Proposed Rules

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This section of the FEDERAL REGISTER contains notices to the public of the proposed issuance of rules and regulations. The purpose of these notices is to give interested persons an opportunity to participate in the rule making prior to the adoption of the final rules.

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 714

Leasing

AGENCY: National Credit Union Administration (NCUA).

ACTION: Proposed regulation.

SUMMARY: The proposed leasing regulation updates and redesignates NCUA's long-standing policy statement on leasing, Interpretive Ruling and Policy Statement (IRPS) 83–3, as an NCUA regulation. IRPS 83–3 authorizes federal credit unions to engage in either direct or indirect leasing and either open-end or closed-end leasing of personal property to their members if such leasing arrangements are the functional equivalent of secured loans. In addition, the proposed regulation formalizes NCUA's position, set forth in legal opinion letters, that FCUs do not have to own the leased property in an indirect leasing arrangement if certain requirements are satisfied.

DATES: Comments must be received on or before December 14, 1999.

ADDRESSES: Direct comments to Becky Baker, Secretary of the Board. Mail or hand-deliver comments to: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428. Fax comments to (703) 518–6319. E-mail comments to boardmail@ncua.gov. *Please send comments by one method only.*

FOR FURTHER INFORMATION CONTACT: Paul M. Peterson, Staff Attorney, Division of Operations, Office of the General Counsel, at the above address or by telephone: (703) 518–6555.

SUPPLEMENTARY INFORMATION:

A. Background

In 1983, the NCUA Board issued Interpretive Ruling and Policy Statement (IRPS) 83–3, Federal Credit Union Leasing of Personal Property to Members, 48 FR 52560 (November 21, 1983), stating that federal credit unions (FCUs) can lease personal property to their members if the leasing of the personal property is the functional equivalent of secured lending. The NCUA Board did not want FCUs engaged in leasing to assume burdens or subject themselves to risks greater than those ordinarily incident to secured lending. The NCUA Board determined that for leasing to be the functional equivalent of secured lending, a lease had to be a net, full payout lease with an estimated residual value not exceeding 25% unless guaranteed. In addition, an FCU engaged in leasing had to retain salvage powers over the leased property and maintain a contingent liability insurance policy with an endorsement for leasing.

In the supplementary section of IRPS 83–3, the NCUA Board stated that FCUs could engage in either direct or indirect leasing. That is, an FCU could either purchase property from a third party for the purpose of leasing such property to a member or purchase the lease and the leased property after the lease had been executed between the third party and the member. Further, FCUs could engage in either open-end or closed-end leasing, that is, an FCU could either require a member to assume the risk and responsibility for any difference in the estimated residual value and the actual value of the property at lease end or assume such risk itself.

After IRPS 83–3 was issued, NCUA received a number of inquiries regarding whether an FCU must own the leased property. NCUA responded through legal opinion letters that, in states requiring an entity engaged in leasing to be a licensed dealer, which involved posting a bond and complying with other state regulatory requirements, an FCU did not have to own the leased property. However, the FCU had to be named as the sole lienholder on the leased property and granted an unconditional, irrevocable power of attorney to transfer title to the leased property to the FCU.

Thereafter, the leasing industry argued that, irrespective of state limitations, an FCU should be able to take a lien on the leased property instead of having to own the property. The leasing industry stated that an FCU would be insulated from tort liability by not being the owner of the leased property and that an FCU's member would receive lower lease payments if a third-party lessor (the leasing company) was able to take advantage of certain tax benefits available only when the leasing company retained ownership of the property. NCUA concluded in legal opinion letters that although the direct and indirect leasing arrangements described in the supplementary section of IRPS 83–3 resulted in an FCU owning the leased property, such ownership was not required. NCUA's position was that the purchase or assignment of a lease and the receipt of a lien on the leased property was a form of permissible indirect leasing if the following requirements were satisfied: (1) The FCU was named as the sole lienholder on the leased property; (2) the FCU was assigned all of the leasing company's rights under the lease; and (3) the FCU obtained an unconditional, irrevocable power of attorney to transfer title in the leased property to the FCU.

NCUA undertook the proposed redesignation of IRPS 83–3 as an NCUA regulation as part of a regulatory review of all of its IRPS. Upon review of IRPS 83–3, the NCUA Board determined that it would be better suited as a regulation. 62 FR 11773 (March 13, 1997). The NCUA Board's goal in redesignating IRPS 83–3 as a regulation is to increase regulatory effectiveness by establishing a rule that states NCUA's current position on leasing, is easy to locate, and sets forth safety and soundness requirements to protect FCUs engaged in leasing.

On October 29, 1998, the NCUA Board issued a notice of proposed rulemaking and request for comment on leasing. 63 FR 57950 (October 29, 1998). The proposed leasing regulation adopted the policy on leasing set out in IRPS 83–3 and incorporated NCUA's position, set forth in legal opinion letters, that FCUs do not have to own the leased property in indirect leasing if certain requirements are satisfied. The comment period expired on January 27, 1999.

B. Comments

NCUA received fourteen comments on the proposed leasing regulation. Comments were received from five federal credit unions, one state-chartered credit union, three state leagues, two national credit union trade associations, one leasing company, one bank trade association, and a joint comment from an auditing company

and a bank consulting company. All commenters, except one, supported the NCUA Board's effort to establish a regulation on the leasing of personal property. The dissenting commenter believed that a leasing regulation was unnecessary because NCUA examiners could monitor an FCU's leasing program during regular examinations.

The NCUA Board has thoroughly evaluated the comments and has incorporated many of the suggested changes. Due to these changes to the original proposed leasing regulation, the Board has decided to issue a second proposed leasing regulation for additional comments.

C. Format

In drafting the proposed leasing regulation, the NCUA Board chose to use a plain English, question and answer format. The Board supports plain English as a means to increase regulatory comprehension and improve compliance among those affected by the regulation. Plain English drafting emphasizes the use of informative headings (often written as a question), lists and charts where appropriate, non-technical language, and sentences in the active voice. The NCUA wrote this proposed regulation as a series of questions and answers. The word ''you'' in an answer refers to an FCU.

Most commenters favored the NCUA Board's use of the question and answer (Q&A) style. One commenter, however, thought that Q&A style increased the potential for misunderstanding and confusion. The NCUA Board agrees that some regulations are more appropriate than others for Q&A. The NCUA Board believes that Q&A works well in the context of the leasing regulation.

D. Section-by-Section Analysis

Proposed Section 714.1—What Does This Part Cover?

Section 714.1 of the proposed regulation stated that Part 714 covers the standards and requirements that an FCU must follow when engaged in the lease financing of personal property. One commenter suggested that the term ''lease financing'' be replaced with ''transactions involving leasing.'' The commenter believes that there is a distinction between the terms ''leasing'' and ''financing,'' thus, using the term ''lease financing'' may lead to confusion. The NCUA Board agrees with the commenter and has changed ''lease financing'' to ''leasing.''

Proposed Section 714.2—What Are the Permissible Leasing Arrangements?

Section 714.2 of the proposed regulation stated that FCUs may engage in either direct or indirect leasing. One commenter suggested certain changes in § 714.2(b) to take into consideration the varying relations that may exist among parties in a leasing arrangement. Specifically, this commenter suggested that the NCUA Board should amend the sentence ''In indirect leasing, you purchase a lease and the leased property for the purpose of leasing such property to your member after the lease has been executed between a third party and your member'' by adding the phrase ''except as provided in § 714.3,'' substituting the word ''having'' for the second ''leasing,'' and inserting the word ''leased'' after the word ''property.'' The NCUA Board has added the phrase, ''except as provided in § 714.3.'' The NCUA Board believes that adding this cross-reference points the reader to a permissible form of indirect leasing which allows for title in the leased property to remain with a third party. However, the NCUA Board has not incorporated the commenter's other suggested changes. The NCUA Board wants the regulation to state clearly that an FCU, not another party, is to lease the personal property to its member. The commenter's suggested changes would imply otherwise.

In addition, the NCUA Board has added the text of prior § 714.6 to this section. Section 714.6 stated that an FCU can engage in either closed-end or open-end leasing, that is, either an FCU can assume the risk for the difference between the estimated residual value and the actual value of property at lease end or the lessee can assume the risk. Also, one commenter noted that the phrase ''relied upon residual value'' should be replaced with the phrase ''estimated residual value.'' The NCUA Board made this change for consistency and accuracy.

Proposed Section 714.3—Must You Own the Leased Property?

Section 714.3 of the proposed regulation states that an FCU does not have to own the leased property in an indirect leasing arrangement if three requirements are met: (1) The FCU receives a full assignment of the lease; (2) the FCU is named as the sole lienholder of the property; and (3) the FCU receives an unconditional, irrevocable power of attorney to transfer title in the leased property to itself.

The commenters supported the NCUA Board's decision not to require that an FCU own the leased property in an indirect leasing arrangement. One commenter noted that owning the leased property is not necessary since, in a loan or credit sale, an FCU does not own the underlying asset, but only has a lien. Three commenters contended that owning the leased property could open an FCU up to potential liability issues, tax issues, and state regulation and licensing requirements.

Six commenters, however, stated that they were against requiring a full assignment of the lease. Four of these commenters believed that the decision of whether to obtain a full assignment of a lease should be made by an FCU based on the circumstances of the leasing arrangement. Another commenter stated that the full assignment requirement was unnecessary because sales of or liens in leases are subject to Uniform Commercial Code (UCC) perfection rules. This commenter contended that a full assignment would not protect an FCU if a leasing company went bankrupt unless the full assignment had been perfected. In addition, one commenter expressed concern that, if a full assignment is required, leasing companies might refuse to do business with FCUs since they would not retain ownership of the leases. The commenter stated that leasing companies receive certain tax benefits from lease ownership and that, without those tax benefits, leasing companies may have no incentive to do business with FCUs.

Three commenters were against requiring an FCU to obtain a power of attorney. Two of the commenters stated that such a decision should be made by an FCU's attorney based on the circumstances of the FCU's leasing arrangement. Further, one of these commenters stated that a power of attorney is unnecessary because Article 9 of the Uniform Commercial Code provides an FCU with the right to take possession and dispose of collateral upon a default without a power of attorney. In addition, one commenter stated that a power of attorney provides little protection to an FCU in the face of a leasing company bankruptcy. The commenter suggested that obtaining a security agreement that grants an FCU a sole lien position in the leased property with the right to foreclose in the event of a default would be more beneficial.

The Board has reconsidered this form of indirect leasing in light of these comments and the recent bankruptcy of a leasing company (*Security Excel Corporation,* No. 96–32410 (Bankr. N.D. Ind.) (hereinafter *Security Excel*). In *Security Excel,* a bankruptcy that affected several credit unions, the trustee argued that the leasing company, not the FCU, owned both the leases and the leased property. The trustee further argued that the FCU had no security interest in either the leases or the leased property and, in the alternative, that whatever security interests might exist

were not properly perfected. Ultimately, the *Security Excel* case was settled, at some significant expense to certain credit unions.

As demonstrated in *Security Excel,* leasing arrangements that involve leaving title to the leased property in the name of the a third-party leasing company are complex and may involve significant risks to the FCU. In most of these leasing company arrangements, the NCUA Board understands that the FCU finances the full, or close to the full, value of the leased property and that the FCU will ultimately recover its full investment only if it collects all the lease payments and recoups all the proceeds from the leasing company's post-lease sale of the property. The FCU must be concerned about both the credit worthiness of the member and the solvency of the leasing company. In the event of insolvency of one or both parties, the FCU must be able to enforce its right to payment under the lease and, if necessary, its right to secure and dispose of the property as the collateral securing receipt of both lease payments and proceeds due from the post-lease property sale.

The fact that the FCU has no authority to lend money to a nonmember leasing company that is not a credit union service organization further complicates these arrangements. For example, the FCU must ensure that, despite the lack of a creditor-debtor relationship with the leasing company, the FCU has a well-defined security interest in the leased property. In addition, the FCU must make sure that its rights in the leased property and its ownership of the lease are properly recorded so as to perfect those rights against bankruptcy trustees and other third-party creditors. To take another example, a vehicle owned by a leasing company may be considered as ''inventory'' under the relevant commercial codes, and protection of a security interest in such inventory may well require steps beyond recording the lien on the certificate of title and filing the certificate with the department of motor vehicles.

In light of these issues, the legal arguments advanced in *Security Excel,* and the comments received on our previously proposed § 714.3, the NCUA Board is proposing that an FCU that does not own the leased property must take certain precautions.

First, the FCU must receive a full assignment of the lease, meaning that the FCU must become the owner of the lease. The NCUA Board believes that, if an FCU receives a full assignment of a lease and the assignment is properly recorded, the lease should not be subject to the claims of a bankruptcy trustee acting on behalf of a leasing company that becomes bankrupt. The Board notes that an assignment of various rights under a lease, such as the right to receive payments, is not the same as a full assignment of the lease. There are varying ways that an acceptable assignment may be drafted. Some examples are: ''Leasing Company assigns this lease to ABC Federal Credit Union'' or ''Leasing Company makes a full assignment of this lease to ABC Federal Credit Union'' or ''Leasing Company conveys all of its right, title, and interest in this lease to ABC Federal Credit Union.'' Language that purports to assign only one or more particular rights or remedies under the lease would not constitute a full assignment of the lease and so is unacceptable.

Second, the FCU must be the sole lienholder of the leased property. This language is consistent with IRPS 83–3, requiring that the lease must be the functional equivalent of a secured loan.

Third, the FCU must enter into a security agreement with the leasing company to protect the FCU's lien on the property. The security agreement must describe the FCU's interest in the property. It must set forth the terms and conditions upon which the leasing company or the member may be in default and thus entitle the FCU to take immediate possession of the property and dispose of it. The security agreement must be signed by the leasing company. The FCU must also take any further steps necessary to ensure that its security is properly perfected to protect the FCU should the leasing company be forced into bankruptcy. Thus, for example, if the leased property constitutes the lessor's inventory under state law, perfection may require filing with the appropriate state agency, such as the Secretary of State. See the Uniform Commercial Code, 9–302 and 9–401.

The NCUA Board believes that a power of attorney may be unnecessary for an FCU holding a well-defined and perfected security interest in the leased property. In the event of a default by leasing company or lessee, the FCU should be able to take possession and dispose of the collateral without the power of attorney. Thus, the new proposed rule no longer contains any requirement for a power of attorney. The Board notes, however, that the proposed rule does not prohibit an FCU from employing a power of attorney, in addition to a security agreement, as the FCU sees fit in any particular leasing arrangement.

Proposed Section 714.4—What Are the Lease Requirements?

Section 714.4 states that leases must be net, full payout leases, with a maximum estimated residual value of 25% of the original cost of the leased property unless guaranteed. One commenter suggested that the NCUA Board revise the description of net lease to allow FCUs to finance certain dealer included services, including mechanical breakdown protection, credit life and disability premiums, and license and registration fees. The Board does not believe that these dealer services, which are generally additional services purchased by a lessee to satisfy his or her obligations under the ''net'' lease concept, should be financed. The Board notes that these costs, if financed by the credit union, may raise safety and soundness issues, particularly if the lessee has made little or no down payment and so there is no value in the collateral to secure the financing of these particular services.

One commenter stated that the wording used to describe the full payout requirement was confusing and failed to specify an FCU's source of recovery to meet the requirement. The NCUA Board agrees with the commenter and has added a sentence stating that an FCU's source of recovery will come from the lessee's payments and the residual value of the leased property at the expiration of the lease term.

Five commenters wanted the NCUA Board to raise the estimated residual value limit. These commenters believed that the 25% estimated residual value limit was restrictive and placed FCUs at a disadvantage against other lenders that were not required to obtain a guarantee when an estimated residual value greater than 25% was used. Further, the five commenters suggested that the NCUA Board allow FCUs to self-insure against the increased risk associated with a higher estimated residual value. One commenter suggested that the NCUA Board allow FCUs to set their own estimated residual values as long as the combination of residual value insurance, manufacturer guarantees, and residual value reserves for loss maintained over the life of the leases is sufficient to cover the residual value risks assumed.

The NCUA Board believes that the risks associated with leasing are substantially reduced due to the 25% limit placed on estimated residual values and has not raised the limit. The NCUA Board notes that the Office of the Comptroller of the Currency (OCC) has very similar rules on estimated residual values. The OCC places a 25%

estimated residual value limit on bank leases, and requires banks to guarantee estimated residual values in excess of the 25% limit. 12 CFR 23.21(a)(2).

The Board also notes that the purpose of the leasing regulation is to facilitate a consumer financing transaction with a member that is roughly the equivalent of a secured loan. In the closed-end lease arrangement, which is the most common arrangement, the member lessee is not liable to the FCU for the payment of the residual value at the end of the lease. As the estimated residual value increases, the member's financial responsibility to the FCU, as a percent of the FCU's total investment, decreases correspondingly. If the NCUA Board were to permit significantly higher estimated residual value amounts, a lease transaction would lose its character of being substantially equivalent to secured lending to its member. Instead, the credit union would be dependent on the sale of the vehicle to recoup a significant part of its investment, and so would be in a business very similar to used car sales. Credit unions may not engage in the business of selling cars. See *M&M Leasing Corporation v. Seattle First National Bank,* 563 F.2d 1377 (9th Cir. 1977), *cert. denied,* 436 U.S. 958 (1978).

Proposed Section 714.5—What Is Required if an Estimated Residual Value Greater Than 25% Is Used?

Section 714.5 of the proposed regulation incorrectly stated the guarantee requirement when the estimated residual value exceeds 25% of the original cost of the leased property. In issuing the proposed regulation, the Board's intention was to adopt the leasing policy and requirements as contained in IRPS 83–3. Proposed § 714.5 incorrectly stated that, if a residual value greater than 25% was used, the *full* estimated residual value of the leased property must be guaranteed. Five commenters noted that a guarantee of the full value should not be required. IRPS 83–3 requires that only the estimated residual value above 25% of the original cost be guaranteed and, in this second proposed regulation, this section now reflects the requirement as stated in IRPS 83–3.

One commenter suggested revising § 714.5 to permit others parties, in addition to a manufacturer or insurance company, to guarantee the estimated residual value. IRPS 83–3 allowed the manufacturer, the lessee, or third party not affiliated with the FCU to guarantee the estimated residual value. The proposed regulation eliminated the lessee as a guarantor on the basis that it would be difficult to collect from a lessee or monitor the lessee's creditworthiness and capacity to meet the guarantee. However, the NCUA Board has revised § 714.5 to allow any financially capable party to guarantee the estimated residual value. Thus, a lessee, if properly qualified, could guarantee the estimated residual value. This approach is consistent with IRPS 83–3.

In addition, four commenters were against requiring insurance companies guaranteeing estimated residual values to have at least a B+ rating. These commenters believed that such a requirement was unnecessary and noted that the OCC's leasing regulation did not establish such a requirement. The NCUA Board believes that establishing a minimum rating standard ensures that the institutional guarantor has the resources to meet the guarantee.

The NCUA Board has amended the rating requirement to read ''The guarantor may also be an insurance company with an A.M. Best rating of at least a B+, or with the equivalent of at least an A.M. Best B+ rating from another major rating company.'' This amendment clarifies the source of the B+ rating and specifies that ratings from other rating companies may be used to establish financial capability.

Proposed Section 714.6—Are You Required To Retain Salvage Powers Over the Leased Property?

Section 714.6 states that an FCU must retain salvage powers over the leased property. One commenter suggested that the NCUA Board add the language ''pursuant to your contractual rights'' contained in subsection (b) to subsection (a) which sets forth a credit union's salvage powers. The NCUA Board does not believe that this additional language is needed and has left this section unchanged. However, the NCUA Board has deleted the reference to the assignment of ''a vendor's interest in a lease'' in § 714.6(b). The FCU must receive an assignment of the entire lease as required by § 714.3(a).

Proposed Section 714.7—What Are the Insurance Requirements Applicable to Leasing?

Section 714.7(a) requires an FCU to maintain a contingent liability insurance policy if it owns the leased property or, if it does not, it must be named as the co-insured. One commenter suggested that the NCUA Board also require an FCU to obtain excess liability insurance as well as the contingent liability insurance. The NCUA Board believes that such additional insurance is not needed to protect FCUs. Section 714.7(b) states that the lessee is to carry liability or collateral protection insurance on the leased property. The NCUA Board intended that both liability and collateral protection insurance were to be purchased, and has changed the word ''or'' to ''and.'' In addition, one commenter stated that, for the most part, FCUs are named as the loss payee on a physical damage coverage policy and as the additional insured on a liability insurance policy and this should be reflected in the proposed leasing regulation. The NCUA Board has adopted the commenter's changes.

Proposed Section 714.8—What Rate of Interest May Be Charged Under a Lease?

Section 714.8 stated that an FCU engaged in leasing may charge an interest rate higher than the usury limit set for FCUs engaged in lending. One commenter stated that § 714.8 reflects a misunderstanding of leases since leases do not have interest rates, only an implicit rate which may or may not be received depending on the ultimate residual recovery. The NCUA Board has reworded this section to eliminate the confusion. The Board also added language to clarify that 12 CFR 701.21(c)(6), prohibiting penalties for early payment, does not apply to leasing arrangements. Early termination is governed by the Consumer Leasing Act, 15 U.S.C. 1667–67f, and Regulation M, 12 CFR part 213.

Proposed Section 714.9—When Engaged in Indirect Leasing, Must You Comply With the Purchase of Eligible Obligation Rules Set Forth in § 701.23 of This Chapter?

Section 714.9 states that an FCU may participate in indirect leasing arrangements under its authority to make loans. The NCUA Board intended § 714.9 to inform FCUs that their participation in an indirect leasing arrangement does not subject them to the purchase of eligible obligation rules. However, two commenters stated that § 714.9 was unclear. Thus, the NCUA Board has added language to clarify this section and has changed the section title.

Proposed Section 714.10—What Other Laws Must You Comply With When Engaged in Leasing?

Section 714.10 sets forth the additional laws that an FCU must comply with when engaged in leasing. One commenter requested that the NCUA Board clarify whether FCUs are subject to state leasing disclosure laws. The NCUA Board amended § 714.10 to point out that credit unions must

comply with the Consumer Leasing Act (the Leasing Act). 15 U.S.C. 1667–67f. Section 1667e of the Leasing Act generally requires that lessors comply with state leasing laws if the state law is not in conflict with the Leasing Act or provides greater consumer protection than the Leasing Act. The Board also notes that, with regard to federal and state lending laws, the proposed language of § 714.10 requires compliance with § 701.21 of this chapter. Subsection 701.21(b) discusses the applicability of other federal and state lending laws in some detail.

Another commenter stated that the disclosure requirements of Regulation M are cumbersome and not easily understood, thus, NCUA should simplify the leasing disclosure requirements and employ something similar to the ''fed box'' used for truth-in-lending disclosures. The Board notes that there are already model disclosure forms in the appendix to Regulation M, and these forms set out leasing disclosures in a manner similar to the truth-in-lending ''fed box.''

E. Additional Comments

Two commenters suggested that the NCUA Board address balloon note programs or guaranteed buy-back programs in the proposed leasing regulation. The commenters did not provide any details explaining the balloon note or guaranteed buy-back programs.

The primary distinction between a loan and a lease is who owns the underlying property. In a loan, the borrower owns the property and the lender is a lienholder. In a lease, the borrower-lessee has no ownership or lienhold interest in the property. Accordingly, it is the NCUA Board's position that programs which involve loans and not leases are significantly different from leasing arrangements, and should not be addressed in a leasing regulation.

However, the NCUA Board would like to note, as stated in legal opinion letters, that balloon note or guarantee buy-back programs giving any borrower on a loan the option of returning property directly to the FCU at the end of the financing period are impermissible. Programs that authorize the borrower to turn the property into a third party for liquidation and cash recoupment may be acceptable.

F. Regulatory Procedures

Regulatory Flexibility Act

The NCUA Board certifies that the proposed regulation will not have a significant impact on a substantial number of small credit unions. Most small credit unions do not offer lease financing arrangements to their members. Accordingly, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

The NCUA Board has determined that the requirement in § 714.5 that an FCU must obtain or have on file statistics documenting that a guarantor has the resources to meet an estimated residual value guarantee constitutes a collection of information under the Paperwork Reduction Act. The NCUA Board estimates that it will take an average of one to two hours to acquire, maintain, and evaluate such documentation. The NCUA Board estimates that approximately 750 FCUs are engaged in leasing, so that the total annual collection burden is estimated to be no more than 1500 hours. The NCUA Board submitted a copy of this rule to the Office of Management and Budget (OMB) for its review. OMB assigned control number 3133–0151 to this information collection. The control number will be displayed in the table at 12 CFR Part 795.

Executive Order 12612

Executive Order 12612 requires NCUA to consider the effect of its actions on state interests. The proposed regulation only applies to federal credit unions. The NCUA Board has determined that the proposed regulation does not constitute a significant regulatory action for the purposes of the Executive Order.

G. Agency Regulatory Goal

NCUA's goal is to promulgate clear and understandable regulations that impose minimal regulatory burden. We request your comments on whether the proposed amendment is understandable and minimally intrusive if implemented as proposed.

List of Subjects in 12 CFR Part 714

Credit unions, Leasing.

By the National Credit Union Administration Board on October 6, 1999.

Becky Baker,

Secretary to the Board.

Accordingly, NCUA proposes to add Part 714 to read as follows:

PART 714—LEASING

Sec.

Authority: 12 U.S.C. 1756, 1757, 1766, 1785, 1789.

§ 714.1 What does this part cover?

This part covers the standards and requirements that you, a federal credit union, must follow when engaged in the leasing of personal property.

§ 714.2 What are the permissible leasing arrangements?

(a) You may engage in direct leasing. In direct leasing, you purchase personal property from a vendor, becoming the owner of the property at the request of your member, and then lease the property to that member.

(b) You may engage in indirect leasing. In indirect leasing, you purchase a lease and, except as provided in § 714.3, the leased property for the purpose of leasing such property to your member after the lease has been executed between a third party and your member.

(c) You may engage in open-end leasing. In an open-end lease, your member assumes the risk and responsibility for any difference in the estimated residual value and the actual value of the property at lease end.

(d) You may engage in closed-end leasing. In a closed-end lease, you assume the risk and responsibility for any difference in the estimated residual value and the actual value of the property at lease end.

§ 714.3 Must you own the leased property in an indirect leasing arrangement?

You do not have to own the leased property in an indirect leasing arrangement if:

(a) You obtain a full assignment of the lease. A full assignment is the assignment of all the rights, interests, obligations, and title in a lease to you, that is, you become the owner of the lease;

(b) You are named as the sole lienholder of the leased property;

(c) You receive a security agreement, signed by the leasing company, granting you a sole lien in the leased property and the right to take possession and dispose of the leased property in the

event of a default by the lessee, a default in the leasing company's obligations to you, or a material adverse change in the leasing company's financial condition; and

(d) You take all necessary steps to record and perfect your security interest in the leased property. Your state's Commercial Code may treat the automobiles as inventory, and require a filing with the Secretary of State.

§ 714.4 What are the lease requirements?

(a) Your lease must be a net lease. In a net lease, your member assumes all the burdens of ownership including maintenance and repair, licensing and registration, taxes, and insurance;

(b) Your lease must be a full payout lease. In a full payout lease, you must reasonably expect to recoup your entire investment in the leased property, plus the estimated cost of financing, from the lessee's payments and the estimated residual value of the leased property at the expiration of the lease term; and

(c) Your estimated residual value may not exceed 25% of the original cost of the leased property unless the amount above 25% is guaranteed. Estimated residual value is the projected value of the leased property at lease end. Estimated residual value must be reasonable in light of the nature of the leased property and all circumstances relevant to the leasing arrangement.

§ 714.5 What is required if an estimated residual value greater than 25% is used?

You may use an estimated residual value greater than 25% of the original cost of the leased property if a financially capable party guarantees the amount above 25% of the original cost of the property. The guarantor may be the manufacturer. The guarantor may also be an insurance company with an A.M. Best rating of at least a B+, or with at least the equivalent of an A.M. Best B+ rating from another major rating company. You must obtain or have on file financial documentation demonstrating that the guarantor has the resources to meet the guarantee.

§ 714.6 Are you required to retain salvage powers over the leased property?

You must retain salvage powers over the leased property. Salvage powers protect you from a loss and provide you with the power to take action if there is an unanticipated change in conditions that threatens your financial position by significantly increasing your exposure to risk. Salvage powers allow you:

(a) As the owner and lessor, to take reasonable and appropriate action to salvage or protect the value of the property or your interests arising under the lease; or

(b) As the assignee of a lease, to become the owner and lessor of the leased property pursuant to your contractual rights, or take any reasonable and appropriate action to salvage or protect the value of the property or your interests arising under the lease.

§ 714.7 What are the insurance requirements applicable to leasing?

(a) You must maintain a contingent liability insurance policy with an endorsement for leasing or be named as the co-insured if you do not own the leased property. Contingent liability insurance protects you should you be sued as the owner of the leased property. You must use an insurance company with a nationally recognized industry rating of at least a B+.

(b) Your member must carry the normal liability and collateral protection insurance on the leased property. You must be named as an additional insured on the liability insurance policy and as the loss payee on the collateral protection insurance policy.

§ 714.8 Are the early payment provisions, or interest rate provisions, applicable in leasing arrangements?

You are not subject to the early payment provisions set forth in § 701.21(c)(6) of this chapter. You are also not subject to the interest rate provisions in § 701.21(c)(7).

§ 714.9 Are indirect leasing arrangements subject to the purchase of eligible obligation limit set forth in § 701.23 of this chapter?

Your indirect leasing arrangements are not subject to the purchase of eligible obligation rules set forth in § 701.23 of this chapter if:

(a) You review the lease and other documents to determine that the arrangement complies with your leasing polices; and

(b) You receive a full assignment of the lease no more than five business days after it is signed by your member and a leasing company.

§ 714.10 What other laws must you comply with when engaged in leasing?

You must comply with the Consumer Leasing Act, 15 U.S.C. 1667–67f, and its implementing regulation, Regulation M, 12 CFR part 213. You must comply with state laws on consumer leasing, but only to the extent that the state leasing laws are consistent with the Consumer Leasing Act, 15 U.S.C. 1667e, or provide the member with greater protections or benefits than the Consumer Leasing Act. You are also subject to the lending rules set forth in § 701.21 of this chapter, except as provided in § 714.8 and § 714.9 of this part. The lending rules in § 701.21 address the preemption of other state and federal laws that impact on credit transactions.

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NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 724 and 745

Trustees and Custodians of Pension Plans; Share Insurance and Appendix

AGENCY: National Credit Union Administration.

ACTION: Notice of proposed rulemaking.

SUMMARY: The National Credit Union Administration (NCUA) proposes to revise its rules regarding a federal credit union's authority to act as trustee or custodian of pension plans. The proposal permits federal credit unions in a territory, including the trust territories, or a possession of the United States, or the Commonwealth of Puerto Rico, to offer trustee or custodian services for Individual Retirement Accounts (IRAs), where otherwise permitted.

DATES: Comments must be received on or before December 14, 1999.

ADDRESSES: Direct comments to Becky Baker, Secretary of the Board. Mail or hand-deliver comments to: National Credit Union Administration, 1775 Duke Street, Alexandria, Virginia 22314–3428. Fax comments to (703) 518–6319. E-mail comments to boardmail@ncua.gov. *Please send comments by one method only.*

FOR FURTHER INFORMATION CONTACT: Dianne M. Salva, Staff Attorney, Division of Operations, Office of General Counsel, at the above address or telephone: (703) 518–6540.

SUPPLEMENTARY INFORMATION: NCUA has received many inquiries concerning the permissibility of federal credit unions (FCUs) in Puerto Rico offering IRA services to members. In the past, the agency has responded that FCUs in Puerto Rico cannot provide the trustee services attendant to an IRA account. Part 724 of NCUA's regulations permits FCUs to serve as trustees for IRA accounts only if the IRA accounts qualify for specific tax treatment under the Internal Revenue Code (IRC), and if they are created or organized in the United States. Part 724 has its roots in the Employee Retirement Income Security Act of 1974 (ERISA). ERISA amended the IRC so that federally-insured credit unions were recognized