



**State of Wisconsin**  
*Department of Financial Institutions*

Scott McCallum, Governor

John F. Kundert, Secretary

April 17, 2002

Representative Scott R. Jensen  
Room 211 West  
State Capitol  
P.O. Box 8952  
Madison 53708-8952

Senator Fred Risser  
Room 220 South  
State Capitol  
P.O. Box 7882  
Madison 53707-7882

Re: Notice of Proposed Rule

Dear Representative Jensen and Senator Risser:

Pursuant to ss. 227.19(2) and (3), Stats., notice is hereby given that CR 02-034 (proposed rule creating ch. DFI—CU 72) is in final draft form. The following documentation accompanies this notice in triplicate:

- report to the legislature
- proposed rule with analysis, note regarding form, and fiscal estimate
- recommendations of legislative council staff

If you have any questions regarding this matter or the enclosed, please do not hesitate to contact me at tel. 267-1705.

Sincerely,

Mark Schlei  
Deputy General Counsel

encls

DATE: April 17, 2002

TO: Senator Fred Risser, President  
Wisconsin State Senate

Representative Scott Jensen, Speaker  
Wisconsin State Assembly

FROM: Mark Schlei, Deputy General Counsel  
Department of Financial Institutions

SUBJECT: Report on CR 02-034

This report is submitted pursuant to s. 227.19 (2) and (3), Stats., regarding CR 02-034 (proposed rule creating ch. DFI—CU 72), relating to member business loans.

1. STATEMENT EXPLAINING THE NEED FOR THE PROPOSED RULE

CR 02-034 provides certain criteria, exemptions, prohibitions and waivers; establishes procedures for programs and criteria for policies; sets forth collateral, security and record keeping requirements; and sets forth limitations, calculations and classifications relating to member business loans. The rule would be the implementing provision under state law authorizing credit unions to make loans to their members. The promulgation of this rule has been approved by the Credit Union Review Board..

2. MODIFICATIONS MADE AS A RESULT OF TESTIMONY RECEIVED AT THE PUBLIC HEARING

No modifications were made as a result of testimony received at the public hearing.

3. PERSONS APPEARING OR REGISTERING FOR OR AGAINST THE PROPOSED RULE AT THE PUBLIC HEARING

The following persons appeared or registered for the proposed rule:

Randy Beck, Royal Credit Union  
David Cogging, Business Lending Group, Inc.  
Larry Anderson, Westby Credit Union  
Paul Newkirk, Westby Credit Union  
Daniel Milbrandt, Blackhawk Credit Union  
Sean Rathjen, Blackhawk Credit Union  
Brett Thompson, Wisconsin Credit Union League

Community First Credit Union  
Tim Wyngaard, Capital Credit Union  
David Kolar, Kohler Credit Union  
Catherine Tierney, Community First Credit Union  
David hall, University of Wisconsin Credit Union  
Eric Chrisinger, Co-op Credit Union  
Chip Coenen, Credit First Credit Union  
Max Michaelson, Co-op Credit Union  
Brian Prunty, CoVantage Credit Union  
Scott D. Edwards, Community First Credit Union  
Todd Miller, Community First Credit Union  
Anthony T. Busch, community First Credit Union  
Sam Huntington, CUNA Credit Union  
Ken Eiden, Banta Community Credit Union and BLG

The following persons appeared or registered against the proposed rule:

Cheryl McCollum, Wisconsin Bankers Association  
Rose Oswald Poels, Wisconsin Bankers Association  
Daryll Lund, Community Bankers of Wisconsin

#### 4. RESPONSE TO LEGISLATIVE COUNCIL RECOMMENDATIONS

Legislative council staff recommendations were accepted in whole except for modifications to industry terms.

#### 5. FINAL REGULATORY FLEXIBILITY ANALYSIS

Pursuant to s. 227.19(3m), a final regulatory flexibility analysis is not required.

PROPOSED RULE  
STATE OF WISCONSIN  
OFFICE OF CREDIT UNIONS

An order to create ch. DFI—CU 72 relating to member business loans. Analysis: Statutory authority: ss. 186.115(1) and (2), 186.235(8) and 227.11(2), Stats. Statutes interpreted: ss. 186.115(1) and (2), 186.235(8), Stats. Summary: The rule provides certain criteria, exemptions, prohibitions and waivers; establishes procedures for programs and criteria for policies; sets forth collateral, security and record keeping requirements; and sets forth limitations, calculations and classifications relating to member business loans. The rule would be the implementing provision under state law authorizing credit unions to make loans to their members. The promulgation of this rule has been approved by the Credit Union Review Board. Agency person to be contacted for substantive questions and responsible for the agency's internal processing: Ginger Larson, Director, Office of Credit Unions, tel. (608) 261-9543. Pursuant to the statutory authority referenced above, the Office of Credit Unions adopts the following:

SECTION 1: CHAPTER DFI—CU 72 is created to read:

CHAPTER DFI—CU 72

MEMBER BUSINESS LOANS

**DFI-CU 72.01 Definitions.** In this chapter:

- (1) "Amount" of a business loan includes all the following:
  - (a) Any unfunded commitment to make the loan.
  - (b) The outstanding balance of the loan.
  - (c) Any undisbursed proceeds of the loan.
- (2) "Associated member" means a person who is associated with another by means of a shared ownership, investment or other pecuniary interest in a business or commercial endeavor.
- (3) "Business purpose loan" means a loan where the borrower intends to use the proceeds for any of the purposes listed in s. DFI-CU 72.02(1).
- (4) "Construction or development loan" means a financing arrangement for acquiring real property or rights to real property, including land or structures, with the intent to develop or improve it for any of the following:
  - (a) Residential housing for sale.

(b) Income property.

(c) Commercial use.

(d) Industrial use.

(e) Any similar uses.

(5) "Director" means the director of the office of credit unions or an authorized representative of the director.

(6) "Loan-to-value ratio" or "LTV ratio" means the amount of all loans by the credit union secured by an item of collateral added to the amount of all outstanding loans by other lenders secured by that item of collateral, that total amount then being divided by the market value of that item of collateral.

(7) "Member business loan" has the meaning set forth in s. DFI—CU 72.02.

(8) "NCUA" means the National Credit Union Administration.

(9) "Net worth" means the retained earnings as defined under Generally Accepted Accounting Principles. Retained earnings include undivided earnings, regular reserves and any other appropriations designated by management or regulatory authorities.

**DFI-CU 72.02 Member business loan.** (1) "Member business loan" means any loan, line of credit, letter of credit or any unfunded commitment to make a loan, where the borrower intends to use the proceeds for any of the following purposes:

(a) Commercial.

(b) Corporate.

(c) Investment property.

(d) Business venture.

(e) Agricultural.

(2) "Member business loan" shall not include any of the following:

(a) A business purpose loan fully secured by a lien on a 1 to 4 family dwelling that is the member's primary residence.

(b) A business purpose loan fully secured by shares or deposits in the credit union making the extension of credit or in other credit unions, or by deposits in other financial institutions.

(c) One or more business purpose loans to a member or an associated member that, in the aggregate, are less than \$50,000. The entire amount of such a loan or loans that equals or exceeds this amount, or that causes the aggregate to exceed this amount is a business loan.

(d) A business purpose loan where a federal or state agency or any of their political subdivisions fully insures repayment, or fully guarantees repayment, or provides an advance commitment to purchase in full.

(e) A loan granted by a corporate credit union to another credit union.

**DFI-CU 72.03 Prohibited member business loans. (1) OFFICERS.** A credit union shall not grant a member business loan to any of its following:

(a) Chief executive officer.

*Example: President, Treasurer or Manager.*

(b) Assistant chief executive officers.

*Example: Assistant President, Vice President, Assistant Treasurer or Assistant Manager.*

(c) Chief financial officer.

*Example: Comptroller.*

(d) Any associated member or immediate family member of anyone listed in this subsection.

**(2) EQUITY AGREEMENTS OR JOINT VENTURES.** A credit union shall not grant a member business loan if any additional income received by the credit union or its senior management employees is tied to the profit or sale of the business or commercial endeavor for which the loan is made.

**(3) DIRECTORS.** A credit union shall not grant a member business loan to one of its directors unless the board of directors approves granting the loan and the director is recused from the decision-making process.

**DFI-CU 72.04 Construction and development loans.** Unless the director grants a waiver, a credit union that makes construction or development loans shall be subject to all of the following:

**(1)** The aggregate of all construction and development loans shall not exceed 15% of the credit union's net worth. In determining the aggregate, the credit union may exclude any portion of a loan that is any of the following:

(a) Secured by shares or deposits in the credit union making the extension of credit or in other credit unions, or by deposits in other financial institutions.

(b) Insured or guaranteed by any agency or subdivision of the state or the federal government.

(c) Subject to an advance commitment to purchase by any agency of the federal government, the state, or any of their political subdivisions.

(2) The borrower shall have a minimum of the following:

(a) 30% equity interest in the project being financed if the loan is for land development.

(b) 25% equity interest in the project being financed if the loan is for construction or for a combination of development and construction.

(3) The funds shall 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.

(4) The credit union shall not make construction or development loans unless it utilizes the services of an individual with at least five years direct experience in construction and development lending.

**DFI-CU 72.05 Implementation of a member business loan program.** (1) The board of directors shall adopt a specific member business loan policy and review it at least annually.

(2) In making member business loans, the credit union shall utilize the services of an individual with at least two years direct experience with the type of lending in which it will engage, except as provided s. DFI-CU 72.04(4).

(3) A credit union does not have to hire staff to meet the requirements of this section. However, credit unions shall ensure that expertise with the type of lending in which it will engage is available.

*Example: A credit union may meet the experience requirement through various approaches, such as the services of a credit union service organization, an employee of another credit union, an independent contractor or other third parties.*

(4) The actual decision to grant a loan shall reside solely with the credit union.

**DFI-CU 72.06 Member business loan policy requirements.** A credit union's member business loan policy shall include all of the following:

- (1) The types of business loans the credit union will make.
- (2) The credit union's trade area.
- (3) The maximum amount of the credit union's assets, in relation to net worth, that it will invest in member business loans.
- (4) The maximum amount of the credit union's assets, in relation to net worth, that it will invest in a given type of business loan.
- (5) The maximum amount of the credit union's assets, in relation to net worth, that it will loan to a member or associated members, subject to s. DFI-CU 72.08.
- (6) The qualifications and experience of personnel involved in making and administering business loans.
- (7) A requirement for analysis and documentation of the ability of the borrower to repay the loan.
- (8) A requirement for the receipt and periodic updating of financial statements and other documentation, including tax returns.
- (9) A requirement for documentation sufficient to support each request to extend credit, or increase an existing loan or line of credit, except where the board of directors finds that the required documentation is not generally available for a particular type of loan and states the reasons for those findings in the credit union's written policies. The documentation shall include all of the following:
  - (a) Balance sheet.
  - (b) Cash flow analysis.
  - (c) Income statement.
  - (d) Tax data.
  - (e) Analysis of leveraging.
  - (f) Comparison with industry average or similar analysis.
- (10) Collateral requirements, including all of the following:
  - (a) Loan-to-value ratios.
  - (b) Determination of value.

- (c) Determination of ownership.
  - (d) Steps to secure various types of collateral.
  - (e) A schedule as to how often the credit union will reevaluate the value and marketability of collateral.
- (11) The interest rates and maturities of the business loans.
  - (12) General loan procedures, including all of the following:
    - (a) Loan monitoring.
    - (b) Servicing and follow-up.
    - (c) Collection.
  - (13) Identification of those individuals prohibited from receiving member business loans.
  - (14) Guidelines for purchase and sale of member business loans and loan participations, if the credit union intends to engage in these activities.

*Note:* The Office of Credit Unions recognizes that all of the provisions of the policy may not apply to every loan.

**DFI-CU 72.07 Collateral and security requirements.** Unless granted a waiver by the director, all of the following shall apply:

- (1) All member business loans shall be secured by collateral in accordance with this section, except for the following:
  - (a) A credit card line of credit granted to nonnatural persons that is limited to routine purposes normally made available under such lines of credit.
  - (b) A loan made by a credit union where the loan and the credit union meet all of the following:
    1. The amount of the loan or loans to any one individual does not exceed 1% of the credit union's net worth.
    2. The aggregate of the unsecured business loans under this paragraph does not exceed 10% of the credit union's net worth.
    3. The credit union has a net worth ratio of at least 7%.

4. The credit union submits reports to the Office of Credit Unions with its NCUA call reports providing numbers and such other details as may be required by the director to demonstrate compliance with this paragraph.

(2) For a member business loan secured by collateral on which the credit union will have a first lien, a credit union may grant the loan with an LTV ratio in excess of 80% only where the value in excess of 80% is as follows:

(a) Covered through acquisition of private mortgage or equivalent type insurance provided by an insurer acceptable to the credit union, and the LTV ratio does not exceed 95%; or

(b) Insured or guaranteed, or subject to advance commitment to purchase, by an agency of the federal government, state, or any of its political subdivisions, and the LTV ratio does not exceed 95%.

(3) For a member business loan secured by collateral on which the credit union will have a second or lesser priority lien, the credit union shall not grant the loan with an LTV ratio in excess of 80%.

(4) For a member business loan secured by the same collateral on which the credit union will have a first lien as well as other lesser priority liens, the credit union may grant the loan with an LTV ratio in excess of 80% only if sub. (2)(a) or (b) is satisfied. In no case shall the LTV ratio exceed 95%.

(5) For a member business loan secured by the collateral on which the credit union will have lesser priority liens but no first lien, the credit union shall not grant the loan with an LTV ratio in excess of 80%.

**DFI-CU 72.08 Amount of loan.** Unless the director grants a waiver for a higher amount, the aggregate amount of business loans to a member or associated members shall not exceed 15% of the credit union's net worth or \$100,000.00, whichever is greater.

**DFI-CU 72.09 Calculating the aggregate 15% limit.** To calculate the aggregate 15% limitation, the credit union shall do the following:

(1) Calculate the numerator by adding together the amount of the member business loans to a member and associated members, if any. From this amount, the credit union shall subtract each of the following:

(a) Any portion secured by shares or deposits in the credit union making the extension of credit or in other credit unions, or deposits in other financial institutions.

(b) Any portion insured or guaranteed by any agency or subdivision of the state or federal government.

(c) Any portion subject to an advance commitment to purchase by any agency or subdivision of the state or federal government.

(2) After completing the calculation in sub. (1), divide the numerator by the credit union's net worth.

**DFI-CU 72.10 Available waivers.** A credit union may seek a waiver for any of the following:

- (1) Construction and development loan requirements under s. DFI-CU 72.04.
- (2) Loan-to-value ratio requirements under s. DFI-CU 72.07.
- (3) Maximum loan amount to a member and associated members under s. DFI-CU 72.08.
- (4) Appraisal requirements under s. 722.3 of NCUA rules.

*Note:* A copy of NCUA rules may be obtained by writing to the Office of Credit Unions, P.O. Box 14137, Madison, WI 53714-0137.

**DFI-CU 72.11 Obtaining a waiver.** (1) To obtain a waiver under s. DFI-CU 72.10, a credit union shall submit a request to the director. The request shall contain all of the following:

- (a) A copy of the member business loan policy.
- (b) The higher limit sought, if applicable.
- (c) An explanation of the need to raise the limit, if applicable.
- (d) Documentation supporting the credit union's ability to manage this activity.
- (e) An analysis of the credit union's prior experience making member business loans, including each of the following:
  1. The history of loan losses and loan delinquency.
  2. Volume, and cyclical or seasonal patterns.
  3. Diversification.
  4. Concentrations of credit to a member and associated members in excess of 15% of net worth.
  5. Underwriting standards and practices.

6. Types of loans grouped by purpose and collateral.

7. The qualifications of personnel responsible for underwriting and administering member business loans.

(2) Upon receipt of the request for waiver, the director shall do all of the following:

(a) Review the information provided in the request.

(b) Evaluate the level of risk to the credit union.

(c) Consider the credit union's historical capital, asset, quality, management, earnings and liquidity ("CAMEL") composite and component ratings.

(d) Notify the credit union when the waiver request is deemed complete.

(e) Notify the credit union of the action taken within 45 calendar days of receiving a complete request.

(3) In connection with a waiver request under s. DFI-CU 72.10(1) through (3), all of the following shall apply:

(a) The director shall provide a copy of the waiver request to the applicable regional director of the NCUA, and shall consult and seek to work cooperatively with the applicable regional director in deciding upon the request.

(b) The waiver shall not be effective until the director approves it.

(c) If the credit union requesting the waiver does not receive notification within 45 calendar days of the date the complete request was received by the director, the waiver request shall be deemed approved by the director.

(d) The director shall promptly notify the applicable regional director of NCUA of his or her decision on the request.

(4) In connection with a waiver request under s. DFI-CU 72.10(4), all of the following shall apply:

(a) If the director approves the request, the director shall promptly forward the request to the applicable regional director of the NCUA for decision under 12 C.F.R. 723.12.

(b) The waiver shall not be effective until the applicable regional director of the NCUA approves it in accordance with 12 C.F.R. 723.12.

(c) The credit union may appeal the regional director's decision in accordance with 12 C.F.R. 723.13.

**DFI-CU 72.12 Classifying non-delinquent member business loans to reserve for potential loss.** Non-delinquent member business loans shall be classified based on factors such as the adequacy of analysis and supporting documentation. A credit union shall classify potential loss loans as either substandard, doubtful or loss. The criteria for determining the classification of loans shall be as follows:

(1) **SUBSTANDARD.** A loan classified substandard is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. The loan must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. The loan is characterized by the distinct possibility that the credit union will sustain some loss if the deficiency is not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in individual loans classified substandard.

(2) **DOUBTFUL.** A loan classified as doubtful has all the weaknesses inherent in one classified substandard, with the added characteristic that the weakness or weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the loan, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition or liquidation actions; capital injection; perfecting liens on collateral; and refinancing plans.

(3) **LOSS.** A loan classified loss is considered uncollectible and of such little value that its continuance as a loan is not warranted. This classification does not necessarily mean that the loan has absolutely no recovery or salvage value, but rather, that it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may occur in the future.

**DFI-CU 72.13 Schedule of reserves.** The following schedule sets the minimum amount a credit union shall reserve for classified member business loans:

<b>Classification</b>	<b>Amount Required</b>
Substandard	10% of outstanding balance, unless other factors indicate a greater or lesser amount is appropriate.  <i>Example: An example of a factor is the history of such loans at the credit union.</i>
Doubtful	50% of the outstanding balance.
Loss	100% of the outstanding balance.

**DFI-CU 72.14 Aggregate member business loan limit.** The aggregate limit on the amount of a credit union's member business loans is the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets.

**DFI-CU 72.15 Exceptions to the aggregate business loan limit.** Credit unions that meet any one of the following criteria qualify for an exception from the aggregate member business loan limit:

- (1) Credit unions that have a low-income designation.
- (2) Credit unions that participate in the Community Development Financial Institutions program.
- (3) Credit unions that are chartered for the purpose of making member business loans, as supported by documentary evidence.

*Example: the credit union's charter, bylaws, business plan, field of membership, board minutes and loan portfolio.*

**DFI-CU 72.16 Obtaining an exception.** (1) The exception under s. DFI-CU 72.15(1) and (2) shall be effective upon written notice to the director of such designation or participation.

(2) To obtain an exception under s. DFI-CU 72.15(3), a credit union shall submit its request to the director. An exception shall not be effective until approved by the director. The exception request shall include documentation demonstrating that the credit union meets the criteria for the exception. The exception shall not expire unless revoked for safety and soundness reasons by the director.

(3) The director shall promptly notify the applicable region of the NCUA of his or her decision on the request.

**DFI-CU 72.17 Record keeping requirements.** A credit union shall separately identify member business loans in its records. On its financial reports, a credit union shall identify member business loans in the aggregate.

This rule shall take effect on the first day of the month following publication in the Wisconsin administrative register as provided in s. 227.22(2)(intro.), Stats.

## NOTE

Pursuant to s. 227.14 (3), Stats., an agency shall include a reference to forms in a note to the proposed rule and shall attach a description of how copies of the forms may be obtained. Pursuant to s. 227.14 (3), copies of forms may be obtained at the following:

Office of Credit Unions  
P.O. Box 14137  
345 W. Washington Avenue, 3<sup>rd</sup> Floor  
Madison, WI 53714-0137

**Fiscal Estimate — 2001 Session**

- Original       Updated  
 Corrected       Supplemental

LRB Number	Amendment Number if Applicable
Bill Number	Administrative Rule Number

**Subject**

Member business loans.

**Fiscal Effect**

State:  No State Fiscal Effect

Check columns below only if bill makes a direct appropriation or affects a sum sufficient appropriation.

- Increase Existing Appropriation       Increase Existing Revenues  
 Decrease Existing Appropriation       Decrease Existing Revenues  
 Create New Appropriation

Increase Costs — May be possible to absorb within agency's budget.

- Yes       No

Decrease Costs

Local:  No Local Government Costs

- |  |   |
|--|---|
| 1. <input type="checkbox"/> Increase Costs<br><input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory | 3. <input type="checkbox"/> Increase Revenues<br><input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory |
| 2. <input type="checkbox"/> Decrease Costs<br><input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory | 4. <input type="checkbox"/> Decrease Revenues<br><input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory |

5. Types of Local Governmental Units Affected:

- Towns    Villages    Cities  
 Counties    Others  
 School Districts       WTCS Districts

**Fund Sources Affected**

- GPR    FED    PRO    PRS    SEG    SEG-S

Affected Chapter 20 Appropriations  
None

**Assumptions Used in Arriving at Fiscal Estimate**

The rule provides certain criteria, exemptions, prohibitions and waivers; establishes procedures for programs and criteria for policies; sets forth collateral, security and record keeping requirements; and sets forth limitations, calculations and classifications relating to member business loans. The rule would be the implementing provision under state law authorizing credit unions to make loans to their members. The promulgation of this rule has been approved by the Credit Union Review Board. The activity will be reviewed as part of the existing examination process by the Office of Credit Unions and therefore has no fiscal impact.

**Long-Range Fiscal Implications**

None

Prepared By: Mark Schlei	Telephone No. 267-1705	Agency DFI
Authorized Signature	Telephone No. 267-1705	Date (mm/dd/ccyy) 03/11/02



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**WISCONSIN LEGISLATIVE COUNCIL  
RULES CLEARINGHOUSE**

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**Ronald Sklansky**  
*Clearinghouse Director*

**Richard Sweet**  
*Clearinghouse Assistant Director*

**Terry C. Anderson**  
*Legislative Council Director*

**Laura D. Rose**  
*Legislative Council Deputy Director*

**CLEARINGHOUSE REPORT TO AGENCY**

[THIS REPORT HAS BEEN PREPARED PURSUANT TO S. 227.15, STATS. THIS IS A REPORT ON A RULE AS ORIGINALLY PROPOSED BY THE AGENCY; THE REPORT MAY NOT REFLECT THE FINAL CONTENT OF THE RULE IN FINAL DRAFT FORM AS IT WILL BE SUBMITTED TO THE LEGISLATURE. THIS REPORT CONSTITUTES A REVIEW OF, BUT NOT APPROVAL OR DISAPPROVAL OF, THE SUBSTANTIVE CONTENT AND TECHNICAL ACCURACY OF THE RULE.]

**CLEARINGHOUSE RULE 02-034**

**AN ORDER to create chapter CU 34, relating to member business loans**

**Submitted by DEPARTMENT OF FINANCIAL INSTITUTIONS**

**03-11-02 RECEIVED BY LEGISLATIVE COUNCIL.**

**04-08-02 REPORT SENT TO AGENCY.**

**RNS:NZ:tlu;ksm**

**LEGISLATIVE COUNCIL RULES CLEARINGHOUSE REPORT**

This rule has been reviewed by the Rules Clearinghouse. Based on that review, comments are reported as noted below:

1. STATUTORY AUTHORITY [s. 227.15 (2) (a)]

Comment Attached      YES       NO

2. FORM, STYLE AND PLACEMENT IN ADMINISTRATIVE CODE [s. 227.15 (2) (c)]

Comment Attached      YES       NO

3. CONFLICT WITH OR DUPLICATION OF EXISTING RULES [s. 227.15 (2) (d)]

Comment Attached      YES       NO

4. ADEQUACY OF REFERENCES TO RELATED STATUTES, RULES AND FORMS  
[s. 227.15 (2) (e)]

Comment Attached      YES       NO

5. CLARITY, GRAMMAR, PUNCTUATION AND USE OF PLAIN LANGUAGE [s. 227.15 (2) (f)]

Comment Attached      YES       NO

6. POTENTIAL CONFLICTS WITH, AND COMPARABILITY TO, RELATED FEDERAL  
REGULATIONS [s. 227.15 (2) (g)]

Comment Attached      YES       NO

7. COMPLIANCE WITH PERMIT ACTION DEADLINE REQUIREMENTS [s. 227.15 (2) (h)]

Comment Attached      YES       NO



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## WISCONSIN LEGISLATIVE COUNCIL RULES CLEARINGHOUSE

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Ronald Sklansky  
*Clearinghouse Director*

Richard Sweet  
*Clearinghouse Assistant Director*

Terry C. Anderson  
*Legislative Council Director*

Laura D. Rose  
*Legislative Council Deputy Director*

### CLEARINGHOUSE RULE 02-034

#### Comments

**[NOTE:** All citations to “Manual” in the comments below are to the **Administrative Rules Procedures Manual**, prepared by the Revisor of Statutes Bureau and the Legislative Council Staff, dated September 1998.]

#### 2. Form, Style and Placement in Administrative Code

a. In s. DFI-CU 72.01 (1) (a), the semicolon should be deleted and replaced with a period.

In s. DFI-CU 72.01 (1) (b), the semicolon and the word “and” should be deleted and replaced with a period. The same change should be made in s. DFI-CU 72.04 (2) (a).

b. Examples should be set forth below the text to which they apply. For example, see s. DFI-CU 72.03 (1) (a) to (c).

c. In several provisions, “may not” should replace “shall not” to express a prohibition. [See s. 1.01 (2), Manual.]

#### 4. Adequacy of References to Related Statutes, Rules and Forms

a. In s. DFI-CU 72.01 (3), the reference to s. DFI-CU 72.02 should be more specific. It could be changed to s. DFI-CU 72.02 (1).

b. In s. DFI-CU 72.07 (1) (b) 2. and 4., reference is made to “par. (b).” The references are unclear since they are set forth in par. (b).

5. Clarity, Grammar, Punctuation and Use of Plain Language

a. In s. DFI-CU 72.01 (2), it would be clearer if “. . . if he or she has . . .” were replaced with “. . . by means of . . .” Further, the definition does not contain a requirement that anyone be a member of the credit union. Surely, an “associated member” must at least be associated with *a member* or be *a member*, himself or herself. Further, the use of the term throughout the rule is confusing.

b. In s. DFI-CU 72.01 (3), either the term that is defined should be changed from “business purpose” to “business purpose loan,” or the definition should be changed to delete “. . . a loan where the borrower intends to use the proceeds for . . .” However, if the defined term is changed to “business purpose loan” how will a “business purpose loan” be different from a “member business loan”?

c. In s. DFI-CU 72.01 (6), the computation of a loan-to-value (LTV) ratio excludes loans that are not member business loans even if such a nonmember business loan is secured by the item of collateral for which the LTV ratio is being computed. Is that the intent?

d. In s. DFI-CU 72.02 (2) (c), the second sentence is unclear. If a member has a number of loans, and an additional loan causes the total amount loaned to that member to exceed \$50,000, is only the additional loan considered a business loan, or are all the loans considered business loans? Further, “any” should be changed to “an” in the first sentence.

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g. In s. DFI-CU 72.03 (1) (d), the wording is awkward. Is the paragraph meant to refer to *any* associated member, or to any associated member who shares a pecuniary interest in a business endeavor with one of the individuals listed in the subsection?

h. In s. DFI-CU 72.03 (2), what is the definition of “additional income”?

i. In s. DFI-CU 72.03 (3), “decision making” should be hyphenated.

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k. In s. DFI-CU 72.04 (1) (c), “. . . the federal government, state, or any . . .” should be changed to “. . . the federal government, the state, or any . . .”

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- m. In s. DFI-CU 72.05 (2), what does "utilize the services of" mean? This phrase appears in a number of places in the rule.
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- p. In s. DFI-CU 72.06 (9), does the credit union's member business loan policy have to contain all this documentation, or does the policy have to contain a requirement for all this documentation.
- q. In s. DFI-CU 72.07 (1) (b) (intro.), the loan and the credit union meet "all of the following:" should be changed to "all of the following apply."
- r. In s. DFI-CU 72.07 (1) (b) 3., the credit union must have a net worth of at least 7% of what?
- s. In several provisions, "an" should precede "LTV" since the pronunciation of the acronym begins with a vowel ("L" is pronounced "el").
- t. In s. DFI-CU 72.07 (2) (a) through (c), the use of both "or" and "and" at the end of the paragraphs makes it unclear which paragraph or paragraphs apply.
- u. In s. DFI-CU 72.07, do subs. (4) and (5) make sub. (3) unnecessary?
- v. In s. DFI-CU 72.09, "to calculate the aggregate 15% limitation . . ." is ambiguous. It seems that the calculation that the section delineates yields not a 15% limitation, but rather the percentage of the credit union's net worth that the member's loans represents. Furthermore, the title and text of the section should be clear about what sections it applies to. Both s. DFI-CU 72.04 and s. DFI-CU 72.08 contain a 15% limitation.
- w. In s. DFI-CU 72.08 what does "a member or associated members" refer to? Does the section's limitation apply to each member and to each group of associated members; does it apply to all associated members collectively; or does it apply to each member and each associated member? A similar problem appears in s. DFI-CU 72.09 (1). In that section, however, the phrase is changed to "a member and associated members." The problem also occurs in s. DFI-CU 72.10 (3). There, the problem is exacerbated by the use of different terms. Section DFI-CU 72.10 (3) uses "member and associated members," but refers to s. DFI-CU 72.08 where the phrase is "member or associated member." Part of the problem might stem from the way in which "associated member" is defined.
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ac. In s. DFI-CU 72.11, the phrase "... respective regional director ..." appears a number of times. The word "respective" should be changed to "appropriate." "Respective" is an adjective relating to two or more things or persons regarded individually. This should be done in s. DFI-CU 72.16 (3) as well.

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af. In s. DFI-CU 72.12 (3), "... but rather, it is ..." should be changed to "... but rather, that it is ..."

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## WISCONSIN LEGISLATIVE COUNCIL RULES CLEARINGHOUSE

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**Ronald Sklansky**  
*Clearinghouse Director*

**Richard Sweet**  
*Clearinghouse Assistant Director*

**Terry C. Anderson**  
*Legislative Council Director*

**Laura D. Rose**  
*Legislative Council Deputy Director*

### CLEARINGHOUSE REPORT TO AGENCY

[THIS REPORT HAS BEEN PREPARED PURSUANT TO S. 227.15, STATS. THIS IS A REPORT ON A RULE AS ORIGINALLY PROPOSED BY THE AGENCY; THE REPORT MAY NOT REFLECT THE FINAL CONTENT OF THE RULE IN FINAL DRAFT FORM AS IT WILL BE SUBMITTED TO THE LEGISLATURE. THIS REPORT CONSTITUTES A REVIEW OF, BUT NOT APPROVAL OR DISAPPROVAL OF, THE SUBSTANTIVE CONTENT AND TECHNICAL ACCURACY OF THE RULE.]

#### CLEARINGHOUSE RULE 02-034

AN ORDER to create chapter CU 34, relating to member business loans

Submitted by **DEPARTMENT OF FINANCIAL INSTITUTIONS**

03-11-02 RECEIVED BY LEGISLATIVE COUNCIL.

04-08-02 REPORT SENT TO AGENCY.

RNS:NZ:tlu;ksm





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# WISCONSIN LEGISLATIVE COUNCIL RULES CLEARINGHOUSE

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## CLEARINGHOUSE RULE 02-034

### Comments

**[NOTE: All citations to “Manual” in the comments below are to the Administrative Rules Procedures Manual, prepared by the Revisor of Statutes Bureau and the Legislative Council Staff, dated September 1998.]**

#### 2. Form, Style and Placement in Administrative Code

a. In s. DFI-CU 72.01 (1) (a), the semicolon should be deleted and replaced with a period.

In s. DFI-CU 72.01 (1) (b), the semicolon and the word “and” should be deleted and replaced with a period. The same change should be made in s. DFI-CU 72.04 (2) (a).

b. Examples should be set forth below the text to which they apply. For example, see s. DFI-CU 72.03 (1) (a) to (c).

c. In several provisions, “may not” should replace “shall not” to express a prohibition. [See s. 1.01 (2), Manual.]

#### 4. Adequacy of References to Related Statutes, Rules and Forms

a. In s. DFI-CU 72.01 (3), the reference to s. DFI-CU 72.02 should be more specific. It could be changed to s. DFI-CU 72.02 (1).

b. In s. DFI-CU 72.07 (1) (b) 2. and 4., reference is made to “par. (b).” The references are unclear since they are set forth in par. (b).

**5. Clarity, Grammar, Punctuation and Use of Plain Language**

a. In s. DFI-CU 72.01 (2), it would be clearer if “. . . if he or she has . . .” were replaced with “. . . by means of . . .” Further, the definition does not contain a requirement that anyone be a member of the credit union. Surely, an “associated member” must at least be associated with *a member* or be *a member*, himself or herself. Further, the use of the term throughout the rule is confusing.

b. In s. DFI-CU 72.01 (3), either the term that is defined should be changed from “business purpose” to “business purpose loan,” or the definition should be changed to delete “. . . a loan where the borrower intends to use the proceeds for . . .” However, if the defined term is changed to “business purpose loan” how will a “business purpose loan” be different from a “member business loan”?

c. In s. DFI-CU 72.01 (6), the computation of a loan-to-value (LTV) ratio excludes loans that are not member business loans even if such a nonmember business loan is secured by the item of collateral for which the LTV ratio is being computed. Is that the intent?

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ad. In s. DFI-CU 72.12 (1), the last sentence seems inconsistent with the rest of the subsection. The first three sentences seem to contemplate a loan-by-loan analysis to determine whether a loan is substandard. The last sentence seems to allow an individual loan to be classified as substandard regardless of whether it meets the standards for a substandard loan.

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PROPOSED RULE  
STATE OF WISCONSIN  
OFFICE OF CREDIT UNIONS

An order to create ch. DFI—CU 72 relating to member business loans. Analysis: Statutory authority: ss. 186.115(1) and (2), 186.235(8) and 227.11(2), Stats. Statutes interpreted: ss. 186.115(1) and (2), 186.235(8), Stats. Summary: The rule provides certain criteria, exemptions, prohibitions and waivers; establishes procedures for programs and criteria for policies; sets forth collateral, security and record keeping requirements; and sets forth limitations, calculations and classifications relating to member business loans. The rule would be the implementing provision under state law authorizing credit unions to make loans to their members. The promulgation of this rule has been approved by the Credit Union Review Board. Agency person to be contacted for substantive questions and responsible for the agency's internal processing: Ginger Larson, Director, Office of Credit Unions, tel. (608) 261-9543. Pursuant to the statutory authority referenced above, the Office of Credit Unions adopts the following:

SECTION 1: CHAPTER DFI—CU 72 is created to read:

CHAPTER DFI—CU 72

MEMBER BUSINESS LOANS

**DFI-CU 72.01 Definitions.** In this chapter:

(1) "Amount" of a business loan includes all the following:

- (a) Any unfunded commitment to make the loan;
- (b) The outstanding balance of the loan; and
- (c) Any undisbursed proceeds of the loan.

(2) "Associated member" means a person who is associated with another if he or she has a shared ownership, investment or other pecuniary interest in a business or commercial endeavor.

(3) "Business purpose" means a loan where the borrower intends to use the proceeds for any of the purposes listed in s. DFI-CU 72.02.

(4) "Construction or development loan" means a financing arrangement for acquiring real property or rights to real property, including land or structures, with the intent to develop or improve it for any of the following:

- (a) Residential housing for sale.

WHAT IS  
THEY? IF  
he doesn't  
include  
loan, his  
AP, then  
member  
business loan?

A member?  
by means of

1  
I don't make sense.  
Should term "member" be changed  
and should 72.02(a)-(e) be changed  
to 72.02(1)(a)-(e)

*The amount of all loans that are secured by a particular item of collateral divided*

- (b) Income property.
- (c) Commercial use.
- (d) Industrial use.
- (e) Any similar uses.

(5) "Director" means the director of the office of credit unions or an authorized representative of the director.

(6) "Loan-to-value ratio" or "LTV ratio" means the amount of all member business loans by the credit union secured by an item of collateral added to the amount of all outstanding loans by other lenders secured by that item of collateral, that total amount then being divided by the market value of that item of collateral.

?

(7) "Member business loan" has the meaning set forth in s. DFI—CU 72.02.

(8) "NCUA" means the National Credit Union Administration.

(9) "Net worth" means the retained earnings as defined under Generally Accepted Accounting Principles. Retained earnings include undivided earnings, regular reserves and any other appropriations designated by management or regulatory authorities.

**DFI-CU 72.02 Member business loan.** (1) "Member business loan" means any loan, line of credit, letter of credit or any unfunded commitment to make a loan, where the borrower intends to use the proceeds for any of the following purposes:

*should include a requirement that the loan be made to a member*

- (a) Commercial.
- (b) Corporate.
- (c) Investment property.
- (d) Business venture.
- (e) Agricultural.

(2) "Member business loan" shall not include any of the following:

- (a) A business purpose loan fully secured by a lien on a 1 to 4 family dwelling that is the member's primary residence.
- (b) A business purpose loan fully secured by shares or deposits in the credit union making the extension of credit or in other credit unions, or by deposits in other financial institutions.

(c) One or more business purpose loans to a member or any associated member that, in the aggregate, are less than \$50,000. The entire amount of such a loan or loans that equals or exceeds this amount, or that causes the aggregate to exceed this amount is a business loan. ) What??

(d) A business purpose loan where a federal or state agency or any of their political subdivisions fully insures repayment, or fully guarantees repayment, or provides an advance commitment to purchase in full.

(e) A loan granted by a corporate credit union to another credit union. *How is a corporate credit union different from a credit union? what does that term mean?*

**DFI-CU 72.03 Prohibited member business loans. (1) OFFICERS.** A credit union shall not grant a member business loan to any of the following:

(a) Chief executive officer. *incl. persons in the title* Example: President, Treasure or Manager.

(b) Assistant chief executive officers. Example: Assistant President, Vice President, Assistant Treasurer or Assistant Manager.

(c) Chief financial officer. Example: Comptroller.

(d) Any associated member or immediate family member of anyone listed in this subsection.

*what is "additional" income*  
(2) **EQUITY AGREEMENTS OR JOINT VENTURES.** A credit union shall not grant a member business loan if any additional income received by the credit union or its senior management employees is tied to the profit or sale of the business or commercial endeavor for which the loan is made.

(3) **DIRECTORS.** A credit union shall not grant a member business loan to one of its directors unless the board of directors approves granting the loan and the director is recused from the decision making process.

**DFI-CU 72.04 Construction and development loans.** Unless the director grants a waiver, a credit union that makes construction or development loans shall be subject to all of the following:

*the credit union's*  
(1) The aggregate of all construction and development loans shall not exceed 15% of net worth. In determining the aggregate, the credit union may exclude any portion of a loan that is any of the following:

(a) Secured by shares or deposits in the credit union making the extension of credit or in other credit unions, or by deposits in other financial institutions.

No CEOs  
of just  
loans  
a just the  
credit union  
CEO

(b) Insured or guaranteed by any agency or subdivision of the state or federal government.

(c) Subject to an advance commitment to purchase by any agency of the federal government, state, or any of their political subdivisions.

(2) The borrower shall have a minimum of the following:

(a) 30% equity interest in the project being financed if the loan is for land development; ~~and~~ <sup>the govt.</sup>

(b) 25% equity interest in the project being financed if the loan is for construction or for a combination of development and construction.

(3) The funds shall 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.

(4) The credit union shall not make construction <sup>or</sup> and development loans unless it utilizes the services of an individual with at least five years direct experience in construction and development lending.

WHAT DOES  
UTILIZES MEAN?  
SERVICES "

**DFI-CU 72.05 Implementation of a member business loan program.** (1) The board of directors shall adopt a specific member business loan policy and review it at least annually.

(2) In making member business loans, the credit union shall utilize the services of an individual with at least two years direct experience with the type of lending in which it will engage, except as provided s. DFI-CU 72.04(4).

(3) A credit union does not have to hire staff to meet the requirements of this section. However, credit unions shall ensure that expertise with the type of lending in which it will engage is available. *Example: A credit union may meet the experience requirement through various approaches, such as the services of a credit union service organization, an employee of another credit union, an independent contractor or other third parties.*

(4) The actual decision to grant a loan shall reside solely with the credit union.

**DFI-CU 72.06 Member business loan policy requirements.** A credit union's member business loan policy shall include all of the following:

(1) The types of business loans the credit union will make.

(2) The credit union's trade area.

(3) The maximum amount of the credit union's assets, in relation to net worth, that it will invest in member business loans.

(4) The maximum amount of the credit union's assets, in relation to net worth, that it will invest in a given type of business loans.

(5) The maximum amount of the credit union's assets, in relation to net worth, that it will loan to a member or associated members, subject to s. DFI-CU 72.08.

(6) The qualifications and experience of personnel involved in making and administering business loans.

(7) A requirement for analysis and documentation of the ability of the borrower to repay the loan.

(8) Receipt and periodic updating of financial statements and other documentation, including tax returns.

(9) Documentation sufficient to support each request to extend credit, or increase an existing loan or line of credit, except where the board of directors finds that the required documentation is not generally available for a particular type of loan and states the reasons for those findings in the credit union's written policies. The documentation shall include all of the following:

(a) Balance sheet.

(b) Cash flow analysis.

(c) Income statement.

(d) Tax data.

(e) Analysis of leveraging.

(f) Comparison with industry average or similar analysis.

(10) Collateral requirements, including all of the following:

(a) Loan-to-value ratios.

(b) Determination of value.

(c) Determination of ownership.

(d) Steps to secure various types of collateral.

could  
make  
info

A requirement  
for

(e) A schedule as to how often the credit union will reevaluate the value and marketability of collateral.

(11) The interest rates and maturities of the business loans.

(12) General loan procedures, including all of the following:

(a) Loan monitoring.

(b) Servicing and follow-up.

(c) Collection.

(13) Identification of those individuals prohibited from receiving member business loans.

(14) Guidelines for purchase and sale of member business loans and loan participations, if the credit union intends to engage in these activities.

*Note:* The Office of Credit Unions recognizes that all of the provisions of the policy may not apply to every loan.

**DFI-CU 72.07 Collateral and security requirements.** Unless granted a waiver by the director, all of the following shall apply:

(1) All member business loans shall be secured by collateral in accordance with this section, except for the following:

(a) A credit card line of credit granted to nonnatural persons that is limited to routine purposes normally made available under such lines of credit.

(b) A loan made by a credit union where ~~the loan and the credit union meet~~ all of the following: ??

1. The amount of the loan or loans to any one individual does not exceed 1% of the credit union's net worth.

2. The aggregate of the unsecured business loans under par. (b) does not exceed 10% of the credit union's net worth.

3. The credit union has a net worth of at least 7%.

4. The credit union submits reports to the Office of Credit Unions with its NCUA call reports providing numbers and such other details as may be required by the director to demonstrate compliance with par. (b).

*Handwritten notes:*  
- A circled '3' with an arrow pointing to item 3.  
- A circled '1' with an arrow pointing to item 1.  
- Next to item 3: "if what? Isn't net worth a \$ amount"  
- Next to item 4: "??"

(2) For a member business loan secured by collateral on which the credit union will have a first lien, a credit union may grant the loan with (a) LTV ratio in excess of 80% only where the value in excess of 80% is as follows:

(a) Covered through acquisition of private mortgage or equivalent type insurance provided by an insurer acceptable to the credit union; or

(b) Insured or guaranteed, or subject to advance commitment to purchase, by an agency of the federal government, state, or any of its political subdivisions, and

(c) The LTV ratio does not exceed 95%.

(3) For a member business loan secured by collateral on which the credit union will have a second or lesser priority lien, the credit union shall not grant the loan with a LTV ratio in excess of 80%.

(4) For a member business loan secured by the same collateral on which the credit union will have a first lien as well as other lesser priority liens, the credit union may grant the loan with (a) LTV ratio in excess of 80% only if sub. (2)(a) or (b) is satisfied. In no case shall the LTV ratio exceed 95%.

(5) For a member business loan secured by the collateral on which the credit union will have lesser priority liens but no first lien, the credit union shall not grant the loan with (a) LTV ratio in excess of 80%.

**DFI-CU 72.08 Amount of loan.** Unless the director grants a waiver for a higher amount, the aggregate amount of business loans to a member or associated members shall not exceed 15% of the credit union's net worth or \$100,000.00, whichever is greater.

*PARALLEL*

**DFI-CU 72.09 Calculating the aggregate 15% limit.** To calculate the aggregate 15% limitation, the credit union shall do the following:

(1) Calculate the numerator by adding together the amount of the member business loans to a member and associated members, if any. From this amount, the credit union shall subtract each of the following:

(a) Any portion secured by shares or deposits in the credit union making the extension of credit or in other credit unions, or deposits in other financial institutions.

(b) Any portion insured or guaranteed by any agency or subdivision of the state or federal government.

(c) Any portion subject to an advance commitment to purchase by any agency or subdivision of the state or federal government.

(2) After completing the calculation in sub. (1), divide the numerator by net worth.

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*Is it the full amount of the loan if any portion of the loan is secured by shares - a financial inst, or is the portion of the loan that is secured by the shares. In other words, would a loan that is only partially secured by shares or deposits be subtracted*

**DFI-CU 72.10 Available waivers.** A credit union may seek waiver for any of the following:

- (1) Construction and development loan requirements under s. DFI-CU 72.04.
- (2) Loan-to-value ratios <sup>requirements</sup> under s. DFI-CU 72.07.
- (3) Maximum loan amount to a member and associated members under s. DFI-CU 72.08.
- (4) Appraisal requirements under s. 722.3 of NCUA rules.

*Note:* A copy of NCUA rules may be obtained by writing to the Office of Credit Unions, P.O. Box 14137, Madison, WI 53714-0137.

**DFI-CU 72.11 Obtaining a waiver.** (1) To obtain a waiver under s. DFI-CU 72.10, a credit union shall submit a request to the director. The request shall contain all of the following:

- (a) A copy of the member business loan policy.
- (b) The higher limit sought, if applicable.
- (c) An explanation of the need to raise the limit, if applicable.
- (d) Documentation supporting the credit union's ability to manage this activity.
- (e) An analysis of the credit union's prior experience making member business loans, including each of the following:
  1. The history of loan losses and loan delinquency.
  2. Volume, and cyclical or seasonal patterns.
  3. Diversification.
  4. Concentrations of credit to a member and associated members in excess of 15% of net worth.
  5. Underwriting standards and practices.
  6. Types of loans grouped by purpose and collateral.
  7. The qualifications of personnel responsible for underwriting and administering member business loans.

(2) Upon receipt of the request for waiver, the director shall do all of the following:

(a) Review the information provided in the request.

(b) Evaluate the level of risk to the credit union.

(c) Consider the credit union's historical capital, asset, quality, management, earnings and liquidity ("CAMEL") composite and component ratings.

(d) Notify the credit union when the waiver request is deemed complete.

(e) Notify the credit union of the action taken within 45 calendar days of receiving a complete request.

(3) In connection with a waiver request under s. DFI-CU 72.10(1) through (3), all of the following shall apply:

(a) The director shall provide a copy of the waiver request to the ~~respective~~ regional director of the NCUA, and shall consult and seek to work cooperatively with the ~~respective~~ regional director in deciding upon the request.

(b) The waiver shall not be effective until the director approves it.

(c) If the credit union requesting the waiver does not receive notification within 45 calendar days of the date the complete request was received by the director, the waiver request shall be deemed approved by the director.

(d) The director shall promptly notify the ~~respective~~ regional director of NCUA of his or her decision on the request.

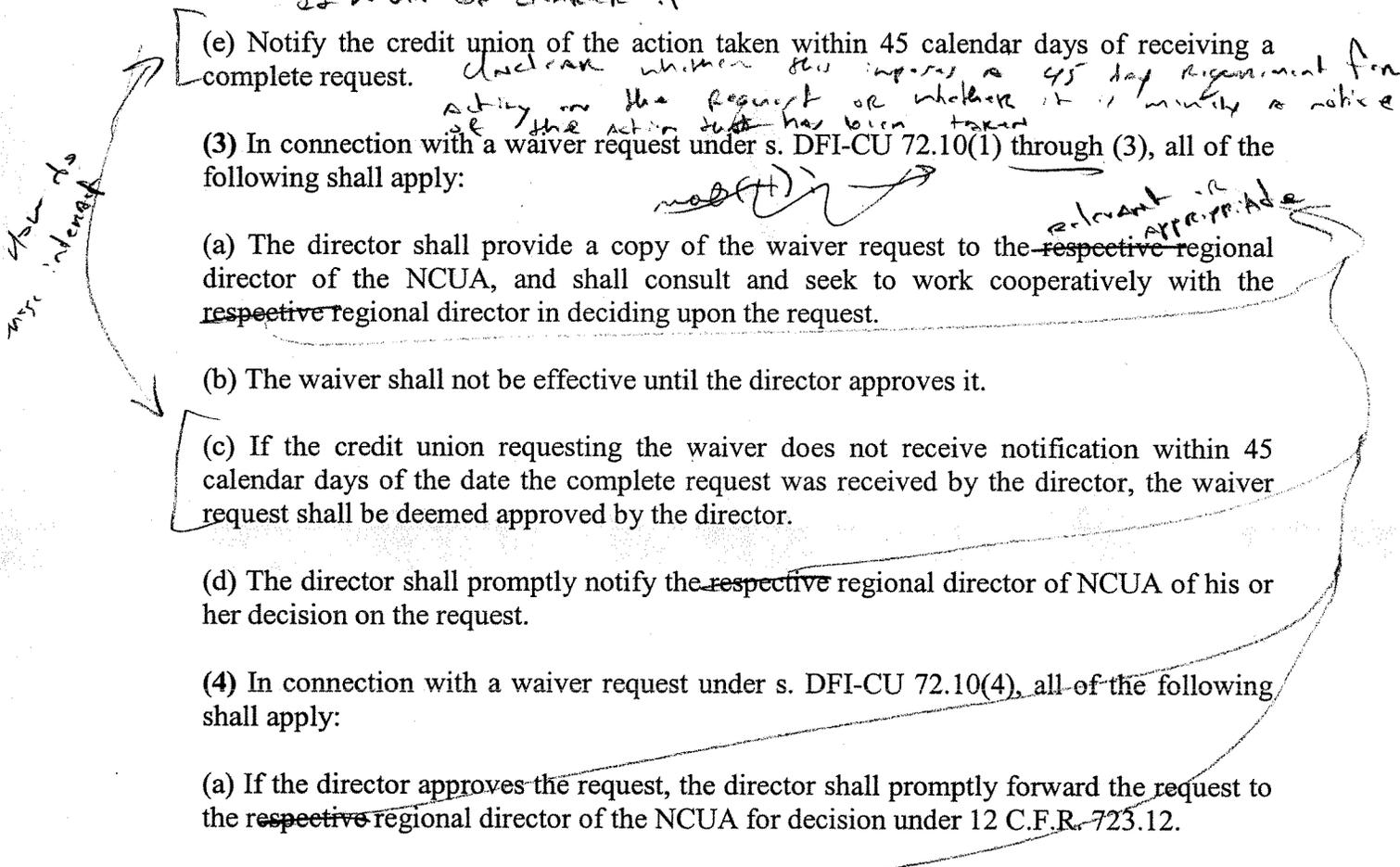
(4) In connection with a waiver request under s. DFI-CU 72.10(4), all of the following shall apply:

(a) If the director approves the request, the director shall promptly forward the request to the ~~respective~~ regional director of the NCUA for decision under 12 C.F.R. 723.12.

(b) The waiver shall not be effective until the ~~respective~~ regional director of the NCUA approves it in accordance with 12 C.F.R. 723.12.

(c) The credit union may appeal the regional director's decision in accordance with 12 C.F.R. 723.13.

**DFI-CU 72.12 Classifying non-delinquent member business loans to reserve for potential loss.** Non-delinquent member business loans shall be classified based on factors such as the adequacy of analysis and supporting documentation. A credit union



shall classify potential loss loans as either substandard, doubtful or loss. The criteria for determining the classification of loans shall be as follows:

(1) **SUBSTANDARD.** A loan classified substandard is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. The loan must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. The loan is characterized by the distinct possibility that the credit union will sustain some loss if the deficiency is not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in individual loans classified substandard.

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(2) **DOUBTFUL.** A loan classified as doubtful has all the weaknesses inherent in one classified substandard, with the added characteristic that the weakness or weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the loan, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition or liquidation actions; capital injection; perfecting liens on collateral; and refinancing plans.

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(3) **LOSS.** A loan classified loss is considered uncollectible and of such little value that its continuance as a loan is not warranted. This classification does not necessarily mean that the loan has absolutely no recovery or salvage value, but rather, it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may occur in the future.

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**DFI-CU 72.13 Schedule of reserves.** The following schedule sets the minimum amount a credit union shall reserve for classified member business loans:

Classification	Amount Required
Substandard	10% of outstanding balance, unless other factors indicate a greater or lesser amount is appropriate. <i>Example: An example of a factor is the history of such loans at the credit union.</i>
Doubtful	50% of the outstanding balance.
Loss	100% of the outstanding balance.

**DFI-CU 72.14 Aggregate member business loan limit.** The aggregate limit on the amount of a credit union's member business loans is the lesser of 1.75 times the credit union's net worth or 12.25% of the credit union's total assets.

**DFI-CU 72.15 Exceptions to the aggregate business loan limit.** Credit unions that meet any one of the following criteria qualify for an exception from the aggregate member business loan limit:

- (1) Credit unions that have a low-income designation.
- (2) Credit unions that participate in the Community Development Financial Institutions program.
- (3) Credit unions that are chartered for the purpose of making member business loans, as supported by documentary evidence. *Example: the credit union's charter, bylaws, business plan, field of membership, board minutes and loan portfolio.*

**DFI-CU 72.16 Obtaining an exception.** (1) The exception under s. DFI-CU 72.15(1) and (2) shall be effective upon written notice to the director of such designation or participation.

(2) To obtain an exception under s. DFI-CU 72.15(3), a credit union shall submit its request to the director. An exception shall not be effective until approved by the director. The exception request shall include documentation demonstrating that the credit union meets the criteria for the exception. The exception shall not expire unless revoked for safety and soundness reasons by the director.

(3) The director shall promptly notify the <sup>relevant/appropriate</sup> respective region of the NCUA of his or her decision on the request.

**DFI-CU 72.17 Record keeping requirements.** A credit union shall separately identify member business loans in its records and in the aggregate on its financial reports.

<sup>? delete "and"??</sup>  
This rule shall take effect on the first day of the month following publication in the Wisconsin administrative register as provided in s. 227.22(2)(intro.), Stats.

## NOTE

Pursuant to s. 227.14 (3), Stats., an agency shall include a reference to forms in a note to the proposed rule and shall attach a description of how copies of the forms may be obtained. Pursuant to s. 227.14 (3), copies of forms may be obtained at the following:

Office of Credit Unions  
P.O. Box 14137  
345 W. Washington Avenue, 3<sup>rd</sup> Floor  
Madison, WI 53714-0137