the policies and controls at least annually to ensure that such compensation is not excessive or expose the credit union to inappropriate risks that could lead to material financial loss. Loan origination employees are prohibited from receiving, in connection with any commercial loan made by the credit union, any compensation from any source other than the credit union. For the purposes of this paragraph, compensation includes non-monetary items and anything reasonably regarded as pecuniary gain or pecuniary advantage, including a benefit to any other person in whose welfare the beneficiary has a direct and substantial interest, but compensation does not include nonmonetary items of nominal value.

(h) Aggregate Member Business Loan Limit.

(1) Limits. The aggregate limit on a credit union's net member business loan balances is the lesser of 1.75 times the actual net worth of the credit union, or 1.75 times the minimum net worth required under 12 U.S.C. Section 1790d(c)(1)(A). For purposes of this calculation, member business loan means any commercial loan, except that the following commercial loans are not member business loans and are not counted toward the aggregate limit on member business loans:

(A) any loan in which a federal or state agency (or its political subdivision) fully insures repayment, fully guarantees repayment, or provides an advance commitment to purchase the loan in full; and

(B) any non-member commercial loan or non-member participation interest in a commercial loan made by another lender, provided the credit union acquired the non-member loans or participation interest in compliance with applicable laws and the credit union is not, in conjunction with one or more other credit unions, trading member business loans to circumvent the aggregate limit under this subsection.

(2) Exceptions. Any loan secured by a lien on a 1 to 4 family residential property that is not a member's primary residence, any loan secured by a lien on a vehicle manufactured for household use that will be used for commercial, corporate, or other business investment property or venture, and any other loan for an agricultural purpose are not commercial loans (if the outstanding aggregate net member business loan balance is $50,000 or greater), and must be counted toward the aggregate limit on a credit union's member business loans under this subsection.

(3) Exemption. A credit union that has a federal low-income designation, or participates in the federal Community Development Financial Institution program, or was chartered for the purpose of making member business loans, or which as of the date of the Credit Union Membership Access Act of 1998 had a history of primarily making commercial loans, is exempt from compliance with the aggregate member business loan limits in paragraph (1) of this subsection.

(4) Method of Calculation for Net Member Business Loan Balance. For the purposes of NCUA form 5300 reporting (call report), a credit union's net member business loan balance is determined by calculating the sum of the outstanding loan balance plus any unfunded commitments and reducing that sum by any portion of the loan that is: secured by shares in the credit union, by shares or deposits in other financial institutions, or by a lien on a borrower's primary residence; insured or guaranteed by any agency of the federal government, a state, or any political subdivision of a state; or subject to an advance commitment to purchase by any agency

of the federal government, a state, or any political subdivision of a state; or sold as a participation interest without recourse and qualifying for true sales accounting under generally accepted accounting principles.

(i) Aggregation and Attribution for Commercial Loans.

(1) General Rule. A commercial loan or extension of credit to one borrower is attributed to another person, and each person will be considered a borrower, when:

(A) the proceeds of the commercial loan or extension of credit are to be used for the direct benefit of the other person, to the extent of the proceeds so used, as provided by paragraph (2) of this subsection;

(B) a common enterprise is deemed to exist between the persons as persons as provided by paragraph (3) of this subsection; or

(C) the expected source of repayment for each commercial loan or extension of credit is the same for each person as provided by paragraph (3) of this subsection.

(2) Direct Benefit. The proceeds of a commercial loan or extension of credit to a borrower is considered used for the direct benefit of another person and attributed to the other person when the proceeds, or assets purchased with the proceeds, are transferred in any manner to or for the benefit of the other person, other than in a bona fide arm's length transaction where the proceeds are used to acquire property, goods, or services from such other person.

(3) Common Enterprise.

(A) Description. A common enterprise is considered to exist and commercial loans to separate borrowers will be aggregated when:

(i) the expected source of repayment for each loan or extension of credit is the same for each borrower and neither borrower has another source of income from which the loan (together with the borrower's other obligations) may be fully repaid. An employer will not be treated as a source of repayment under this subparagraph because of wages and salaries paid to an employee, unless the standards of clause (ii) of this subparagraph are met:

(ii) the loans or extension of credit are made:

(I) to borrowers who are related directly or indirectly through control as defined by subsection (a) of this section; and

(II) substantial financial interdependence exists between or among the borrowers. Substantial financial interdependence is deemed to exist when fifty (50) percent or more of one borrower's gross receipts or gross expenditures (on an annual basis) are derived from transactions with the other borrower. Gross receipts and expenditures include gross revenues/expenses, intercompany loans, dividends, capital contributions, and other similar receipts or payments;

(iii) separate persons borrow from a credit union to acquire a business of enterprise of which those borrowers will own more than fifty (50) percent of the voting securities of voting interest, in which case a common enterprise is deemed to exist between the borrowers for purposes of combining the acquisition loans; or

(iv) the Department determines, based upon an evaluation of the facts and circumstances of particular transactions, that a common enterprise exists.

(B) Commercial Loans to Certain Entities. A commercial loan or extension of credit:

(i) to a partnership or joint venture is considered to be a commercial loan or extension of credit to each member of the partnership or joint venture. Excepted from this subdivision is a partner or member who: is not held generally liable, by the terms of the partnership or membership agreement or by applicable law, for the debts or actions of the partnership, joint venture, or association, provided those terms are valid against third parties under applicable law; and has not otherwise agreed to guarantee or be personally liable on the loan or extension of credit.

(ii) to a member of a partnership, joint venture, or association is generally not attributed to the partnership, joint venture, or associations, or to other members of the partnership, joint venture, or association, except as otherwise provided by paragraphs (2) and (3) of this subsection, provided that a commercial loan or extension of credit made to a member of a partnership, joint venture or association for the purpose of purchasing an interest in the partnership, joint venture or association, is attributed to the partnership, joint venture or association.

(C) Guarantors and Accommodation Parties. The derivative obligation of a drawer, endorser, or guarantor of a commercial loan or extension of credit, including a contingent obligation to purchase collateral that secures a commercial loan, is aggregated with other direct commercial loans or extensions of credit to such a drawer, endorser, or guarantor.

(j) Commercial Loans to One Borrower Limit. The total aggregate dollar amount of commercial loans by a credit union to any borrower at one time may not exceed the greater of fifteen (15) percent of the credit union's net worth or $100,000, plus an additional ten (10) percent of the credit union's net worth if the amount that exceeds the credit union's fifteen (15) percent general limit is fully secured at all times with a perfected security interest in readily marketable collateral. 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 commercial loan in full, is excluded from this limit.

(k) Finance Code Limitation. In addition to the other limitations of this section, a credit union may not make a loan to a member or a business interest of the member if the loan would cause the aggregate amount of loans to the member and the member's business interests to exceed an amount equal to 10 percent of the credit union's total assets as provided by TEX. FIN. CODE §124.003.

(l) Commercial Loans Regarding Federal or State Guaranteed Loan Programs. A credit union may follow the loan requirements and limits of a guaranteed loan program for loans that are part of a loan 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 if that program has requirements that are less restrictive than those required by this section.

(m) Transitional Provisions.

(1) Waivers. Upon the effective date of this section, any waiver approved by the Department concerning a credit union's commercial lending activity is rendered moot, except for waivers granted for the commercial loan to one borrower limit. Borrowing relationships granted by waivers will be grandfathered however, the debt associated with those relationships may not be increased.

(2) Administrative Constraints. Limitations or other conditions imposed on a credit union in any written directive from the Department are unaffected by the adoption of this section. As of the effective date of this section, all such limitations or other conditions remain in place until such time as they are modified by the Department.

(n) Effective Date. This section takes effect on January 1, 2017.

§91.710. Overdraft Protection.

(a) Written Policy. 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 written policies and procedures adequate to address the credit, operational, and other risks associated with this type of program. The policy must:

1. 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;

2. Establish a time limit no later than 60 calendar days from the date first overdrawn to charge off the overdraft balance if the member does not repay the overdraft balance, or does not obtain an approved loan from the credit union;

3. Limit the dollar amount of overdrafts the credit union will honor per account;

4. Institute prudent practices related to suspension of overdraft protection services; and

5. Establish the fee, if any, the credit union will charge members for honoring overdrafts.

(b) Safety and Soundness Requirements. A credit union must manage the risks associated with an overdraft protection program in accordance with safe and sound credit union principles. Accordingly, a credit union must establish and maintain effective risk management and control processes over its program. Such processes include appropriate recognition, treatment, and financial reporting, in accordance with generally accepted accounting principles, of income, expenses, assets, liabilities, and all expected and unexpected losses associated with the program. A credit union also shall assess the adequacy of its internal control and risk mitigation activities in view of the nature and scope of its overdraft protection program.

(c) Communications with Member. A credit union shall carefully review its overdraft protection program to ensure that marketing and other communications concerning the program do not mislead members to believe that the program is a traditional line of credit or that payment of overdrafts is guaranteed. In addition, a credit union shall take reasonable precautions to make sure members are not misled about the correct amount of their account balance, or the costs or scope of the overdraft protection offered, and that it does not encourage irresponsible member financial behavior that potentially may increase risk to the credit union.

(d) Other Requirements. A credit union shall also comply with the overdraft service requirements contained within Part 205 of the Federal Reserve System Rules and Regulations (Regulation E).

§91.711. Purchase and Sale of Member Loans.

(a) Policies. A credit union may sell or purchase all or part of a participation interest in a member loan or pool of member loans in accordance with written policies adopted by the board of directors that address the following matters:

(1) The type of entities to which the credit union is authorized to sell participation interests in member loans;

(2) The types of member loans in which the credit union may purchase or sell a participation interest and the types of participation interests which may be purchased or sold;

(3) The underwriting standards to be applied in the purchase of participation interests in member loans;

(4) Limitations on the aggregate principal amount of participation interest in member loans that the credit union may purchase from a single entity as necessary to diversify risk, and limitations on the aggregate amount the credit union may purchase from all entities;

(5) Provision for the identification and reporting of member loans in which participation interests are sold or purchased; and

(6) Requirements for providing and securing in a timely manner adequate credit and other information needed to make an independent judgment.

(b) Purchase and Sale Agreements. The sale or purchase of a member loan or participation interest must be based on a written agreement between the parties. Agreements to purchase or sell a member loan or a participation interest shall, at a minimum:

(1) Identify the particular member loan(s) to be covered by the agreement;

(2) Provide for the transfer of credit and other borrower information on a timely and continuing basis;

(3) Provide for sharing, dividing, or assigning collateral;

(4) Identify the nature of the participation interest(s) sold or purchased;

(5) Set forth the rights and obligations of the parties and the terms and conditions of the sale; and

(6) Contain any terms necessary for the appropriate administration of the member loan and the protection of the participation interests of the credit union.

(c) Member Loan Servicing. A credit union may sell to or purchase from any participant the servicing of any member loan in which it owns a participation interest. If a party other than the credit union will be servicing the member loan(s), the credit union shall ensure that all contracts require the servicer to administer the member loan(s) in accordance with prudent industry standards, and provide for a possible change of the servicer if performance is inadequate.

(d) Definition. For purposes of this section, a member loan means a loan or extension of credit where the borrower(s) is a member of the credit union or a member of another participating credit union.

(e) Independent Credit Judgment. A credit union that purchases a participation interest in a member loan has the responsibility of conducting member loan underwriting procedures on the member loan to determine that it complies with the policies of the credit union and meets the credit union's credit standards. The credit union shall make a judgment on the creditworthiness of the borrower that is independent of the originating lender and any intermediary seller prior to the purchase of the participation interest and prior to any servicing action that alters the terms of the original agreement. This credit judgment may not be delegated to any person that is not an employee or independent agent of the credit union. A credit union that purchases a participation interest in a member loan may use information, such as appraisals or collateral inspections, furnished by the originating lender, or any intermediary seller; however, the purchasing credit union shall independently evaluate such information when exercising its independent credit judgment. The independent credit judgment shall be documented by a credit analysis that considers the underwriting, documentation, and compliance standards that would be required by a prudent lender and shall include an evaluation of the capacity and reliability of the servicer.

(f) Other Requirements. A credit union purchasing a participation interest in a member loan from a lender that is not a credit union insured by the National Credit Union Share Insurance Fund, must also comply with applicable requirements contained within Part 741 of the National Credit Union Administration Rules and Regulations.

(g) Sales with Recourse. When a member loan or participation interest is sold with recourse, it shall be considered, to the extent of the recourse, an extension of credit by the purchaser to the seller, as well as an extension of credit from the seller to the borrower(s).

§91.712. Plastic Cards.

(a) Definitions. The following words and terms, when used in this chapter, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Card Activation – process of sending new plastic cards from the issuer to the legitimate cardholder in an "inactive" mode. Once the legitimate cardholder receives the card, they must call the issuer/processor and go through a member verification process before the card is "activated".

(2) Card Security Code – a set of unique numbers encoded on the magnetic strip of plastic cards used to combat counterfeit fraud.

(3) Neural Network – a computer program that monitors usage patterns of an account and typical fraud patterns. The program analyzes activity to determine fraud risk scores to detect potentially fraudulent activity.

(4) Plastic Cards – includes credit cards, debit cards, automated teller machine (ATM) or specific network cards; and predetermined stored value and smart cards with micro-processor chips.

(b) Credit cards. A credit union may issue credit cards in accordance with the credit union's written policies, which shall include at a minimum:

(1) Credit policies to set individual limits for credit card accounts:

(2) A process for reviewing each member's payment and/or credit history periodically for the purpose of determining risk; and

(3) The credit underwriting standards for each type of card program offered.

(c) Program Review.

(1) A credit union shall review, on at least an annual basis, its plastic card program with particular emphasis on:

(A) The amount of losses caused by theft and fraud;

(B) The loss prevention measures (and their adequacy) currently employed by the credit union;

(C) The availability and possible implementation of other loss prevention measures such as card activation, card security codes, neural networks, and other evolving technology; and

(D) A cost benefit analysis of supplemental insurance coverage for theft and fraud related losses.

(2) The review shall be documented in writing, with any approved changes to the plastic card program being entered into the minutes of the board meeting.

§91.713. Indirect Lending.

(a) Indirect Lending Program. Credit unions may implement a program of indirect financing of motor vehicles and other tangible personal property. As used in this chapter, an indirect financing is the credit union's purchase of a member's retail installment contract that is originated by a seller to finance the purchase of the motor vehicle or other property.

(b) Contracts Treated as a Loan. For the purposes of this chapter, a retail installment contract purchased under this authority may be treated as a loan on the books and records of the credit union and is subject to the same limitations and restrictions imposed upon loan transactions. As with other lending, the credit union is responsible for making the final underwriting decision. The seller may initially determine whether the prospective buyer is a member or eligible for membership in the credit union, but the final determination of membership eligibility is the credit union's responsibility.

(c) Authorization. Credit unions may purchase or hold retail installment contracts when authorized by applicable law. The retail installment contract must provide for a rate or amount of time price differential that does not exceed a rate or amount authorized by applicable law.

(d) Written Policies. The board of directors shall establish, implement, and maintain prudent and reasonable written policies that are appropriate for the size and complexity of the credit union's indirect lending program. The board must also ensure that the credit union has sufficient staff with the expertise to purchase, service, and monitor the program and the contract portfolio consistent with safe and sound credit union practices. The policies must be specific and detailed enough to foster prudent and compliant credit practices.

(e) Third Party Providers. A credit union may rely on services provided by third parties to support its indirect lending activities. The board of directors must ensure that the credit union exercises appropriate due diligence before entering into third party arrangements, and maintains effective oversight and control throughout the arrangement. This oversight and control should

include a periodic review of each material seller's retail installment contract statistics to ensure compliance with credit union credit criteria and to avoid undue concentrations of risk.

(f) Subprime Indirect Lending. If a credit union conducts a program that includes subprime indirect lending, it must perform comprehensive due diligence before engaging in and during that type of activity. At a minimum, due diligence shall focus on understanding the higher levels of credit, compliance, reputation, and other risks involved, plus the likelihood that origination, servicing, collections, operating, and capital costs will increase. The strategic decision to engage in subprime indirect lending must also be supported by a sound business plan that establishes measurable financial objectives as well as limitations on growth, volume, and concentrations. For the purposes of this section, "subprime indirect lending" refers to programs that target borrowers with weakened credit histories typically characterized by payment delinquencies, previous charge-offs, judgments, or bankruptcies. Such programs may also target borrowers with questionable repayment capacity evidenced by low credit scores or high debt-burden ratios.

§91.714. Leasing.

(a) Definitions. For the purposes of this section:

(1) The term net lease means a lease under which the credit union will not, directly or indirectly, provide or be obligated to provide for:

(A) the servicing, repair or maintenance of leased property during the lease term;

(B) the purchasing of parts and accessories for the leased property, except that improvements and additions to the leased property may be leased to the lessee upon its request in accordance with the full-payout requirements of subsection (c)(2)(A) of this section;

(C) the loan of replacement or substitute property while the leased property is being serviced;

(D) the purchasing of insurance for the lessee, except where the lessee has failed to discharge a contractual obligation to purchase or maintain insurance; or

(E) the renewal of any license, registration, or filing for the property unless such action by the credit union is necessary to protect its interest as an owner or financier of the property.

(2) The term full-payout lease means a lease transaction in which any unguaranteed portion of the estimated residual value relied on by the credit union to yield the return of its full investment in the lease property, plus the estimated cost of financing the property over the term of the lease, does not exceed 25% of the original cost of the property to the lessor. In general, a lease will qualify as a full payout lease if the scheduled payments provide at least 75% of the principal and interest payments that a lessor would receive if the finance lease were structured as a market-rate loan.

(3) The term realization of investment means that a credit union that enters into a lease financing transaction must reasonably expect to realize the return of its full investment in the leased property, plus the estimated cost of financing the property over the term of the lease from:

(A) Rentals; and

(B) The estimated residual value of the property at the expiration of the term of the lease.

(b) Permissible Activities. Subject to the limitations of this section, a credit union may engage in leasing activities. These activities include becoming the legal or beneficial owner of tangible personal property or real property for the purpose of leasing such property, obtaining an assignment of a lessor's interest in a lease of such property, and incurring obligations incidental to its position as the legal or beneficial owner and lessor of the leased property.

(c) Finance Leasing.

(1) A credit union may conduct leasing activities that are functional equivalent of loans made under those leases. Such financing leases are subject to the same restrictions that would be applicable to a loan.

(2) To qualify as the functional equivalent of a loan:

(A) The lease must be a net, full-payout lease representing a non-cancelable obligation of the lessee, notwithstanding the possible early termination of the lease;

(B) The portion of the estimated residual value of the property relied upon by the lessor to satisfy the requirements of a full-payout lease must be reasonable in light of the nature of the leased property and all relevant circumstances so that realization of the lessor's full investment plus the cost of financing the property depends primarily on the creditworthiness of the lessee, and not on the residual market value of the leased property; and

(C) At the termination of the financing lease, either by expiration or default, property acquired must be liquidated or released on a net basis as soon as practicable. Any property held in anticipation of releasing must be reevaluated and recorded at the lower of fair market value or the value carried on the credit union's books.

(d) General Leasing. A credit union may invest in tangible personal property, including vehicles, manufactured homes, equipment, or furniture, for the purpose of leasing that property. In contrast to financing leases, lease investments made under this authority need not be the functional equivalent of loans.

(e) Leasing Salvage Powers. If a credit union believes that there has been an unanticipated change in conditions that threatens its financial position by significantly increasing its exposure to loss, it may:

(1) As the owner and lessor, take reasonable and appropriate action to salvage or protect the value of the property or its interest arising under the lease;

(2) As the assignee of a lessor's interest in a lease, become the owner and lessor of the leased property pursuant to its contractual right, or take any reasonable and appropriate action to salvage or protect the value of the property or its interest arising under the lease; or

(3) Include any provision in a lease, or make any additional agreements, to protect its financial position or investment in the circumstances set forth in paragraphs (1) and (2) of this subsection.

(f) Written Policies. A credit union engaged in lease underwriting must adopt written policies and develop procedures that reflect lease practices that control risk and comply with applicable laws. Any leasing activity must be consistent with the lending policies and underwriting requirements in §91.701 of this title (relating to Lending Powers). Any credit union engaged in making or buying leases also must adopt written policies and procedures that address the additional risks associated with leasing.

(g) Insurance Requirements. A credit union must maintain a contingent liability insurance policy with an endorsement for leasing or be named as the co-insured if the credit union does not own the leased property. Contingent liability insurance protects the credit union if it is sued as the owner of the leased property. A credit union must use an insurance company with a nationally recognized industry rating of at least a B+. Credit union members must still carry the normal liability and property insurance on the leased property and the credit union must be named as an additional insured on the liability insurance policy and as the loss payee on the property insurance policy.

(h) Holding Period. At the expiration of the lease (including any renewals or extensions with the same lessee), or in the event of a default on a lease agreement prior to the expiration of the lease term, a credit union shall either liquidate the off-lease property or re-lease it under a conforming lease as soon as practicable. The credit union must value off-lease property at the

lower of current fair market value or book value promptly after the property becomes off-lease property.

§91.715. Exceptions to the General Lending Policies.

(a) Credit unions may provide for the consideration of loan requests from creditworthy members whose credit needs do not fit within the credit union's general lending policies. A credit union may provide for prudently underwritten exceptions to its lending policies. However, the Board is responsible for establishing written standards for the review and approval of exception loans.
(b) Each credit union establishing exceptions to its general lending policies shall establish an appropriate internal process for the review and approval of loans that do not conform to its own internal policy standards. The approval of any such loan shall also be supported by a written justification that clearly sets forth all of the relevant credit factors that support the underwriting decision. The justification and approval documents for such loans will be maintained as a part of the permanent loan file. Each credit union shall monitor compliance with its lending policies and individually report exception loans of a significant size to its board of directors.
(c) Exception loans shall be identified in the credit union's records and their aggregate amount reported at least annually to the board of directors. The aggregate amount of all such loans shall not exceed 10 percent of the credit union's net worth.

§91.716. Prohibited Fees.

A credit union shall not make any loan or extend any credit if, either directly or indirectly, any commission, fee, or other compensation from any person or entity other than the credit union is to be received by the credit union's directors, committee members, senior management employees, loan officers, or any immediate family members of such individuals, in connection with underwriting, insuring, servicing, or collecting the loan or extension of credit.

§91.717. More Stringent Restrictions.

The Commissioner may impose more stringent restrictions on a credit union's loans if the Commissioner determines that such restrictions are necessary to protect the safety and soundness of the credit union.

91.718. Charging Off or Setting Up Reserves.

(a) The commissioner, after a determination of value in accordance with generally accepted accounting principles, may order that assets in the aggregate, to the extent that such assets have depreciated in value, or to the extent the value of such assets, including loans, are overstated in value for any reason, be charged off, or that a special reserve or reserves equal to such depreciation or overstated value be established.
(b) A credit union's financial statements 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 position; and all income and expenses necessary to present fairly the results of operations for the period concerned.
(c) The Board of directors is responsible for ensuring that the credit union has controls in place to consistently determine the allowance for loan and lease losses (ALLL) in accordance with its written polices, generally accepted accounting principles, and relevant supervisory guidance.

Policies shall be appropriately tailored to the size and complexity of the credit union and its loan and lease portfolio. As a minimum, a credit union shall develop, maintain, and document the methodology used to determine the amounts of an appropriate ALLL and provisions for loan and lease losses. Adjustments to the ALLL shall be made prior to the end of each calendar quarter in order to accurately reflect the loss exposure on the quarterly call reports.

§91.719. Loans to Officials and Senior Management Employees.

(a) Prohibition on Preferential Rates, Terms, and Conditions. The rates, terms, conditions, and availability of any loan or other extension of credit made to, or endorsed or guaranteed by, a director, senior management employee, member of the credit committee, or an immediate family member of any such individual shall not be more favorable than the rates, terms, conditions, and availability of comparable loans or credit to other credit union members.

(b) Approval of Governing Board. Before making a loan, extending credit, or becoming contractually liable to make a loan or extend credit to a director, senior management employee, member of the credit committee, or an immediate family member of such individual, the board of directors must approve the transaction if the loan or the extension of credit or aggregate of outstanding loans and extensions of credit to any one person, the person's business interests, and the members of the person's immediate family is greater than 15% of the credit union's net worth. A loan fully secured by shares in the credit union or deposits in other financial institutions shall not be subject to, or included in, the aggregate amounts included in this section.

(c) Definition. For purposes of this section, senior management employees shall include the chief executive officer, any assistant chief executive officers (e.g. vice presidents and above), and the chief financial officer; and immediate family members shall include a person's spouse or any other person living in the same household.

(d) Aggregate Limit on Insider Loans. The aggregate of all outstanding loans or extensions of credit made to, or endorsed or guaranteed by, all directors, credit committee members, senior management employees, and immediate family members of all such individuals, shall not exceed 20% of the credit union's total assets. The requirements described in this subsection shall apply unless waived in writing by the commissioner for good cause shown.

(e) Reports to Governing Board. At least annually, the president shall make a report to the board of directors on the outstanding indebtedness of all directors, credit committee members, senior management employees, and immediate family members of such individuals. The Board's review shall be included as part of the minutes of the meeting at which the report was presented. The report required by this section shall include the following information:

(1) The amount of each indebtedness; and

(2) A description of the terms and conditions (including the interest rate, the original amount and date, maturity date, payment terms, security, if any, and any other unusual term or condition) of each extension of credit.

(f) Governing Board Option. At the discretion of the Board, the reporting requirement of subsection (e) of this section may be waived for any individual if the aggregate amount of all outstanding loans and extensions of credit to that person, the person's business interests, and the members of the person's immediate family do not exceed the greater of $25,000 or one-quarter of one percent (.25%) of the credit union's net worth.

§91.720. Small-Dollar, Short-Term Credit.

(a) General. Credit unions are encouraged to offer small-dollar credit products that are affordable, yet safe and sound, and consistent with applicable laws. The goal in offering these

small-dollar credit products should be to help members avoid, or transition away from, reliance on high-cost debt. To accomplish this goal, credit unions should offer products with reasonable interest rates, low fees, and payments that reduce the principal balance of the loan or extension of credit.

(b) Definition. For purposes of this section, small-dollar, short term credit product is defined as a low denomination loan or extension of credit having a term of 6 months or less, where the amount financed does not exceed $1,100. Each credit union is responsible for establishing appropriate dollar limits and terms based upon its size and sophistication of operations, and its net worth.

(c) Limitation. Accessibility and expediency are important factors for many members with emergency or other short-term needs. Therefore, small-dollar credit products must balance the need for quick availability of funds with the fundamentals of responsible lending. Sound underwriting criteria should focus on a member's history with the credit union and ability to repay a loan within an acceptable timeframe. Given the small dollar amounts of each individual credit request, documenting the member's ability to repay can be streamlined and may need to include only basic information, such as proof of recurring income. The aggregate total of streamlined underwritten small-dollar credit products outstanding, however, shall not exceed 20% of the credit union's net worth.

(d) Fees. A credit union may require a member to pay reasonable expenses and fees incurred in connection with making or closing a loan. With respect to expenses and fees being assessed on small-dollar, short–term credit products, the expenses and fees are presumed to be reasonable if the aggregate total is $20 or less. In addition, if the credit union refinances a small-dollar, short-term credit product, it may charge such expenses and fees only once in a 180-day period. Credit unions may also charge a late fee as permitted by Finance Code §124.153.

(e) Payments. Credit unions should structure payment programs in a manner that reduces the principal owed. For closed-end products, loans should be structured to provide for affordable and amortizing payments. Lines of credit should require minimum payments that pay off principal. Excessive renewals or the prolonged failure to reduce the outstanding balance are signs that the product is not meeting the member's credit needs and will be considered an unsound practice.

(f) Required Savings. Credit unions may structure small-dollar credit programs to include a savings component. The funds in this account may also serve as a pledge against the loan or extension of credit.

C. (c) Discussion, Consideration, and Possible Vote to Recommend that the Credit Union Commission Take Action to Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.709 Concerning Member Business and Commercial Loans.

BACKGROUND: The Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 (Pub. L. 115-174, S. 2155) was signed into federal law by President Trump on May 24, 2018. Among other things, the bill amends the Federal Credit Union Act to remove certain loans from the statutory Member Business Loan (MBL) cap – loans that are fully secured by a lien on a 1 to 4 family dwelling that is not the primary residence of the member borrower. Under previous law, a residential loan could only be excluded from the MBL cap, if the loan was secured by dwelling that was the member's primary residence.

Federal law imposes an aggregate limit on a federally insured credit union's net member business loan balances (MBL cap). The MBL cap is the lesser of 1.75 times the actual net worth of the credit union, or 1.75 times the minimum net worth required under 12 U.S.C. Section 1790d(c)(1)(A).

NCUA has recently approved changes to its MBL regulation (Part 723) that remove the member's occupancy requirement for loans secured by liens on 1- to 4-family dwellings. This change, however, does not apply to Texas-chartered credit unions since credit unions under the jurisdiction of the Department are exempted from compliance with Part 723 and are required to comply with the provisions of 7 TEX. ADMIN. CODE Section 91.709 (Member Business and Commercial Loans). Existing Rule 91.709 requires a 1- to 4-family dwelling to be the primary resident of a member in order to be excluded from the definition of a member business loan. As a result, loans secured by a non-owner occupied 1- to 4- family dwelling are still considered to be MBLs and they continue to count towards the aggregate MBL cap.

Part 723 provides that federally insured credit unions in a given state are exempted from compliance with Part 723, if the state administers a state commercial and member business loan rule for use by federally insured credit unions in that state, provided that the state rule at least covers all the

provisions in Part 723 and is no less restrictive (based on NCUA's determination). Existing Rule 91.709 was deemed, in October 2016, to be no less restrictive and to have covered the provisions in Part 723.

The proposed amendments to Rule 91.709 conform the rule to the recent changes in Part 723 as a result of the new federal law. It is important to keep in mind, like in 2016, any changes to Rule 91.709 needs NCUA's approval before the Commission can ultimately consider adoption of the proposal.

RECOMMENDED ACTION: The Department requests that the Committee recommend to the Commission approve the proposed amendments for publication and comment.

RECOMMENDED MOTION: I move that the Committee recommend that the Commission take action to approve for publication and comment the proposed amendments to **7 TAC Section 91.709** concerning member business and commercial loans.

TITLE 7. BANKING AND SECURITIES
Part 6. Credit Union Department
Chapter 91. General Rules
Subchapter G. Lending Powers

The Credit Union Commission (the Commission) proposes amendments to 7 TAC, Chapter 91, Subchapter G, Section 91.709, concerning member business and commercial loans. The amended rule is proposed to amend the definition of member business loan (MBL) with respect to 1- to 4-family dwellings to conform with recent amendments to 12 U.S.C. 1757a(c)(1)(B)(i).

In general, the purpose of the proposal regarding Section 91.709 is to implement changes resulting from the Commission's review of the Chapter 91, Subchapter G under Texas Government Code, Section 2001.039. The notice of intention to review 7 TAC Chapter 91, Subchapter G, was published in the *Texas Register* on April 20, 2018 (43 TexReg 2455). The agency did not receive any comments on the notice of intention to review.

On May 24, 2018, the President signed the Economic Growth, Regulatory Relief, and Consumer Protection Act, S. 2155, 115th Cong (2018) (Economic Growth Act), which among other things, amended the definition section of the MBL provisions of the Federal Credit Union Act. Prior to the Economic Growth Act, the Federal Credit Union Act defined an MBL, in relevant part, as any loan, line of credit, or letter of credit, the proceeds of which will be used for commercial, corporate or other business investment property or venture, or agricultural purpose but does not include and extension of credit that is fully secured by a lien on a 1- to 4- family dwelling *that is the primary residence of a member.*

The Economic Growth Act removed from that definition the words "that is the primary residence of a member." As a result, the federal definition of an MBL, now excludes all extensions of credit that are fully secured by a lien on a 1- to 4- family residential property regardless of the borrower's occupancy status. Because these kinds of loans are no long considered MBLs, they do not count towards the aggregate MBL cap imposed on each federal credit union by the Federal Credit Union Act.

The purpose of the proposal regarding Section 91.709 is a result of the change to the federal definition of MBL as discussed above. The proposed amendments will provide credit unions parity, under Texas Finance Code Section 123.003, with federal credit unions engaged in the business of making MBLs in Texas.

In general, the proposed amendments will clarify that mortgage loans for non-owner occupied 1-4 family residential properties are no longer considered commercial loans or member business loans. The proposal will reduce regulatory burden for credit unions concerned about going up against the MBL lending cap and also for smaller credit unions that can now lend money for second homes without triggering MBL obligations.

STATE AND LOCAL GOVERNMENTS

Harold E. Feeney, Commissioner, has determined that for the first five-year period the rule changes are in effect there will be no fiscal implications for state or local government as a result of enforcing or administering the rule changes.

STATEMENT OF PUBLIC COST AND BENEFITS

Mr. Feeney has also determined that for each year of the first five years the rule changes are in effect, the public benefits anticipated as a result of the changes will be greater clarity regarding the rule's requirements and significant regulatory relief for credit unions. There is no economic cost anticipated to the credit union system or to individuals required to comply with the rule changes as proposed.

SMALL AND MICRO BUSINESSES AND RURAL COMMUNITIES

Mr. Feeney has also determined that for each year of the first five years the rule changes are in effect, there will be no adverse economic effect on small businesses, micro-businesses, or rural communities.

GOVERNMENT GROWTH IMPACT STATEMENT

Except as may be described below to the contrary, for each year of the first five years that the rules will be in effect, the rules will not:

- Create or eliminate a government program;
- Require the creation of new employee positions or the elimination of existing employee positions;
- Require an increase or decrease in future legislative appropriations to the agency;
- Create new regulations;
- Expand or repeal an existing regulation;
- Increase fees paid to the department;
- Increase or decrease the number of individuals subject to the rule's applicability; or
- Positively or adversely affect this state's economy.

For each year of the first five years that the rule will be in effect, the rule will limit an existing regulation with respect to loans that are fully secured by a lien on a 1- to 4- family dwelling regardless of the borrower's occupancy status.

Written comments on the proposed amendments may be submitted in writing to Harold E. Feeney, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register.* At the conclusion of business on the 31st day after the proposal is published in the *Texas Register*, no further written comments will considered or accepted by the commission.

The rule changes are proposed under Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Title 3, Subchapter D of the Texas Finance Code, and under Texas Finance Code Section 124.001, which authorizes the Commission to adopt rules regarding loans to members.

The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Chapter 124.

§91.709. Member Business and Commercial Loans.

(a) Definitions. Definitions in TEX. FIN. CODE §121.002, are incorporated herein by reference. As used in this section, the following words and terms shall have the following meanings, unless the context clearly indicates otherwise.

(1) "Borrower" means a member or any other person named as a borrower, obligor, or debtor in a loan or extension of credit; or any other person, including, but not limited to, a comaker, drawer, endorser, guarantor or surety who is considered to be a borrower under the requirements of subsection (i) of this section concerning aggregation and attribution for commercial loans.

(2) "Commercial loan" means a loan or an extension of credit to an individual, sole proprietorship, partnership, corporation, or business enterprise for commercial, industrial, agricultural, or professional purposes, including construction and development loans, any unfunded commitments, and any interest a credit union obtains in such loans made by another lender. A commercial loan does not include a loan made for personal expenditure purposes; a loan made by a corporate credit union; a loan made by a credit union to a federally insured credit union; a loan made by a credit union to a credit union service organization; a loan secured by a 1- to 4-family residential property (whether or not the residential property is the borrower's primary residence); a loan fully secured by shares in the credit union making the extension of credit or deposits in another financial institution; a loan secured by a vehicle manufactured for household use; and a loan that would otherwise meet the definition of commercial loan and which, when the aggregate outstanding balance plus unfunded commitments less any portion secured by shares in the credit union to a borrower, is equal to less than $50,000.

(3) "Control" means a person directly or indirectly, or acting through or together with one or more persons who:

(A) own, control, or have the power to vote twenty-five (25) percent or more of any class of voting securities of another person;

(B) control, in any manner, the election of a majority of the directors, trustees, or other persons exercising similar functions of another person; or

(C) have the power to exercise a controlling influence over the management or policies of another person.

(4) "Immediate family member" means a spouse or other family member living in the same household.

(5) "Loan secured by a lien on a 1- to 4-family residential property" means a loan that, at origination, is secured wholly or substantially by a lien on a 1- to 4-family residential property for which the lien is central to the extension of the credit; that is the borrower would not have been extended credit in the same amount or on terms as favorable without the lien. A loan is wholly or substantially secured by a lien on a 1- to 4-family residential property if the estimated value of the real estate collateral at origination (after deducting any senior liens held by others) is greater than fifty (50) percent of the principal amount of the loan.

(6) "Loan secured by a lien on a vehicle manufactured for household use" means a loan that, at origination, is secured wholly or substantially by a lien on a new and used passenger car or other vehicle such as a minivan, sport-utility vehicle, pickup truck, and similar light truck or heavy-duty truck generally manufactured for personal, family, or household use and not used as a fleet vehicle or to carry fare-paying passengers, for which the lien is central to the extension of credit. A lien is central to the extension of credit if the borrower would not have been extended

credit in the same amount or on terms as favorable without the lien. A loan wholly or substantially secured by a lien on a vehicle manufactured for household use if the estimated value of the collateral at origination (after deducting any senior liens held by others) is greater than fifty (50) percent of the principal amount of the loan.

(7) "Loan-to-value ratio for collateral" means the aggregate amount of all sums borrowed and secured by the collateral, including outstanding balances plus any unfunded commitment or line of credit from another lender that is senior to the credit union's lien, divided by the current collateral value. The current collateral value must be established by prudent and accepted commercial loan practices and comply with all regulatory requirements.

(8) "Member business loan" has the meaning assigned by 12 C.F.R. Part 723.

(9) "Net worth" has the meaning assigned by 12 C.F.R. Part 702.2.

(10) "Readily marketable collateral" means financial instruments and bullion that are salable under ordinary market conditions with reasonable promptness at a fair market value determined by quotations based upon actual transactions on an auction or similarly available daily bid and ask price market.

(11) "Residential property" means a house, townhouse, condominium unit, cooperative unit, manufactured home, a combination of a home or dwelling unit and a business property that involves only minor or incidental business use, real property to be improved by the construction of such structures, or unimproved land zoned for 1- to 4-family residential use but does not include a boat, motor home, or timeshare property, even if used as a primary residence. This applies to such structure whether under construction or completed.

(b) Parity. A credit union may make, commit to make, purchase, or commit to purchase any member business loan it could make if it were operating as a federal credit union domiciled in this state, so long as for each transaction the credit union complies with all applicable regulations governing such activities by federal credit unions. However, all such loans must be documented in accordance with the applicable requirements of this chapter.

(c) Commercial Loan Responsibilities and Operational Requirements. Prior to engaging in the business of making commercial loans, a credit union must address the responsibilities and operational requirements under this subsection:

(1) Written policies. A credit union must establish comprehensive written commercial loan policies approved by its board of directors instituting prudent loan approval, credit underwriting, loan documentation, and loan monitoring standards in accordance with this paragraph. The board must review its policies at least annually and, additionally, prior to any material change in the credit union's commercial lending program or related organizational structure, in response to any material change in the credit union's overall portfolio performance, or in response to any material change in economic conditions affecting the credit union. The board must update its policies when warranted. Policies under this paragraph must be designed to identify:

(A) type(s) of commercial loans permitted;

(B) trade area;

(C) the 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;

(D) credit underwriting standards including potential safety and soundness concerns to ensure that action is taken to address those concerns before they pose a risk to the credit union's net worth; the size and complexity of the loan as appropriate to the size of the

credit union; the scope of the credit union's commercial loan activities; the level and depth of financial analysis necessary to evaluate financial trends and the condition of the borrower and the ability of the borrower to meet debt service requirements; requirements for a borrower-prepared projection when historic performance does not support projected debt payments; the financial statement quality and degree of verification sufficient to support an accurate financial analysis and risk assessment; the methods to be used in evaluating collateral authorized, including loan-to-value ratio limits; the means to secure various types of collateral; and other risk assessment analyses including analysis of the impact of current market conditions on the borrower.

(E) loan approval standards including consideration, prior to credit commitment, of the borrower's overall financial condition and resources; the financial stability of any guarantor; the nature and value of underlying collateral; environmental assessment requirements; the borrower's character and willingness to repay as agreed; the use of loan covenants when warranted; and the levels of loan approval authority commensurate with the proficiency of the individuals or committee of the credit union tasked with such approval authority in evaluating and understanding commercial loan risk, when considered in terms of the level of risk the borrowing relationship poses to the credit union;

(F) loan monitoring standards including a system of independent, ongoing credit review and appropriate communication to senior management and the board of directors; the concentration of credit risk; and the risk management systems under subsection (d) of this section; and

(G) loan documentation standards including enabling the credit union to make informed lending decisions and assess risk, as necessary, on an ongoing basis; identifying the purpose of each loan and source(s) of repayment; assessing the ability of each borrower to repay the indebtedness in a timely manner; ensuring that any claim against a borrower is legally enforceable; and demonstrating appropriate administration and monitoring of each loan.

(2) Qualified Staff. A credit union must ensure that it is appropriately staffed with qualified personnel with relevant and necessary expertise and experience for the types of commercial lending in which the credit union is engaged, including appropriate experience in underwriting, processing, overseeing and evaluating the performance of a commercial loan portfolio, including rating and quantifying risk through a credit risk rating system and collections and loss mitigation activities for the types of commercial lending in which the credit union is engaged. At a minimum, a credit union making, purchasing, or holding any commercial loans must internally have a senior management employee that has a thorough understanding of the role of commercial lending in the credit union's overall business model and establish risk management processes and controls necessary to safely conduct commercial lending as provided by subsection (d) of this section.

(3) Use of Third-Party Experience. A third party may provide the requisite expertise and experience necessary for a credit union to safely conduct commercial lending if:

(A) the third party has no affiliation or contractual relationship with the borrower;

(B) the third party is independent from the commercial loan transaction and does not have a participation interest in a loan or an interest in any collateral securing a loan that the third party is responsible for reviewing, or an expectation of receiving compensation of any sort that is contingent on the closing of the loan, with the following exceptions:

(i) the third party may provide a service to the credit union that is related to the transaction, such as loan servicing;

(ii) the third party may provide the requisite experience to a credit union and purchase a loan or a participation interest in a loan originated by the credit union that the third party reviewed; and

(iii) the third party is a credit union service organization and the credit union has a controlling financial interest in the credit union service organization as determined under generally accepted accounting principles.

(C) the actual decision to grant a commercial loan resides with the credit union; and

(D) qualified credit union staff exercise ongoing oversight over the third party by regularly evaluating the quality of any work the third party performs for the credit union.

(4) De Minimis Exception. The responsibilities and operational requirements described in paragraphs (1) and (2) of this subsection do not apply to a credit union if it meets all of the following conditions:

(A) the credit union's total assets are less than $250 million;

(B) the credit union's aggregate amount of outstanding commercial loan balances (including any unfunded commitments, any outstanding commercial loan balances and unfunded commitments of participations sold, and any outstanding commercial loan balances and unfunded commitments sold and serviced by the credit union) total less than fifteen (15) percent of the credit union's net worth; and

(C) in a given calendar year, the amount of originated and sold commercial loans and the amount of originated and sold commercial loans the credit union does not continue to service, total fifteen (15) percent or less of the credit union's net worth.

(D) A credit union that relies on this de minimis exception is prohibited from engaging in any acts or practices that have the effect of evading the requirements of this subsection.

(d) Commercial Loan Risk Management Systems.

(1) Risk Management Processes. A credit union's risk management process must be commensurate with the size, scope and complexity of the credit union's commercial lending activities and borrowing relationships. The processes must, at a minimum, address the following:

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

(B) periodic loan review, consistent with loan covenants and sufficient to conduct portfolio risk management, which, based upon current market conditions and trends, loan risk, and collateral conditions, must include a periodic reevaluation of the value and marketability of any collateral, and an updated loan-to-value ratio for collateral calculation;

(C) a credit risk rating system under paragraph (2) of this subsection; and

(D) a process to identify, report, and monitor commercial loans that are approved by the credit union as exceptions to the credit union's loan policies.

(2) Credit Risk Rating System. The credit risk rating system must be a formal process that identifies and assigns a relative credit risk rating to each commercial loan in a credit union's portfolio, using ordinal ratings to represent the degree of risk. The credit risk score must be determined through an evaluation of quantitative factors based on the financial performance of each commercial loan and qualitative factors based on the credit union's management, operational, market, and business environment factors. A credit risk rating must be assigned to each commercial loan at the inception of the loan. A credit risk rating must be reviewed as

frequently as necessary to satisfy the credit union's risk monitoring and reporting policies, and to ensure adequate reserves as required by generally accepted accounting principles.

(3) Independent Review. Periodic independent reviews should be conducted by a person who is both qualified to conduct such a review and independent of the function being reviewed. The review should provide an objective assessment of the overall commercial loan portfolio quality and verify the accuracy of ratings and the operational effectiveness of the credit union's risk management processes. A credit union is not required to hire an outside third party to conduct this independent review, if it can be done in-house by a competent person that is considered unconnected to the function being reviewed.

(e) Collateral and Security for Commercial Loans.

(1) Collateral. A commercial loan must be secured by collateral commensurate with the level of risk associated with the size and type of the commercial loan. The collateral must be sufficient to ensure the credit union is protected by a prudent loan-to-value ratio for collateral along with appropriate risk sharing with the borrower and principal(s). A credit union making an unsecured commercial loan must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk of making an unsecured loan.

(2) Personal Guarantees. A credit union that does not require the full and unconditional personal guarantee from all principals of the borrower who have a controlling interest, as defined by subsection (a)(3) of this section, in the borrower must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.

(f) Construction and Development Loans.

(1) Terms. In this subsection:

(A) "construction or development loan" means any financing arrangement to enable the borrower to acquire property or rights to property, including land or structures, with the intent to construct or renovate an income producing property, such as residential housing for rental or sale, or a commercial building, that may be used for commercial, agricultural, industrial, or other similar purposes. It also means a financing arrangement for the construction, major expansion or renovation of the property types referenced in this subsection. The collateral valuation for securing a construction or development loan depends on the satisfactory completion of the proposed construction or renovation where the loan proceeds are disbursed in increments as the work is completed. A loan to finance maintenance, repairs, or other improvements to an existing income-producing property that does not change the property's use or does not materially impact the property is not a construction or development loan.

(B) "cost to complete" means the sum of all qualifying costs necessary to complete a construction project and documented in an approved construction budget. Qualifying costs generally include on- or off-site improvements; building construction; other reasonable and customary costs paid to construct or improve a project, including a general contractor's fees; other expenses normally included in a construction contract such as bonding and contractor insurance; the value of the land, determined as the sum of the cost of any improvements to the land and the lesser of appraised market value or purchase price; interest as provided by this subparagraph; project costs as provided by this subparagraph; a contingency account to fund unanticipated overruns; and other development costs such as fees and related pre-development expenses. Interest expense is a qualifying cost only to the extent it is included in the construction budget and is calculated based on the projected changes in the loan balance up to the expected "as-complete" date for owner-occupied non-income-producing commercial real property or the "as stabilized" date for income-producing real estate. Project costs for related parties, such as

developer fees, leasing expenses, brokerage commissions and management fees, are included in qualifying costs only if reasonable in comparison to the cost of similar services from a third party. Qualifying costs exclude interest or preferred returns payable to equity partners or subordinated debt holders, the developer's general corporate overhead, and selling costs to be funded out of sales proceeds such as brokerage commissions and other closing costs.

(C) "prospective market value" means the market value opinion determined by an independent appraiser in compliance with the relevant standards set forth in the Uniform Standards of Professional Appraisal Practice. Prospective value opinions are intended to reflect the current expectations and perceptions of market participants, based on available data. Two (2) prospective value opinions may be required to reflect the time frame during which development, construction, or occupancy occur. The prospective market value "as-completed" reflects the real property's market value as of the time that development is to be completed. The prospective market value "as-stabilized" reflects the real property's market value as of the time the real property is projected to achieve stabilized occupancy. For an income producing property, stabilized occupancy is the occupancy level that a property is expected to achieve after the real property is exposed to the market for lease over a reasonable period of time and at comparable terms and conditions to other similar real properties.

(2) Policies. A credit union that elects to make a construction or development loan must ensure that its commercial loan policies under subsection (c) of this section meets the following conditions:

(A) qualified personnel representing the interest of the credit union must conduct a review and approval of any line item construction budget prior to closing the loan;

(B) a requisition and loan disbursement process approved by the credit union is established;

(C) release or disbursement of loan funds occurs only after on-site inspections which are documented in a written report by qualified personnel who represents the interest of the credit union and certifies that the work requisitioned for payment has been satisfactorily completed, and the remaining funds available to be disbursed from the construction and development loan is sufficient to complete the project; and

(D) each loan disbursement is subject to confirmation that no intervening liens have been filed.

(3) Establishing Collateral Values. The current collateral value must be established by prudent and accepted commercial loan practices and comply with all regulatory requirements. The collateral value depends on the satisfactory completion of the proposed construction or renovation where the loan proceeds are disbursed in increments as the work is completed and is the lesser of the project's cost to complete or its prospective market value.

(4) Controls and Processes for Loan Advances. A credit union that elects to make a construction and development loan must have effective commercial loan control procedures in place to ensure sound loan advances and that liens are paid and released in a timely manner. Effective controls should include segregation of duties, delegation of duties to appropriate qualified personnel, and dual approval of loan disbursements.

(g) Commercial Loan Prohibitions.

(1) Ineligible borrowers. A credit union may not grant a commercial loan to the following:

(A) any senior management employee directly or indirectly involved in the credit union's commercial loan underwriting, servicing, and collection process, and any of their

immediate family members;

(B) any person meeting the requirements of subsection (i) of this section concerning aggregations and attribution for commercial loans, with respect to persons identified in subparagraph (A) of this paragraph; or

(C) any director, unless the credit union's board of directors approves granting the loan and the borrowing director was recused from the board's decision making process.

(2) Equity Agreements and Joint Ventures. A credit union may not grant a commercial loan if any additional income received by the credit union or its senior management employees is tied to the profit or sale of any business or commercial endeavor that benefits from the proceeds of the loan.

(3) Fees. No director, committee member, volunteer official, or senior management employee of a credit union, or immediate family member of such director, committee member, volunteer official, or senior management employee, may receive, directly or indirectly, any commission, fee, or other compensation in connection with any commercial loan made by the credit union. Employees, other than senior management, may be partially compensated on a commission or performance based incentive, provided the compensation is governed by a written policy and internal controls established by the board of directors. The board must review the policies and controls at least annually to ensure that such compensation is not excessive or expose the credit union to inappropriate risks that could lead to material financial loss. Loan origination employees are prohibited from receiving, in connection with any commercial loan made by the credit union, any compensation from any source other than the credit union. For the purposes of this paragraph, compensation includes non-monetary items and anything reasonably regarded as pecuniary gain or pecuniary advantage, including a benefit to any other person in whose welfare the beneficiary has a direct and substantial interest, but compensation does not include nonmonetary items of nominal value.

(h) Aggregate Member Business Loan Limit.

(1) Limits. The aggregate limit on a credit union's net member business loan balances is the lesser of 1.75 times the actual net worth of the credit union, or 1.75 times the minimum net worth required under 12 U.S.C. Section 1790d(c)(1)(A). For purposes of this calculation, member business loan means any commercial loan, except that the following commercial loans are not member business loans and are not counted toward the aggregate limit on member business loans:

(A) any loan in which a federal or state agency (or its political subdivision) fully insures repayment, fully guarantees repayment, or provides an advance commitment to purchase the loan in full; [and]

(B) any non-member commercial loan or non-member participation interest in a commercial loan made by another lender, provided the credit union acquired the non-member loans or participation interest in compliance with applicable laws and the credit union is not, in conjunction with one or more other credit unions, trading member business loans to circumvent the aggregate limit under this subsection[.]; and

(C) any loan that is fully secured by a lien on a 1- to 4- family dwelling.

(2) Exceptions. Any loan secured by a lien on a [1 to 4 family residential property that is not a member's primary residence, any loan secured by a lien on a] vehicle manufactured for household use that will be used for commercial, corporate, or other business investment property or venture, and any other loan for an agricultural purpose are not commercial loans (if the outstanding aggregate net member business loan balance is $50,000 or greater), and must be

counted toward the aggregate limit on a credit union's member business loans under this subsection.

(3) Exemption. A credit union that has a federal low-income designation, or participates in the federal Community Development Financial Institution program, or was chartered for the purpose of making member business loans, or which as of the date of the Credit Union Membership Access Act of 1998 had a history of primarily making commercial loans, is exempt from compliance with the aggregate member business loan limits in paragraph (1) of this subsection.

(4) Method of Calculation for Net Member Business Loan Balance. For the purposes of NCUA form 5300 reporting (call report), a credit union's net member business loan balance is determined by calculating the sum of the outstanding loan balance plus any unfunded commitments and reducing that sum by any portion of the loan that is: secured by shares in the credit union, by shares or deposits in other financial institutions, or by a lien on a borrower's primary residence; insured or guaranteed by any agency of the federal government, a state, or any political subdivision of a state; or subject to an advance commitment to purchase by any agency of the federal government, a state, or any political subdivision of a state; or sold as a participation interest without recourse and qualifying for true sales accounting under generally accepted accounting principles.

(i) Aggregation and Attribution for Commercial Loans.

(1) General Rule. A commercial loan or extension of credit to one borrower is attributed to another person, and each person will be considered a borrower, when:

(A) the proceeds of the commercial loan or extension of credit are to be used for the direct benefit of the other person, to the extent of the proceeds so used, as provided by paragraph (2) of this subsection;

(B) a common enterprise is deemed to exist between the persons as persons as provided by paragraph (3) of this subsection; or

(C) the expected source of repayment for each commercial loan or extension of credit is the same for each person as provided by paragraph (3) of this subsection.

(2) Direct Benefit. The proceeds of a commercial loan or extension of credit to a borrower is considered used for the direct benefit of another person and attributed to the other person when the proceeds, or assets purchased with the proceeds, are transferred in any manner to or for the benefit of the other person, other than in a bona fide arm's length transaction where the proceeds are used to acquire property, goods, or services from such other person.

(3) Common Enterprise.

(A) Description. A common enterprise is considered to exist and commercial loans to separate borrowers will be aggregated when:

(i) the expected source of repayment for each loan or extension of credit is the same for each borrower and neither borrower has another source of income from which the loan (together with the borrower's other obligations) may be fully repaid. An employer will not be treated as a source of repayment under this subparagraph because of wages and salaries paid to an employee, unless the standards of clause (ii) of this subparagraph are met:

(ii) the loans or extension of credit are made:

(I) to borrowers who are related directly or indirectly through control as defined by subsection (a) of this section; and

(II) substantial financial interdependence exists between or among the borrowers. Substantial financial interdependence is deemed to exist when fifty (50) percent

or more of one borrower's gross receipts or gross expenditures (on an annual basis) are derived from transactions with the other borrower. Gross receipts and expenditures include gross revenues/expenses, intercompany loans, dividends, capital contributions, and other similar receipts or payments;

(iii) separate persons borrow from a credit union to acquire a business of enterprise of which those borrowers will own more than fifty (50) percent of the voting securities of voting interest, in which case a common enterprise is deemed to exist between the borrowers for purposes of combining the acquisition loans; or

(iv) the Department determines, based upon an evaluation of the facts and circumstances of particular transactions, that a common enterprise exists.

(B) Commercial Loans to Certain Entities. A commercial loan or extension of credit:

(i) to a partnership or joint venture is considered to be a commercial loan or extension of credit to each member of the partnership or joint venture. Excepted from this subdivision is a partner or member who: is not held generally liable, by the terms of the partnership or membership agreement or by applicable law, for the debts or actions of the partnership, joint venture, or association, provided those terms are valid against third parties under applicable law; and has not otherwise agreed to guarantee or be personally liable on the loan or extension of credit.

(ii) to a member of a partnership, joint venture, or association is generally not attributed to the partnership, joint venture, or associations, or to other members of the partnership, joint venture, or association, except as otherwise provided by paragraphs (2) and (3) of this subsection, provided that a commercial loan or extension of credit made to a member of a partnership, joint venture or association for the purpose of purchasing an interest in the partnership, joint venture or association, is attributed to the partnership, joint venture or association.

(C) Guarantors and Accommodation Parties. The derivative obligation of a drawer, endorser, or guarantor of a commercial loan or extension of credit, including a contingent obligation to purchase collateral that secures a commercial loan, is aggregated with other direct commercial loans or extensions of credit to such a drawer, endorser, or guarantor.

(j) Commercial Loans to One Borrower Limit. The total aggregate dollar amount of commercial loans by a credit union to any borrower at one time may not exceed the greater of fifteen (15) percent of the credit union's net worth or $100,000, plus an additional ten (10) percent of the credit union's net worth if the amount that exceeds the credit union's fifteen (15) percent general limit is fully secured at all times with a perfected security interest in readily marketable collateral. 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 commercial loan in full, is excluded from this limit.

(k) Finance Code Limitation. In addition to the other limitations of this section, a credit union may not make a loan to a member or a business interest of the member if the loan would cause the aggregate amount of loans to the member and the member's business interests to exceed an amount equal to 10 percent of the credit union's total assets as provided by TEX. FIN. CODE §124.003.

(l) Commercial Loans Regarding Federal or State Guaranteed Loan Programs. A credit union may follow the loan requirements and limits of a guaranteed loan program for loans that

are part of a loan 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 if that program has requirements that are less restrictive than those required by this section.

(m) Transitional Provisions.

(1) Waivers. Upon the effective date of this section, any waiver approved by the Department concerning a credit union's commercial lending activity is rendered moot, except for waivers granted for the commercial loan to one borrower limit. Borrowing relationships granted by waivers will be grandfathered however, the debt associated with those relationships may not be increased.

(2) Administrative Constraints. Limitations or other conditions imposed on a credit union in any written directive from the Department are unaffected by the adoption of this section. As of the effective date of this section, all such limitations or other conditions remain in place until such time as they are modified by the Department.

[(n) Effective Date. This section takes effect on January 1, 2017].

PLASTIC CARDS

C. (d) Discussion, Consideration, and Possible Vote to Recommend that the Credit Union Commission Take Action to Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.712 Concerning Plastic Cards.

BACKGROUND: The purpose of the proposed amendments is to implement changes resulting from the Commission's review of Chapter 91, Subchapter G under the Texas Government Code Section 2001.039. The proposed amendments would update a requirement to recognize the advancement of electronic communications. In specific, it would permit a plastic card to be activated by logging on to the card issuer/processor's website to go through a member verification process.

RECOMMENDED ACTION: The Department requests that the Committee recommend to the Commission approve the proposed amendments for publication and comment.

RECOMMENDED MOTION: I move that the Committee recommend that the Commission take action to approve for publication and comment the proposed amendments to **7 TAC Section 91.712** concerning plastic cards.

TITLE 7. BANKING AND SECURITIES
Part 6. Credit Union Department
Chapter 91. General Rules
Subchapter G. Lending Powers

The Credit Union Commission (the Commission) proposes amendments to 7 TAC, Chapter 91, Subchapter G, Section 91.712, concerning plastic cards. The amended rule is proposed to update requirements to recognize the advancement of electronic communication.

In general, the purpose of the proposal regarding Section 91.712 is to implement changes resulting from the Commission's review of the Chapter 91, Subchapter G under Texas Government Code, Section 2001.039. The notice of intention to review 7 TAC Chapter 91, Subchapter G, was published in the *Texas Register* on April 20, 2018 (43 TexReg 2455). The agency did not receive any comments on the notice of intention to review.

The proposed amendments to paragraph (a), subparagraph (1) would allow a plastic card to be activated by logging on to the card issuer/processor's website to go through a member verification process.

STATE AND LOCL GOVERNMENTS

Harold E. Feeney, Commissioner, has determined that for each year of the first five years the rule changes are in effect there will be no fiscal implications for state or local government as a result of enforcing or administering the rule changes.

STATEMENT OF PUBLIC COST AND BENEFITS

Mr. Feeney has also determined that for each year of the first five years the rule changes are in effect, the public benefits anticipated as a result of the changes will be that the commission's rules will more accurately reflect the way plastic cards may be activated. There will be no anticipated cost to persons who are required to comply with the proposed amendments. There will be no adverse economic effect on small businesses, micro-businesses, or rural communities, as compared to large businesses. There is no economic cost anticipated to the credit union system or to individuals required to comply with the rule changes as proposed.

SMALL AND MICRO BUSINESSES AND RURAL COMMUNITIES

Mr. Feeney has also determined that for each year of the first five years the rule changes are in effect, there will be no adverse economic effect on small businesses, micro-businesses, or rural communities. There is no economic cost anticipated to the credit union system or to individuals required to comply with the rule changes as proposed.

GOVERNMENT GROWTH IMPACT STATEMENT

Except as may be described below to the contrary, for each year of the first five years that the rules will be in effect, the rules will not:

- Create or eliminate a government program;
- Require the creation of new employee positions or the elimination of existing employee positions;
- Require an increase or decrease in future legislative appropriations to the agency;
- Create new regulations;
- Expand, limit, or repeal an existing regulation;
- Increase fees paid to the department;
- Increase or decrease the number of individuals subject to the rule's applicability; or
- Positively or adversely affect this state's economy.

Written comments on the proposed amendments may be submitted in writing to Harold E. Feeney, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register.* At the conclusion of business on the 31st day after the proposal is published in the *Texas Register*, no further written comments will considered or accepted by the commission.

The rule changes are proposed under Texas Finance Code, Section 15.402(b-1), which authorizes the Commission to adopt reasonable rules for administering Title 3, Subchapter D of the Texas Finance Code, and under Texas Finance Code Section 124.001, which authorizes the Commission to adopt rules regarding loans to members.

The statutory provisions affected by the proposed amendments are contained in Texas Finance Code Section 15.402 and in Finance Code Chapter 124.

§91.712. Plastic Cards.

(a) Definitions. The following words and terms, when used in this chapter, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Card Activation – process of sending new plastic cards from the issuer to the legitimate cardholder in an "inactive" mode and making the card usable. [Once the legitimate cardholder receives the card, they] Upon receiving the card, the legitimate cardholder must call or log on to the issuer/processor's website [the issuer-processor] and go through a member verification process before the card is "activated".

(2) Card Security Code – a set of unique numbers encoded on the magnetic strip of plastic cards used to combat counterfeit fraud.

(3) Neural Network – a computer program that monitors usage patterns of an account and typical fraud patterns. The program analyzes activity to determine fraud risk scores to detect potentially fraudulent activity.

(4) Plastic Cards – includes credit cards, debit cards, automated teller machine (ATM) or specific network cards; and predetermined stored value and smart cards with micro-processor chips.

(b) Credit cards. A credit union may issue credit cards in accordance with the credit union's written policies, which shall include at a minimum:

(1) Credit policies to set individual limits for credit card accounts:

(2) A process for reviewing each member's payment and/or credit history periodically for the purpose of determining risk; and

(3) The credit underwriting standards for each type of card program offered.

(c) Program Review.

(1) A credit union shall review, on at least an annual basis, its plastic card program with particular emphasis on:

(A) The amount of losses caused by theft and fraud;

(B) The loss prevention measures (and their adequacy) currently employed by the credit union;

(C) The availability and possible implementation of other loss prevention measures such as card activation, card security codes, neural networks, and other evolving technology; and

(D) A cost benefit analysis of supplemental insurance coverage for theft and fraud related losses.

(2) The review shall be documented in writing, with any approved changes to the plastic card program being entered into the minutes of the board meeting.

COMPLAINT NOTIFICATION

C. (e) Discussion, Consideration, and Possible Vote to Recommend that the Credit Union Commission Take Action to Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.121 Concerning Complaint Notification.

BACKGROUND: The Sunset Advisory Commission utilizes a Licensing and Regulation Model in evaluating licensing and regulatory agencies. One of the standard reflected in this Model is that an agency's procedures for dealing with complaints should be guided by comprehensive rules covering all phases of the process, including receipt, investigation, adjudication, dismissal or closure, and disclosure to the complaint parties. It is our understanding the Model indicates that detailed rules documenting all phases of complaint investigations help policymaking bodies set expectations and check results for appropriate and fair actions with both the public and licensees. In addition, consistent complaint rules and reporting procedures should also improve oversight by allowing comparisons to identify concerning trends or best practices among similar regulatory programs.

While the Department has previously prepared public interest information describing procedures for filing and resolving complaints, the purpose of the proposed amendments is intended to be explanatory in nature and generally relate to four areas: (1) how to file a complaint with the Department, (2) how a complaint is handled after receipt, (3) the authority of the Department in reviewing complaints, and (4) the privacy of information provided in a complaint.

RECOMMENDED ACTION: The Department requests that the Committee recommend to the Commission approve the proposed amendments for publication and comment.

RECOMMENDED MOTION: I move that the Committee recommend that the Commission take action to approve for publication and comment the proposed amendments to **7 TAC Section 91.121** concerning complaint notification.

Title 7. BANKING AND SECURITIES
Part 6. Credit Union Department
Chapter 91, Section 91.121 Complaint Notification

The Credit Union Commission (the Commission) proposes amendments to 7 TAC, Chapter 91, Section 91.121 concerning complaint notification. The purpose of the proposed amendments is to implement Finance Code Section 15.409, which provides that the Commission shall maintain a system to promptly and efficiently act on complaints filed with the Credit Union Department (Department).

The proposed rule changes are intended to be explanatory in nature and generally relate to four areas: (1) how to file a complaint with the Department, (2) how a complaint is handled after receipt, (3) the authority of the Department in reviewing complaints, and (4) the privacy of information provided in a complaint.

The proposed amendments to paragraph (a) delineate the purpose of the section.

The proposed new paragraph (c) describes the Department's process for filing, receipt and handling of complaints.

The proposed new paragraph (d) explains the circumstances under which a complaint may be closed with no action by the Department beyond its review.

The proposed new paragraph (e) makes clear that any information provided with a complaint will be used in investigating a complaint and that personal, confidential, or sensitive information should not be included with the complaint.

STATE AND LOCAL GOVERNMENTS

Harold E. Feeney, Commissioner, has determined that for the first five-year period that the rule changes are in effect there will be no fiscal implications for state and local government as a result of enforcing or administering the rule changes.

STATEMENT OF PUBLIC COST AND BENEFITS

Mr. Feeney has also determined that for each year of the first five years the rules are in effect, the public will benefit from the adoption of the proposed amendments because they will have access to information which will assist them in making complaints and will allow a better understanding of the process by which complaints are reviewed by the Department. There will be no anticipated cost to persons who are required to comply with the proposed amendments.

SMALL AND MICRO BUSINESSES AND RURAL COMMUNITIES

Mr. Feeney has also determined that for each year of the first five years the rule changes are in effect, there will be no adverse economic effect on small businesses, micro-businesses, or rural communities. There is no economic cost anticipated to the credit union system or to individuals required to comply with the rule changes as proposed.

GOVERNMENT GROWTH IMPACT STATEMENT

Except as may be described below to the contrary, for each year of the first five years that the rules will be in effect, the rules will not:

- Create or eliminate a government program;
- Require the creation of new employee positions or the elimination of existing employee positions;
- Require an increase or decrease in future legislative appropriations to the agency;
- Create new regulations;
- Expand, limit, or repeal an existing regulation;
- Increase fees paid to the department;
- Increase or decrease the number of individuals subject to the rule's applicability; or
- Positively or adversely affect this state's economy.

Written comments on the proposed amendments may be submitted to Harold E. Feeney, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To allow the Commission sufficient time to fully address all the comments it receives, all comments must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register*.

The rule changes are proposed under Texas Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Texas Finance Code Title 2, Chapter 15 and Title 3, Subchapter D.

The statutory provision affected by the proposed amendments is Texas Finance Code, Section 15.409, regarding consumer information and complaints.

§91.121. Complaint Notices and Procedures [Notification].

(a) Purpose. This section implements Finance Code §15.409, which requires the Department to maintain a system to promptly and efficiently act on each complaint filed with the Department. [(a) Definition. For purposes of this section "required notice" means a notice in the form set forth or provided for in subsection (b)(1) of this section].

(b) Required Notice.

(1) Credit unions must provide their members with a notice that substantially conforms to the language and form of the following notice in order to let its members know how to file complaints:

"If you have a problem with the services provided by this credit union, please contact us at:

(Your Name) Credit Union

Mailing Address

Telephone Number or e-mail address

The credit union is incorporated under the laws of the State of Texas and under state law is subject to regulatory oversight by the Texas Credit Union Department. If any dispute is not resolved to your satisfaction, you may also file a complaint against the credit union by contacting the Texas Credit Union Department through one of the means indicated below: In Person or U.S. Mail: 914 East Anderson Lane, Austin, Texas 78752-1699, Telephone Number: (512) 837-9236, Facsimile Number: (512) 832-0278; email: **complaints@cud.texas.gov**, Website: **www.cud.texas.gov**.

(2) The title of this notice shall be "COMPLAINT NOTICE" and must be in all capital letters and boldface type.

(3) The credit union must provide the notice as follows:

(A) In each area where a credit union typically conducts business on a face-to-face basis, the required notice must be conspicuously posted. A notice is deemed to be conspicuously posted if a member with 20/20 vision can read it from the place where he or she would typically conduct business or if it is included in plain view on a bulletin board on which required communications to the membership (such as equal housing posters) are posted.

(B) If a credit union maintains a website, the required notice or a link to the required notice must be conspicuously posted on the homepage of the website.

(C) If a credit union distributes a newsletter, it must include the notice on approximately the same date at least once each year in any newsletter distributed to its members.

(D) If a credit union does not distribute a newsletter, the notice must be included with any privacy notice the credit union is required to provide or send its members.

(c) Filing, receipt, and handling of complaints.

(1) The Department shall make available, on its public website (www.cud.texas.gov) and at its office, information on how to file a complaint.

(2) A person who alleges that a credit union has committed an act, or failed to perform at act that may constitute a violation of the Texas Credit Union Act or Department rules may file a complaint in writing with the Department. The complainant may complete and submit to the Department the complaint form the Department maintains at the Department's office and on its public website, or the complainant may submit a complaint in a letter that addresses the matters

covered by the complaint form. At a minimum, all complaints should contain information necessary for the proper processing of the complaint by the Department, including, but not limited to:

(A) Complainant's name and how the complainant may be contacted;

(B) Name and address of the credit union against whom the complaint is made;

(C) A brief statement of the nature of the complaint and relevant facts, including names of persons with knowledge, times, dates, and location; and

(D) Copies of any documents or records related to the complaint. (original records should not be sent with a complaint.)

(3) Anonymous complaints may be accepted by the Department, but the lack of a witness or the inability of the Department to secure additional information from the anonymous complainant may result in the Department's inability to secure sufficient evidence to pursue action against a credit union.

(4) The Department will review all complaints to determine whether they are within the Department's jurisdiction or authority to resolve, and will send an acknowledgement letter to the complainant within five (5) business days of receipt of a complaint. At least quarterly until final disposition of the complaint, the Department shall provide status updates to the complainant and respondent credit union, orally or in writing.

(5) Upon determining that a complaint is within the Department's jurisdiction, the Department will inform the credit union respondent of the complaint and will request a written response from the credit union. Along with a request for response, the Department will transmit to the credit union a copy of the complaint and any attachments. Within fifteen (15) days from the date of the request for response, unless the period is extended by the Department, the credit union shall provide a substantive response and set forth the credit union's position with respect to the allegations in the complaint, which shall include all data, information and documentation supporting its position, or a description of corrective measures taken or intended to be taken. The Department may request and the complainant and respondent shall provide to the Department additional information or further explanation at any time during the review of the complaint.

(6) Once the Department has received the documentation from both parties, the Department will review the information and will process the complaint in accordance with the rules of the Department. The Department will advise both parties in writing of the final disposition of the complaint.

(7) The Department shall maintain a file on each complaint filed with the agency. The file shall include:

(A) the name of the complainant;

(B) the date the complaint is received by the Department;

(C) the subject matter of the complaint;

(D) a summary of the results of the review of the complaint; and

(E) an explanation of the reason the file was closed, if the Department closed the file without taking action other than to review the complaint.

(8) The Department will maintain a database of complaints in order to identify trends or issues related to violations of state laws under the Department's jurisdiction.

(d) Complaints Closed with No Action Beyond Review. Certain complaints and disputes may be closed with no action taken other than to review the complaint. Such complaints may include those that are not within the Department authority to investigate or adjudicate, and which

may be referred to as non-jurisdictional complaints. The Department, for example, will not address complaints concerning contractual matters or internal credit union practices that are not governed by the statutes or rules that the Department implements or enforces. The Department also may close without taking action other types of complaints, including undocumented factual disputes between a person and a credit union and complaints involving matters that are the subject of a pending lawsuit. The Department does not offer legal assistance and cannot represent individuals in settling claims or recovering damages. The Department does not own, operate, or control credit unions, and the Department does not establish their operating policies and procedures. Therefore, the Department may close without taking action complaints concerning the range of services a credit union offers, complaints about bad customer service, and disagreements over specific credit union policies, practices, or procedures, or about other matters that are not governed by a law or rule under the Department's jurisdiction. The Department will inform the complainant and respondent credit union when a complaint is closed with no action taken, and will inform them of the reason for closing the case.

(e) Privacy. The information collected from complainants and respondents is solicited to provide the Department with information that is necessary and useful in reviewing complaints received from persons regarding their interactions with a credit union. A complainant is not required to give the Department any information; however, without such information, the Department's ability to complete a review, to investigate, or to prosecute a matter may be hindered. It is intended that the information a person provides to the Department will be used within the Department and for the purpose of investigating and prosecuting a complaint. A person should not include personal or confidential information such as social security, credit card, or account numbers, or dates of birth when corresponding with the Department. If it is necessary to supply a document that contains personal or confidential information, the information should be redacted before the document is submitted to the Department.

DEBT CANCELLATION PRODUCTS; FEDERAL PARITY

C. (f) Discussion, Consideration, and Possible Vote to Recommend that the Credit Union Commission Take Action to Approve for Publication and Comment the Proposed Amendments to 7 TAC Section 91.403 Concerning Debt Cancellation Products; Federal Parity.

BACKGROUND: A debt cancellation product is an optional term in a consumer credit agreement that is designed to protect a borrower from defaulting on a loan or paying late fees. Under a debt cancellation product, the borrower voluntarily agrees to pay an additional fee to the credit union in exchange for the credit union's promise to cancel or temporarily suspend payments on the debt. These products may be offered contemporaneously with the underlying credit transaction or after a loan has been closed.

The Texas Department of Insurance has long classified debt cancellation products as insurance, however, the Legislature has not given that agency the authority to license credit unions as underwriters with respect to these products. During the 78th Legislative Session, the Legislature did pass and the governor signed legislation that amended Subtitle B, Title 4 of the Finance Code to carved out a class of lenders who could underwrite debt cancellation products under similar terms and conditions as such products may be offered by a bank. The Texas Credit Union Act (Act), however, specifically provides that the provisions Subtitle B, Title 4 do not apply to loans or extensions of credit written under the Act.

The Department of Insurance has previously acknowledged interpretive ruling issued by the National Credit Union Administration (NCUA) that found that federal credit unions have the legal authority to underwrite debt suspension products as principal and the agency has indicated that it will not challenge these ruling with respect to the power of federal credit unions under their enabling statutes to underwrite these products. Although NCUA has subsequently codified its legal opinions with revisions to Part 721 of its Rules and Regulation (Incidental Powers), the agency has chosen not to adopt comprehensive regulations that govern debt cancellation products but has instead directed federal credit union to review the Office of the Comptroller of the Currency (OCC) rule on debt cancellation programs, 12 C.F.R. Part 37, for guidance as to best practices in the industry regarding these programs.

Beyond the OCC's rule, the Federal Reserve Board issued regulations under the Truth in Lending Act, which creditors must follow when offering debt cancellation products. The Federal Reserve Board's Regulation Z, which largely adopted the principles contained in the OCCs rules, requires several disclosure related to debt cancellation products that apply to debt protection offerings for personal, family, or household purposes, regardless of creditor.

A credit union may invoke the powers of a federal credit union pursuant to Finance Code Section 123.003 (Enlargement of Powers). These are powers specifically granted to a credit union by the Texas Legislature. Thus, by invoking "federal parity" or the enlargement of powers' provision, a credit union may assume the incidental powers of a federal credit union. A credit union may invoke and rely upon the determination of the NCUA that offering debt cancellation products is an incidental power not subject to Department of Insurance regulation.

The Department has been invested by the Texas Legislature with the plenary authority to regulate and examine credit unions to assure their safety and soundness and protect their members, including review of how each credit union exercises their respective incidental powers.

Therefore, the Commission still has authority to regulate the offering and administration of debt cancellation products in the interest of safety and soundness and protecting consumers.

The proposed amendments will update the standards governing debt cancellation products in order to clarify the expectation for credit unions that offer such products to their members. More specifically, the proposed changes to:

1. subsection (a) make clear that credit unions must comply with the Truth in Lending Act (15 U.S.C. 1601) and the applicable provisions of Regulation Z (12 C.F.R. Part 226);
2. subsection (b) removes language that could be construed to prohibit the offering of a no refund debt cancellation product in a manner that is permitted for federal credit unions; and
3. new subsection (f) adopt and incorporate by reference the guidance issued by NCUA in its Letter to Federal Credit Unions No. 03-FCU-06 and directs credit unions to look to 12 C.F.R. Part 37, for guidance as to best practices related to the offer and sale of debt cancellation products.

RECOMMENDED ACTION: The Department requests that the Committee recommend to the Commission approve the proposed amendments for publication and comment.

RECOMMENDED MOTION: I move that the Committee recommend that the Commission take action to approve for publication and comment the proposed amendments to **7 TAC Section 91.403** concerning Debt Cancellation Products; Federal Parity.

TITLE 7. BANKING AND SECURITIES
Part 6. Credit Union Department
Chapter 91. General Rules
Subchapter D. Powers of Credit Unions

The Credit Union Commission (the Commission) proposes amendments to 7 TAC, Chapter 91, Subchapter G, Section 91.403, concerning debt cancellation products consistent with competitive parity with federal credit unions. The amended rule is proposed to update standards governing debt cancellation products to encourage credit unions to provide such products consistent with safe and sound credit union practices and subject to appropriate consumer protections.

A debt cancellation product is a loan term or a contractual arrangement modifying loan terms linked to a credit union's extension of credit, under which the credit union agrees to cancel or suspend all or part of a member's obligation to repay an extension of credit from that credit union upon the occurrence of a specified event. A debt cancellation product includes a debt cancellation contract (DCC) and a debt suspension agreement (DSA).

The Department has long opined that credit unions may enter into debt cancellation contracts to the same extent as federal credit unions. Interpretive rulings issued by the National Credit Union Administration (NCUA) found that a federal credit union may sell debt cancellation products to its member as an activity that is incidental to federal credit union's express power of lending. NCUA codified this authority when it adopted its incidental powers regulation, which expressly noted debt cancellation and debt suspension agreements as permissible loan-related products (12 C.F.R. Section 721.3(g)). Pursuant to the authority set forth in Finance Code §123.003, relating to enlargement of powers and parity, a credit union may offer debt cancellation products. In addition, debt cancellation products are deemed to be loan products and not insurance products. The fee that may be charged with the sale of a debt cancellation is also authorized by Finance Code §124.101, relating to borrower payment of loan expenses.

The proposed amendments to subsection (a) clarify that credit unions must comply with the Truth in Lending Act (15 U.S.C. 1601 and the applicable provisions of Regulation Z (12 C.F.R. Part 226). The proposal also makes clear that a credit union's authority to offer debt cancellation products for a fee is based upon the authority set forth in Finance Code Sections 123.003 and 124.101.

The proposed amendments to subsection (b) removes language that could be construed to prohibit the offering of a no-refund debt cancellation product because such products are permitted for federal credit unions. The amendment reflects an effort to preserve and promote parity with federal credit unions. The amendment clarifies that if the debt cancellation product does provide for a refund of unearned fees, the unearned fees must be calculated using a method that produces a result at least as favorable to the member as the actuarial method.

New subsection (f) designates certain standards that credit unions should look to for guidance and apply as best practices with respect to the offer and sale of debt cancellation products. The Commission believes that guidance is necessary to facilitate members' informed choice about whether to purchase debt cancellation products and to discourage inappropriate or abusive sales practices. In addition, the guidance promotes safety and soundness by encouraging credit unions that provide these products to maintain adequate loss reserves. The proposed rule reflects the Commission's expectation that debt cancellation products will be offered in a safe and sound manner and consistent with appropriate consumer protections. The National Credit Union Administration (NCUA) has provided as guidance to federal credit unions, the requirements set forth in the rules of the U.S. Office of the Comptroller of the Currency (12 C.F.R. Part 37), related to DCCs and DSAs. The Commission adopts and incorporates by reference the guidance issued by NCUA in its Letter to Federal Credit Unions No. 03-FCU-06. The Commission also directs credit unions to look to 12 C.F.R. Part 37, for guidance as to best practices related to the offer and sale of debt cancellation products.

STATE AND LOCAL GOVERNMENTS

Harold E. Feeney, Commissioner, has determined that for each year of the first five years the rule changes are in effect there will be no fiscal implications for state or local government as a result of enforcing or administering the rule changes.

STATEMENT OF PUBLIC COST AND BENEFITS

Mr. Feeney has also determined that for each year of the first five years the rule changes are in effect, the public benefits anticipated as a result of the changes will be clear guidance on best practices by credit unions may implement that are safe and sound and that afford consumer protection with regard to the offer and sale of debt cancellation products. There will be no anticipated cost to persons who are required to comply with the proposed amendments. There is no economic cost anticipated to the credit union system or to individuals required to comply with the rule changes as proposed.

SMALL AND MICRO BUSINESSES, LOCAL ECONOMY, AND RURAL COMMUNITIES

Mr. Feeney has also determined that for each year of the first five years the rule changes are in effect, there will be no adverse economic effect on small businesses, micro-businesses, local economy, or rural communities. There is no economic cost anticipated to the credit union system or to individuals required to comply with the rule changes as proposed.

GOVERNMENT GROWTH IMPACT STATEMENT

Except as may be described below to the contrary, for each year of the first five years that the rules will be in effect, the rules will not:

- Create or eliminate a government program;

- Require the creation of new employee positions or the elimination of existing employee positions;
- Require an increase or decrease in future legislative appropriations to the agency;
- Create new regulations;
- Expand, limit, or repeal an existing regulation;
- Increase fees paid to the department;
- Increase or decrease the number of individuals subject to the rule's applicability; or
- Positively or adversely affect this state's economy.

Written comments on the proposed amendments may be submitted in writing to Harold E. Feeney, Commissioner, Credit Union Department, 914 East Anderson Lane, Austin, Texas 78752-1699 or by email to CUDMail@cud.texas.gov. To be considered, a written comment must be received on or before 5:00 p.m. on the 31st day after the date the proposal is published in the *Texas Register.* At the conclusion of business on the 31st day after the proposal is published in the *Texas Register*, no further written comments will considered or accepted by the commission.

The rule changes are proposed under Finance Code, Section 15.402, which authorizes the Commission to adopt reasonable rules for administering Finance Code Title 2, Chapter 15 and Title 3, Subchapter D of the Texas Finance Code, and under Finance Code Sections 123.003 and 124.001, which authorizes the Commission to adopt rules regarding loans to members.

§91.403. Debt Cancellation Products; Federal Parity; Adoption by Reference.

(a) Authority. Provided it complies with this section, the Truth in Lending Act (15 U.S.C. 1601), and the applicable provisions of Regulation Z (12 C.F.R. Part 226), a credit union may offer any debt cancellation product, including a debt cancellation contract (DCC) and a debt suspension agreement (DSA), a federal credit union is permitted to offer. For the purposes of this section, a debt cancellation product is a two-party agreement between the credit union and the member under which the credit union agrees to waive, suspend, defer, or cancel all or part of a member's obligation to pay an indebtedness under a lease, loan, or other extension of credit upon the occurrence of a specified event. Debt cancellation products are considered loan products governed by this section and applicable provisions of the Finance Code, not insurance products and, consequently, are not regulated by the Texas Department of Insurance. The credit union may offer debt cancellation products for a fee pursuant to the authority set forth in Finance Code §123.003, relating to enlargement of powers and parity and the authority federal credit unions have to offer such products; the fee also is authorized by Finance Code §124.101, relating to borrower payment of loan expenses. If the debt cancellation product is offered for a fee [basis], the [then] member's participation in the debt cancellation program must be optional, and the member must be informed of the fee and that participation is optional.

(b) Anti-tying and Refund Rules. For any debt cancellation product offered by a credit union:

(1) The credit union may not extend credit nor alter the terms or conditions of an extension of credit conditioned upon the member entering into a debt cancellation product with the credit union; and

(2) If the debt cancellation product provides for a refund of unearned fees, the [The debt cancellation product must provide for refunding or crediting to the member any unearned fees resulting from termination of the member's participation in the product, whether by prepayment of the extension of credit or otherwise. Any] unearned fees must be calculated using a method that produces a result at least as favorable to the member as the actuarial method. Before the member purchases the debt cancellation product, the credit union must state in writing that the purchase of the debt cancellation product is optional, the conditions for and method of calculating any refund of the debt cancellation fee, including when fees are considered earned by the credit union, and that the member should carefully review all of the terms and conditions of the debt cancellation agreement prior to signing the agreement.

(c) Notice to Department. A credit union must notify the commissioner in writing of its intent to offer any type of debt cancellation product at least 30 days prior to the product being offered to members. The notice must contain a statement describing the type(s) of debt cancellation product(s) that the credit union will offer to its membership.

(d) Risk Management and Controls. Before offering any debt cancellation products, each credit union's board of directors, shall adopt written policies that establish and maintain effective risk management and control processes for these products. Such processes include appropriate recognition and financial reporting of income, expenses, assets and liabilities, and appropriate treatment of all expected and unexpected losses associated with the products. A credit union should also assess the adequacy of its internal control and risk mitigation activities in view of the nature

and scope of its debt cancellation program. In addition, the policies shall establish reasonable fees, if any, that will be charged, the appropriate disclosures that will be given, and the claims processing procedures that will be utilized.

(e) For purposes of this section "actuarial method" means the method of allocating payments made on a debt between the amount financed and the finance charge pursuant to which a payment is applied first to the accumulated finance charge and any remainder is subtracted from, or any deficiency is added to, the unpaid balance of the amount financed.

(f) Best Practices. The Commission seeks to preserve and promote parity with regard to federal credit unions, foreign credit unions, and other depository institutions, as referenced in Finance Code §§15.402(b-1) and 123.003. The National Credit Union Administration (NCUA) has provided as guidance for federal credit unions the standards set forth in the rules of the U.S. Office of the Comptroller of the Currency (OCC), related to DCCs and DSAs. The Commission, therefore, adopts by reference the guidance issued by NCUA in May 2003 (Letter No. 03-FCU-06). Credit unions should also look to OCC's rules, codified at 12 C.F.R. Part 37, for guidance as to best practices in the industry regarding the offer and sale of DCCs and DSAs. A copy of the NCUA letter and of the OCC rules may be obtained on the Department website at: **www.cud.texas.gov**.

NCUA LETTER TO FEDERAL CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA

DATE: **May 2003** **LETTER NO.: 03-FCU-06**

TO: **Federal Credit Unions**

SUBJ: **Debt Cancellation and Suspension Programs**

ENCL: **Debt Cancellation/Suspension Program Questionnaire**

Dear Board of Directors:

Recently, NCUA examiners were provided with the enclosed questionnaire in an effort to assist them in evaluating Debt/Cancellation Suspension (DCS) programs. This information may be helpful as you evaluate your current DCS or proposed program. The questionnaire is available on the NCUA website at:

http://www.ncua.gov/Resources/Documents/LFCU2003-06ENC.pdf

A brief overview of the operational and potential legal issues associated with DCS programs follows as well as recommended accounting for such programs.

Background and Operational Risks

Debt cancellation or debt suspension products are loan terms or contractual arrangements. These agreements provide for cancellation or suspension of all or part of the member's obligation to repay a loan if a specified event occurs, usually the borrower's death or disability. These products differ from credit life insurance because they do not involve the sale of a third-party insurer's products to the member.

The revisions made to NCUA Rules and Regulations Part 721 codify NCUA legal opinions which provide that federal credit unions may establish DCS programs. These programs have certain inherent risks and should be evaluated prior to implementation.

While debt cancellation is a form of self-insurance, credit insurance is a three-party contract in which an insurance company takes on the underwriting risk. DCS programs, therefore, can pose a greater potential risk. Due to the increased risk, examiners will be reviewing DCS programs differently than credit insurance products, such as credit life and disability.

Debt cancellation products can vary widely by the types of loans and triggering events covered under the terms of the DCS agreement. They can provide for cancellation of all or part of the member's debt upon the occurrence of certain events, such as death, disability, involuntary unemployment, or the total loss of a vehicle. They can also defer all or a portion of monthly payments. Programs could also be established which share qualities of both cancellation and suspension approaches. The benefits can be provided monthly or in a lump sum, and the duration of benefits can be limited or cover the entire loan term. For example, a Guarantee Auto Protection program pays any remaining balance after application of insurance settlements when the member's collateral is destroyed or stolen. Fees for DCS programs are assessed either as a lump sum or in periodic installments.

Credit unions are expected to adhere to safety and soundness principles when managing the risks associated with DCS programs. Likewise, credit unions should establish and maintain effective risk management and control processes over DCS programs. Such processes include appropriate recognition and financial reporting of income, expenses, assets and liabilities, and appropriate treatment of all expected and unexpected losses associated with the products. Credit unions also should assess the adequacy of internal control and risk mitigation activities in view of the nature and scope of DCS programs. Examiners will determine that the credit union's methodologies support participation in DCS programs, as well as policies and procedures for these supporting processes are appropriate.

While stop-loss insurance coverage is not legally required under NCUA Rules and Regulations, credit unions may want to consider such coverage from a third party provider as an appropriate means to effectively manage risk. For credit unions with liability insurance coverage, regardless of the amount, credit union management must have procedures in place to evaluate the third party who provides the coverage. NCUA Letter to Credit Unions 01-CU-20, Due Diligence Over Third Party Service Providers, should be used as guidance for both federal and state-chartered credit unions.

Legal Issues and Compliance Risk

At least one court has established that a debt cancellation agreement is not an insurance product regulated by state insurance regulators. It is, in fact, a two-party contract between the lender and its borrower, outside the purview of insurance laws.

NCUA's Office of General Counsel has determined that insurance coverage is not required for the at-risk balance of loans covered by these programs. Credit unions have the option of insuring all or part of the risk. Expanded examination procedures will be considered when examining those credit unions where full contractual liability coverage is not obtained.

Truth in Lending regulations set forth certain requirements if the fees for these programs are not itemized as a finance charge. These requirements include:

1. A written statement that the DCS is not required by the creditor to obtain the loan,
2. Disclosure of the fee or premium and term of coverage in certain situations, and
3. A signed affirmative request for coverage.

Credit unions should also review the Office of the Comptroller of the Currency rule on DCS programs, 12 C.F.R. Part 37, for guidance as to best practices in the industry regarding these programs at www.occ.treas.gov/ftp/release/2002-73.pdf.

Accounting

Credit unions should account for DCS programs in accordance with Generally Accepted Accounting Principles. Accounting procedures for DCS programs can be complex, and credit unions may want to consider consulting with a CPA or other accounting professional in determining the accuracy of their accounting treatment. Examiners will be evaluating credit union management's provisions for accurate accounting treatment, due diligence, and internal controls over these programs.

If you have any questions on DCS programs, please contact your examiner or NCUA regional office.

Sincerely,

/S/

Dennis Dollar
Chairman

Enclosure

Electronic Code of Federal Regulations

e-CFR data is current as of June 21, 2018

Title 12: Banks and Banking

PART 37—DEBT CANCELLATION CONTRACTS AND DEBT SUSPENSION AGREEMENTS

Contents

AUTHORITY: 12 U.S.C. 1 *et seq.*, 24(Seventh), 93a, 1818.

SOURCE: 67 FR 58976, Sept. 19, 2002, unless otherwise noted.

§37.1 Authority, purpose, and scope.

(a) *Authority.* A national bank is authorized to enter into debt cancellation contracts and debt suspension agreements and charge a fee therefor, in connection with extensions of credit that it makes, pursuant to 12 U.S.C. 24(Seventh).

(b) *Purpose.* This part sets forth the standards that apply to debt cancellation contracts and debt suspension agreements entered into by national banks. The purpose of these standards is to ensure that national banks offer and implement such contracts and agreements consistent with safe and sound banking practices, and subject to appropriate consumer protections.

(c) *Scope.* This part applies to debt cancellation contracts and debt suspension agreements entered into by national banks in connection with extensions of credit they make. National banks' debt cancellation contracts and debt suspension agreements are governed by this part and applicable Federal law and regulations, and not by part 14 of this chapter or by State law.

§37.2 Definitions.

For purposes of this part:

(a) *Actuarial method* means the method of allocating payments made on a debt between the amount financed and the finance charge pursuant to which a payment is applied first to the accumulated finance charge and any remainder is subtracted from, or any deficiency is added to, the unpaid balance of the amount financed.

(b) *Bank* means a national bank and a Federal branch or Federal agency of a foreign bank as those terms are defined in part 28 of this chapter.

(c) *Closed-end credit* means consumer credit other than open-end credit as defined in this section.

(d) *Contract* means a debt] cancellation contract or a debt suspension agreement.

(e) *Customer* means an individual who obtains an extension of credit from a bank primarily for personal, family or household purposes.

(f) *Debt cancellation contract* means a loan term or contractual arrangement modifying loan terms under which a bank agrees to cancel all or part of a customer's obligation to repay an extension of credit from that bank upon the occurrence of a specified event. The agreement may be separate from or a part of other loan documents.

(g) *Debt suspension agreement* means a loan term or contractual arrangement modifying loan terms under which a bank agrees to suspend all or part of a customer's obligation to repay an extension of credit from that bank upon the occurrence of a specified event. The agreement may be separate from or a part of other loan documents. The term *debt suspension agreement* does not include loan payment deferral arrangements in which the triggering event is the borrower's unilateral election to defer repayment, or the bank's unilateral decision to allow a deferral of repayment.

(h) *Open-end credit* means consumer credit extended by a bank under a plan in which:

(1) The bank reasonably contemplates repeated transactions;

(2) The bank may impose a finance charge from time to time on an outstanding unpaid balance; and

(3) The amount of credit that may be extended to the customer during the term of the plan (up to any limit set by the bank) is generally made available to the extent that any outstanding balance is repaid.

(i) *Residential mortgage loan* means a loan secured by 1-4 family, residential real property.

§37.3 Prohibited practices.

(a) *Anti-tying.* 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.

(b) *Misrepresentations generally.* A national bank may not engage in any practice or use any advertisement that could mislead or otherwise cause a reasonable person to reach an erroneous belief with respect to information that must be disclosed under this part.

(c) *Prohibited contract terms.* A national bank may not offer debt cancellation contracts or debt suspension agreements that contain terms:

(1) Giving the bank the right unilaterally to modify the contract unless:

(i) The modification is favorable to the customer and is made without additional charge to the customer; or

(ii) The customer is notified of any proposed change and is provided a reasonable opportunity to cancel the contract without penalty before the change goes into effect; or

(2) Requiring a lump sum, single payment for the contract payable at the outset of the contract, where the debt subject to the contract is a residential mortgage loan.

§37.4 Refunds of fees in the event of termination or prepayment of the covered loan.

(a) *Refunds.* If a debt cancellation contract or debt suspension agreement is terminated (including, for example, when the customer prepays the covered loan), the bank shall refund to the customer any unearned fees paid for the contract unless the contract provides otherwise. A bank may offer a customer a contract that does not provide for a refund only if the bank also offers that customer a *bona fide* option to purchase a comparable contract that provides for a refund.

(b) *Method of calculating refund.* The bank shall calculate the amount of a refund using a method at least as favorable to the customer as the actuarial method.

§37.5 Method of payment of fees.

Except as provided in §37.3(c)(2), a bank may offer a customer the option of paying the fee for a contract in a single payment, provided the bank also offers the customer a *bona fide* option of paying the fee for that contract in monthly or other periodic payments. If the bank offers the customer the option to finance the single payment by adding it to the amount the customer is borrowing, the bank must also disclose to the customer, in accordance with §37.6, whether and, if so, the time period during which, the customer may cancel the agreement and receive a refund.

§37.6 Disclosures.

(a) *Content of short form of disclosures.* The short form of disclosures required by this part must include the information described in appendix A to this part that is appropriate to the product offered. Short form disclosures made in a form that is substantially similar to the disclosures in appendix A to this part will satisfy the short form disclosure requirements of this section.

(b) *Content of long form of disclosures.* The long form of disclosures required by this part must include the information described in appendix B to this part that is appropriate to the product offered. Long form disclosures made in a form that is substantially similar to the disclosures in appendix B to this part will satisfy the long form disclosure requirements of this section.

(c) *Disclosure requirements; timing and method of disclosures*—(1) *Short form disclosures.* The bank shall make the short form disclosures orally at the time the bank first solicits the purchase of a contract.

(2) *Long form disclosures.* The bank shall make the long form disclosures in writing before the customer completes the purchase of the contract. If the initial solicitation occurs in person, then the bank shall provide the long form disclosures in writing at that time.

(3) *Special rule for transactions by telephone.* If the contract is solicited by telephone, the bank shall provide the short form disclosures orally and shall mail the long form disclosures, and, if appropriate, a copy of the contract to the customer within 3 business days, beginning on the first business day after the telephone solicitation.

(4) *Special rule for solicitations using written mail inserts or "take one" applications.* If the contract is solicited through written materials such as mail inserts or "take one" applications, the bank may provide only the short form disclosures in the written materials if the bank mails the long form disclosures to the customer within 3 business days, beginning on the first business day after the customer contacts the bank to respond to the solicitation, subject to the requirements of §37.7(c).

(5) *Special rule for electronic transactions.* The disclosures described in this section may be provided through electronic media in a manner consistent with the requirements of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. 7001 *et seq.*

(d) *Form of disclosures*—(1) *Disclosures must be readily understandable.* The disclosures required by this section must be conspicuous, simple, direct, readily understandable, and designed to call attention to the nature and significance of the information provided.

(2) *Disclosures must be meaningful.* The disclosures required by this section must be in a meaningful form. Examples of methods that could call attention to the nature and significance of the information provided include:

(i) A plain-language heading to call attention to the disclosures;

(ii) A typeface and type size that are easy to read;

(iii) Wide margins and ample line spacing;

(iv) Boldface or italics for key words; and

(v) Distinctive type style, and graphic devices, such as shading or sidebars, when the disclosures are combined with other information.

(e) *Advertisements and other promotional material for debt cancellation contracts and debt suspension agreements.* The short form disclosures are required in advertisements and promotional material for contracts unless the advertisements and promotional materials are of a general nature describing or listing the services or products offered by the bank.

§37.7 Affirmative election to purchase and acknowledgment of receipt of disclosures required.

(a) *Affirmative election and acknowledgment of receipt of disclosures.* Before entering into a contract the bank must obtain a customer's written affirmative election to purchase a contract and written acknowledgment of receipt of the disclosures required by §37.6(b). The election and acknowledgment information must be conspicuous, simple, direct, readily understandable, and designed to call attention to their significance. The election and acknowledgment satisfy these standards if they conform with the requirements in §37.6(d) of this part.

(b) *Special rule for telephone solicitations.* If the sale of a contract occurs by telephone, the customer's affirmative election to purchase may be made orally, provided the bank:

(1) Maintains sufficient documentation to show that the customer received the short form disclosures and then affirmatively elected to purchase the contract;

(2) Mails the affirmative written election and written acknowledgment, together with the long form disclosures required by §37.6 of this part, to the customer within 3 business days after the telephone solicitation, and maintains sufficient documentation to show it made reasonable efforts to obtain the documents from the customer; and

(3) Permits the customer to cancel the purchase of the contract without penalty within 30 days after the bank has mailed the long form disclosures to the customer.

(c) *Special rule for solicitations using written mail inserts or "take one" applications.* If the contract is solicited through written materials such as mail inserts or "take one" applications and the bank provides only the short form disclosures in the written materials, then the bank shall mail the acknowledgment of receipt of disclosures, together with the long form disclosures required by §37.6 of this part, to the customer within 3 business days, beginning on the first business day after the customer contacts the bank or otherwise responds to the solicitation. The bank may not obligate the customer to pay for the contract until after the bank has received the customer's written acknowledgment of receipt of disclosures unless the bank:

(1) Maintains sufficient documentation to show that the bank provided the acknowledgment of receipt of disclosures to the customer as required by this section;

(2) Maintains sufficient documentation to show that the bank made reasonable efforts to obtain from the customer a written acknowledgment of receipt of the long form disclosures; and

(3) Permits the customer to cancel the purchase of the contract without penalty within 30 days after the bank has mailed the long form disclosures to the customer.

(d) *Special rule for electronic election.* The affirmative election and acknowledgment may be made electronically in a manner consistent with the requirements of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. 7001 *et seq.*

[67 FR 58976, Sept. 19, 2002, as amended at 73 FR 22252, Apr. 24, 2008]

§37.8 Safety and soundness requirements.

A national bank must manage the risks associated with debt cancellation contracts and debt suspension agreements in accordance with safe and sound banking principles. Accordingly, a national bank must establish and maintain effective risk management and control processes over its debt cancellation contracts and debt suspension agreements. Such processes include appropriate recognition and financial reporting of income, expenses, assets and liabilities, and appropriate treatment of all expected and unexpected losses associated with the products. A bank also should assess the adequacy of its internal control and risk mitigation activities in view of the nature and scope of its debt cancellation contract and debt suspension agreement programs.

Appendix A to Part 37—Short Form Disclosures

• This product is optional

Your purchase of [PRODUCT NAME] is optional. Whether or not you purchase [PRODUCT NAME] will not affect your application for credit or the terms of any existing credit agreement you have with the bank.

• Lump sum payment of fee

[Applicable if a bank offers the option to pay the fee in a single payment]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You may choose to pay the fee in a single lump sum or in [monthly/quarterly] payments. Adding the lump sum of the fee to the amount you borrow will increase the cost of [PRODUCT NAME].

• Lump sum payment of fee with no refund

[Applicable if a bank offers the option to pay the fee in a single payment for a no-refund DCC]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You may choose [PRODUCT NAME] with a refund provision or without a refund provision. Prices of refund and no-refund products are likely to differ.

• Refund of fee paid in lump sum

[Applicable where the customer pays the fee in a single payment and the fee is added to the amount borrowed]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

[Either:] (1) You may cancel [PRODUCT NAME] at any time and receive a refund; or (2) You may cancel [PRODUCT NAME] within __ days and receive a full refund; or (3) If you cancel [PRODUCT NAME] you will not receive a refund.

• Additional disclosures

We will give you additional information before you are required to pay for [PRODUCT NAME]. [If applicable]: This information will include a copy of the contract containing the terms of [PRODUCT NAME].

• Eligibility requirements, conditions, and exclusions

There are eligibility requirements, conditions, and exclusions that could prevent you from receiving benefits under [PRODUCT NAME].

[Either:] You should carefully read our additional information for a full explanation of the terms of [PRODUCT NAME] *or* You should carefully read the contract for a full explanation of the terms of [PRODUCT NAME].

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Appendix B to Part 37—Long Form Disclosures

• This product is optional

Your purchase of [PRODUCT NAME] is optional. Whether or not you purchase [PRODUCT NAME] will not affect your application for credit or the terms of any existing credit agreement you have with the bank.

• Explanation of debt suspension agreement

[Applicable if the contract has a debt suspension feature]

If [PRODUCT NAME] is activated, your duty to pay the loan principal and interest to the bank is only suspended. You must fully repay the loan after the period of suspension has expired. [If applicable]: This includes interest accumulated during the period of suspension.

• Amount of fee

[For closed-end credit]: The total fee for [PRODUCT NAME] is __.

[For open-end credit, either:] (1) The monthly fee for [PRODUCT NAME] is based on your account balance each month multiplied by the unit-cost, which is ___; *or* (2) The formula used to compute the fee is _____].

• Lump sum payment of fee

[Applicable if a bank offers the option to pay the fee in a single payment]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You may choose to pay the fee in a single lump sum or in [monthly/quarterly] payments. Adding the lump sum of the fee to the amount you borrow will increase the cost of [PRODUCT NAME].

• Lump sum payment of fee with no refund

[Applicable if a bank offers the option to pay the fee in a single payment for a no-refund DCC]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You have the option to purchase [PRODUCT NAME] that includes a refund of the unearned portion of the fee if you terminate the contract or prepay the loan in full prior to the scheduled termination date. Prices of refund and no-refund products may differ.

• Refund of fee paid in lump sum

[Applicable where the customer pays the fee in a single payment and the fee is added to the amount borrowed]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

[Either:] (1) You may cancel [PRODUCT NAME] at any time and receive a refund; or (2) You may cancel [PRODUCT NAME] within __ days and receive a full refund; or (3) If you cancel [PRODUCT NAME] you will not receive a refund.

• Use of card or credit line restricted

[Applicable if the contract restricts use of card or credit line when customer activates protection]

If [PRODUCT NAME] is activated, you will be unable to incur additional charges on the credit card or use the credit line.

• Termination of [PRODUCT NAME]

[Either]: (1) You have no right to cancel [PRODUCT NAME]; *or* (2) You have the right to cancel [PRODUCT NAME] in the following circumstances: _____.

[And either]: (1) The bank has no right to cancel [PRODUCT NAME]; *or* (2)The bank has the right to cancel [PRODUCT NAME] in the following circumstances: _____.

• Eligibility requirements, conditions, and exclusions

There are eligibility requirements, conditions, and exclusions that could prevent you from receiving benefits under [PRODUCT NAME].

[Either]: (1) The following is a summary of the eligibility requirements, conditions, and exclusions. [The bank provides a summary of any eligibility requirements, conditions, and exclusions]; *or* (2) You may find a complete explanation of the eligibility requirements, conditions, and exclusions in paragraphs ___ of the [PRODUCT NAME] agreement.

FINANCE CODE

TITLE 3. FINANCIAL INSTITUTIONS AND BUSINESSES

SUBTITLE D. CREDIT UNIONS

CHAPTER 123. GENERAL POWERS

SUBCHAPTER A. GENERAL POWERS

Sec. 123.001. GENERAL POWERS. A credit union may exercise any power necessary or appropriate to accomplish the purposes for which it is organized and any power granted a corporation authorized to do business in this state, including any power specified in this chapter.

Acts 1997, 75th Leg., ch. 1008, Sec. 1, eff. Sept. 1, 1997.

Sec. 123.002. INCIDENTAL POWERS. A credit union may exercise any right, privilege, or incidental power necessary or appropriate to exercise its specific powers and to accomplish the purposes for which it is organized.

Acts 1997, 75th Leg., ch. 1008, Sec. 1, eff. Sept. 1, 1997.

Sec. 123.003. ENLARGEMENT OF POWERS. (a) A credit union may engage in any activity in which it could engage, exercise any power it could exercise, or make any loan or investment it could make, if it were operating as a federal credit union.

(b) Notwithstanding any other law, and in addition to the powers and authorities conferred under Subsection (a), a credit union has the powers or authorities of a foreign credit union operating a branch in this state if the commissioner finds that exercise of those powers or authorities is convenient for and affords an advantage to the credit union's members and maintains the fairness of competition and parity between the credit union and any foreign credit union. A credit union does not have the field of membership powers or authorities of a foreign credit union operating a branch in this state.

INTERAGENCY AGREEMENT
REGARDING IMPLEMENTATION OF S.B. 1429

OCTOBER 23, 2003

AT THE DIRECTION OF THE GOVERNOR, this Interagency Agreement Regarding Implementation of S.B. 1429 (this "Agreement") is made as of October 23, 2003 by and among the undersigned parties.

WHEREAS, Senate Bill No. 1429, enacted by the Legislature during the 78th Regular Session, permits regulated lenders to offer debt cancellation, debt suspension and gap waiver agreements; and

WHEREAS, the Governor of the State of Texas directed, in his signature message accompanying Senate Bill No. 1429 (attached hereto as Exhibit A), that the Department of Banking, Savings and Loan Department, Office of Consumer Credit Commissioner and Credit Union Department be diligent and aggressive in assuring that consumer protections are in place and that all regulated Texas lenders conduct themselves properly in regards to the activities now permitted under Senate Bill No. 1429, in Texas's quest for a truly competitive market;

NOW, THEREFORE, the parties, in consideration of the mutual covenants and agreements herein contained do mutually agree as follows:

1. **Implementation of SB 1429.** As directed by the Governor, the Texas Department of Banking, Savings and Loan Department, Office of Consumer Credit Commissioner and Texas Credit Union Department hereby agree to be diligent and aggressive in assuring that all applicable consumer protections are in place and that all regulated Texas lenders conduct themselves properly in regards to the activities now permitted under Senate Bill No. 1429, enacted by the Legislature during the 78th Regular Session, in Texas's quest for a truly competitive market. The Department of Insurance agrees to act, upon request, as a resource to such agencies in their efforts under this Agreement.

2. **Contract Period.** This Agreement shall become effective as of the date first referenced above and shall not terminate unless terminated in accordance with the provisions herein.

3. **Termination.** This Agreement may be terminated by any party upon thirty (30) days written notice to any other party.

4. **Amendments.** No amendment, change or modification to this Agreement may be made except in a writing signed by the parties.

5. **Counterparts.** This Agreement may be executed in any number of counterparts, each of which shall be enforceable, and all of which together shall constitute one instrument.

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IN WITNESS WHEREOF, the parties have duly executed and delivered this Interagency Agreement Regarding Implementation of S.B. 1429 as of the date first set forth above.

Texas Department of Banking

Name: RANDALL S. JAMES
Title: BANKING COMMISSIONER

Date: 10/22/2003

Office of Consumer Credit Commissioner

Name: LESLIE PETTIJOHN
Title: CONSUMER CREDIT COMMISSIONER

Date: 10/23/03

Savings and Loan Department

Name: DOUGLAS B. FOSTER
Title: INTERIM COMMISSIONER

Date: 23 October 2003

Texas Credit Union Department

Name: HAROLD E. FEENEY
Title: COMMISSIONER

Date: OCTOBER 23, 2003

Texas Department of Insurance

Name:
Title:

Date: October 24, 2003

AS DIRECTED AND APPROVED BY THE GOVERNOR:

Rick Perry
Governor

EXHIBIT A:

GOVERNOR'S SIGNATURE MESSAGE
ACCOMPANYING SB 1429

STATE OF TEXAS

OFFICE OF THE GOVERNOR

MESSAGE

I am signing Senate Bill No. 1429 which permits regulated lenders, including banks, savings banks and finance companies, to offer debt cancellation, debt suspension and gap waiver agreements.

Currently, national lending institutions are permitted to offer these types of agreements. I believe it is important that Texas lenders remain competitive with their national counterparts while maintaining strong safeguards to protect the consumers of the state of Texas.

By way of this message, I am directing the Department of Banking, Savings and Loan Department, Office of Consumer Credit Commissioner and the Credit Union Department to be diligent and aggressive in assuring that consumer protections are in place and that all Texas lenders conduct themselves properly in our quest for a truly competitive market.

IN TESTIMONY WHEREOF, I have signed my name officially and caused the Seal of the State to be affixed hereto at Austin, this 20th day of June, 2003.

Rick Perry

RICK PERRY
Governor of Texas

ATTESTED BY:

Gwyn Shea

GWYN SHEA
Secretary of State

FILED IN THE OFFICE OF THE SECRETARY OF STATE
3:30 p.m. O'CLOCK
JUN 21 2003

NEXT MEETING AND ADJOURNMENT

C. (g) Discussion of and Vote to Establish Date for Next Committee Meeting.

BACKGROUND: If necessary, the next regular meeting of the Committee will be scheduled for November 1, 2018, at 1:00 p.m. in Austin.

ADJOURNMENT