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Regulatory Treatment for Paycheck Protection Program Loans

NCUA LETTER TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22314

Date
April 2020
Letter No
20-CU-11
20-CU-11 / April 2020
Regulatory Treatment for Paycheck Protection Program Loans
To
Federally Insured Credit Unions
Subject
Member Business Lending
Status

Active
To
Federally Insured Credit Unions
Subj
Member Business Lending

Dear Boards of Directors and Chief Executive Officers:

The NCUA Board recently approved an interim final rule amending regulatory requirements related to the Small Business Administration's (SBA) Paycheck Protection Program (PPP) loans and the Board of Governors of the Federal Reserve System's PPP Lending Facility (PPPLF) advances. These regulatory changes will become effective upon publication of the interim final rule in the *Federal Register*.

This letter discusses these regulatory changes and provides clarifications on PPP loans to credit union officials and non-members based on the most recent information from the SBA. The NCUA previously provided information about the PPP through Letter to Credit Unions 20-CU-06, [Small Business Administration Loan Programs to Help Small Businesses and Members during the COVID-19 Pandemic](#). Subsequently, the SBA issued [additional guidance \(opens new window\)](#) on the PPP, including their responses to [frequently asked questions \(opens new window\)](#).

SBA's Paycheck Protection Program Loans

Regulatory Changes

The NCUA Board approved multiple regulatory changes related to how the SBA's PPP loans are classified for regulatory capital and commercial underwriting purposes. First, to conform with the [Coronavirus Aid, Relief, and Economic Security Act \(opens new window\)](#) (CARES Act), NCUA regulations § 702.104 was amended to include PPP loans as low-risk assets for purposes of calculating a credit union's risk based net worth ratio. PPP loans will receive a zero-percent risk weight.¹

The interim final rule also includes a provision that clearly excludes PPP loans from the commercial loan definition in § 723.2 of the NCUA's regulations. Thus, PPP loans will not be subject to the enhanced underwriting and monitoring requirements for commercial loans. In addition, PPP loans will not be included in a credit union's net member business loan calculation for purposes of determining compliance with the statutory member business loan limit.²

PPP Loans to Officials

In general, [SBA regulations \(opens new window\)](#) prohibit a financial institution from extending an SBA loan to a business in which the lender or its Associates owns an equity interest.³ However, unlike other SBA loan programs, PPP loans are uniform for all borrowers, and the standard underwriting process does not apply because a creditworthiness assessment is not required for PPP loans.

The SBA notes that many directors and equity holders of lenders making PPP loans are owners of unrelated businesses and certain SBA prohibitions regarding eligible borrowers for SBA loans are not applicable to PPP loans.⁴ Thus, the SBA's most recent [interim final rule on the PPP loan program \(opens new window\)](#) appears to clarify that a credit union can extend a PPP loan to a small business owned, in part or in whole, by a member of the credit union's board of directors if the small business meets PPP eligibility requirements, provided the director is not a key employee or officer of the credit union. If you have any questions regarding eligibility, you should contact the SBA. Credit unions are still prohibited from making SBA loans, including PPP loans, to small businesses owned in part, or in whole by, officers and key employees of the credit union.

Credit unions that consider making PPP loans to a business owned in part, or in whole by, a member of the board of directors should ensure they comply with [§ 701.21 of the NCUA's regulations \(opens new window\)](#), which places certain restrictions on loans and lines of credit to officials.⁵ Specifically, a federal credit union's board of directors must approve loans and lines of credit to officials that, in aggregate, exceed \$20,000. In addition, the rate, terms, and conditions on loans and lines of credit to officials may not be more favorable than those offered to other credit union members.

PPP Loans to Non-Members

The Federal Credit Union Act prohibits federal credit unions from originating loans to non-members.⁶ If a potential borrower is not a current member, the credit union must ensure the borrower becomes a member by the time of loan closing.

Federal Reserve System's PPP Lending Facility

Background

The Federal Reserve established the PPPLF to bolster the effectiveness of the SBA's PPP. Under the PPPLF, the Federal Reserve will supply liquidity to participating financial institutions through term financing backed by PPP loans. Only SBA-guaranteed PPP loans that are originated by an eligible institution may be pledged as collateral to the Federal Reserve Banks. Please visit the Federal Reserve's [PPPLF website \(opens new window\)](#) for more information.

Treatment for Calculating Net Worth

The NCUA Board approved changes to § 702.2 of the NCUA's regulations related to the calculation of a credit union's net worth ratio. This change allows credit unions to exclude PPP loans pledged as collateral for a non-recourse loan that is provided as part of the PPPLF from the calculation of total assets for the purpose of calculating its net worth ratio. In effect, this amendment neutralizes the regulatory capital effects of PPP loans pledged to the PPPLF. Due to the non-recourse nature of the Fed's extension of credit to the credit union, the credit union is not exposed to credit or market risk from the pledged PPP covered loans.

Only PPP loans pledged to the PPPLF will be excluded from the net worth ratio calculation. Unpledged PPP loans will still be included in total assets for purposes of calculating the net worth ratio, but all PPP loans will continue to receive a zero-percent risk weight for purposes of risk based net worth, as discussed above.

Conclusion

The CARES Act provided relief to credit union members through PPP loans. To encourage credit union participation in this program, the NCUA Board has made necessary changes to the NCUA's regulations. Future NCUA Call Report instructions will include guidance on how to categorize PPP loans and advances obtained through the PPPLF on the Call Report.

The NCUA will continue to provide clarifications on the PPP program as necessary through the Frequently Asked Questions section of its [COVID-19 Information webpage](#). Please contact your NCUA regional office or state supervisory authority if you have questions about specific regulatory requirements or relief efforts.

Sincerely,

/s/

¹ This treatment will also be applicable to the NCUA's risk based capital rule, which currently has an effective date of January 1, 2022. The NCUA will make this conforming change to the risk-based capital rule in a future rulemaking prior to that regulation going into effect.

² PPP loans are excluded from the member business loan definition in § 723.8 because they are fully guaranteed by a federal agency.

³ An Associate is defined as an officer, director, key employee, or holder of 20 percent or more of the value of the lender's stock or debt instruments, or an Agent involved in the loan process. An Agent is an authorized representative, including an attorney, accountant, consultant, packager, lender service provider, or any other individual or entity representing an Applicant or Participant by conducting business with the SBA.

⁴ 85 FR 21747 (Apr. 20, 2020).

⁵ Section 701.21(d)(5) concerning non-preferential treatment for loans and lines of credit to officials is applicable to federally insured, state-chartered credit unions under §741.203.

⁶ 12 U.S.C. § 1757(5)

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National Credit Union Administration, 1775 Duke Street, Alexandria, VA 22314

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