

**Handout for MBL Rulemaking Meeting  
June 9, 2016 1:30pm to 3:00 pm  
Department of Financial Institutions Room 319**

1. Compare 12 CFR 723.6 to WAC 208-460-030 Development and Construction Lending – see pages 1-5
2. Compare 12 CFR 723.5 to WAC 208-460-060 Secured and Unsecured Standards – see page 6-15

Federal (2016)	State	Proposed
<p style="text-align: center;"><b>§ 723.6—Construction and Development Loans</b></p> <p>In addition to the foregoing, the following requirements apply to a construction and development loan made by any federally insured credit union.</p> <p>(a) For the purposes of this section, 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, such as 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 section. The collateral valuation for securing a construction or development loan</p>	<p style="text-align: center;"><b>WAC 208-460-030 What are the requirements for MBL development &amp; construction lending?</b></p> <p>Unless the director grants a waiver, a credit union that makes MBL development or construction loans is subject to the following requirements:</p> <p>(1) The aggregate of all such loans may not exceed fifteen percent of net worth. To determine the aggregate, you may exclude any portion of a loan that is:</p> <p>(a) Secured by shares or deposits in the credit union making the extension of credit or in other credit unions, and by deposits in other financial institutions; or</p> <p>(b) Insured or guaranteed, or subject to an advance commitment to purchase, by any federal or state agency (or any political subdivision of a state);</p> <p>(2) The borrower on such loans must have a minimum of:</p> <p>(a) Thirty percent equity interest in the project being financed if the loan is for land development; and</p>	<p style="text-align: center;"><b>WAC 208-460-030 Requirements for MBL Development &amp; Construction</b></p> <p>Unless the director grants a waiver pursuant to WAC 208-460-090, a credit union that makes commercial land development or construction loans is subject to the following requirements:</p> <p>(1) Aggregate credit union limit. The aggregate of all such loans may not exceed fifteen percent of net worth. To determine the aggregate amount, a credit union may exclude any portion of a loan that is:</p> <p>(a) Secured by shares or deposits in the credit union making the extension of credit; or</p> <p>(b) Insured or guaranteed, or subject to an advance commitment to purchase, by any federal or state agency (or any political subdivision of a state);</p> <p>(2) Equity interest of the borrower. The borrower on such loans must have a</p>

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<p>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 improvements to an existing income producing property that does not change its use or materially impact the property is not a construction or development loan.</p> <p>(b) A federally insured credit union that elects to make a construction or development loan must ensure that its commercial loan policy includes adequate provisions by which the collateral value associated with the project is properly determined and established. For a construction or development loan, collateral value is the lesser of the project's cost to complete or its prospective market value.</p> <p>(1) For the purposes of this section, 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 general contractor's fees, and other expenses</p>	<p>(b) Twenty-five percent equity interest in the project being financed if the loan is for construction or for a combination of development and construction;</p> <p>(3) The funds for such loans may be released only after on-site inspections, documented in writing, by qualified personnel and according to a preapproved draw schedule and any other conditions as set forth in the loan documentation; and</p> <p>(4) The credit union may not make such loans unless it utilizes the services of an individual with at least five years direct experience in development and construction lending.</p>	<p>minimum of:</p> <p>(a) Twenty-five percent equity interest in the project being financed, if the loan is for land development or a combination of land development and construction.</p> <p>(b) Twenty percent equity interest in the project being financed if the loan is for a construction project that is commercial or multifamily in nature (including condominiums, planned unit developments, and cooperatives) or has another nonresidential purpose (e.g., an office building, retail strip-mall, warehouse, or manufacturing facility).</p> <p>(c) Fifteen percent equity interest in the project being financed, if the loan is for one-to-four family residential speculative construction;</p> <p>(3) Draw inspections and release of funds. The funds for such loans may be released only after on-site inspections, documented in writing, by qualified personnel and according to a preapproved draw schedule and any other conditions as set forth in the loan documentation, with confirmation prior to each loan</p>

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<p>normally included in a construction contract such as bonding and contractor insurance. Qualifying costs include the value of the land, determined as the lesser of appraised market value or purchase price plus the cost of any improvements. Qualifying costs also include interest, 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 estate 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</p>		<p>disbursement that no intervening liens have been filed; and</p> <p>(4) Credit union experience. A credit union may not make such loans unless it utilizes the services of qualified staff or qualified independent contractors with direct experience in development and construction lending.</p> <p>(5) Determination of collateral value. For a land development or construction loan, the collateral value is the lesser of the project’s cost to complete or its prospective market value. For purpose of this section: (a) The “project’s cost to complete” means the sum of all qualifying costs necessary to complete a construction project as documented in an approved budget; and (b) the “prospective market value” means the market value opinion determined by an independent appraiser in compliance with the standards set for in the Uniform Standards of Professional Appraisal Practice (USPAP).</p>

<b>Federal (2016)</b>	<b>State</b>	<b>Proposed</b>
<p>sales proceeds such as brokerage commissions and other closing costs.</p> <p>(2) For the purposes of this section, 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 prospective value opinions may be required to reflect the time frame during which development, construction, and occupancy occur. The prospective market value “as completed” reflects the property’s market value as of the time that development is to be completed. The prospective market value “as-stabilized” reflects the property’s market value as of the time the 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 property is exposed to the market for lease over a reasonable period of time and at comparable terms and conditions to other similar properties.</p> <p>(c) A federally insured credit union that elects to make a construction and</p>		

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<p>development loan must also assure its commercial loan policy meets the following conditions:</p> <p>(1) Qualified personnel representing the interests of the federally insured credit union must conduct a review and approval of any line item construction budget prior to closing the loan;</p> <p>(2) A credit union approved requisition and loan disbursement process is established;</p> <p>(3) Release or disbursement of loan funds occurs only after on-site inspections, documented in a written report by qualified personnel representing the interests of the federally insured credit union, certifying 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</p> <p>(4) Each loan disbursement is subject to confirmation that no intervening liens have been filed.</p>		

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<p><b>§ 723.5 Collateral and Security</b></p> <p>(a) A federally insured credit union must require collateral commensurate with the level of risk associated with the size and type of any commercial loan. Collateral must be sufficient to ensure adequate loan balance protection along with appropriate risk sharing with the borrower and principal(s). A federally insured credit union making an unsecured loan must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.</p> <p>(b) A federally insured credit union that does not require the full and unconditional personal guarantee from the principal(s) of the borrower who has a controlling interest in the borrower must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.</p> <p>(1) <i>Transitional provision.</i> A federally insured credit union that, between May 13, 2016 and January 1, 2017, makes a member business loan and does not require the full and unconditional</p>	<p><b>WAC 208-460-060 What are the collateral and security requirements?</b></p> <p>Unless the director grants a waiver:</p> <p>(1) All member business loans must be secured by collateral in accordance with this section, except the following:</p> <p>(a) A credit card line of credit granted to non-natural persons that is limited to routine purposes normally made available under such lines of credit; and</p> <p>(b) A loan made by a credit union where the loan and the credit union meet each of the following criteria:</p> <p>(i) The amount of the loan does not exceed one hundred thousand dollars;</p> <p>(ii) The aggregate of unsecured MBL under (b) of this subsection does not exceed ten percent of the credit union's net worth;</p> <p>(iii) The credit union has a net worth of at least seven percent; and</p> <p>(iv) The credit union submits reports to the division of credit unions with its NCUA 5300 reports, providing figures and other detail as may be requested by the director to demonstrate compliance with (b) of this subsection;</p>	<p><b>WAC 208-460-060 Standards for secured and unsecured lending</b></p> <p>(1) <b>Personal guarantees.</b> If a credit union requires personal guarantee(s) in connection with a commercial loan where the borrower is an entity other than an individual, the personal guarantee(s) must be from individual(s) who are controlling persons of the borrower-entity, and may be from individual(s) who are not controlling person(s) if deemed commercially reasonable under the circumstances and not otherwise impermissible under applicable law. A credit union that does not require a full and unconditional personal guarantee in connection with the loan must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.</p> <p>(2) <b>Secured lending.</b> In relation to commercial loans secured by collateral of</p>

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<p>personal guarantee from the principal(s) of the borrower who has a controlling interest in the borrower is not required to seek a waiver from the requirement for personal guarantee, but it must determine and document in the loan file that mitigating factors sufficiently offset the relevant risk.</p>	<p>(2) In the case of a member business loan secured by collateral on which the credit union will have a first lien, you may grant the loan with a LTV ratio in excess of eighty percent only where the value in excess of eighty percent is:</p> <p>(a) Covered through acquisition of private mortgage or equivalent type insurance provided by an insurer acceptable to the credit union; or</p> <p>(b) Insured or guaranteed, or subject to advance commitment to purchase, by any federal or state agency (or any political subdivision of a state).</p> <p>In no case may the LTV ratio exceed ninety-five percent;</p> <p>(3) In the case of a member business loan secured by collateral on which the credit union will have a second or lesser priority lien, you may not grant the loan with a LTV ratio in excess of eighty percent; and</p> <p>(4) In the case of member business loans secured by the same collateral:</p> <p>(a) On which the credit union will have a first lien as well as other lesser priority liens, you may grant the loans with a LTV ratio in excess of eighty percent only if subsection (2)(a) or (b) of this section is satisfied. In no case may the LTV ratio exceed ninety-five percent; and</p> <p>(b) On which the credit union will have</p>	<p>any kind, the following standards are applicable:</p> <p>(a) <b>Collateral standards in general.</b> All secured commercial loans must be secured by collateral commensurate with the level of risk associated with the size and type of any commercial loan. Collateral must be sufficient to ensure adequate loan balance protection along with appropriate risk sharing with the borrower and the principal or principals.</p> <p>(b) <b>Real estate as collateral – loan-to-value limits.</b> A credit union’s lending policies must contain internal loan-to-value limits for the making of commercial loans having real estate as collateral, and these internal loan-to-value limits must be applied to the underlying real estate that collateralizes the commercial</p>

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	<p>lesser priority liens but no first lien, you may not grant the loans with a LTV ratio in excess of eighty percent.</p>	<p>real estate loans the credit union makes.</p> <p>(i) <b>Commercial real estate loan-to-value limits.</b> A credit union's internal loan-to-value limits for commercial real estate loans must not exceed the following limits: (see chart below)</p> <p>(c) <b>Non-real estate collateral loan-to-value limits.</b> A credit union's lending policies must contain internal loan-to-value collateral and these internal loan-to-value limits must be applied to the underlying personal property that collateralizes the commercial real estate loans the credit union makes. The loan-to-value limit for commercial loans with non-real estate collateral should not exceed eighty percent.</p> <p>(d) <b>Transactions excluded from the loan-to-value limits listed in subsections (2)(b) and (2)(c) above.</b> There are a number of commercial lending</p>



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		<p>situations in which other factors significantly outweigh the need to apply the loan-to-value limits. These include but are not limited to the following:</p> <ul style="list-style-type: none"> <li>(i) A commercial loans guaranteed or insured by the U.S. government or its agencies (e.g., the Small Business Administration), provided that the amount of the guaranty or insurance is at least equal to the portion of the loan that exceeds the loan-to-value limits listed in sections (2)(b) and (2)(c) above;</li> <li>(ii) A commercial loans backed by the full faith and credit of a state government, provided that the amount of the assurance is at least equal to the portion of the loan that exceeds the credit union's loan-to-value limit;</li> <li>(iii) A commercial loan guaranteed or insured by a state, municipal or local government, or an agency thereof, provided that the amount of the guaranty or insurance is at least equal to the portion of the loan that exceeds the loan-to-value limits listed in subsections (2)(b) and (2)(c) above, and provided that the credit union has determined that the guarantor</li> </ul>

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		<p>or insurer has the financial capacity to perform under the terms of the guaranty or insurance agreement;</p> <p>(iv) A commercial loan adequately insured by private mortgage insurance or equivalent type of insurance, and provide that the credit union has reasonably determined that the private mortgage insurer has the capacity to perform under the terms of the insurance policy and that the terms and conditions of the policy are commercially reasonable within the industry for the type of commercial loan in question.</p> <p>(v) A commercial loan that is to be sold promptly after origination, without recourse, to a financially responsible third party who has made a commitment to purchase the loan prior to or contemporaneously with the loan's origination;</p> <p>(vi) A commercial loans that is renewed, refinanced, or restructured without the advancement of new funds or an increase in the line of credit (except for reasonable closing costs), or commercial loan that is renewed, refinanced, or restructured in</p>

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		<p>connection with a workout situation, which is part of a clearly defined and well-documented program to achieve orderly liquidation of a commercial loan debt, reduce risk of loss, or maximize the recovery on a commercial loan;</p> <p>(vii) A commercial loan that facilitates the sale of real estate or personal property acquired by the credit union in the ordinary course of collecting a debt; and</p> <p>(viii) A commercial loan for which a waiver of an applicable loan-to-value limit set forth in subsections (2)(b) and (c) of this section has been granted pursuant to WAC 208-460-090.</p> <p><b>(3) Unsecured lending standards.</b> A credit union making an unsecured commercial loan must determine and document in the loan file that mitigating factors sufficiently offset the relevant risks. All unsecured commercial loans, including but not limited to a credit card line of credit, must meet the following conditions:</p> <p>(a) The amount of an</p>

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		<p>unsecured commercial loan may not exceed two hundred fifty thousand dollars;</p> <p>(b) The aggregate of all unsecured commercial loans of a credit union may not exceed ten percent of the credit union's net worth; and</p> <p>(c) The credit union must have a net worth ratio of at least eight percent.</p>

Loan Category	Loan-to-Value Limit
Raw land	70%

Land development	75%*
Construction:	
Commercial, multifamily (including condominiums, planned unit developments, and cooperatives) and other nonresidential projects	80%*
One-to-four family residential (speculative) construction	85%*
Combined land development and construction	75%*
Existing commercial-purpose buildings	85%
Agricultural real estate (excluding crops)	80%*

\* See WAC 208-460-030(2).

Federal (2016) definitions	State definitions	Proposed definitions
<i>Commercial loan</i> means any loan, line of credit, or letter of credit (including any unfunded commitments), and any		<b>“Commercial loan”</b> means any loan, line of credit, letter of credit (including any unfunded commitments), or other

<p>interest a credit union obtains in such loans made by another lender, to individuals, sole proprietorships, partnerships, corporations, or other business enterprises for commercial, industrial, agricultural, or professional purposes, but not for personal expenditure purposes. Excluded from this definition are loans made by a corporate credit union; loans made by a federally insured credit union to another federally insured credit union; loans made by a federally insured credit union to a credit union service organization; loans secured by a 1- to 4-family residential property (whether or not it is the borrower's primary residence); loans fully secured by shares in the credit union making the extension of credit or deposits in other financial institutions; loans secured by a vehicle manufactured for household use; and loans that would otherwise meet the definition of commercial loan and which, when the aggregate outstanding balances plus unfunded commitments less any portion secured by shares in the credit union to a borrower or an associated borrower, are equal to less than \$50,000.</p>		<p>extension of credit, and any interest a credit union obtains in such an extension of credit made by another lender, for commercial, industrial, agricultural, or professional purposes, but not for personal, family or household purposes, provided that "commercial loan" specifically excludes: loans made by a corporate credit union; loans made by a federally insured credit union to another federally insured credit union; loans made to a credit union service organization; loans secured by a one-to-four family residential property (whether or not it is the borrower's primary residence); loans fully secured by shares in the credit union making the extension of credit; loans secured by a vehicle manufactured for household use and which is not part of a fleet of vehicles; and loans that would otherwise meet the definition of "commercial loan" and which, when the aggregate outstanding balances plus unfunded commitments less any portion secured by shares in the credit union to a borrower or an associated borrower, equal an amount less than \$50,000.</p> <p><b>"Agricultural real estate"</b> means real property which the primary (51% or more) use is for agricultural purposes, including, without limitation, farming, livestock, grazing, or aqua-culture.</p>
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