NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

Loans to officials

March 26, 1992

George Mann
President
L & N Federal Credit Union
4700 Southern Parkway
Louisville, KY 40214

Re: Loan to Officials (Your February 28, 1992, Letter)

Dear Mr. Mann:

According to your letter, L & N Federal Credit Union (the FCU) would like to make a loan to a corporation which was formed to purchase a golf course. Of the 47 investors in the corporation, 41 are members of the FCU. Six of those are on the FCU's board. In light of the board members' pecuniary interest in the transaction, you have asked whether the loan may be made.

The fact that not all of the investors in the corporation are members of the FCU raises a preliminary question about the permissibility of the loan. With exceptions not relevant here, Section 107(5) of the FCU Act, 12 U.S.C. §1757(5), only authorizes an FCU to make loans to its members. Assuming the six nonmember investors are eligible for membership and the FCU's field of membership includes "organizations of such persons," the loan would constitute a member loan. If either of those conditions is not met, the corporation itself would have to become a member of the FCU. A request to amend the field of membership should be directed to the NCUA's regional office in Atlanta.

The fact that the proceeds of the loan will be used for a commercial purpose raises a second preliminary question about the permissibility of the loan. Section 701.21(h)(4)(i) of the National Credit Union Administration (NCUA) Rules and Regulations, 12 C.F.R. §701.21(h)(4)(i), prohibits an FCU from making a member business loan to any member of the board of directors who is compensated as such or to any associated member of such an individual. If any FCU board member who has invested in the corporation is compensated solely for his

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or her service on the board, the FCU may be prohibited from making the loan to the corporation.

The next question raised is that of approval of the loan. Sections 107(5)(A)(iv) and (v) of the FCU Act require the approval of the board of directors in any case where the aggregate of loans to an official and loans on which that official serves as endorser or guarantor exceeds $10,000 plus pledged shares. Your letter does not state the amount of the loan, but does state that the purpose of the loan is to refinance a variable-rate loan of $455,000. Presumably the FCU's loan would approximate that amount, thus requiring board approval.

This requirement creates a dilemma, however, as Article XIX, Section 4, of the Standard FCU Bylaws prohibits a board member from participating in the deliberation upon or the determination of any question affecting his or her pecuniary interest or the pecuniary interest of any corporation in which he is interested. Thus, the six board member investors are prohibited from determining whether the loan should be approved. While the remaining director has the authority to provide that approval, we recommend that board decisions made in such circumstances be ratified by the membership. We understand that the membership has done so in this case. Therefore, if the membership requirement is met and no board member investor is compensated, the loan meets NCUA's legal requirements. It remains the responsibility of the NCUA examiner and regional office to address any safety and soundness concerns.

Sincerely,

Hattie M. Ulan

Hattie M. Ulan
Associate General Counsel

GC/LH:sg
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92-0308

cc: Board Member Swan
Region III Director